Real Estate and Hotel Practice
Views
November 2016

Market trends update

Matt Keeping, Head of Broking for Willis Towers Watson, made the following observations in the October 26, 2016 Willis Towers Watson 2017 Marketplace Realities report:

“The mix of increases and decreases, while subject to some change line by line, overall remains steady. The marketplace continues to offer opportunities for buyers, but as always, strategic planning yields the best results. The key point for buyers is to understand the nuances of the market so they can optimize their risk management programs.

“In the property market, the ongoing declining rate trend, which has caused observers to declare for several years that the market has bottomed out, continues. Catastrophe-exposed programs, having led the softening cycle last year, continue to lead the declines. Property rates are expected to decline 7.5% to 10% for companies without significant exposure to natural disasters and 10% to 12.5% for those more exposed.

“For general liability, rates for 2017 are expected to be -5% to flat, although buyers with recent claims can anticipate increases of 5% to 10%. Workers compensation costs are forecast to remain steady, with small increases or decreases for most buyers. In the auto liability line, an increase in the frequency and severity of losses is driving up rates as much as 10%. International casualty rates, included in the Marketplace Realities report as a stand-alone segment for the first time, are predicted to remain flat or fall by up to 10%.”

You can view the full Marketplace Realities report for all of our commercial

In this issue, we:

... review the latest trends in the insurance market as the soft market continues with smaller decreases forecast for most lines in 2017.

... provide the highlights of the Fifth Annual Real Estate, Hotel and Gaming Symposium that took place in Plano, Texas on September 12-14, 2016.

... explore the five key steps for preventing and responding to an active shooter event.

... examine the exposures covered by a real estate managers professional liability insurance policy.

... summarize the Internal Revenue Service’s Revenue Procedure 2016-24, which provides indexing adjustments for certain provisions under the Patient Protection and Affordable Care Act (PPACA).

... investigate the opportunity for owners and operators of real estate to consider installing automated external defibrillators (AEDS) and training their staff in their use to aid customers or business invitees who may suffer cardiac arrest while on their properties.

However, we continue to monitor the financial results reported by the carriers with whom we do business to determine potential changes in their approach to pricing. As always, a major caveat remains with respect to the impact that large catastrophic losses could have on industry profitability, surplus and the direction of rates.

The chart to the right provides a summary of our rate expectations by line of coverage for 2017.
2016 Willis Towers Watson Real Estate, Hotel and Gaming Practice symposium

The Real Estate, Hotel and Gaming Practice held its fifth symposium in Plano, Texas on September 12-14, 2016. While the sessions as noted below received excellent reviews, one of our senior risk management clients stated that the real value he took from the Willis Towers Watson Real Estate Symposium is the collected wisdom of very senior and talented risk managers who attend each year. He believes that it is an amazing group composed of some of the best risk managers in the real estate industry. The networking, tips and stories shared by attending risk managers are of great value to him and useful after the event.

The first morning included joint construction and real estate general sessions.

Paul Becker, Chairman, North America Construction, Willis Towers Watson opened the first session on *Rapid Change in Construction & Insurance Industries. Are Demographic and Technology Changes About to Shift How We Look at Risk?*

Stephen Jones, Senior Director of Industry Insights Research with Dodge Data and Analytics followed with a presentation on *Managing Uncertainty and Expectations.*

Tom Fuller, Manager of Risk Management Consulting Group at Liberty Mutual presented: *How Analytics and Predictive Modeling Can Impact Your Operations and Improve Your Results.*

The final joint session was: *Transforming the Construction Industry Through Technology, Innovation and People.* They developed and shared some terrific take-away tips for attendees.

The real estate sessions began after lunch with 2-¼ hour round table sessions, run and controlled by the risk managers. They shared ideas and tips for improving risk management strategies and operations in their companies.

We ended day one with an excellent and practical session on *Mergers and Acquisitions — A Risk Manager’s Guide and Critical Success Factors,* filled with great tips and stories, led by Janice Ochenkowski, International Director, Global Risk Management, Jones Lang LaSalle; Mark Meyers, Director of Risk Management, Blackstone Real Estate; and Bill Monat, EVP of M&A, Willis Towers Watson.

