

How does the Fund Provide Property Coverage?

Texas water districts and authorities participate in the Texas Water Conservation Risk Management Fund to protect their most important assets. A Fund member covers their employees for injuries on the job through workers' compensation. Their vehicles and equipment are protected if they cause injury or property damage to members of the public and the district is protected if its operations, premises or facilities cause harm to others. The district's board of trustees, officers and employees are also protected against allegations that their decisions or actions have caused harm. Property, including buildings, office contents, equipment and vehicles owned by the district are also protected against loss. The following description of property coverage is provided for general knowledge and does not replace, amend or alter the language in the coverage document.

The Fund provides very broad property coverage for members' property. The insuring agreement in the coverage document grants the coverage based on the idea that if something is not specifically excluded or insured by some other type of coverage, then the property listed on the policy is covered. The actual agreement says:

INSURING AGREEMENT

*This **agreement** covers property, as described in this **agreement**, against ALL RISKS OF PHYSICAL LOSS OR DAMAGE, except as hereinafter excluded, while located as described in this **agreement**.*

The property owned by the Member can include buildings, office and shop contents, water related equipment, motor vehicles, mobile equipment like backhoes and mowers and other miscellaneous equipment like tools and metering instruments used in the field. If a property is not owned by the member but a contract or lease agreement requires the member to cover it, that property can be included for coverage. This is a typical situation for leased equipment like backhoes or office copiers.

The type, location and value of the property must be listed in the schedules attached to the coverage document for the Fund to provide coverage. Here are the major types of property and how they are described in the schedules with an actual example from a member's property schedule:

- Building – by its address, occupancy, square footage, type of construction and value:
600 E. Euclid Main Office & Laboratory (occupancy) 30,000(square feet area) MNC
 (construction type) \$5,899,100(building value) \$112,192(contents value)*

**MNC is a rating class for buildings that are constructed of masonry, (and considered) non-combustible*

- Contents – same descriptive terms as a building and the contents’ value at that location
- Boiler and Machinery – description of equipment, location, serial number (if available) and value

Belt Filter Press 1.5 Meter w/ 9638 Schaeffer Road, Converse 2.5M 3DP \$425,000

- Electronic Data processing Equipment – make, model and type of component, location, serial number and value

Dell Precision T5500 Workstation 600 E. Euclid San Antonio 243PZQ1 \$6,012

- Mobile Equipment – description, serial number, value, date purchased

2004 Caterpillar Backhoe w/E Stick 420DITCB4E - BLN08437 \$78,875 ACV 2004 01/29/04

- Miscellaneous Property – description, location, serial number if any, value

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|--|----------------------|--------------------|------------------|
| <i>In ground Flood Lights</i> | <i>600 E. Euclid</i> | <i>San Antonio</i> | <i>\$5,100</i> |
| <i>Parking Lights</i> | <i>600 E. Euclid</i> | <i>San Antonio</i> | <i>\$10,200</i> |
| <i>Digital Sign (40x20x20' HT)</i> | <i>600 E. Euclid</i> | <i>San Antonio</i> | <i>\$242,760</i> |
| <i>Metal Sign</i> | <i>600 E. Euclid</i> | <i>San Antonio</i> | <i>\$33,048</i> |
| <i>(2) Flagpoles</i> | <i>600 E. Euclid</i> | <i>San Antonio</i> | <i>\$ 6,528</i> |
| <i>1080 Ft of Wrought Iron Fencing</i> | <i>600 E. Euclid</i> | <i>San Antonio</i> | <i>\$107,100</i> |

In addition to the listed property, there are extensions of coverage that provide automatic and additional amounts of coverage. The Property Coverage Contribution Worksheet that is included with each coverage document lists some of the important provisions about valuation, deductibles and ancillary coverages like Flood and Windstorm. One of these “automatic provisions” is very important for protecting each member fully. The Worksheet includes the “Blanket Limit Each Occurrence” provision that serves as a failsafe for individual properties that may not be valued sufficiently to meet the replacement cost. This provision states simply that in the event of a claim the total insured value of all properties scheduled for the member is available to pay for the loss. In the example of covered properties illustrated above, the building is valued at \$5,899,100. The total value of all insured property on the coverage document is \$96,649,646. In the event that the building is totally destroyed and the actual cost to replace the building is \$7,500,000, it would be covered because the total limit of \$96 million is available to pay the full amount of the building loss. Effective coverage for the member still depends on proper valuation of properties, but the Blanket Value provision protects the member if something is overlooked, there are mistakes in the valuation process or construction costs are rising more rapidly than the annual re-valuation process can keep up with.

