

## PROPERTY RISK CONTROL SERVICES FOR THE REAL ESTATE INDUSTRY



The investment assets of real estate firms are subject to a wide range of risks given not only the variety of physical properties and locations involved, but also the variety of tenants occupying these properties.

Property loss inevitably involves uncertainty. Whether a fire or an explosion; a natural hazard event such as a flood, violent storm, hurricane, or earthquake; or a devastating terrorist attack—these can significantly impact a business and property loss—and the consequences for real estate firms are all too clear. Loss of physical assets and operational capabilities can quickly translate into lost market share, revenue, brand equity, and shareholder value. In this uncertain environment,

mitigating property losses and their impact hinges on the ability to effectively identify, qualify, assess, and manage the full spectrum of physical, financial, and operational risks affecting real assets.

Common perils such as fire and natural hazards are the primary threats to real estate investments. Successful real estate companies manage these risks to drive informed decision making and minimize uncertainty. Risk decisions can contribute to the portfolio valuation and to its defense against common losses. With an active risk management program, investors' responses to how these perils are managed should be fact-based and positive. Successful attraction of investors, as well as defense of the asset, is best supported by a strong team of professional risk control consultants.

Real estate firms face numerous property perils that often directly impact the return on investment of their portfolios. Real estate firms can benefit from risk-based management of the following five key perils:

Hurricanes	Hurricanes are focused in exposure, but widespread when occurring. Risk financing and insurance coverages can be difficult. Furthermore, properties in hurricane zones are subject to construction variances and oftentimes local code inadequacies. The history of hurricanes over the last ten years, and the anticipated increasing cycle, continues to position hurricane as the leading peril for property owners and managers in Atlantic and Gulf Coast states in the United States. In other parts of the world, hurricane (or typhoon, or cyclone) have similar effects and are similarly treated. Storm intensity, actual damage, frequency of occurrence, and financial impact must be managed closely for investments to pay off in any of these regions.
Earthquake	For zoned areas, earthquake is an exposure for which everyone anticipates “the big one”, yet day-to-day tends to generalize the issue. Some of the highest real estate investment returns are located in some of the most hazardous earthquake regions. All such regions can have “the big one” at any time. As such, the probabilities of occurrence must be understood in order to successfully manage the risk. As with properties in hurricane zones, variations in construction styles, standards, and codes deepens the challenge of evaluating risk.
Flood	Flood hazard is relatively standardized in the United States, but unfortunately not quantified over a portfolio. Flood zone delineation lags well behind physical environment or man-made changes in a particular area. Floods less frequent than 100-year equivalents can impact an investment’s feasibility. Multiple site exposure cannot be readily understood from common flood mapping.

Fire	Fire is a classic exposure whose prevalence and impact is typically dependent on building codes and enforcement. A compliance view of property risk neglects the actual value of an asset and treats all assets the same. Prevention programs that comply with fire codes may be severely lacking in scope and execution. When codes change, grandfathered provisions, while satisfactory from a compliance view, can leave an important asset with less protection than warranted.
Water Damage	Insidious and extensive, water damage is like fire in that if it is not initially controlled, it can lead to the total loss of a building. Codes do not address maintenance, responsiveness, and recoverability from pipe leakage, window and roof leaks, and various other sources of liquids. Unattended, mold can set in and become the defining quality of the building.

## HOW REAL IS THE VALUE OF MY REAL ESTATE?

Real estate firms deal with the risk qualities of their assets and investments at three important times in the asset lifecycle:

- **At Acquisition:** Standard work focuses on property valuation for taxation and marketability; replacement costs for insurance or risk purposes are not addressed. Likewise the asset itself is reviewed under due diligence studies to define its compliance. However, its risk is rarely defined in terms of probabilities of major loss. Risk views of acquisition work give the investor important information as to the quality of the investment and helps properly value the asset. Without such perspective, the costs of risk upgrades, actual valuation, and insurance are often pure guesswork, resulting in surprises and discomfort after acquisition.
- **During Ownership:** Each property affects the overall risk profile of the portfolio. Maintaining the quality of the risk requires attention to operations and maintenance programs that assure the asset continues to appreciate not deteriorate. Vigorous, intense, and consistent safety programs, risk assessments, and hazard communications drive the property manager to keep the asset performing and safeguarded against losses. Further, continual monitoring of the asset's position in the portfolio will give the best picture of the changing portfolio risk.
- **At Divestiture:** The good work that has gone into the property during ownership pays off: buyers are well informed as to how well risks are controlled, their probabilities of occurrence, and the precise details of the property. Elimination of unknowns increases informed decision making, reduces uncertainty, and arms the seller with data usually missing from the offering.

## SPECIFIC PROPERTY RISK ENGINEERING SERVICES

Marsh Risk Consulting's (MRC) Global Property Risk Consulting (PRC) Practice has extensive expertise and experience across the spectrum of risks to which real estate firms are exposed, and the imagination to look beyond. Our tailored and customized services track with the real estate life cycle and include:

### ACQUISITION

When pursuing an acquisition, developers, managers, and investors in real estate assets need assistance with not only code compliance, but the safety and insurance implications related to ongoing operating costs. MRC's pre-acquisition risk assessment helps to define the strengths and weaknesses of an asset and uncover other risks which could impact the asset's value. Through a comprehensive site and asset survey process, our property risk consultants:

- assist with the evaluation of the portfolio to be acquired and its compliance with a real estate firm's corporate standards, based on the availability of information;
- provide acquisition managers with a strong negotiation tool that enables them to calculate the operational and investment costs connected with risk based upon a fair and clear opinion and detailed information;
- in earthquake and windstorm regions in particular, define the impact of additional assets in those regions to the portfolio;
- for certain machinery, equipment, and systems, provide the acquisition manager with information on their flexibility/leasability in respect to protection and permits;

- help to satisfy traditional underwriter requirements and enable underwriters to evaluate the true nature of a real estate portfolio; and
- provide replacement cost valuations of assets for an accurate assessment of exposures and consequential insurance costs.

