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Chapter 3: Homeowners' insurance: Understanding structural coverage, personal property protection, and liability policies

3.1. Introduction to Homeowners' Insurance

Homeowners' insurance is a necessary element of financial freedom that serves to protect individuals as well as families from physical and monetary loss. This type of property insurance includes several types of coverage under one policy. The coverage options are unique and numerous but generally fall under three distinct categories: dwelling protection, personal property protection, and liability coverage. The actual coverage provided for the dwelling, contents, and potential liability claims are unique to individuals or family circumstances (Campbell et al., 2023; Ahmed et al., 2024; Jennings et al., 2024).

Policies are generally aimed at offering protection to the majority of customers; however, changes can be made to provide additional protection at an increased cost. The three areas of coverage must all be addressed in order to provide the best policies. The dwelling such as the house, garage, and basement must be insured against numerous catastrophic events. Personal property must be protected from certain catastrophic losses, such as theft. The possibility of a lawsuit arising from some other person's injury or property loss must also be addressed. Important outside factors help determine the type and amount of coverage required. The first issue that should be addressed is the unique differences in policies. The first important decision to make is the amount of coverage on the house and contents. If either is under insured, the homeowner will be responsible for some or all of the cost of what is lost. In addition, it will limit the amounts reimbursed when damage occurs. This is particularly sensitive if the homeowner experiences a complete loss, that is, if the dwelling is destroyed and everything inside the dwelling is lost. Similar coinsurance provisions apply to personal property but with somewhat different limits (Patel et al., 2023; Wang et al., 2025).

3.1.1. Homeowners' Insurance: An Introduction to Coverage and Protection

Every homeowner needs insurance, but no one wants to spend extra money on it. We buy insurance to cover us for that awful day when something awful happens. For most of us, our home is our most expensive investment, and our possessions are irreplaceable collections of the stories of our lives. Unfortunately, most of us will never meet our insurance representative in a friendly social setting and, too often, when we do meet, it will be at a funeral or in a time of crisis. That is when we will find out if we truly understand our insurance. Regardless of the circumstances, you have a right to expect your representative to give you the best advice at the proper cost.

What is homeowners’ insurance? It is protection against financial losses to your home or injuries suffered outside your home. It provides reimbursement for loss or damage done by others to your furniture, clothing, appliances, and other personal belongings. It also can cover a wide variety of situations that will make your life miserable if you do not obtain insurance to protect you from them. In short, homeowners’ insurance is part of the American way of life. Even as you learn about your homeowners’ insurance, you will also be learning about how this product has made America what it is and how to protect it from the devastation that can occur without it.