There are three forms of property valuation, replacement cost, actual cash value and agreed value. Replacement cost is generally defined as the current cost to replace a property with something of similar kind and quality. Each year about 20% of members benefit from a professional, physical appraisal of their property. The rest are subject to revaluation based on a formula that updates property values using national construction cost factors modified by zip code factors to provide a “best estimate” of what it would cost to replace. The other common method of valuation is “actual cash value” which represents the depreciated value of property at a particular time. This is the basis of value of mobile equipment like forklifts and mowers. In most cases, the actual cash value is less than replacement cost. In rare cases an “agreed amount” may be assigned to property that is unique, rare or for which there is difficulty in determining an actual or replacement cost basis.

The coverage for all of the classes of property described above is for “***ALL RISKS OF PHYSICAL LOSS OR DAMAGE, except as hereinafter excluded.***” The next question then is “what are the exclusions?” The enumeration of exclusions is a tedious process but it may help to think of them in several broad categories. One major category of exclusions in all property policies is for manmade events that are essentially uninsurable because of their widespread and catastrophic nature. Nuclear contamination, war and “hostile or warlike action in time of peace,” insurrection or rebellion and detonation of a nuclear device are actions that are excluded or for which there is only limited coverage. Other “manmade” acts that are excluded are dishonest acts committed by any “director, trustee, officer or employee” of the member. (Crime coverage or public official’s bonds may respond to criminal or illegal actions by these people.)

Neglect in maintenance, wear and tear, rust, corrosion and faulty workmanship are also excluded. Damage caused by insects, animals or vermin is excluded. Loss of use and the cost of remediation due to fungal pathogens, asbestos, fungus, mold or mildew are also excluded. A common element of these exclusions relates to the process of maintaining property so that it is clean, in good repair and subject to efforts that help prevent damage or deterioration. In other words, the coverage assumes that the member will take good care of their property.

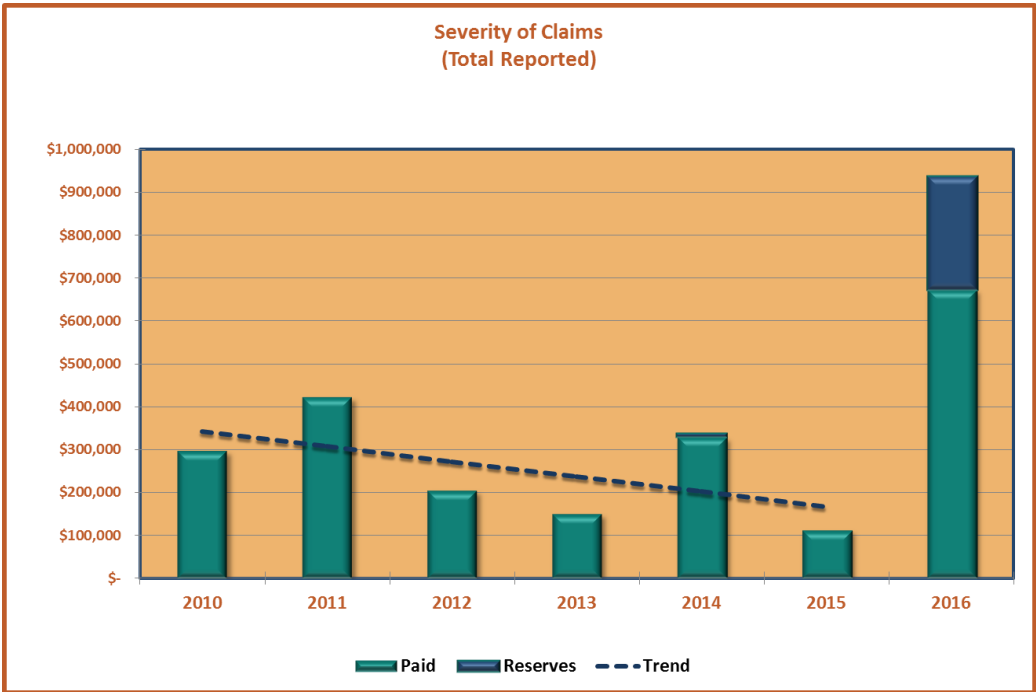
Natural events that are not covered include flooding in a “high hazard flood zone” as determined by FEMA’s National Flood Insurance Program. This is generally flood zone A or within the designated area of a 100 year flood plain or storm surge zone. Flood damage occurring outside of zone A is covered by the Fund up to \$7,500,000 per occurrence. Other natural occurrences such as changes in temperature or humidity are excluded from property coverage. The incursion of rain, sleet, hail, snow, sand or dust into a building is excluded unless the building first sustains damage to its roof or walls that allows it in.

