

Risk Management: Homeowners Insurance

Your home probably accounts for the largest single expenditure your family will ever make. Your household furnishings and personal belongings make up another sizable investment. Moreover, a lawsuit could seriously jeopardize your financial future. Most families would face serious financial loss and upheaval without adequate insurance against lawsuits and losses to their home and personal property.

You can protect your property and family by purchasing homeowners insurance. Insurers offer seven standard policies—five for homeowners, one for renters, and one for townhouse or condominium owners. The coverage provided by each is shown in Table 1. The basic provisions of the policies are similar from company to company.




This fact sheet will highlight the major features of homeowners insurance. Specific details are contained in your policy. Be aware that, although coverage is fairly standard among companies, some points vary. Read your insurance policy thoroughly to understand the details of your coverage.

A homeowners policy provides protection for your property and for the liability to others in a single package policy. The policy covers damages to the dwelling and other structures, loss of personal property, and living expenses while your home is being repaired. Liability coverage includes personal liability, medical payments to others, and several supplementary coverages, including physical damage to the property of others.

HO-1, HO-2, HO-3, and HO-5 policies are specifically for homeowners. The HO-4 policy for renters provides personal property and liability coverage. The HO-6 policy for condominium or townhouse owners insures the interior portion of the owner's unit, personal property and liability to others. Owners of older homes are insured by the HO-8 policy. HO-1 policies are not widely available.

Table 1. Types of policies and perils covered

Basic HO-1	Broad HO-3	Special HO-3	Renter's HO-4	Comprehensive HO-5	Condo-minium HO-6	Old home HO-8	Perils
							Fire or lightning
							Loss of property, removed from premises, endangered by fire, or other perils ^a
							Windstorm or hail
							Explosion
							Riot or civil commotion
							Aircraft
							Vehicles
							Smoke
							Vandalism and malicious mischief
							Theft
							Breakage of glass constituting a part of the building
							Falling objects
							Weight of ice, snow and sleet or any part thereof
							Collapse of building(s) or any part thereof
							Sudden and accidental tearing asunder, cracking, burning or bulging of a steam or hot water heating system or of appliances for heating water
							Accidental discharge, leakage or overflow of water or steam from within a plumbing, heating or air-conditioning system or domestic appliance
							Freezing of plumbing, heating, and air-conditioning system or domestic appliances
							Sudden and accidental injury from artificially generated currents, to electrical appliances, devices, fixtures and wiring (TV and radio not included)
							All perils except flood, earthquake, war, nuclear accident and other perils specified in your policy. Check your policy for a complete listing of perils excluded.

 Dwelling and personal property
 Dwelling only
 Personal property only

^aIncluded as a peril in traditional forms of the homeowners policy as an additional coverage in the simplified (HO-76) policies.

Property Coverage

Your Home

Dwelling coverage generally protects you against damage to the structure of your home resulting from

such things as fire, lightning, civil commotion, smoke, hail, and vehicle damage. The face amount of your dwelling protection is the most important figure on your homeowners policy. Most of your other property loss limits will be stated as a percentage of the amount of insurance carried on your dwelling.

Most insurance companies require the policyholder to insure the home and detached structures for their replacement cost rather than their market value. The standard way of determining replacement cost is to multiply the local construction costs per square foot by the number of square feet in the house. This figure will vary depending on region and the quality of your home. You may want to ask your insurance agent for assistance. Insurance agents usually have forms and cost data that will enable you to develop a reasonably accurate estimate. You also could have a professional appraiser conduct a replacement cost appraisal.

Insurance companies generally require you to insure your dwelling for at least 80 percent of its replacement cost to receive full payment for a partial loss. You must insure your dwelling for 100 percent of replacement cost to receive full payment if it is destroyed.

For example, suppose your home has a replacement cost of \$100,000 and you insure it for the required 80 percent, or \$80,000. If you incur a \$20,000 loss from fire you will receive full payment for the partial loss. But suppose you have your home insured for less than the required \$80,000, say \$40,000, and you suffer the same \$20,000 loss. The company will make two damage estimates and pay you whichever is larger. The first estimate is the actual cash value, which is replacement cost minus a depreciation factor. In this example, assume the first estimate to be \$7,500. The second estimate is based on your coverage as compared with adequate coverage. Since your house is insured for only \$40,000, you have only 50 percent as much coverage as requested. The company will only pay 50 percent, or \$10,000, of the \$20,000 claim. In this case you will receive the \$10,000 because it is the larger of the two estimates. You will have to assume the remaining \$10,000 cost of replacing your loss.

The insurance company is never obligated to pay more for a loss than the amount of insurance carried. Should you carry the required 80 percent replacement cost on your \$100,000 dwelling and it is destroyed, you will be reimbursed for \$80,000.