Day two began with our underwriting panel session.

The panel agreed that a buyer’s market will continue unabated. Circumstances could change rapidly with a major surplus-depleting event, such as a catastrophe related to hurricane, earthquake or terrorism. Opinion on the size of the event necessary to firm pricing ranged from a low of $50 billion to a high of $75 billion. It was noted that surplus is now over $650 billion and that, prior to September 11, surplus was approximately $290 billion. Thus, the industry has a much larger financial cushion to absorb catastrophic events.

All panelists expressed concerns relating to:

1. A low interest rate environment that is reducing investment income and placing increasing emphasis on underwriting profit. Insurers are seeking a return on equity of at least 10%, a goal that has eluded many insurers. Interest income is not the panacea it once was and insurers are not expecting this economic situation to change anytime soon.
2. A prolonged period of rate decreases for almost all lines of coverage.
3. Medical cost inflation is rising, particularly the cost of pharmaceuticals, faster than the overall rate of inflation for all products and services.
4. The issues arising from the abuse of opioids.
5. The adequacy of reserves. Insurers have been releasing reserve redundancies into earnings increasing net income. The question now is whether the industry has enough reserves and whether the practice of releasing excess reserves has abated.
6. The panelists agreed that automobile insurance results are a drag on earnings and insurers will need to take corrective measures. Automobile insurance is one of the largest single lines of insurance and can have a significant impact on overall earnings.
7. Property underwriters expressed concern with global warming and expect that it will increase the severity of storms and, when combined with rising sea levels, will especially impact the frequency and severity of floods.
8. A recurring theme, articulated by many underwriters, was tort cost inflation. This is caused by two factors: the rising cost of settlements impacted by, among other things, medical cost inflation, and the erosion of defenses in tort cases. Some underwriters believe that the duty of care rises to the point where de facto strict liability, or liability without fault, is often the standard in premises and operations claims.

9. There is some expectation that excess casualty premiums may rise as the result of a few carriers cutting back on their writings. The forces of supply and demand are at work; if carriers reduce their writings (essentially, the supply of insurance), the remaining markets may raise prices. We have seen some evidence of this and will continue to monitor developments in the excess casualty market.

All the panelists agreed that a market turn toward higher rates may not be precipitated by one large catastrophe loss, but may occur as the result of a prolonged period of rate decreases year over year. This would be similar to the hard market of 2000 which was caused by a 13-year period of uninterrupted rate decreases and exacerbated by the events of September 11.

The belief is that with inflation rising, albeit at historically low levels, claim costs will require higher rates at some point; essentially, premiums cannot continue to decline forever while costs rise. The low interest rate environment may serve to reduce the length of the soft market as interest income cannot offset underwriting losses.

The panel consisted of senior underwriting executives from:

- AIG — Steve Cousins, Head of U.K Commercial Property & Lex London Property Executive
- AWAC — Kevin Maloney, Real Estate and Financial Institutions Practice Leader
- Chubb — Thomas “Ted” Aitken, Assistant Vice President — Executive Underwriter, Real Estate & Hospitality Industry Practice
- Endurance — Michael Chang, CEO Global Risk Solutions
- FM Global — David Thoman, Operations Manager
- Liberty Mutual — David Blessing, SVP, Chief Underwriting Officer — National Insurance Casualty
- Zurich — Wayne Hanson, Regional Vice President Commercial Markets — South Zone

This was followed by a session on cyber claims and coverage issues led by Heather Wilkinson, SVP with the Willis Towers Watson Cyber Practice, and Josh Gold, coverage counsel with Anderson Kill. They discussed recent coverage issues, trends seen in coverage restrictions on non-cyber policies, court cases and a path towards making sure that risk managers do not have after-the-fact surprises.

There was also a session on the importance of communication on security issues to a multitude of stakeholders:

- Employees at various levels, including executives, who may be traveling and find themselves in a terrorism, active shooter or disaster event, should be prepared/trained to act appropriately to optimize their safety.
- Tenants (office/retail/multi-family)
- Crisis management/press communications

Tim Kraft, Risk Manager for JBG Companies, discussed the reality of being deposed and how the questions and a company’s procedures/policy/actual actions are attacked/tested in excruciating detail.

