

EPISODE 1193

[INTRODUCTION]

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Aaron Kelsoe (AK): When you're underwriting a property, find a broker that will spend time with you and look into the property, see if there's any crime in the area, is familiar with the area. A long story short, you can have two people, you could have two properties paying \$500 a door here in Texas, one might be getting a good deal and one might be overpaying, and there's just kind of a variety of factors that need to be taken into account to kinda know that.

[INTERVIEW]

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Sam Rust (SR): This is your daily Real Estate Syndication Show. I'm your host, Sam Rust. With us today is Aaron Kelsoe from Ramey King. Aaron is a broker and consultant for multifamily insurance, who helps investors through all phases of a deal, from underwriting through closing, well-versed in working with a variety of lenders and their insurance requirements, which gives him the necessary expertise to be able to anticipate problems before they arise. Aaron, welcome to the show, thanks for joining us today.

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AK: Thanks for having me, Sam, I appreciate it.

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SR: So, Aaron, as we look over the landscape of multifamily, the industry, it's always changing, it's always moving. Different factors that we have to respond to. But over the last five years, the insurance markets have changed drastically, I feel like I talked to my agent and my carriers about every six months, and I have my breath taken away every single time. I'm curious, as we get started here, could you give us kind of an overview of the insurance market and why we are where we are. I know you're based out of Texas, we own a lot of stuff in the Rockies, but as best you can kind of share with our audience what's happened in insurance markets the last couple of years, why rates are climbing like they are, and is there relief in sight?

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AK: Yeah, so there's no doubt about it. Rates are up across the board, especially here in Texas, obviously, and this is mostly due to the weather problems that we had, so in Texas, back in February, we had that winter storm that paid out about \$15 billion in damage, we got the wildfires in California. And then last year was, I believe, the most active Atlantic hurricane season that we've had on record. Aside from that, and then Covid happened, you kinda have the supply and demand issue with materials and labor that now your reconstruction costs are up. There's been a lot of times where you have to increase the coverage at renewal to keep up with where the market is, to make sure that your clients are adequately insured, and not even property coverage, Sam. It's also the liability, so we've had claim payouts increase over the years. A lot of insurance companies, they wanna avoid the cost of going to court and they just won't even fight it, and they'll pay. I had one of these recently where I had a client and we knew it was fraud, a fraudulent claim, and the insurance company, and I try to explain this to the adjuster over and over again and the insurance company, just kind of explained, look, it's just easier for us to settle, especially with court costs and that can go on forever, and then also the exclusions are starting to become more common where insurance companies are protecting themselves instead of their insureds, which is what they were created to do.

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AK: And so that's just kind of why we're at where the weather patterns that we're seeing, and also kind of the increase in court settlements over the years have kind of affected the rates across the board.

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SR: You mentioned exclusions, and that's something I wanted to quiz you about a little bit. In Colorado, we've seen an uptick in carriers who have a separate wind-hail deductible. So, it's not quite an exclusion, but maybe you have a \$25,000 property damage deductible, but you've got a 3 or 4% wind-hail deductible because those are significant events for us out here, I would imagine you're seeing a lot of that in Texas, but what are some common exclusions or maybe exclusions that are becoming more common that you're seeing carriers start to push out into the marketplace?

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AK: Yeah, so one of the main ones is assault and battery exclusion or even a sub-limit, so essentially, instead of giving you the full million on your General Liability, what they'll do is they'll supplement it to, let's say 100,000 per occurrence or 300,000 per occurrence. As an owner, if somebody was to be assaulted on your property and sues you for saying, hey, you didn't provide enough lighting on the property, you put me in danger, and I typically start to see these when the area has bad crime. I use a couple of different crime sites, I'm underwriting a property, but every carrier is kind of different, some of them will say, I know this one came back fine, and then another carrier say, no, we have to sublimit the assault battery, and then I'll try and get that increase for additional premium. So, assault battery is a very common one, also an animal exclusion, that's another one that we're starting to come across a lot. Punitive exemplary damages exclusion. And so if you're found guilty in a court of law, and the judge wants to make an example out, that's why it's called exemplary, because they're essentially paying, either making you pay so that others learn a lesson and don't do what you did, that's become a common exclusion. One that I've seen recently come up more common over the past few years was actually called the habitability exclusion, if I can say it right. This is essentially where you can get sued, tenants can sue an owner by saying, hey, you didn't provide livable conditions for me. Now we start to see insurance companies start an exclusion in that regard. And so you always wanna consult with your broker and may make sure that you're using a broad that, make sure you're covered with these exposures, I can't tell you how many times I've come across people that I didn't know they had in a salt battery sublime or even an exclusion. Obviously, the policy was cheaper, but when things are cheaper, it's usually for a reason, and then another one that I've seen is an insect solution, so bed bugs. There was actually a family in California that was awarded \$1.6 million from a bed bug lawsuit.