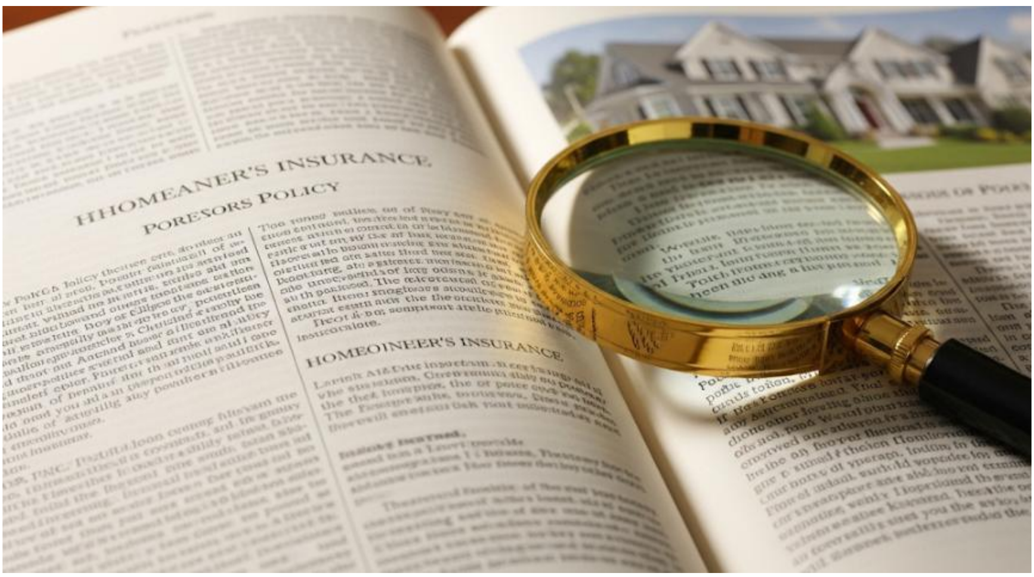

Fig 3 . 1 : Understanding Your Homeowners Policy

3.2. Key Components of Homeowners' Insurance

Homeowners' insurance can be a complicated mix of different types of insurance that protect your home, belongings, finances, and more, but by breaking it down into understandable sections, it may prove simpler. Each part of homeowners' insurance has a different name and covers a different area. Most homeowners' insurance policies include:

- Structural coverage: Covers the house, garage, shed, fence, and any other structures that are permanently fixed to the property. Types of damage that are usually covered are fire, lightning, hail, windstorms, theft, and vandalism.

- Personal property protection: Covers your belongings inside your home. This not only includes furniture and clothing, but also electronics like TVs, video game systems, computers, and smaller appliances like microwaves, dishwashers, and refrigerators.

- Liability policies: Protect you in case someone gets hurt on your property and sues you. This can include injuries from falls, dog bites, a trip-and-fall injury, and more. Liability coverage may also cover damage caused by a member of your household.

Navigating Homeowners' Insurance Basics

Many homeowners wonder if they need to be concerned with the various types of homeowners' insurance available today, and the short answer is yes. Why? Homeowners' insurance is meant to protect your biggest investment - your home. If your home suffered a fire, natural disaster, or any other major loss and you didn't have insurance, you would most likely be forced to build it back from scratch. Depending on your financial situation at that point, this may not be feasible. Therefore, by taking out homeowners' insurance that's right for you, it can prevent an enormous amount of hardship. By understanding common insurance vocabulary words and what making a claim might entail, your choices may become easier.

3.2.1. Navigating Homeowners' Insurance Basics

Homeowners' insurance is a complex maze that encompasses multiple coverages for a wide variety of situations involving a home and its owners. Homeowners' insurance packages can vary greatly among insurers. However, most coverages will protect the owner against large repair expenses or repairs themselves, personal property theft or damage, and liability for damage to the property or damage or injury to another person. Homeowners' insurance policies are generally written for an annual premium, and it is important to review coverages at least annually to be sure that special situations are covered and that someone is not paying for excessive coverage for minimal risk.

Homeowners' insurance policies cover personal exposure and typically are not available in the form of a business policy to cover business-related claims.

Homeowners' insurance packages generally provide three types of coverage: structural coverage, personal property protection, and liability policies. Homeowners' insurance policies differentiate among home ownership types: A homeowner is generally someone who occupies the insured property; an insured is someone who may or may not occupy the insured property; a tenant is someone who does not own or occupy the insured property but rents or leases the premises; and a condo owner is someone who owns a condo unit but does not own the structure enclosing the unit. Coverage is not available under these policies for business use, hotel, or advertising agencies, but separate policies are available for such business-related uses. The homeowners' policies are made up of three parts: Coverages, the Definitions Section, and the Conditions. The Coverages section describes the things insured, the types of risk covered, and the limits on recoverable damages.

3.3. Structural Coverage

Homeowners' insurance doesn't provide the best coverage for your home; structural coverage does. Why is it so important? Because if your house burned down and your homeowners' insurance policy reimbursed you at its actual cash value, you would end up with less than what you would need to rebuild it. This happens because insurance policies have special formulas that determine how much you get back when you file a claim. These formulas factor in depreciation, leading to significantly lower reimbursement amounts than a structural policy. It is structural insurance that provides a promised amount based on the full replacement cost at the time of the loss. In fact, structural insurance operates no differently than life insurance: If you die, your loved ones need a specific amount to cover your absence and go on with their lives. This is no different for your home. If you die while it is standing, your loved ones need a specific amount to knock it down and start all over again.

