

# Drought and the increased risk of fire

Tony Gouldson

*It has always been difficult to insure against the direct effects of drought. But it is less difficult to insure the increased risks of fire triggered by a period of drought. The risk of fire can affect forest owners in three very different areas of insurable risk.*

The first and most obvious is the direct risk of fire damage to the trees. Fire insurance for standing timber has been readily available for many years and it continues to be available even in drought conditions, although several insurers are reluctant to issue new cover during the summer months. This is understandable if you think about the fire season in some parts of the world, such as Australia and the United States.

While New Zealand has a different risk profile in respect of fire, the insurance companies who insure forestry risks are mostly controlled by larger European insurers, including Lloyd's of London, who tend to take a global view of most things. Like it or not, New Zealand is still only a small part of the total global insurance spend and we do not have as much influence on some aspects of our business as we perhaps want or deserve.

Second, there is the risk of damage to the property of others caused by fire spread from your forest, known as public liability insurance. This again is readily available. The third area of risk is the levy which might be payable within the framework of the Forest and Rural Fires Act, 1977. This legislation is based on a principle of law, which is fundamentally 'guilty until proven innocent'. In a nutshell, a forest owner is liable for the costs of fighting a fire which spreads to a neighboring property unless it can be proved that their actions did not give rise to the fire.

The forest owner will also be liable for the costs of containing and controlling the fire on their own property. The Forest and Rural Fires Act cover is also readily available, but forest owners should beware of policies that grant this cover for relatively small amounts of cover. It is not uncommon to see policies with cover of \$50,000, up to \$250,000. If your forest is in a remote area or adjacent to other forests you should check and consider very carefully the adequacy of your cover. Recent fires have seen Forest and Rural Fires Act levies of as much as a million dollars being imposed on forest owners.

## Different values

One feature of forestry insurance which sets it apart from many other forms of insurance is the basis on which a claim is paid. An agreed value formula is used and the formula should be different for each forest owner.

Forest plantations are often planted progressively over a period of years and as the trees grow, they increase in value. Log prices and exchange rates will fall and rise constantly and these rises and falls will directly affect the value of the forest. Other aspects that will have a significant effect on the value of your forest include the distance the logs have to be shipped to the mill or the wharf, the topography of the land, which will affect the cost of extracting the logs, and then the quality of the logs themselves.

## Insure for growth

Year-by-year the value of trees should increase and you should make sure that your insurance reflects this growth. This is particularly important with forestry insurance because most policies are written on what is termed an agreed value basis. For example, if your trees at 10 years of age are valued at \$8,000 a hectare and 20 year old trees are \$21,000 a hectare, and you lose 20 hectares of each, insurers will pay the claim on the basis as shown below –

20 hectares times \$8,500	=	\$170,000
20 hectares times \$21,000	=	\$420,000
Total insurable loss	=	\$590,000

These figures exclude any excess on the policy and any salvage that might have been made from the damaged trees.

The importance of maintaining a close watch on forest values cannot be emphasised enough. Many small-scale forest plantations are getting close to maturity. Depending on value factors mentioned earlier,

it is possible that a mature stand of radiata pine could be valued in the region of \$35,000 a hectare or even more.

Many forestry policies will also include cover for other costs. These include clearing the site ready for replanting, the costs of replanting, damage to infrastructure such as bridges, roadways or fences as well as the cost of retaining a consultant to help prepare your claim.

But you do need to beware. There are some farm policies which include a giveaway cover for forest fire damage, without detail on the valuation basis or the benefits of the added extras listed earlier

### How much cover do you need?

A simple answer is that you need as much cover as you can get and more than you think you need. If this sounds like scaremongering you should consider a recent case.

A South Island couple were recently ordered to pay more than \$1.2 million after a fire, which started on their property, destroyed a neighbouring forest and home in 2009. The couple bought their rural property 13 years earlier and built three tourist cabins to run as a bed and breakfast business through their company. However, it appears that they did not insure their property as a business, but as a lifestyle property.

In November 2009, one of the owners dumped the ash from a cabin wood-burner after visitors had stayed there. That afternoon a fire, driven by a strong breeze, spread 4.7 kilometres destroying a forest and neighbouring home.

Following the court order they received a demand from the Fire Service Commission and the local Rural Fire Committee for \$703,000 and from the Forest owner for more than \$550,000. In addition, their public liability policy would, no doubt, have been called upon to compensate for the loss of the nearby homestead.

While this case does not involve farm forestry it highlights several things which need real consideration by forest owners. The law regarding liability for fire spread is heavily weighted against the owner of the land where the fire began. The Forest and Rural Fires Act also imposes liabilities which are heavily weighted against on the land owner. Fire spread can be rapid and unpredictable with unforeseen wind changes. If the worst can happen, it eventually will.

Back to the original question of how much cover you might need. For public liability policies we would recommend a minimum of \$2 million, but preferably \$5 million. This level of cover should be readily available

and at a relatively low cost from most insurers. For the Forest and Rural Fires Act it seems quite clear that standard offerings of \$50,000 to \$250,000 will not be sufficient if things really go wrong. Be aware that some insurers will not be too happy about increasing the cover amounts they offer so this might trigger the need to shop around or talk to a broker.

### Importance of policy conditions

Insurance policies are legally binding contracts, and like any other contracts you sign, there are certain terms and conditions that must be complied with. Most important is the implied or written condition that the owner or manager of the forest must exercise all due care in the management of the risk.

In times of extreme drought this condition takes a higher priority where fire risks are concerned. It is also important to remember that all insurers now give greater scrutiny to the validity of claims, especially large claims. As a general rule, the larger the claim the greater the level of scrutiny an insurer will apply.

If you are employing contractors in your forest you must ensure that they have proper management controls and emergency practices in place. You cannot relieve yourself of responsibility just by saying that a fire was caused by someone else. As the owner of the land and the forest you still have responsibility for ensuring safety and risks are managed.

If your fire-fighting capabilities depend on natural water sources, and water levels are seriously low, it may even pay to consider postponing work until water levels and ground conditions improve. Eliminating public access during and after periods of drought is one way of reducing the fire risk. It has often been said that the three most common causes of fire are men, women and children. A breach of insurance policy conditions may lead to any claim being denied and this is not a situation we wish to see our clients faced with.

There are no hard and fast rules other than to take maximum care and to ensure the safety and security of the forest. If this means excluding public access and limiting the use of equipment and machinery, or accessing extra safety and security measures, it is probably a reasonable price to pay for the added safety and security of your forest and maintaining the integrity of your insurance.

*Tony Gouldson is a broker at Crombie Lockwood Risk Partners based in Auckland. He was instrumental in the development of the Standsure forestry product which introduced the widespread and readily available cover for wind damage. 🌲*