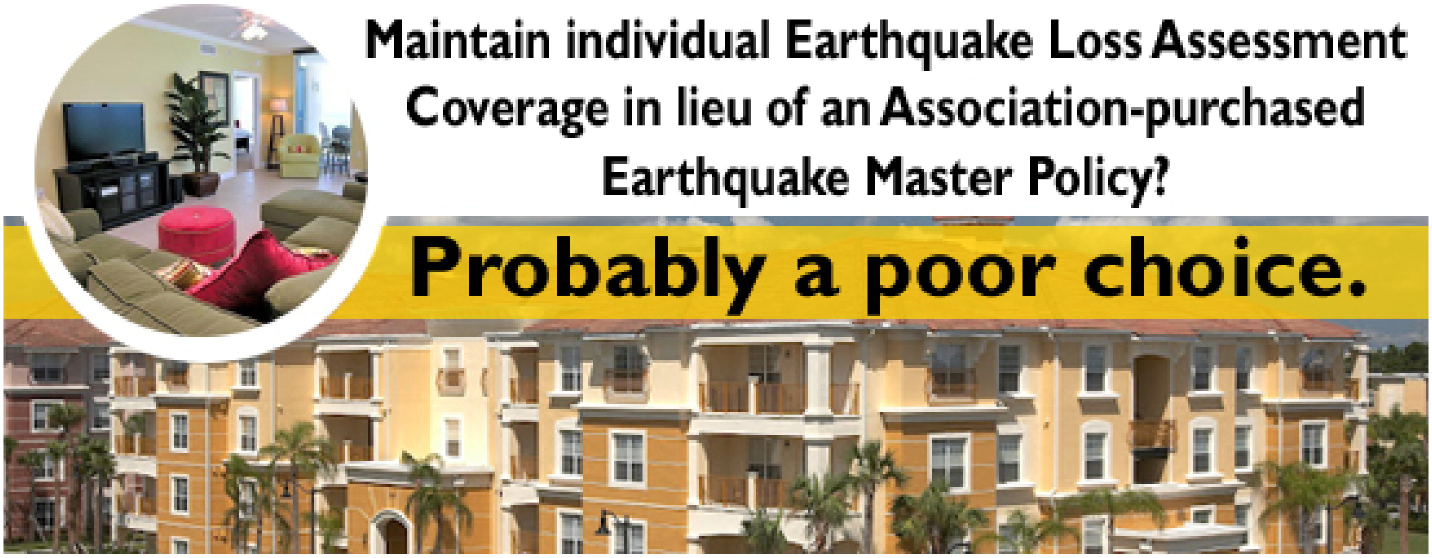


Some condominium association Boards have suggested encouraging individual owners to purchase Earthquake Loss Assessment Coverage (EQLA) effectively provides the equivalent to purchasing Master Earthquake Insurance for the Association. Several Associations have even considered developing an "incentive" approach offering to reimburse owners should they elect to maintain individual EQLA coverage, as if to suggest that such coverage is equal to maintaining a master earthquake policy. It's not. There are numerous problems with this approach:

Inadequate Limits

Let's look at an "average" condominium association that has 70 owners and an estimated replacement cost of $16 million. If each of the 70 owners purchased the maximum Earthquake Loss Assessment (EQLA) limit available from the California Earthquake Authority (CEA), it would only provide 32.8% of the necessary earthquake protection required (70 Owners X $75,000 = $5,250,000), leaving the Association with a $10.75 million shortfall. If individual owners maintained the lower $50,000 EQLA limit, the shortfall would be even greater ($12.5 million).

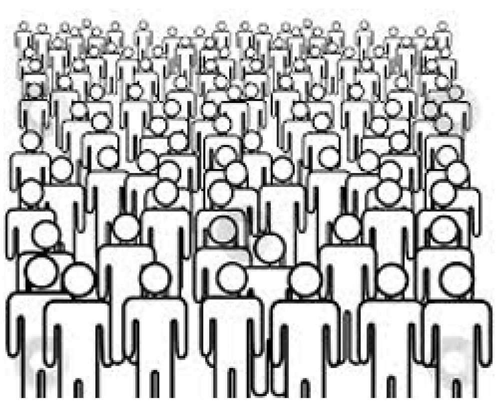
Value vs. Cost Benefit

From a value/cost-benefit standpoint, dropping the Association's Master EQ policy in favor of requiring the individual owners to maintain EQLA doesn't shake out. In the more earthquake-prone zip codes the CEA charges $799 per year for a $75,000 limit – this means that collectively, the 70 owners would be paying $55,930 for a total of $5,250,000 in coverage – and that's IF all of the owners actually go through with purchasing the coverage. Compare this with a traditional master earthquake policy where, depending on the age, parking type and location of the development, the Association is likely paying a rate more like $30,000 to $40,000 for $10,000,000 in coverage. While the deductible is higher for a master EQ policy (10% or 15% of the values at risk, as opposed to $11,250 per unit owner with the CEA), there are some distinct advantages. For one thing, the claim payment will be issued to the HOA, not the unit owner – which means the earthquake proceeds might actual go towards the reconstruction effort, not the individual unit owner's pocket.