As previously mentioned, structural insurance covers the replacement cost of your home, subject to certain defined exclusions. Unlike a homeowners' insurance policy, which includes an actuary's best guess for how much your home is worth, structural insurance actually provides a specific number that the insurance company agrees to pay in the event your home is lost or destroyed - it's a one-number policy. The structural amount might include a little more than the cost to rebuild your house; it would also include associated site infractions, particularly if the site is hilly or rocky. However, it doesn't include your property - the landscape bushes and trees or the furniture, appliances, clothing, etc., located inside your house.

3.3.1. Definition and Importance

Homeowners' insurance includes many different types of coverage. First and foremost, homeowners' insurance provides structural coverage. Structural coverage is insuring protection for a homeowner's most valuable asset, their home. Without proper structural coverage, a homeowner could lose tens or hundreds of thousands of dollars in the event of a fire, theft, or other insured occurrence. It is important for homeowners to obtain the proper structural coverage because it is typically the largest component of their homeowners' insurance policy. Homeowners should also be aware that many homes do not have adequate structural coverage. Coverage amounts are often set based on automated estimates, without an actual appraisal, and home values can exceed those estimates significantly. Not having enough structural coverage can be an expensive mistake. If a home has limited structural coverage and has been destroyed, the homeowner may receive only limited money to rebuild the home. This can contribute to a financial disaster.

3.3.2. What is Covered Under Structural Coverage?

What structural coverage generally covers

Structural coverage protects the structure of your home. The standard homeowners' insurance policy explains the basic structure of a house, which typically includes the following: walls, roofs, ceilings, floors, windows, doors, and any attached fixtures such as plumbing and heating systems; permanently installed air conditioning systems; built-in dishwasher and microwave oven; columns, beams, and foundation; porches, patios, garages, and carports; and any attached structures. Also, any structure used to store personal property related to the structure of the home itself, such as furnaces, water heaters, and central vacuums.

Homeowners' insurance protects against covered risks that cause a covered loss. Each homeowners' insurance policy identifies both a list of covered risks and a list of exclusions that describes risks that are not covered. Many standard homeowners' policies use the phrase "all perils except those that are listed" to indicate that all risks except for the listed exclusions are covered events. Potential covered events for structural coverage generally include the following: fire and smoke; lightning; windstorm; hail; riot and civil commotion; damage by vehicles; damage by aircraft; explosion; vandalism; theft; falling objects; weight of snow, ice, or sleet; overflow of water; sudden damage from steam; sudden, accidental freezing; sudden and accidental tearing; electrical damage; and damage caused by animals.

3.3.3. Exclusions in Structural Coverage

There is nothing scarier than coming home to a house that has been severely damaged by a tornado, hurricane, flood, or fire. No one wants to feel the constant stress of having to repair the structure that shelters them from the elements. Most people rely on homeowners' insurance to help cover the repair costs when something unexpectedly happens to their home. However, not all damage is covered. The shopper should make sure that they understand what damage will be covered and not covered before purchasing a policy.

Exclusions are the items or events that are not protected by your homeowners' insurance policy. Although specific exclusions vary by provider, the following is a list of the more common things that typically are not covered under a homeowners' insurance structural coverage policy.

1. Neglect and wear and tear—Your insurance company will not pay for damage that resulted from not taking care of your home or the natural aging process.

2. Earthquakes or floods—If you live in a known flood- or earthquake-prone area, you should consider purchasing flood insurance and a separate earthquake policy.

3. New homeals—Homeowners' insurance is designed to cover unexpected events. Damage to your home as a result of new homeals is not covered.

4. War—Unless something is officially called World War III, don’t expect any coverage related to war damage.

5. Foundation Damage—Your homeowners' insurance will cover most damage to your home, but usually not damage done to your home's foundation.

6. High-Value Items—High-value items, like collectibles and jewelry, often need adjusted value limits in your policy. If those high-value items are damaged, your content will usually only be reimbursed for the adjusted value you agreed upon, not the replacement price.