The loss of incoming electricity, water, gas steam, refrigerant or outgoing sewage caused by events away from the covered premises are generally not covered, either. The concept of utility also includes “incoming or outgoing voice, data or video.” These exclusions take effect when the event that causes an outage occurs away from the covered property. An example of this would be a lightning strike at a power substation a mile away that interrupted electrical service to the member’s administrative offices. A lightning strike to the administrative offices would be covered.

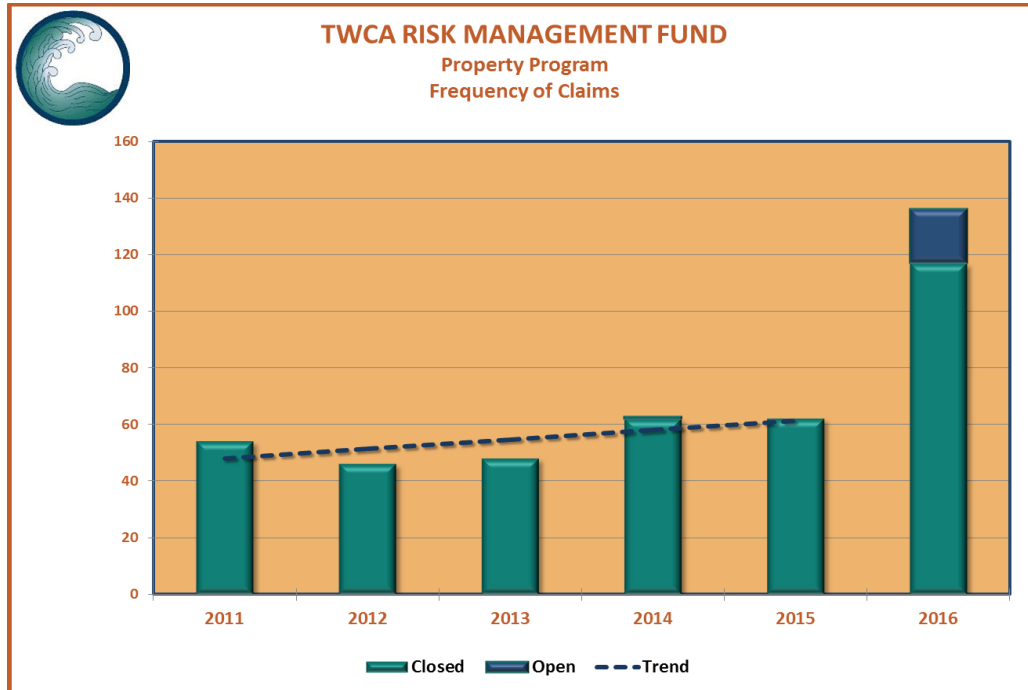
There are other exclusions to the effect of laws or ordinances, and “faulty, inadequate or defective” planning, zoning, design, surveying, construction, maintenance, remodeling, materials and other activities related to building processes. So, the grant of coverage in the insuring agreement is broad and the list of exclusions seems extensive. But the exclusions focus mainly on events that are intentional in some way, the result of neglect, actions by government or don’t directly affect the buildings or contents covered. What is covered is quite broad and the next section lists some of the common kinds of claims covered by the Fund to illustrate the breadth of coverage.

