

Corporate Exposure: Property Rating

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For different insurance companies to establish property insurance rates based on their individual experiences would be a difficult and expensive task. Establishing fair rates requires a highly technical analysis of building construction, occupancy, and services—not to mention a sophisticated claims reporting system. Realizing this, insurance companies collaborated to form a rating bureau that collects all the information and, using that information, suggests appropriate rates to be applied against specific building values. This central rating agency is the Insurance Services Organization (ISO). Besides developing rates, ISO has standardized many of the property policies. The pooling of information by the carriers is advantageous because the larger the sampling base, the greater the predictability.

The advantages to having a standard policy contract are numerous for the consumer. Among the most important advantages:

- There is no need to compare policy provisions or language from carrier to carrier because all carriers use the same contract form.
- When losses involve two or more insurance carriers, uniform provisions in each policy helps minimize settlement objections.
- Having similar contracts improves the consistency of loss data, which improves rate determination.

Of course, the major disadvantage of

standardized contracts is that they may not satisfy your specific needs or requirements.

Figuring the rates

Nonetheless, ISO considers a number of items when calculating rates, including the building's construction, occupancy, location, fire protection, and services. For example, buildings located in municipalities that have paid fire departments and that are within 500 feet of a fire department are considered "protected" risks (buildings that do not meet these criteria, not surprisingly, are considered "unprotected"). This is one of many variables used to help establish a rate on

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your building. All else being equal, two identically constructed office buildings in the same town will have the same fire rating. But, clearly, the buildings will have different tenants, different preventive maintenance procedures, etc., and thus there will likely be some adjustment in the fire rate.

Insureds can request a copy of their building rating schedule to review the factors that have gone into calculating the rate. Upon analyzing this exhibit, an insured can determine what, if any, steps can be taken to bring down the rate. For example, you may elect to install sprinklers in the building (you can perform a cost-benefit analysis to calculate your premium reduction versus the capital expense required to install the system). Simpler yet, your rate can be affected if there has been a dramatic change in the tenant mix in your building. If the build-

ing at one time had a light manufacturing operation on the entire first floor but is now occupied solely by an office environment, the rate should go down. Your agent can assist you in understanding the rating schedule and offer input in your cost-benefit analysis.

Changes for ISO

Although this rating approach has sufficed for years, ISO is undergoing substantive changes; these adjustments should be complete by the end of the decade. The greatest motivation for these changes? Some \$46 billion in property losses in the past five years. This figure is higher than the figure for total recorded losses for a 38-year span before this five-year period. An example: In 1992, hurricane Andrew struck Florida heavily, causing \$15 billion in property losses. Closer review determined that one quarter of this figure was directly attributable to building owners' failure to comply with building codes. ISO is now correcting the provisions to closely monitor building code compliance as well as the quality of services available from the municipality. These factors will weigh heavily in assigning a new rate. Overall, we believe that this significant change in property rate evaluations and rate structuring should be beneficial to the policyholder by bringing the rate closer in line with actual risk factors. Until this transition is accomplished, we encourage all our readers to review their rating schedules. It would not be surprising if you found that the rating schedule does not accurately represent current conditions at your facility. ■

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