CEA requires an underlying HO6 Policy

A requirement for purchasing EQLA coverage through CEA is also maintaining an underlying personal fire policy with a CEA-participating carrier. In those circumstances where the Association is offering a reimbursement "incentive," the unit owner can't simply purchase a standalone CEA policy and immediately seek reimbursement from the Association. Instead, the owner must purchase a companion Condominium Unit Owner Policy (HO6) from a participating carrier at a significant expense. There are a few issues at play here: 1) Would the reimbursement for EQLA be a sufficient incentive for an owner to buy a companion HO6 policy? 2) If an individual unit owner has a long-standing relationship with a carrier that does not participate with the CEA, would they be forced to jettison a long-standing relationship and move to a CEA participating carrier in order to recoup the HOA incentive ($496 or $799, depending on the amount)? A retired person, for example, who has been purchasing coverage through AARP's program (through Hartford, a non-CEA participant) may have to move their policies to a new carrier who may not have the same degree of service/loyalty because the owner is considered a "new client" to them.

70 Moving Pieces = One Administrative Nightmare



Seventy (70) individual unit owners represents 70 different effective dates to track! Also, there is no "Notice of Cancellation" in favor of the Association.

So, if a unit owner produced evidence of a CEA policy in order to receive reimbursement from the Association one week, then turned around and canceled the CEA coverage the next (and pocketed the refund) there would be no way to know.

Furthermore, once the underlying HO6 Policy is cancelled, so is the CEA Coverage. According to the CEA web site: "The CEA policy and its companion policy share the same renewal dates. If the companion policy is terminated or cancelled, the CEA policy is cancelled as of the same date."

Logistic Hurdles

The California Department of Insurance indicates that in 2012 the CEA participating carriers represented 75.15% of the marketplace. This means that 24.85% (or about one out of every four owners) has insurance placed with an insurance carrier that does NOT participate in the CEA. The amount of EQLA coverage available (if any) and the premium charged for this coverage from these non-CEA carriers will vary significantly. These non-participating carriers have their own proprietary forms and independently-filed rates. Some carriers may offer EQLA coverage but at drastically low limits ($1,000 or $5,000 per occurrence).

Potential for Diverted Funds at the Time of Loss

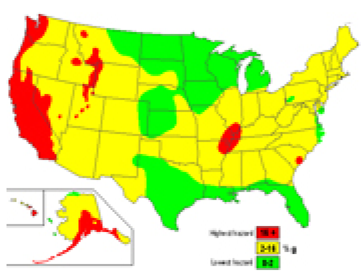
One of the drawbacks with the CEA's EQLA coverage is the proceeds for the Loss Assessment claim are payable directly to the individual unit owner, not to the Association. If a unit owner is upside-down in their investment (owes more to the bank than the unit is worth), they could be inclined to pocket the $50,000 or $75,000 of EQLA proceeds and walk away.

Individual homeowners in California have a reputation for ignoring their earthquake exposure

Encouraging individual owners to do the “right thing” and purchase earthquake insurance to protect their investment is a consistent and uphill battle. In the same aforementioned 2012 Department of Insurance statistical study, it was reported that, on average, only 10.6% of homeowners in the State of California purchase earthquake protection. That means 89.4% of individual homeowners have not taken any steps to protect their real estate investment against damage by this potentially catastrophic loss.

Directors & Officers Exposure

The Board may still be sued for “failure to maintain” earthquake coverage. Directors & Officers Liability policies have an outright “property damage” exclusion which eliminates coverage for any “act, error or omission” which might arise as a result of damage to, destruction of, or loss of use of any tangible property. If the project were to sustain earthquake damage and the Board were to be challenged by unit owners questioning the Board’s decision to jettison a more traditional earthquake policy in favor of a reimbursement program for individually-maintained EQLA policies, there would be no defense or indemnity under the D&O policy. For this reason it’s strongly recommended the Board consult with legal counsel for professional guidance should they consider pursuing this alternative approach.



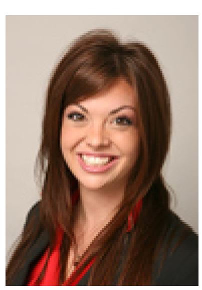
“California has two-thirds of the nation’s earthquake risk. Some 2,000 known faults crisscross the state producing an average of 102 earthquakes a day – more than 37,000 each year.”

-The CEA (California Earthquake Authority)

Current Earthquake Loss Assessment Rates (by zip code) for Condominium Policies Cost for $75,000 of coverage (subject to 15% deductible)	
92602 (Orange County/Irvine)	$529
92211 (Palm Desert)	$799
91101 (Pasadena)	$529
92501 (Riverside)	$799
94102 (San Francisco)	$799
93101 (Santa Barbara)	$529
95051 (Santa Clara)	$799
90401 (Santa Monica)	$529

By Timothy Cline, CIRMS

Timothy Cline Insurance Agency, Inc.



By AJ Scott

Timothy Cline Insurance Agency, Inc.

This letter contains only a general description of coverage and is not a statement of contract. For a more detailed description of the policy conditions and exclusions, please consult the policy itself.

For more information please visit us at: www.timothycline.com

or call us today at: (800) 966.9566