One of the sessions receiving extremely high survey scores was “Real Estate Risk Managers’ Perspective on Development and Construction Issues and Strategies to Protect the Owners.” The panel was led by Tim Kraft, Carol Musumeci, VP of risk management with Silverstein Properties and Ira Lebovic, attorney with The Lebovic Law Firm and provided real stories that took us from the issues to practical strategies for developing protocols to be negotiated with your general contractors as well as program structure and internal strategies.

In all sessions, we had excellent attendee involvement and participation with good questions and additional pearls of wisdom that contributed to a very successful symposium.
Five key learnings for preventing and responding to an active shooter

Gun violence and mass killing active shooter events have, to date, mostly been seen in overseas hotel, gaming and mixed-use commercial real estate settings. While horrific attacks against these sorts of venues have taken place in recent years in Amman, Mogadishu, Mumbai and Nairobi, what is to prevent similar acts of crime or terrorism from soon occurring more frequently in North America? We have certainly experienced movie theatre and school killings, as well as outlaw biker gang violence at casinos and restaurants, and even sophisticated acts of extremist-inspired terrorism in public places. Potential violent threats to “soft target” places of lodging, resorts, casinos and shopping/office buildings abound, whether originating from disgruntled employees, disturbed individuals, violent criminals, extremists or jihadists.

The American Hotel & Lodging Association has expressed concern over perceived threats, pointing out that since 2001, more than 62 attacks have occurred in hotels in more than 20 countries. Willis Towers Watson’s Security Risk Consulting Practice is active in the American Society for Industrial Security (ASIS), resulting in our participation in ASIS’s Hospitality, Entertainment and Tourism Council and in its Commercial Real Estate Council; involvement in these advisory and information-sharing professional councils by leading member firms demonstrates the growing worries over countering active shooter threats to these U.S. and Canada critical business sectors.

Still, the risk is manageable! Appropriate threat-based application of security resources (i.e., physical security systems, guards and operations) may serve effectively to deter violence. Law enforcement and private sector liaison must be ensured. All active shootings and related terrorist actions are preceded by a period of hostile surveillance during which the prospective shooter(s) observe the target location and gather intelligence. Most workplace shooters also exhibit “red flag” behavior that may tip off coworkers or others to their potential for violence. Adopt a security mindset and embed security in your organization’s DNA. Make it a cultural trait.

We assist clients in avoiding, preparing for and responding to violent encounters in the workplace. Our security risk consulting methodology and deliverables provide you with actionable security protocols for deterring victimization and include a site-specific active shooter plan. The likelihood of your firm experiencing gun violence at work is very low; however, the harmful and negative impact of such an event is so damaging and disruptive that correct risk mitigation must be undertaken.

**Follow these five key learnings for preventing and responding to an active shooter:**

1. **Conduct a thorough security risk assessment** of your businesses (i.e., determine any aggravating threat factors to your executives, properties, tenants. Understand local crime and terrorism risks).

2. **Carry out physical security reviews** and determine consistent minimum security practices and standards. Remediate any exposures.

3. **Educate employees through security awareness training sessions**, to include active shooter and workplace violence prevention and response content.

4. **Develop and implement a workplace violence prevention policy.**

5. **Create site-specific active shooter plans** for your firm. Communicate the plans to stakeholders and staff and exercise or drill them regularly. Make them part of your crisis management plan and your emergency response toolkit.

For further information contact Nicholas A. Smith, Jr., CPP, Security Practice Leader, Risk Control & Claim Advocacy Practice, Willis Towers Watson at 610 651 7704 or nicholas.a.smith@willistowerswatson.com.
Property managers provide professional management services to third-party property owners under a contract for a fee. Like all professional service contracts, the property owner typically requires the service provider to evidence a professional liability insurance policy in its indemnity provisions. The contract between property manager and clients may transfer most or all management responsibilities to the property manager. Professional liability insurance is intended to provide comprehensive coverage for claims arising from allegations by the property owner for failure (errors and omissions) to adequately manage the property, which subsequently led to a financial loss. The policy can be tailored to meet the specific needs of the property manager’s professional services. Generally speaking, a firm or person that claims to have special skills or expertise (“intellectual capital”) will be held to a higher standard of care than someone performing manual activities.