Other Structures

Detached structures such as a toolshed or garage are covered for losses up to 10 percent of the amount of the dwelling. Detached structures often are referred to in your policy as other structures, appurtenant structures or private structures.

Personal Property

The loss of unscheduled personal property (items not specifically listed in the policy) from damage to or theft from the home generally will be covered for 50 percent of the dwelling coverage. Do not assume that you will receive the full amount (50 percent of the dwelling coverage) as reimbursement; the amount set is the actual value of the personal property at the time of the loss. If your dwelling is insured for full replacement cost of \$100,000, personal property then is covered for up to \$50,000. If the actual value of your personal property is less, say \$36,000, then you will receive \$36,000.

Most homeowners package policies have strict dollar limits for coverage on valuables such as coins, stamps, jewelry, furs, and silverware. Additional protection for valuables can be purchased under a separate personal articles floater policy or a scheduled personal property endorsement to your policy. Both offer all risk (peril) coverage (with certain exceptions listed in the policy or endorsement) on the insured items. Normally you will be required to list each article to be insured, giving a complete description of the item and the amount of insurance you desire. Usually the company will request evidence of ownership and verification of the item's value, such as an appraisal, bill of sale and

photograph. Ask your agent's advice on adequate coverage for your valuables.

Listing personal property (scheduling) in the policy can cost from a few cents to a few dollars per \$ 100 of coverage, depending on the item. Premiums vary with location and crime rate.

The key to a good personal property insurance program is a complete, up-to-date inventory of your belongings. An inventory will enable you and your agent to determine if you have enough insurance coverage on your personal property and whether you own items that may need additional insurance protection. In addition, your household inventory can be a great help in a claims settlement. It is impossible to remember everything you owned after disaster happens.

Develop your inventory room by room. Include a brief description of each item, the date it was purchased or acquired, and the purchase cost.

Take pictures or videotape each room, closet, and open drawer at different angles. Keep the inventory list, photographs or videotape, and receipts for expensive items in a safe-deposit box or any safe place outside your home.

In addition to the coverage mentioned, your personal property away from home is covered for at least 10 percent of the value of the personal property on the premises.

Additional Living Expenses

The additional living expense coverage pays increased living expenses when you and your family must live elsewhere temporarily as a result of damage to your home caused by an insured peril. The limit on this coverage usually is expressed as 10 or 20 percent of dwelling protection prorated for the amount of time spent out of the house or as a stated period over which additional expenses will be paid.

Exclusions

Certain types of property, such as pets and motor vehicles, are excluded from your homeowners coverage. Property used to conduct business in your home generally is excluded. Personal property you rent from or rent to others is not covered when off your premises. Also, the property of any boarders or tenants is excluded.

Credit Card Losses

Homeowners policies generally include up to \$500 coverage for losses resulting from forgeries, counterfeit money, or unauthorized use of credit cards. Therefore, buying separate credit card insurance generally is considered a waste of money.

Trees and Plants

Plants surrounding your home are insured for 5 percent of the amount of coverage on your house up to \$500 per item but only for certain perils.

Liability Coverage

All types of homeowners policies insure against personal liability, medical payments to others, and physical damage to the property of others.

Personal Liability

Personal liability coverage is critical. It is designed to protect you against a lawsuit and related legal costs that could cripple you financially. The coverage applies, both on and off your premises, to bodily injury to others or damage to their properties caused by you, a member of your family, or your pets. Legal defense is provided by the insurance company whether you are proven legally liable (at fault) or not. If it is determined that you are legally liable, the company will pay the damages assessed against you up to the limits stated in your policy.

Medical Payments

The medical payments coverage provides for payment of small medical bills arising from minor accidental injuries to nonfamily members that occur on your premises, regardless of who is at fault. Coverage also applies to injuries occurring elsewhere that are caused by you, a family member, or your pets.

This coverage makes possible the prompt payment of medical bills because there is no need to go through the sometimes time-consuming process of establishing legal liability.

Supplemental Coverage

A supplemental provision covers minor damage that you or a family member might accidentally cause to another person's property, regardless of fault. Damage caused by children under age 13 is covered, whether accidental or intentional.

The amount of liability insurance that comes with standard policies may not be enough. This is especially true if children play on your property or if your pets bite. You may want to increase your coverage to prevent financial ruin because of an accident or injury to another person. Homeowners policies in recent years offer a minimum of \$25,000 to \$100,000 liability coverage. You can increase this coverage from \$100,00 to \$300,000 for \$10 to \$20 a year, depending on your insurance company. This is considered well worth the cost.

If you run a business out of your home, be sure you are adequately covered. The liability protection provided by your homeowners policy does not cover bodily injury or property damage you might cause in the course of your work. Ask your insurer if you need extra coverage for the work you do at home.