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SR: It sounds punitive and exemplary to me if I were gonna use those terms correctly.

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AK: It does. Yeah, I did, I read up on it actually, and it kind of goes to show that sometimes those things you think aren't really a big deal can cost millions, and so you wanna make sure that you're protected correctly with your insurance company.

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SR: Maybe we can talk to the folks who are beginning their syndication path or are looking to get

into deals themselves. Yeah, there's a lot more than meets the eye that goes into insurance, and I think working with a specialist is part of the process, but there's a lot of these hidden gotchas that can creep out. So, when you're starting a process, when you're evaluating a property, how do you underwrite from an insurance perspective, especially if you have an LOI on it, you don't have any Lawson data, anything like that, you're kind of just working with what you can find in the public domain, where do you encourage people to do their due diligence as far as researching your insurance costs ahead of time?

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AK: My number one answer to this is to find a broker, find somebody that specializes in your area and they can help do the underwriting for you. I see a lot of investors that will use a per door number in their underwriting or even go off of the sellers' T12 number. (Don't do that.) I've seen it. And here in Texas, after that breeze, what somebody paid 12 months ago is not what you're gonna pay the next 12 months. I'm quoting one right now, where the guy, the seller, took a 10% wind/hail deductible to significantly lower his premium, which was a smart gamble on his end, because he was able to increase his NOI and increase the value of his property, he lowers insurance cost significantly, and so you really never know how the seller might be insured or they might be significantly underinsured. I've also come across situations in that regard. When you're underwriting a property, find a broker that will spend time with you and look into the property, see if there's any crime in the area, is familiar with the area. So here in Dallas, Fort Worth, Texas, I know the rates at the back of my mind, if somebody reaches out to me on a property in Des Moines, Iowa, okay, I don't insure anything in Des Moines, Iowa, but I can always call my underwriters and say, hey, 1985-year built assumed no claims, what kind of rates are you kind of looking at, and then I can give them a solid ballpark estimate on what they're gonna pay. Long story short, you can have two people, you could have two properties think \$500 a door here in Texas. One might be getting a good deal and one might be overpaying, and there's just kind of a variety of factors that need to be taken into account to kinda know that.

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SR: That makes a lot of sense. There's a lot of high impact areas generally, we're talking to flood zones, things like that, but what are some other things that you wanna be looking out for just in a general area when you're moving in and looking at crime as something you've mentioned, any other items that folks should pay attention to.

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AK: Yeah, so crime and flood zones are the main ones, and obviously claims. Claims in the area, certain areas are known to get hit by hail more often. Or if you're in Oklahoma, you might be dealing with an EF5 tornado. And that kinda goes back to my point of why you should always use a specialist, because somebody is, if you're moving into Phoenix, Arizona, every insurance broker's gonna have a competitive carrier for Phoenix, Arizona because they don't have any weather problems. Try Dallas, try more Texas, or try Oklahoma or even Florida. Now, it's kind of a different story where you wanna be working with someone that is kind of studying a day-to-day and kind of knows who the main players are. But crime is a huge one. Crime is definitely one that you always wanna be on the lookout for, because not only is it gonna impact your liability rates, it also might lead to the insurance company trying to exclude certain coverages.

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SR: You mentioned earlier that there's a couple of places that you go to look up crime statistics, and I know that insurance carriers vary, but generally, what are some of the statistics that they care about, and could you share any of those resources with our audience that they might be able to use in their research.

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AK: Yeah, absolutely. So, one is called, see community crime map is one that I use, communitycrimemap.com is the main one that I use, and then also bestplaces.net/find. Two of my go-to options where I look for crime. And that could be anything, that could be a robbery and assault, even a murder. A lot of times if I'm underwriting a property, I'll Google the name of the apartment complex. And I'll say shooting after it, and I'll try and find something, and there was one I quoted in San Antonio that actually they found a body in the dumpster behind the apartment, it always helps to do your due diligence and see what you're able to find.

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SR: There's a lot of product out there that's linked on by the agencies. And I'm curious from an insurance perspective, if you know you're looking at a property that has an agency loan on it, can you make some really broad assumptions about the type of coverage that they have on that property currently because of the commonality of guidelines among agency loans?