Some examples of allegations that may lead to financial loss for a property manager are:

- Loss of property value and lost rental income due to improper or negligent maintenance of the property
- Misrepresentation of the potential opportunities of the property generally or resulting from their development consulting as an ancillary service
- Loss of tax incentives due to failure of their due diligence
- Failure to properly secure the premises against third-party criminal activities
- Personal injury torts involving wrongful eviction, malicious prosecution and defamation
- Failure to collect or properly account for rent monies
- Failure to supervise subcontractors or vendors when providing construction management as an ancillary service
- Negligence in screening prospective tenants who may have criminal backgrounds
- Discrimination (race, ethnicity, religion, disability) in tenant leasing activities

A property manager’s commercial general liability (CGL) policy is intended to cover third-party bodily injury, property damage and personal and advertising injury claims arising from business operations or products. Coverage is limited for the most part to accidental events and is not meant to address errors and omissions claims stemming from the failure to perform work or provide services that meet a certain level of performance. Also, most CGL policies specifically exclude liability arising from professional services.

Directors and officers (D&O) liability insurance does not eliminate the need for professional liability coverage, as it usually does not cover employees who are not officers and directors. In the case of a publicly held corporation, the D&O policy may not cover the corporate entity for its own liability except for security-related claims. Coverage for liability arising from professional services may also be excluded.

Care should be taken to ensure that the CGL policy does not exclude bodily injury and physical damage claims arising from professional services through a designated professional services endorsement. Few CGL policies have this endorsement so a request should be made to have it removed if it is present. If this is not possible, the professional liability coverage should be modified to limit bodily injury, property damage and personal injury exclusions so that any exclusion would only apply to an intentional injury. A final option is to place both coverages with the same insurance carrier to address any gray areas of coverage. This may not be possible, however, as some professional liability insurance carriers may not offer CGL policies.

Real estate professional liability coverage is designed for the types of allegations discussed above and, most importantly, to provide defense costs which can be substantial, even if the allegations are unfounded. Unfortunately, many property managers do not carry this coverage as they believe these types of claims will be addressed by either their CGL or D&O insurance policies.

Please consult your Willis Towers Watson real estate professional if you wish to discuss your firm’s professional liability exposures and the potential need for insurance coverage.
The Internal Revenue Service (IRS) recently released Revenue Procedure 2016-24, which provides indexing adjustments for certain provisions under the Patient Protection and Affordable Care Act (PPACA). Of interest to employers is the index adjustment of the contribution percentage used for purposes of determining affordability under the employer shared responsibility (pay or play) mandate. Employers looking to avoid pay or play penalties will need this information to assist in the decision-making process relative to plan designs and employer funding.

Background

To avoid pay or play penalties, applicable large employers (ALE) must offer full-time employees minimum essential coverage (MEC) that is both affordable and provides minimum value (i.e., actuarial value of at least 60%). Under applicable rules, health care coverage is affordable if the employee's required contribution for the lowest cost self-only option offered by the employer is 9.5% (as adjusted annually) or less of the employee's household income. The statute defines “household income” as the modified adjusted gross income of the taxpayer and the members of the taxpayer's family, and modified adjusted gross income is defined as adjusted gross income plus certain types of income that would otherwise be excluded from the taxpayer's income (i.e., foreign earned income and housing costs, tax exempt interest, and the excludable portion of the taxpayer's Social Security income).