7. Pest Infestation—Your homeowners' insurance usually will not cover damage caused by insects or rodents in your home.

3.3.4. How to Determine Coverage Amount

In determining the amount of money required to reconstruct a home, there are generally two schools of thought. The first and most intuitive one is to use a Dollar amount per square foot. In other words, your insurance company would likely have a standard sheet that says, on average, to rebuild a home of 2000 square feet, it will cost X. Please note that this could be wrong, and I will explain why in a second. The second method is to take a construction cost estimator classifying materials needed for the project and calculating a total based on physical amounts of those materials and also labor cost.

For most of my readers, I would recommend going with the method of the average per square foot cost given how time-intensive and expensive the second method is since all you have to do is provide a number and your insurance company would use that number to come up with the Dollar amount to cover the cost. However, I caution you that insurance companies have to make money and that is why it is common to see them under-insure and over-charge their customers at the same time. This is allowed and is considered fair because despite the fact that there is a lot of competition between insurance companies, it is heavily regulated by the government. What that means is that it is easier for insurance companies to win customers by advertising than by actually giving competitive coverage prices. That is why I say that the average is called a standard sheet, the standard sheet information could be out of date, incorrect and different from what actual construction costs are.

3.4. Personal Property Protection

Generally, your homeowners' insurance policy will cover more than just your home's structural damage from a covered loss. It will also provide for the loss of your personal property or its destruction. Personal property generally includes all of your contents and belongings that are not attached to the physical structure of your home. Coverage A, Dwelling, only covers your home itself and any attached structures, such as a garage or portico. Coverage B provides coverage for other structures on your property that are detached from your home, such as a tool shed or gazebo. Both Coverage A and Coverage B insure against damage to the structure itself.

Property in Coverage C includes your personal property, such as clothing, furniture, appliances, and electronics, while Coverage D pays for living expenses incurred when you can't live in your home due to a covered loss. Coverage C will also generally cover a limited amount of certain items stolen or damaged off your premises, such as jewelry, firearms, furs, or business-related property, typically for up to 10 percent of the amount listed on your policy although higher coverage limits are available. Also, keep in mind that Coverage C usually covers perils, or causes of damage or loss, at a different level than the coverage for the structure itself. For instance, your personal property is probably insured on a “named peril” basis, meaning that the coverage only applies to specific types of risks, such as fire, theft, or vandalism.

3.4.1. Understanding Personal Property Coverage

When a disaster strikes, the first thing homeowners often think of is their property: the walls, ceilings, appliances, furniture, and everything in between that help make a house a home. And while many homeowners' insurance companies offer structural coverage for damages to your home, it's important to pay attention to the personal property protection section of your insurance package, which helps replace treasured items that might be lost. With most policies, loss or damage to personal possessions such as your family's clothing, beds, kitchenware, computers, and furnishings is covered only up to a certain amount. Additionally, homeowners' insurance protects homeowners from specific types of loss: damage from something like wind, lightning, or theft might be covered, while damage from floods, earthquakes, or lack of home maintenance might not be.

From televisions to clothing, your home's contents can be expensive. Personal property coverage in your homeowners' insurance policy helps replace items if they're stolen or damaged by a covered peril. It can come in the form of replacement cost coverage or actual cash value coverage. With replacement cost coverage, items are replaced with new ones that are functionally similar to the old ones. For example, if your 5-year-old couch is stolen, the insurance policy would cover the cost of buying a new couch. Actual cash value coverage considers depreciation and pays the insured for the value of the items at the time of loss, which is usually much lower than the replacement cost. In the same example, if that couch was worth half of what you originally paid for it at the time it was stolen, that is the payout you would receive.

3.4.2. Valuation Methods: Actual Cash Value vs. Replacement Cost

Homeowners' insurance is a contract that, when fulfilled, helps the policyholder to recover financially from insured losses. One of the key features that determine how much the policyholder is reimbursed when they submit a claim is the valuation method in the policy. The two most common approaches are either Actual Cash Value (ACV), which looks at the value of the property at the time of the loss, or Replacement Cost, for which the policyholder is compensated for the cost of replacing the item with a new one of like kind and quality, without taking into account depreciation. Take the example of a 10-year-old television that has little value left but must be replaced if damaged. If the homeowners' policy used RCV, the policyholder would receive a payment ample enough to purchase a brand new television, regardless of depreciation, while if the policy used ACV, the payout would be significantly less after taking depreciation into account.

