

## How Do You Know If You Have Enough of The Right Kind of Insurance?

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Homeowners throughout San Diego County suffered devastating losses of their homes in October 2007. Multiple fires burned consecutively in all regions of the County and people helplessly watched as firefighters battled to extinguish the fires.

Once residents were given the authority to return to their homes, they discovered the extent of their damage. Homeowners immediately filed claims with their insurance carriers and began the long claims process. As early as March, 2008 insurers were claiming that 97% of all October 2007 fire claims had been settled. The reality is as of December 2008, many homeowners have not settled their insurance claims. United Policyholders and RB United, two local non-profit companies, are currently assisting approximately 700 fire survivors. Of the approximate 1500 homes that were damaged or destroyed, these two groups are working with nearly 50% of the total survivors. These figures do not include the number of claims being adjusted on behalf of homeowners by professional public insurance adjusters or by any other outside assistance. *How can insurers claim 97% of the claims are resolved when nearly 50% of those claims are still in process?*

At Quality Claims Management ([www.qualityclaims.com](http://www.qualityclaims.com)), what we find most disturbing is that 14 months after the fires, homeowners losses continue to increase.

The main reason for the increase of loss is due to the widespread issue of homeowners being underinsured. Fire survivors have learned a very important lesson. Relying upon their insurance agent or insurance company to set the limits of their policy can be a very detrimental act. Unfortunately, it is an act that only hurts the homeowner, without repercussion to the insurance agent or insurance company. If it is later determined the insurance limits are not sufficient to rebuild their damaged or destroyed home, what actions can the homeowner take?

- 1) It is necessary to know exactly how much you are underinsured by
  - a. Obtain an estimate from a licensed contractor to rebuild the damaged house
  - b. Have a line-item Scope of Loss prepared to use as the basis of your claim.
- 2) Once it has been determined how much the property is underinsured by, a request can be made to the insurance company to reconsider the limits they have set. In some cases, the insurance company will make an attempt to reform the policy. This is a time-consuming process that will require the insured to answer a lengthy questionnaire and return it to the insurer. Regardless of how you answer the questionnaire, inevitably the insurer will state the responsibility to determine the appropriate levels of insurance lies with the insured. It is uncommon for the insurer to accept responsibility and increase limits.
- 3) The homeowner can file a Request For Assistance (RFA) with the California Department of Insurance. The instructions and form for this can be obtained on the Department's website at: [www.insurance.ca.gov](http://www.insurance.ca.gov).

It has been my experience that many homeowners have not reached a favorable outcome to the action steps outlined above. So, how do you prevent this from occurring in the future?

Quality Claims Management recommends that you be sure to purchase a Replacement Cost (RC) policy. A Replacement Cost policy will cover the total amount necessary to rebuild your property, up to the policy limits. However, the insurance company will only pay you the Actual Cash Value (ACV) of the property until the repairs are complete or the property has been replaced. Some insurance companies calculate ACV by determining the amount of the RC and then subtract depreciation. However, ACV should be calculated as the Fair Market Value (FMV) of the property. This is very important when valuing personal property. Insurers like to rely upon the age of an item to determine the amount of depreciation. The problem with this methodology is that it fails when the value of an item *increases* over time. Likewise, how do you address 20 year-old carpet that is still in like-new condition? Based upon the insurers view, *you would owe them money!* I suggest that depreciation should be based upon the *remaining life expectancy* of the property.

Insurers claim it is the responsibility of the homeowner to determine the appropriate levels of insurance for their property. The agent or broker will not know your property as well as you do. Accept the responsibility to properly insure your house. If you do not purchase the appropriate amounts of coverage, the loss will be yours to suffer.

When shopping for coverage, be sure to provide the agent/broker with all relevant information. For example: Do you have an office at home? Do you run a business from your home? Do you have any special hobbies or interests that includes special equipment? Do you have expensive collectables or antiques? Riders and endorsements can be added to your policy to ensure you have sufficient coverage to insure those items.

Some of the most commonly overlooked areas are:

Additional Structures - Additional Structures includes outbuildings, sheds, walls, fences, decks, driveways, pools, and other structures not attached to the residence Dwelling. Be sure you describe your additional structures to your broker. Additional structures are typically insured for 10% of the Coverage A limits. Coverage A insures your Dwelling. This amount can be increased if needed.

Landscaping - Landscaping is not typically insured as a separate category, but rather is included in the policy as an Additional Coverage. This coverage insures trees, plants and shrubs up to \$500 each. The total limits are generally capped as 5% of Coverage A. For many people that live in rural areas or have large parcels, this will not be adequate to replace all of their trees, plants and shrubs. Be sure to ask for increased limits if you do not think 5% of your Coverage A limits will be sufficient.