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AK: When I was prospecting like on Yardi, and you see that somebody's with Sabal or Arbor, then I'm kind of able to know what their requirements are. That's a huge thing because I've had investors tell me you're not gonna come back to me and say, oh, your premium increased because of your lender, sorry. Over time, early in my career, yes, that would happen. Sometimes you have to fall on your face early before you truly become an expert, but once you start to work with, done acquisitions, with a variety of lenders, you'll kind of know, hey, lender X requires 18 months on the loss of rent coverage instead of 12. So, I'll go ahead and make sure my quote includes 18 months. Lender Y requires a higher umbrella and kind of things of that nature, where you can kinda be more prepared, and that kinda goes back to my point of why you should always just use somebody who does it on a day-to-day basis.

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SR: We hate using insurance, it's there in case, but there are those moments where it comes into play and sometimes it happens at the most inopportune times. How would you advise somebody if they're in the middle of a transaction and for instance, a building catches fire and maybe 20% of your units are offline and you're under contract. There's the legal side of that. What does the PSA say? What's the casualty clause, etcetera. But just as you're trying to figure out damages and insurance and is the claim assignable, is there anything from an insurer's perspective that you would advise people to look for or engage in as they're trying to just figure out that process?

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AK: Hey. An open claim is a deal killer for a lot of carriers, especially depending on the size. So, what I would definitely advise is see if that carrier will agree to stay on the property for the buyer. The same carrier that insured for the seller. That's the first thing I would advise. Now, regarding the proceeds, if that's not the case, it will probably push your closing, but you're gonna wanna look into having that claim closed before you take ownership, because we all have carriers offering claims, but your first insurance costs might skyrocket just because of that one open claim. I've had situations where proceeds were given to the buyer to make the repairs, so I've seen that before. Typically, you wanna make sure that claim is handled before closing happens and it's closed. Kind of what you explained to me. Yeah, there are those very unfortunate events where you're already under contract, something happens.

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SR: That's why we have insurance ultimately, right, it's for that protection. For that umbrella for the

rainy day. (Exactly.) Well, as we get close to winding up here, Aaron, I'm curious, if you could share with us maybe some way that you've improved your business in the last six months that we could take and apply in our businesses.

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AK: Well, obviously networking, that's kind of for most careers, but especially real estate investors. I've realized the value that networking can bring to them. I'd introduce some of my clients and some of my other clients. And then now they're talking about working on a deal together that can be very helpful and just staying on top of things. And another way that you could kind of improve your business is put yourself out there as much as you can. What I've been doing is you guys can come off like consultants to your passive investors, I come off as a consultant to my clients. I advise them what they need to do, even if that's not in my best interest, sometimes. I've lost deals in the past because I said, you need to see if you can stay on that management company's master policy because with two open claims, I'm gonna be significantly higher. I would rather lose on that one deal as the insurance broker, than lose the trust and hit them with a premium quote that is twice what they were expecting to pay. Just being honest, upright and always trying to consult people for what's in their best interest.

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SR: I think the operating and integrity is really important, and we all give that lip service, I don't think there's anybody that goes into the world thinking, or very few people that say, I'm not gonna be acting in integrity or be honest, but that temptation is there, we all wanna make that sale in the moment, we all wanna raise that extra 50,000 or whatever it is, but making sure that you're doing it completely above board. Completely. Ethically, it's very important. I really appreciate you joining us today, Aaron, and if folks have more questions about insurance or they're looking at their policy and they just wanna learn more about that side of our business and multifamily, how can they reach out to you?

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AK: So, I can be reached at Aaron Kelsoe and that's A-A-R-O-N and K-E-L-S-O-E. And that's at Ramey and that's R-A-M as in Mary, E as in Eric, Y as in Yellow, and then King, K I N G dot com (aaronkelsoe@rameyking.com). And then our website is rameyking.com and I can also be reached on my cell at any time at 940-395-6606.

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SR: Awesome, well, thanks for joining us today, Aaron. Thank you to our audience for joining us on another episode of the Real Estate Syndication show. This is your host, Sam Rust, signing off.

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Whitney Sewell: Thank you for being a loyal listener of the Real Estate Syndication Show, please subscribe and like the show, share it with your friends so we can help them as well. Don't forget to go to LifeBridgeCapital.com, where you can sign up and start investing in real estate today. Have a blessed day.

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