There is a need for Property Coverage to be as straightforward as possible, and homeowners' insurance policies have tended to give less coverage for personal property than for the exterior features of the home, such as the roof and the walls. For an understanding of how personal property coverage is determined, we detail here the two available valuation methods and the pros and cons of each option. It is important to note that many policies state that only Building Coverage tends to use Replacement Cost Valuation provisions. Policies may also state that they will reimburse losses up to the policy limits, for actual cash value, or for repairs paid directly by you. In most policies, there are dollar limits or different sub-limits applicable to certain types or categories of personal property.

3.4.3. Common Exclusions in Personal Property Coverage

Most homeowners' policies state which perils are covered but do not provide a full list of covered perils. Instead, they exclude certain perils from coverage. The most common exclusions typically include the following:

Inherent Damage. Personal property is subject to certain types of damage as a result of its inherent nature. For example, furniture may fade from sun exposure, and wool rugs may be damaged by moths. By stating that losses due to inherent damage are excluded, insurers avoid the burden of replacing property in such cases.

Wear and Tear. Households are typically filled with items that are lived with, loved, and used every day. Everything from worn clothes to chipped China and scratched furniture provides testimony to the household's life. Such damage is simply a part of life, so damages resulting from wear and tear are excluded.

Mechanical Breakdown. Mechanical breakdowns occur frequently with personal property such as electronic equipment and appliances. Computer and entertainment center failures due to hard drive, power supply, or software problems can be devastating, but are typically not considered property losses. Rather, they are viewed as either product liability claims or issues with workmanship, and therefore, they are excluded.

Neglect or Faulty Design. Any structure, whether a house or an item of personal property, is subject to evolving technology. As managers of that structure, homeowners must recognize that certain aspects may be flawed or weakened. Neglect or faulty design is excluded not only to protect insurers, but also to encourage homeowners to take responsibility and the necessary steps.

Deterioration. As personal property ages, there will inevitably be some level of deterioration. Insurers cannot monitor and replace goods as they age. Consequently, losses that occur due to deterioration are usually excluded on a property policy.

3.4.4. Inventory and Documentation of Personal Property

A crucial aspect of ensuring suitable limits for the personal property coverage in the homeowner's insurance policy is to have a current and accurate record of property and the estimated value of each item. This task is commonly overlooked and, at the time of a claim, policyholders will wish they had completed the task prior to the loss.

Over time, homeowners acquire personal property, such as clothing, appliances, furniture, books, jewelry, collectibles, and sports equipment, that may have considerable value. Homeowners should conduct a room-by-room inventory of all items in the house. Each room should be documented, along with a value assigned to each item. For items that are uniquely identified by receipt or identification numbers, such as electronics and appliances, making a list of those items and including the identification numbers associated with them is helpful. Additionally, receipts or estimates for any items of considerable value should be retained in a safe deposit box, fire-resistant safe, or another safe place.

Homeowners can ask themselves questions such as "What furniture would I miss most if it were lost?" and "What items in my house could I sell for the most money?" Think about items in other rooms, as well, such as a collection of stamps in the den, a collection of baseball cards in the back of the closet, or the expensive ruby ring in the jewelry box. Additionally, photographs and videos are invaluable records of property ownership and make loss verification considerably easier. The policyholder should store photographs or videos at the house or condominium, and copies should also be stored in a fire-resistant safe or other secure location off the premises.

3.5. Liability Policies

Liability coverage protects the insured from liability arising from negligence-based lawsuits. Such coverage is included in all homeowners' policies. There are two types of liability coverage provided by a homeowners' policy: bodily injury and property damage. Bodily injury coverage protects your liability for medical expenses incurred by others as a result of the insured's negligence. Property damage liability protects your liability for damage to other people's property. Your homeowners' policy will pay only if you are legally liable. Typical dangers include dog bites and injury caused by children or by the ownership or maintenance of a swing set, trampoline, or swimming pool.