Personal Property – Many homeowners have hobbies or interests that lead them to build collections of various items. Some people collect figurines, wine, vintage watches, stamps, guns, art, antiques, dolls, sports memorabilia, well, you get the idea. Most homeowners policies have limits on the amount the policy will pay for these types of items. The good news is there is

always additional insurance you can purchase to protect yourself from losses in these areas. Ask your broker/agent about endorsements that may add additional coverages for those items. Most of the endorsements I've seen provide much broader coverage to that personal property than is contained in the standard homeowner's policy. For example, jewelry riders provide worldwide coverage for your jewelry which is broader than offered in the standard homeowner's policy.

Liability Coverage – Section II of your standard homeowners policy insures you for damages for which the insured is legally liable for. This means if someone gets hurt while visiting your property, they could sue you for the bodily injury or property damage they suffer. This coverage also provides your legal defense for the suits against you.

Additional liability insurance can be purchased via an Umbrella Policy. An Umbrella Policy will increase your limits on all of your liability coverages, including those on your automobile policy, a boat owner's policy or any other policy you may have that insures property. Umbrella policies are very inexpensive for the amount of additional insurance you receive.

When setting the limits for your Dwelling, the following steps will help you determine the appropriate limits.

- 1) Talk to a licensed contractor to obtain current building costs. Ask what the average per square-foot costs are to rebuild your home. Keep in mind if you have a partial loss, it is more costly to repair your house than it is for new-construction.
- 2) Refer to a real estate appraisal or talk to a real estate appraiser to find out what their Replacement Cost Values calculate to.

Other factors affecting your coverages are:

Extended Replacement Cost Endorsements – Is the insurer offering to increase your limits with an Extended Replacement Cost Endorsement? This is the new way of attempting to increase your limits. The old way was to sell Guaranteed Replacement Cost Policies. The trouble with those policies were the insurers found it was very difficult to limit their exposure, so they switched to Extended Replacement Cost Endorsements.

One of the problems this coverage creates for the homeowner is being able to comprehend your coverage limits. You see, these endorsements typically increase your limits on all coverages. In effect, the limits will *float up* or increase limits in your other categories – such as Additional Structures, Personal Property, Loss of Use, Additional Living Expense, etc.

Another problem this coverage creates for the homeowner are the *additional* conditions that must be met in order for coverage to apply. So, not only do you have the regular policy conditions to meet, you also have the additional policy conditions for the Extended Replacement Coverage. How does this help the homeowner? Seems to me this only benefits the insurer. Wouldn't it have simply been easier to increase the stated Dwelling limits? You may sense a bit of skepticism, but I deal with real people on real claims and this is my experience. It is rare that an insurance company makes a change

that somehow benefits the insured. We often learn later these changes have only helped the insurer.

Discrepancies on Square Footage – Some insurers are turning to Tax Assessors records to determine the amount of square footage the insured property had. Guess who this creates a problem for? Obviously, the homeowner now has one more thing to deal with. It is a rare occurrence to see the records of the Tax Assessors Office reflect exactly the same amount of square feet that is listed on the Declarations Page of the insurance policy. What can you do to address this discrepancy?

- 1) Refer to the insurance policy first. Your policy covers your property *as described on the Declarations Page*. As long as your property is correctly described, with the correct number of square feet, then you have paid insurance for the number of square feet listed.
- 2) Most Tax Assessors Records only include the square feet of livable area of your house. This does not normally include a garage. So, one reason for a discrepancy could be the garage. Your insurance policy should include the *total number* of square feet for your house and should not be limited to *livable* square feet.
- 3) Ask the insurer in writing to explain to you how they would resolve a discrepancy if the Tax Assessors Records reflected a larger number of square feet than is stated on your Declarations Page. Would they increase your limits or pay more than is stated in your policy? I doubt that very much.

Insurance Requirements Under A Mortgage or Deed of Trust - Another area of importance is relative the requirements under a Mortgage or Deed of Trust. The homeowner is referred to as the Borrower and has certain obligations and requirements to maintain appropriate levels of Replacement Cost insurance.

Typically, the lender will require Replacement Cost limits up to the amount of the Unpaid Principal Balance (UPB). A word of caution – do not rely solely upon the minimum requirements your mortgage company requires. It most likely will not be sufficient.

As you can see, there are many areas of coverage to consider when purchasing insurance. I have tried to focus on the areas that I believe will give you the biggest challenge if you ever have the need to file a claim. One thing is certain, unless you suffer a total loss, you will never fully comprehend the full effect of having enough of the right kind of insurance.

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