In the spring of 2016 many parts of Texas were pummeled by hail storms. As of October 1, 2016 the Fund had paid or reserved over \$1 million to pay for damage to roofs, windows, siding, cars, pick-ups, awnings and signs. Other types of recent weather related claims to buildings, contents and building equipment included lightning strikes, wind damage, freezing of water pipes, ice storm damage to gutters, vents and roof and flood damage (not in Flood Zone A). Other types of claims included vandalism, theft of ATV’s, theft of fuel, motor damage caused by a power surge and lightning strikes to flowmeters, transmitters and pressure reducer valves. Member vehicles were damaged in collisions with other vehicles and collisions with deer, a horse and a train. A John Deere 160D excavator fell in a canal, a boat capsized and a tree fell on an F150 pick-up. All of these examples have occurred in the last five years. Since 2004, claims were also paid because of hurricanes Ike, Rita, Gustav, Dolly and tropical storm Hermine.

The following chart illustrates the amounts of claims paid by the Fund for damage to members’ property since 2010 as of June 30 2016. The peaks and valleys in the chart reflect the nature of Texas weather in addition to the activities of thieves and poor drivers. The 2016 Fund year shows a large increase over the totals and average of the previous six years.



The next chart illustrates the frequency of property claims for the same period. It is easy to see the effect of the severe weather Texas has experienced this year. The number of reported claims this year has more than doubled from prior years, due primarily to widespread hail storms.



As mentioned in the first section of this report there is a provision in the coverage that extends the blanket limit of liability to each and every item of property that the member schedules with the Fund. That is only one of many extensions of coverage that help protect members of the Fund. The following discussion will explain and list these extensions of coverage found both in the coverage document and the declarations. In some instances the extensions of coverage begin to whittle away at the exclusions. In others, they are outright expansions of coverage that remove ambiguity or add limits of liability.

One of the most important extensions of coverage is automatic coverage for newly acquired property up to \$1,500,000 in value for a period of 90 days. This coverage comes into play when someone forgets to notify someone else, usually the Fund. But, the failure to notify can be internal to the member as well when the staff members involved in an acquisition or construction project forget to tell the staff member responsible to report changes to the Fund. The Fund will add the property to the schedule back to the date the property was acquired or put into service by the member.

Extensions of coverage also relate to the aftermath of property damage to member property that results in claims to the Fund. After serious claims that result in heavy damage to buildings and facilities there is often a significant clean-up cost before repairs or re-construction can start. The coverage document affords up to \$500,000 for debris removal. An additional

extension provides up to \$1,000,000 for demolition costs when a building is beyond repair. Another significant aspect of rebuilding is also covered – the increased cost to conform to new building codes that were not in effect when a building was first built. An example of this is the change in building codes that occurred after the devastation from Hurricane Andrew in 1992. Significant changes were made in requirements for strengthening roof structures and securing them to the walls of buildings and houses. Although these changes are not that expensive they do add to the cost of rebuilding a structure that was originally built before 1992. Texas adopted these new building codes in 2003 and 2006.

New property in the course of construction is also covered with an automatic \$1,000,000 limit of liability. Re-construction after a claim is also covered by this provision.

Another part of the coverage afforded members is for loss brought about by an interruption of the member’s business. After Hurricane Ike, several members were significantly affected by the storm. One member was essentially out of business for a short time and unable to derive income from the delivery of water or treatment of wastewater. “Gross Earnings” coverage will reimburse a member for lost revenue up to \$3,000,000 that can be reasonably documented during a period of business interruption. The loss is adjusted by deducting expenses that do not continue during the period of interruption. If a water treatment plant is damaged by a storm and the district is unable to sell water, the loss of billable revenue would be covered but utility costs that do not continue while the plant is under repair would be excluded. Two other extensions of coverage augment the limits of liability available to pay for loss of revenue caused by the risks covered by the coverage document. “Extra Expenses” paid by the member to resume services more quickly would also be covered up to \$2,000,000. An example would be the extra cost to rent pumps to begin moving water while damaged pumps at the plant are repaired. The process of determining the extent of loss is based on historical records and fixed ongoing expenses that do continue during the period of interruption. Included in the Extra Expense coverage is “Expediting Expense” which pays for the cost of transporting and acquiring parts and equipment that could help the member get back in business sooner.