Your homeowners' policy contains a significant exclusion for a very narrow range of liability. The narrow range of liability that is excluded from your policy covers certain types of ultra-hazardous activities or certain types of reckless and intentional conduct, such as causing bodily injury to someone you do not know. Business liability is not covered. This means that business liability is covered by a homeowner's policy only if the business is incidental to the residence premises, such as a part-time babysitting business or a business that is carried on in a spare room in your home. For this reason, business liability is typically covered by a commercial general liability insurance policy, which has broader coverage and higher limits.

A homeowners' policy provides one of the most important coverages you will ever purchase; the potential for a lawsuit resulting in a court judgment against you for negligence is greater today than ever before. A standard homeowners' policy provides coverage for bodily injury and property damage liability. Higher limits of liability coverage are also available. However, the uninsured or underinsured motorist coverage you purchase for your automobile policy provides broader coverage if you are injured as a result of someone else's negligent conduct.

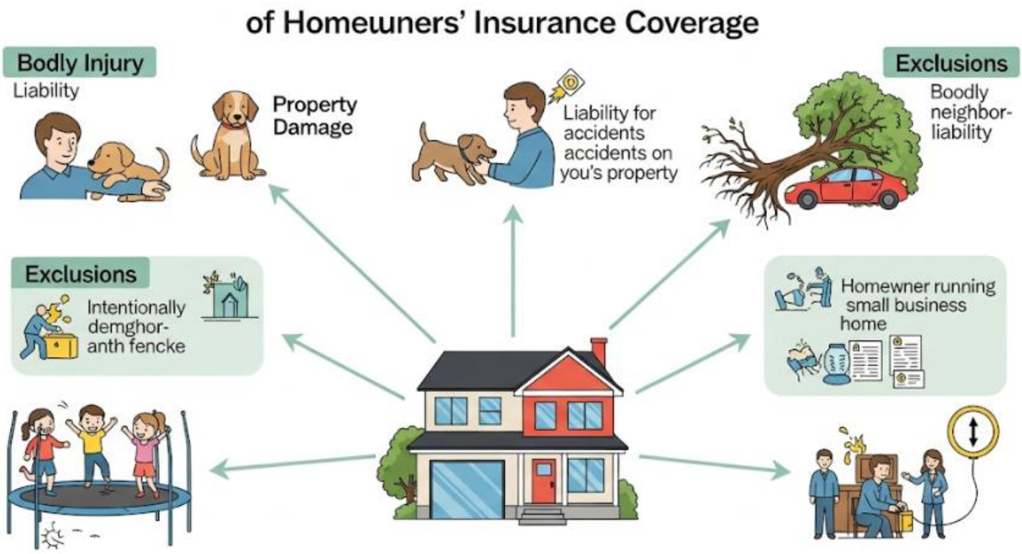

Fig 3 . 2 : Understanding Liability Risks in Homeownership

3.5.1. Overview of Liability Coverage

Liability coverage helps protect you from the costs of harming other people or their property. This portion of homeowners' insurance kicks in when you're responsible for the mishap. Liability coverage pays for the damages, freeing you from financial loss. You get a predictable and affordable way to handle what could be a huge expense. Liability coverage in homeowners' policies pays for lawsuits, injuries, medical payments for covered accidents, and damages to someone else's property. Homeowners' insurance and certain other residential insurance policies offer liability coverage. It is sometimes called personal liability insurance. It's one of the main ways you protect yourself from liability losses.

Homeowners' insurance policies include both liability coverage for bodily injury and liability coverage for property damage. Typically, liability insurance pays for the portion of a claim someone else would have been paid, whose injury or whose property was damaged in the accident: To put it simply, whenever you're the wrongdoer or the cause of an accident, liability coverage will come into play. The coverage can be triggered by either bodily injury or property damage conditions, on someone else's part, or on their property, due to your wrongful act. There are generally two sections of liability coverage on a homeowners' insurance policy: Section I covers property and Section II covers liability. Part 1 begins with Coverage C, which ensures all of your personal property. Section II contains two Coverages: Coverage E, which includes personal liability protection, and Coverage F, which covers medical payments to others.