The comprehensive pre-acquisition risk assessment will reflect the real estate firm's acquisition goals and objectives, namely to prevent unexpected and uncontrollable negative impact on financial performance. For mortgages and lease-dependent properties, we provide a specialized study which considers the casualty/condemnation clauses of a mortgage or lease. From these clauses, we can advise the owner/investor of the probabilities of loss of mortgage or lease revenue due to "fortuitous losses" that permit the lessee or mortgagee to abrogate the mortgage or lease agreement. These studies prove to be especially valuable when bundling leases and mortgages into investment instruments.

## OWNERSHIP

Maintaining the quality of the asset, its defenses against loss, and its relative risk position in a portfolio are critical success factors supported by MRC's property risk specialists. Our services include:

### Portfolio Analysis

Real estate companies manage a vast number of risk management activities related to their portfolios. Important to this is the corporate risk management strategy and the current state of portfolio risk management. Current state analysis involves property inspections, documentation review, and assessment of the knowledge and expertise within the organization. MRC's risk ranking system can provide an easy overview of the current state with regard to construction, occupancy, protection, safety, and natural hazards.

Later phases of our Real Estate Portfolio Analysis involve building a portfolio database, making risk improvement suggestions, measuring improvement, and communicating results to identified stakeholders. The process and all that it entails can be tailored to individual needs. For example, further services for all or specified premises can include a reconstruction estimate (time to replace) and/or a casualty/

condemnation study (loss of tenant) for thorough loss-of-rent analysis.

### Cat Modeling and Loss Estimates

Using state-of-the-art modeling tools, our consultants can model your buildings and portfolio to determine probability of loss levels for windstorm, earthquake, flood, tornado, and other natural catastrophes. Modeling provides specific building-loss probabilities, annual aggregated loss levels, and allocation schemes identifying the relative risk between locations. Modeling is the most important tool in demonstrating fiduciary responsibility in terms of insurance retentions and limits. It also is a powerful marketing tool for negotiating insurance programs.

### Training and Education

We provide a range of training and education on risk management and loss control to help you meet your business needs and objectives. Our training and education programs can be classroom-based or computer-based and can include:

- emergency response planning and management;
- table top exercises for emergency response;
- property risk control program design and implementation; and
- construction project loss control programs.

We also can help you provide training to your property management staff, equipping them with critical risk management knowledge and information for instant use.

### The Marsh Engineered Solution<sup>sm</sup>

Large and small real estate firms are facing new challenges resulting from a changing insurance market. This requires a new approach to managing property risks—actions and solutions must be dynamic and better aligned with a corporation's business goals and objectives.

The Marsh Engineered Solution is a tailored approach focused on the client's needs by delivering a unique integrated solution of property risk expertise in one cohesive plan. Meeting multiple internal needs of an organization, the Marsh Engineered Solution aligns Marsh's property risk engineering, loss control, and insurance expertise and services with your business environment and objectives.

# MARSH RISK CONSULTING

## Property Risk Information and Data Management Systems

Technology supporting all aspects of business is the standard today. Risk information and data management has been enormously facilitated by advances in communications, data storage, and data processing technologies. However, to reap the rewards of these advances, such technology must be married with a breadth and depth of risk and issue expertise. MRC provides superior exposure knowledge and advanced applications designed to help real estate firms manage property and operational risk information and data, supporting their business objectives. Our goal is to provide a flexible system that meets our clients' specific needs, and that allows our clients' to own and use their information and data as needed. We view this as critical to a successful partnership with our clients.

## DIVESTITURE

When the moment arrives to divest individual assets or an entire portfolio, MRC works with real estate firms to present their product to market. Maintenance of risk information, claims data, modeling statistics, and loss control descriptions are all vital to successfully moving the property. One of the challenges to a buyer is the entire range of pre-acquisition data. Real estate firms that can provide this data, along with history and activity of the site along the way, possess a competitive advantage in the marketplace. Where portfolios are of concern, the entire portfolio analysis becomes a vital support to the divestiture. MRC works with real estate clients to package this information in the appropriate, positive, and accurate representation of the risk in order to meet the objectives of the divestiture.

## WHY MARSH

MRC's Global Property Risk Consulting Practice works together with Marsh brokerage colleagues and real estate specialists to support clients throughout the entire real

estate life cycle. Our collaborative approach helps real estate clients to minimize the liability and maximize the competitive advantages that come from effective risk management.

We help to create and maintain value for property portfolios through:

- quantification of risk and reduced volatility, which improves portfolio attractiveness to investors;
- risk identification and assessment, which helps minimize insurance load to investment;
- insurance program definition, which permits higher deductibles, retentions, and lower limits where appropriate; and
- operational risk control programs, which reduce the chance of physical loss and introduce efficiency in execution of loss control, further reducing costs.

Our combination of insurance, claims, risk control, and specialty services provides an unmatched resource for data and expertise for real estate firms. Our approach leverages traditional skills and processes with modern risk assessment tools to create value from risk for your real estate portfolio.

## CONTACT US

For additional information about our property risk control services for real estate, please contact your local PRC or Marsh representative or:

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You can find further insight on [www.marsh.com](http://www.marsh.com) or [www.marshriskconsulting.com](http://www.marshriskconsulting.com).

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