

CANADA

Insurance Implications of Natural Disasters: An Overview of the Fort McMurray Wildfires

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The Fire

On May 1, 2016, a wildfire began in Fort McMurray, Alberta, that has raged on for weeks. At the time of writing this article, the fire is still not under control, destroying or damaging over 2,400 buildings and covering over 500,000 hectares. At one point, the entire population of Fort McMurray (80,000) was evacuated. The wildfire may ultimately prove to be the costliest natural disaster in Canadian history. Early estimates of insured damages range from \$2 to \$9 billion. Losses arising from natural disasters are increasing within Canada. The Fort McMurray conflagration follows on the heels of the 2013 Alberta floods (\$1.8 billion in insured losses); the 2013 Southern Ontario floods (\$1 billion in insured losses); and the 2011 Alberta Slave Lake wildfire (\$740 million in insured losses). The Fort McMurray disaster provides an opportunity to assess insurance implications arising from natural disasters. This article briefly summarizes key issues impacting the insurance and brokerage community.

Insurer Response

The response of insurers to the Fort McMurray disaster, although of unprecedented size and complexity, has been quite swift. The Canadian industry has applied lessons learned from other recent disasters. Insurers immediately sent teams to staging areas located outside the affected area to assess losses and manage both habitational as well as commercial claims. Many carriers set up temporary claims centres at evacuation centres. Some insurers began issuing emergency cheques to their insureds, many of whom had to leave their homes with only a few minutes advance notice. Other carriers have increased their phone capacity to handle the heavier than normal volume of claims.

Insurers were not the only entities that mobilized quickly. Certain adjusting firms, as well as construction firms, also mobilized for quick loss adjustment, clean up, and re-construction. Commercial loss is also being promptly assessed.

Home Insurance

Current reports indicate that approximately 10% of the buildings in town have either been destroyed or damaged. The majority of the buildings are residential. Homeowners and other forms of habitational policies will respond. Unlike the 2013 Alberta floods where some homeowners were advised that coverage was excluded because of a form of "overland" flood exclusion, this loss is



caused by an insured peril. That said, issues may still arise.

One issue that may arise revolves in part out of the pre-existing economic circumstances. As a result of declining oil prices, Fort McMurray was experiencing an economic decline pre-loss. Certain individuals, whether tenants or homeowners, were weighing departure from this northern center. The loss of homes has sparked some debate as to whether certain insureds, especially those approaching retirement age, will rebuild. As oil prices have declined in recent times, so have house prices and job prospects. For those who wish to take this opportunity to relocate, they must decide whether to rebuild and move, or take a settlement based on actual cash value. Certain habitational policies only pay on a replacement cost basis if the house is rebuilt on the same site. If rebuilt elsewhere, the policy may only pay for actual cash value.

Homeowner and some other habitational policies generally provide additional living expenses while the insured is unable to live in the insured dwelling. Given the mass scale of the evacuation, not to mention the protracted time before return is permitted, insurers will face considerable expenditure. Exposure is complicated by various factors including the high number of buildings damaged, the inevitable increased cost of supplies and contractors, not to mention the short building season in Fort McMurray.

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Auto Insurance

Automobile policies will not be significantly impacted. That said, media coverage has depicted abandoned vehicles on the side of the roads, as well as burnt automobiles and recreational vehicles. Many gas stations ran out of fuel due to high demand during the evacuation. Those fleeing the fire had to abandon their vehicles. Most will be recovered but some will have sustained damage. Of interest, there have been some anecdotal reports of certain insurers initially refusing to pay for rental vehicles unless the insured could prove their vehicles were damaged. There are further reports of those insurers reconsidering their decisions and providing such coverage.

Commercial Insurance

Most businesses whose properties were directly affected by the fire will have coverage under their commercial property policies. Many businesses, including some oil sands operations, did not experience direct damage to their operations. However, many businesses could not operate as their staff had been evacuated. Some larger businesses used work camps - that under normal circumstances were used by their oil workers - as temporary housing for evacuees. While many oil sands operations were left undamaged by the fire, supplies were interrupted, workers in some cases were evacuated, and distribution impacted. There was a reported production loss of approximately 1,000,000 barrels per day.

Many of the affected businesses will assert claims under the business interruption coverage of their commercial property insurance contracts. Lost profits and increased expenses (some have had to fly key staff in and out of sites) will be at issue. Any above-normal cost to maintain operations at facilities that did not shut down will be the subject of claims.

Contingent business interruption coverage will be at issue for those businesses who were not directly affected by the fire but had key suppliers or customers impacted by the fire. Claims will be significant and in some instances contentious.

Liability Policies

So far, no person or entity has been blamed for the cause or for the spread of the fire. At initial glance, liability policies would not be thought to be triggered. That said, loss arising from other fires (see for example the Kelowna fires in British Columbia), gave rise to claims

against liability policies. By way of example, losses were alleged to have been contributed to in part by poor municipal "reaction" to initial reports, inadequate response, poor monitoring and other alleged failures. The possibility of insurers experiencing investigative and defence costs, if not indemnity payout, cannot be dismissed at this time. Claims could include allegations that environmental damage was caused by materials kept (possibly, unsafely) at insureds' operations that were released into the environment during the fire. Such claims have been advanced in circumstances where loss arose initially from natural disasters.

Reinsurance

Given the magnitude of the loss, reinsurance treaties or facultative cover will be a factor. By way of comparison, two thirds of the \$1.8 billion in insured losses arising from the 2013 Alberta floods were ceded to reinsurers.

Reinsurance response will not be without issue. Aggregation will be one issue that could arise. Will it be argued that there was one conflagration or several distinct fires, separate in time and location, leading to distinct ultimate net loss? Alberta forest fire occurrences have been trending up in recent times, and not all the fires in the area may be linked to one major wildfire.

An ex gratia payment "defence" may be advanced. In some other claims arising from natural disasters, reinsurers have submitted that certain payments by primary markets were made for reasons of politics or optics, and not because there was any actual coverage under the policies. Will this argument arise again after the Fort McMurray losses are resolved and recovery requests submitted?

Other issues may arise. The Fort McMurray fires have been burning for an extended period. Certain policies have clauses that deem losses occurring within a defined time frame, to be one occurrence. Policy limits are impacted. Query whether reinsurers will agree with primary carrier decisions in respect of number of occurrences, given the extended time frame of the fire(s).

Other coverage issues will arise. This article has identified briefly a few of the issues the insurance community will face in respect of Canada's most recent and probably largest natural disaster.

(The author gratefully acknowledges the considerable assistance of Blaney McMurtry coverage group associate Michael Ahmadi in research for and preparation of this article.)