3.5.2. Types of Liability Coverage

Liability coverage is most commonly written in two types of policies. The first—and what many homeowners are likely to have—is a personal liability policy, also called personal liability insurance. This insurance protects the homeowner from liability for general negligence losses falling outside the business, automobile, professional, and other largely specified fields. This liability policy meets the homeowner's greatest need for coverage. The other liability policy is a personal umbrella policy. It protects homeowners who have assets that could be depleted by a lawsuit. An umbrella policy extends the limits of the personal liability policy and fills in some of the gaps in coverage that may exist in an underlying policy. Not all umbrella policies are alike, and it is important for policyholders to fully understand how these policies work, what risks may not be covered, and what the policy limits are. For most states and types of coverage, these gaps in coverage will include automobile and certain types of liability losses as well as most business exposures. Generally, the minimum limits for a personal liability policy will be $100,000, while a minimum personal umbrella policy limit will be $1 million. Catastrophic events resulting in a lawsuit exposure in excess of only these minimums are likely to occur only infrequently, making small personal liability policy limits a realistic choice for many policyholders. Nevertheless, it is wise always to consider increasing these limits to a level that would provide financial protection.

3.5.3. Common Exclusions in Liability Policies

Although a homeowner's liability policy is meant to provide very broad coverage, there are some common exclusions that should be noted. For example, liability that arises from a premises where business activities are conducted or from a rental unit is usually excluded. Liability that arises from the insured's participation in business activities or that arises from damages resulting from the rendering of or failure to render professional services is also excluded. If your home has a swimming pool, trampoline, firearm, or dog, special coverage consideration should be given to those exposures. Another common exclusion is that liability to others using your premises or property with your permission (other than for a business or rental purpose) may be limited or excluded; liability to members of your household is usually excluded; liability to others for the maintenance, use, or operation of an aircraft, vehicle, or watercraft is excluded except under certain conditions; and liability for damages resulting from work-related exposures is usually excluded.

3.5.4. Limits of Liability Coverage

The unique characteristic and strength of a homeowner's insurance policy is the section that provides for protection against claims or lawsuits resulting from your negligence or that of an insured party. But this protection has its limits, and liability insurance, in most cases, is not all you may need. Most homeowner's insurance may limit the maximum that will be paid out for a single occurrence to from to . Higher limits may be purchased, but if you are sued for more than the limits of your policy and lose, you may find that your personal assets are at risk. Also, liability insurance does not provide coverage for every possible type of claim. Give some thought to the types of claims that could happen in your case. If you are in an industry in which lawsuits are common, such as construction or health care, it may be necessary to purchase additional malpractice or negligence insurance, for instance. If, on the other hand, you own and operate a business at or from your home, possible claims against you may be denied coverage under your homeowner's insurance policy. Discuss your concerns in detail with an insurance agent to help determine whether you need additional coverage, in addition to that provided by your homeowner's insurance policy. Historically, flood and earthquake damage has been excluded from liability coverage. But as unusual weather events continue to occur and climate change becomes an increasing concern, many other typical types of weather-caused damage are being debated. If you feel you live in an area where such an event could occur, ask your insurance agent what claims are covered and consider requesting those exclusions be removed from your policy.

3.6. Additional Coverages and Endorsements

Homeowners' insurance policies have been designed to meet the specific needs of most policyholders. However, many people may need additional coverage or selected endorsements to make their policies reflective of their total exposure to potential loss.

The amount of standard insurance may not cover all possible losses, and depending on your residence, some unique features may also need to be covered.

One additional coverage that an increasing number of homeowners have discovered is flood insurance. Homeowners' insurance policies in the average situation do not cover flood losses. Flood loss is defined as the inundation of two acres or more of normally dry land area or of at least two properties, at least one of which is a permanent structure, from overflow of inland or tidal waters, or from unusual and rapid accumulation or runoff of surface waters from any source.