The following list of extensions of coverages is also included in the Property Coverage Contribution Worksheet that is part of each member’s coverage document:

| Coverage for | Limit of Liability |
|----------------------------------|--------------------|
| Fine Arts | as scheduled |
| Leasehold Interest | \$500,000 |
| Personal Effects | as scheduled |
| Vacant Buildings | as scheduled |
| Trees and Shrubs | as scheduled |
| Gross Earnings | \$3,000,000 |
| Extra Expense/Expediting Expense | \$2,000,000 |

| Coverage for | Limit of Liability |
|---|---|
| Errors and Omissions | \$5,000,000 |
| Computer Systems Non Physical Damage | \$500,000 |
| Valuable Papers and Records | \$ 5,000,000 |
| Terrorism | \$25,000,000 or Blanket limit whichever is less |
| Flood-Zone A/No designation | NO COVERAGE |
| Flood - Other than Zone A Above | \$7,500,000 |
| Research and Development | \$500,000 |
| Automatic Coverage | \$1,500,000 |
| Property in the Course of Construction | \$1,000,000 |
| Law and Ordinance | Included in Blanket Limit |
| Transportation | \$500,000 |
| Rental Insurance | \$750,000 |
| Earth Movement | \$5,000,000 |
| Debris Removal | \$500,000 |
| Ingress/Egress | Included in Blanket Limit |
| Service Interruption Property Damage/Time | \$500,000 |
| Soft Costs | Included in Blanket Limit |
| Contingent Time Element | \$1,000,000 |
| Miscellaneous Property | \$1,000,000 |
| Off Premises Data Services Property Damage | \$50,000 |
| Accounts Receivable | Included in Blanket Limit |
| Accidental Interruption of Services | Included in Blanket Limit |
| Attraction Property | Included in Blanket Limit |
| Crisis Management/Civil or Military Authority | Included in Blanket Limit |
| Communicable Disease Response | \$10,000 |
| Interruption by Communicable Disease | \$10,000 |
| Rented Equipment | as scheduled |

The list of extensions to coverage represents the Fund's commitment to providing the broadest possible coverage for members. A more detailed description of the various extensions is available from the MGA Team that underwrites and services members' coverages.

One of the key principles of self-insurance is risk sharing. The Fund shares risk with its members through the Fund's structure and the fact that member equity in the Fund is at risk in the event of catastrophic losses that exceed the very high levels of reinsurance protection in place. The Fund purchases reinsurance from insurance companies that specialize in it. A reinsurance program is structured in layers. The first layer is the Fund's retention when the Fund pays the entire claim amount that falls within the layer. Currently the retention is the first \$200,000 of any property claim. Above \$200,000 the reinsurance company picks up all claim costs up to \$500,000,000. Above a claim for that amount, the Fund's assets would be at risk.

Another type of risk sharing is a deductible that must be borne by the member before losses are paid by the Fund. In general, the standard deductible for a property loss ranges from \$1,000 to \$25,000 for losses to buildings, office contents, mobile equipment and any other scheduled property. A member with a \$1,000 deductible would have that amount withheld from a \$25,000 claim for a roof damaged by hail. In the determination of contributions paid for property coverage there is a credit applied to the rates based on the size of the deductible. The larger the deductible, the larger the discount so that at the higher levels a portion of the deductible might be offset by the credit applied to the rates.

This description of the property coverage provided to members by the Fund is not meant to replace any of the terms, conditions, definitions or limitations contained in the coverage document. The intent is to provide a general understanding of what is and is not covered. Any determination of coverage for a claim is based on the presence of the property on the schedule and the actual language of the coverage in relation to the circumstances of the claim. This determination can only be made by Fund claims adjusters working with the member whose property has been damaged or impaired.