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INSURANCE DILEMMA FOR CONDOMINIUM ASSOCIATIONS

F.S. 718.111(11) contains the insurance-related provisions in the Condominium Statute. The theory of the Statute, which I had the pleasure to assist in the drafting in 2008, is that where the Condominium Statute obligates the association to carry property insurance for building components, the association is responsible to reconstruct, repair or replace those damaged building components and every owner in the condominium shares in the cost. There are some exceptions as are addressed later on in this memorandum. As such, there are **three tiers** in the equation, namely (1) the insuring obligation of the association; (2) the association's reconstruction, repair and replacement obligation of damaged building components; and (3) the unit owners' sharing of the cost for the reconstruction, repair and replacement by the association. It is important to understand that this provision in the Statute only applies to where there is an insurable event which caused the damage; F.S. 718.111(11)(j) makes it clear that where there is not an insurable event, the Statute would not apply, but instead the association would be governed by the maintenance provisions in the declaration or by-Laws.

Tier 1 – Insuring Obligation of the Association

F.S. 718.111(11)(f) defines the insuring obligation of the association. There are two areas of mandated insurance. The first is for the condominium property as originally installed or replacement of like kind and quality in accordance with the original plans and specifications. The second is, any alterations or additions made to the condominium property or association property covered by F.S. 718.113(2). This Statute also contains certain exclusions, mainly unit finishings, which are not covered by the association master policy.

The problematic provision is the alteration or additions made to the exterior of property which are typically common elements. The Statute referenced (F.S. 718.113[2]) relates to material alterations and substantial additions to the common elements, which section applies whether it was an association-effected alteration or addition or one effected by the owner; owner-effected alterations and improvements subject to the Statute include, but are not limited to, screen and glassed-in rooms, and windows and doors with impact glass replaced by the unit owners (and not the association) which were not part of the original construction of the building. (If an owner-affected alteration or addition is one added to the unit as defined in the Declaration, then this problem goes away. The Declaration should be reviewed to determine legal character of the property.) Both the insurance appraisal and insurance agent industries have interpreted the alteration or addition provision in the Statute to **exclude** owner-effected alterations or additions. We would agree with that position if the section contained the words "association-effected" as a modifier to alterations or additions. However, the Statute was not drafted as such (I personally attempted to have this modifier added in 2008, but the drafter of that section did not see the necessity of clarification). Because the courts have held that statutes are to be constructed literally and pursuant to their words in their entirety, it is clear that the statute mandates insurance coverage contrary to the position of the insurance industry. I would also agree with that position if a unit and not a common element is the one being altered.

Why is this a problem? First, insurance appraisers will provide an appraisal to the association. The typical appraiser will not include these owner-added properties. The insurance agent will then provide an insurance policy which mirrors the insurance appraisal. If an appraisal is not performed in the year of a policy renewal, agents will typically offer insurance policies which will not include these owner-added properties. Because the insurance industry has taken a position contrary to the wording of the statute, directors and officers will not be aware that they are potentially underinsuring the condominium property. Additionally, many HO-6 carriers do not insure for these improvements, leaving a "gap" in coverage.

What does underinsuring the property mean? First, if these owner-added properties are damaged in a storm, an owner will look to his or her individual HO6 insurance policy, which most often does not insure for these added properties. The owner will then look to the association to pay for the replacement. The association is exempted from having to pay for such improvements under F.S. 718.111(11)(n), but the association must still insure them. This in essence means that the financial obligation for that particular repair belongs to the owner. If the owner finds out that the association did not insure for those installations, the financial obligation to the owner will be greater (i.e., without any insurance proceeds available toward the repair), resulting in a potential claim by the owner against the association for not properly insuring that component under the statute. A second problem is that if the insurance company determines that the statute did require that these items be included in the appraised value of the property and therefore the association should have insured for a greater amount, the association has a risk of a co-insurance penalty. Co-insurance means that the association must insure at least the insurance policy's stated

percentage of the full appraised value without a penalty. For example, if the co-insurance percentage is 90% (which is most customary, with 100% actually in some policies), then to the extent that the association insured less than that percentage, that lesser percentage is deducted from the amount paid to the association on its claim. This means that the association would be penalized by receiving a lower amount of insurance proceeds, with the effect that there is less insurance to cover the cost, with the difference to be paid for by the unit owners. Owners could take the position that the association underinsured the property in violation of the Statute, creating liability to the association and even possibly to the individual directors and officers.

The best solution is to amend F.S. 718.111(11)(f)(2) to make it clear that the alterations referenced only mean those effected by the association. Until such legislative change, associations and their boards face liability because the insurance industry has taken an interpretation of the Statute that does not comport with the plain language of the Statute.

Tier 2 – Association Reconstruction, Repair and Replacement

F.S. 718.111(11)(j) provides that the general rule is that the association must reconstruct, repair or replace those damaged building components which the association is obligated to insure under F.S. 718.111(11)(f), which would include owner-added property to the common elements on the exterior of the units.

Tier 3 – Unit Owners Obligation to Pay

Barring exceptions mentioned below, it is clear that all owners share in the cost of the reconstruction, repair and replacement as a common expense of the condominium. (F.S. 718.111[11][k] does give an association the ability to opt out of the sharing of expenses and allocate the cost to the individual owner whose unit received the damage.)

F.S. 718.111[11][j] provides exceptions to the general rule that all owners share in the cost of reconstruction. Sub-section "(j)(1)" provides that an owner is "responsible for the cost" of the repair if the damage is caused by the intentional conduct, negligence or failure to comply with the declaration or rules by the owner. Because of the language "responsible for the cost", it is not totally clear whether the association must actually outlay the cost of the reconstruction and seek reimbursement from the owner. There is another exception where if the owner untimely files a claim with the association, the association is not obligated to pay for such repairs of property losses; because of the language "not obligated to pay", we believe that the association still has the obligation to effect the repairs, but only if the owner "fronts" the money required under the contract for repairs.

Due to the wording of F.S. 718.111[11][n] (Owner-Installed Improvements), as mentioned above, it is clear that the association has no obligation to pay for reconstruction or repair expenses. It is the

position of the firm that this sub-section "(n)" does not take away the responsibility of the association to effect the repairs, but the association is not obligated to enter into a contract for the repairs unless the owner pays to the association the difference between the contract price and the amount of insurance proceeds received for the particular item. Of course if the insurance industry position holds, then the association would not have the repair obligation in the first place.

Conclusion

These issues present a definite conundrum for condominium associations. The association and its board risk liability to the owners and risk a possibility that the insurance company itself will construe the Statute literally, and if the court agrees, there may be a resulting co-insurance penalty. If in the alternative a court is willing to view the alteration or addition language under the insuring obligation of the association to mean only association-effected alterations, then the association's risk pretty much goes away; unfortunately, a court would have to re-write the Statute and not construe it by its plain language – contrary to a mandate on all courts. It is the position of the firm that the risk is not worth taking and that associations should be questioning insurance appraisers and insurance agents when owner-added properties are excluded from coverage. The association is well advised to confer with its legal counsel prior to renewing an insurance policy to discuss these issues and also to determine which unit owner alterations relate to the common elements which the association must insure, as opposed to unit alterations which the association does not.