You might want to consider a supplementary umbrella liability policy, to insure liability losses above the limits of your regular insurance policies. These policies generally offer coverage in the area of \$1 million and are relatively inexpensive. (Refer to Risk Management: Auto Insurance Fact Sheet 438 for more information on umbrella liability insurance. It can be obtained from your county Extension office.)

Endorsements

For an additional fee, you can change the limits of coverage on your policy by adding an endorsement—a paragraph amending the original policy. For example, you might insure your personal property for an amount equal to 75 percent of the coverage on your house rather than the usual 50 percent. Or you might want to extend your liability coverage from \$25,000 to \$300,000.

Personal Property Replacement Cost Endorsement

In the past, insurance adjusters used depreciation schedules to determine the market value of goods lost or stolen. Today insurance policies increasingly are allowing you to purchase coverage for your personal

property's replacement cost and not the depreciated value, for an additional premium, normally 5 to 15 percent of the policy's total premium. The claim's settlement is sufficient to purchase a new item exactly like the one that was destroyed or stolen, although some replacement cost policies limit the coverage to 400 percent of the actual cash value. If your personal property is 7 years old, this replacement coverage for personal property—normally in the form of an endorsement to your policy's personal property coverage—can be valuable. Items of personal property destroyed but not replaced, however, will be valued at their actual cash value (depreciated value).

With both replacement cost and actual cash-value policies, the insurer has the right to repair an item or replace it instead of paying you. If you would rather have the money than the insured item, the insurer typically has the right to pay you only wholesale price.

Inflation Guard Endorsement

The coverage you now have on your home may be too low. Construction costs have doubled in the past 10 years. Each year you should look at your coverage and bring the value up to date with current building costs. Some policies offer an inflation clause that automatically increases the coverage and premium each year. However, with an inflation guard you can end up with too much coverage after a few years. Every few years you should check to be sure you have not become overinsured. If you suffer a total loss, your insurer will only pay the true replacement cost.

Supplementary Policies

Flood Insurance

About half of all homeowners mistakenly believe their policies protect them from floods. They do not. Flood coverage is excluded routinely from nearly all policies. The Federal Insurance Administration of the U.S. Department of Housing and Urban Development administers a program to make flood insurance available in flood-prone areas at low cost. To qualify for flood insurance, your property must be located in a community that has agreed to plan and carry out land-use control measures to reduce future flood damage. Flood insurance is available in over 17,000 communities throughout the United States. The policies are sold by private insurance agents who are reimbursed for losses by the government. In some areas, lenders may require home buyers to carry flood insurance as a condition of the mortgage.

Federal Crime Insurance

Many locations in Maryland experience high crime rates. You can qualify for the Federal Crime Insurance Program if you live in a high-crime area and have the required locks and security devices. Coverage is limited to loss due to burglary or robbery. For additional information call your insurance agent.

Farmowners Policies

Farmowners policies are available to farm families as protection against hazards that affect them. These policies may be written to cover dwellings, private structures, personal property, additional living expenses, barns, and other buildings.

This package policy covers the main farm dwelling, accompanying private structures, personal property on and away from the premises, additional living expenses, comprehensive personal liability with medical payments, and physical damage to both personal and real property. Farm personal property (animals and grain), barns, buildings, and structures may be added.

Superior farm dwellings and barns may qualify for lower rates. Credit is allowed for approved lightning rods and a solid foundation for dwellings. Barns and outbuildings may qualify for lower rates if they are not over one story, have a solid foundation, incombustible floors, and do not have open sheds or hay storage.

The hazards that may be covered are fire, extended coverage perils, vandalism, limited glass breakage, and theft in the Basic (FO-1) form and additional perils in the Broad (FO-3) form policies. Employer's liability for hazards to farm employees may be included.

Older Homes Coverage

Many older homes, because of unique construction styles or designs, have high replacement costs, particularly in relation to their market value. Replacement cost coverage on such a home would require a high premium and the insurance company would face considerable costs in duplicating or replacing such property. In fact, for this reason, most companies provide an older home package policy. Older home policies cover the same perils as the Basic (HO- 1) form. The difference is that this policy insures the house for its actual cash value, not replacement cost. Form HO- 8 is used for this type of policy.

Mobile Home Coverage

There are special policies for people who own and occupy mobile homes that are at least 10 feet long. The typical mobile home policies provide basically the same coverage as the Homeowners Broad (HO-2) form or Special (HO-3) form. Premiums for a mobile home policy can be substantially higher than for a similar policy on a conventional house because of the difference in construction and the greater susceptibility of mobile homes to wind damage.