The provision in the PPACA statute that established 9.5% of an employee’s household income as the general affordability standard also provided for indexing of that standard beginning in 2015. Indexing of that 9.5% standard is done in the same manner as for the indexing of the percentages used to calculate the amount of premium subsidy payable to a taxpayer who qualifies for a subsidy in connection with the purchase of exchange coverage. In Revenue Procedure 2014-37, issued July 25, 2014, the IRS announced the first adjustment to the household income affordability standard by increasing 9.5% to 9.56%, effective in 2015. Subsequently on November 21, 2014, the IRS announced in Revenue Procedure 2014-62 that the household income affordability standard would increase to 9.66%, effective in 2016.

The IRS did not address the household income standard in its employer shared responsibility regulations. Instead, it established a choice of three safe harbors that employers could use to demonstrate compliance with the affordability standard, all of which limit the determination of affordability to employee self-only coverage. Those safe harbor affordability standards include the Form W-2 Safe Harbor (based on the employee's W-2, Box 1 reported wages for that year), the Rate of Pay Safe Harbor (based on an employee's hourly rate times 130 hours per calendar month), and the Federal Poverty Line Safe Harbor (based on the annual federal poverty line for a single individual divided by 12). The final employer shared responsibility regulations had stated that each of those standards is applied by multiplying the applicable wage amount by 9.5%.

Initially, the adjustments the IRS announced in 2014 were not applicable to the 9.5% standard used in connection with the safe harbor affordability standards, since all of those safe harbors were established by IRS regulations, and those regulations did not provide for indexing. However, Notice 2015-87, issued in December 2015, confirmed that the IRS intends to issue regulations to amend the affordability safe harbors to allow those employers relying on them to use the indexed numbers.

Affordability

For purposes of the employer shared responsibility mandate, the required contribution percentage has increased for 2017 to 9.69% (from 9.66% in 2016). This means that if an employee's share of the premium (in 2017) for the lowest cost self-only option offered by the employer is more than 9.69% of his or her household income (or the applicable standard if using one of the affordability safe harbors), the coverage is not considered affordable for that employee and the ALE may be liable for a penalty if that employee obtains a premium tax credit for health coverage purchased through the public exchange.

The Willis Towers Watson Human Capital Practice offers a variety of health care reform-related tools, publications and presentations. We invite you to click here to review the archive of available information.

We update our site as new developments occur and new guidance published, so please check back often.
Sudden cardiac arrest (SCA) is the #1 single killer in the U.S., striking every 90 seconds and resulting in more than 600,000 deaths a year. This is the equivalent of ten 747 airplanes crashing every single day. Sadly, it is also the #1 killer of student athletes, reminding us that this affects young healthy people, not just the older and/or health compromised. When SCA occurs, time is critical because the chance of survival decreases 10% per minute. An AED onsite, as well as trained responders nearby, offers the best chance of survival nearing 75%, whereas a victim without being proximate to an AED, in an area dependent on waiting for EMS, has only a 7% percent chance for a positive outcome. A very stark difference.

AEDs are safe and affordable. An AED will not allow a shock to be delivered to a person who is not suffering a cardiac arrest so you cannot hurt someone by using an AED. They typically cost from about $900 – $1500 and last about 8 – 10 years. They are also incredibly easy to use as evidenced by multiple studies done with untrained middle school students who were able to successfully deploy the device within seconds of the times of the comparative group of trained medical professionals.

However, just purchasing an AED for a hotel, office building or shopping center is not enough. Staff need to be aware of the presence of the device and must be trained to use it. The more people trained at a given property the better. This can sometimes be a challenge in a high-turnover environment. Gathering people together, away from their daily job functions, to take part in training can also be a hurdle. In recent years, many hotels and other public facing venues have come to employ with great success online training options. This allows for abundantly more people to be trained with far less expense and considerably less headache. They are also using interactive tracking systems that ensure the device and as its batteries and pads are up to date. This is critical, since an AED with a dead battery or expired pads is a devastating discovery in the face of a cardiac emergency by not only delaying critical lifesaving care but also exposing the property to legal risk.

Legislation is evolving regarding AEDs as well, and we are seeing municipal codes that now require places of business that meet certain size and/or occupancy to have robust AED programs in place.
Contacts

For additional information on this issue’s topics, or any others for which our Real Estate & Hotel Practice might provide assistance, please visit our website at willis.com.

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