Factors Affecting Your Cost

The price homeowners pay for insurance on homes and furnishings is based on a number of factors. One of the most important of these is the amount of money insurance companies have spent to settle claims filed by or against their policyholders during a given period.

Your premium depends on the breadth of the coverage you select, the amount of insurance you buy, the locality of your house, and the insurance company. There are additional factors that must be considered. They include the fire-fighting equipment of your fire department and the efficiency of its personnel; the dependability of the fire alarm system; and the nearness of a water supply suitable for fighting a fire. The type of material from which your home is constructed is taken into consideration in determining what you pay for your insurance. All other things being equal, it costs more to insure an all-wood house than a house made of brick or stone.

Tips for Saving Premium Dollars

As a smart consumer, you want to make the best use of your insurance dollars. You can start saving those dollars by paying your premium annually to save finance charges. Generally speaking, the less bookkeeping for the company, the lower the premium. You also can choose a large deductible. Approximately one-third of all losses for damage to homes and contents are for less than \$100. These small losses frequently are as costly to process as large losses. To keep the cost as low as possible for insurance that pays for the larger losses, insurance companies today include a deductible clause in homeowners policies. This means that the policyholder is responsible for all losses up to that amount.

There is a basic \$250 deductible on all forms of the homeowners policy. Larger deductibles are available

at premium savings of as much as 20 percent. A \$100 deductible is available as an option.

Installing safety devices such as a burglar alarm, sprinkler system, smoke detector, or dead bolt locks might reduce your insurance premium. Check with your agent to see what devices qualify for discounts. Some companies offer a discount if the residents of the home are nonsmokers.

Retirees may be eligible for discounts on premiums. Retired people are considered a better risk because they often spend more time at home where they can look after their properties.

Many insurers offer lower premiums to owners of new homes. New homes are less subject to insurance claims because of the newness of the construction, wiring, and safety features. A discount of 10 percent the 1st year is normal for a new house. Each year for the next 5 to 9 years the discount goes down.

Insurance Selection

Take the time to carefully select an insurance agent. Look for someone who is knowledgeable, professional and who demonstrates concern for your well-being. You should never hesitate to call your agent for insurance guidance and advice. Your premium dollars should buy service as well as an insurance policy.

When developing your home insurance program, remember to use your home insurance dollars to first protect against risks that would result in major financial losses to your family.

Read your insurance policies and know what you are covered for. Pay particular attention to policy exclusions and limitations. Ask your agent to explain anything you do not understand. Be sure to periodically review and update your coverage with the assistance of your agent.

Finally, remember if you have a question, problem, or complaint about insurance, you should contact the Maryland Insurance Commissioner located in Baltimore.

Guide to Choosing Insurance

Before shopping for insurance, you must decide what coverage you need. Record this information on Table 2. Then use Table 2 to compare rates among a number of companies before you select one.

Table 2. Insurance coverage list

Your home

- The replacement value of your home is \$ _____
- Will you insure it for 80 or 100 percent of this value?
_____yes, _____% _____no
- What policy type (coverage) do you want?

- How large a deductible do you want?

- Will an inflation guard rider be worth the extra cost?
_____yes _____no
- How old is your home?
_____ (years) _____ (months)
- What safety devices are installed in your home?

- Do you qualify for flood insurance?
_____yes _____no

Your personal property

- Do you have a personal property inventory?
_____yes _____no
- How much insurance is needed to cover the value of your personal property less depreciation?

- Is your personal property worth insuring for full replacement value?
_____yes _____no
- Which items need to be scheduled (listed) under a special rider?

Your liability coverage

- How much liability coverage does your family need? \$ _____
- Write down the type of policy, the deductible and the amount of coverage you want.
Call insurance agents that sell in your area.
Compare the total costs on annual basis.
- Do you need to supplement the standard coverage?
_____yes _____no

Annual premium

Public type _____	Company A _____	B _____	C _____	D _____
Deductible _____	\$ _____	\$ _____	\$ _____	\$ _____
Amount of coverage:				
House _____	_____	_____	_____	_____
Extra liability _____	_____	_____	_____	_____
Scheduled property _____	_____	_____	_____	_____
Total premium _____	_____	_____	_____	_____

Claims

- Know how to file a claim before an accident happens.
- Have an inventory list ready when you need it.
- Report any theft or vandalism to the police. You will need a complaint number from the police before your insurer will act.

- Keep the receipts for motel rooms, meals, and extra transportation should you have to stay somewhere else because of a disaster. You can expect reimbursement for your living expenses.
- Try to make temporary repairs and protect your property from further damage.
- Get estimates from experts for repairs for structural damage.

Insurance adjusters try to be fair, but sometimes mistakes are made. If you disagree with the settlement offer, talk it over with your agent. If you are still not satisfied, contact the Maryland Insurance Commissioner.

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