Although flood insurance is available for properties, flood insurance may need to be purchased for those properties represented as being at a low risk of flood loss. Generally, in such areas, a minimum amount of coverage is required; the amount of coverage is significantly less than would be required to cover the potential loss of the property. Flood insurance is not offered as an endorsement on homeowners' insurance policies. Instead, homeowners must deal with the designated flood insurance program offices located in the various states. For homeowners and property owners particularly sensitive to flood loss potential, deductibles are required and are priced accordingly when determining the cost of flood insurance.

3.6.1. Flood Insurance

Flood insurance should be considered if the home is in a flood zone. Flood insurance is a separate policy from the homeowners' insurance policy. In many instances, this coverage is required to obtain a mortgage. Most homeowners are not aware that, unlike other water damage claims, such as sewage back-up or broken pipes, the flood coverage does have a 30-day waiting period if purchased directly. Many people find themselves waiting for that flood coverage to start when they initially purchased it from an insurance agent who writes this coverage as part of an umbrella policy, giving them immediate coverage.

The reason flood insurance is not available under the HO-3 and most other homeowners' policies is that the insurance industry has not been able to accurately develop flood models that can predict when a flood will or will not occur. There can be differences between the flood zones shown on the maps and the risk of a residence that are not tied directly to the river or lake but instead to existing homes that are much lower than the surrounding area. And why would anyone pay a premium for coverage? The reason is that while the increase in value of the home occurs slowly, it is also true that if a flood occurs, the total damage can be extensive.

3.6.2. Earthquake Insurance

In most areas of the United States, earthquakes are considered seasonal phenomena and risks are estimated to be minimal. This has caused most fluctuation insurance policies to exclude earthquakes, while eliminating coverage for damage that may be caused by earth movements. Earth movements are not just attributed to earthquakes; other earth movements, such as landslides, or damage from landslides resulting from artificial means, such as excavation or dredging, are also excluded. Earthquake insurance provides a way to add protection against the nearly catastrophic financial damage an earthquake can unearth.

A dwelling policy, coverage part A, is used to provide the dwelling limit, while the broad policy provides other separate structures, a personal property limit, and coverage for silos, fences, and parking lots. Earthquake insurance provides a full limit for sudden and accidental land sinking inflicted by an earthquake shock. Business and farm owners can also add earthquake insurance to the commercial building and personal property coverage. Earthquake insurance can also be purchased in some states through government programs that back private insurance policies, generally including California, but government assistance rarely covers the total loss.

Earthquakes are more common in some states than in others. Three factors are used to determine the cost of insuring a structure: the insured’s location, the condition and type of construction materials, and the amount of coverage requested. The insurance agent will normally ask where the home is located. Is it on a hillside, a fault line with an uncovered basement, or does it rest on solid ground? The answers to these questions give the insurer a place to start premium calculations.

3.6.3. Personal Umbrella Insurance

Sometimes you may purchase a personal umbrella insurance policy to provide additional liability insurance over and above your homeowner's liability limit and the liability limits on your automobile insurance. Personal umbrella liability policies provide higher limits than are generally available on your homeowner's and auto insurance, usually beginning at $1 million. Umbrella policies also apply to claims that might not be covered on your other liability policies. For example, the maximum limit on your boats, RVs, and other vehicles, other than those you use on land, is usually a low $1,500. An umbrella policy can also address a claim for property damage or bodily injury caused by your child or pet. Typically, a personal umbrella insurance policy protects you and your family against lawsuits for damage to someone else's property or for personal injury caused by you or a member of your household anywhere in the world. Personal umbrella liability insurance usually also includes a defense for lawsuits regardless of whether a claim is determined to be valid or not. Premiums for personal umbrella policies tend to be very low, given the coverage they provide. The cost of a $1 million personal umbrella policy averages less than $300 a year, though costs vary depending upon the characteristics of your family or household. If you can afford it, buying an umbrella policy is an excellent way to protect your family from financial catastrophe. Umbrella policies usually kick in when your homeowners', automobile, or other liability coverage has reached its limit. Umbrella coverage can do this even if the other coverage is not purchased from the same insurer.

3.6.4. Scheduled Personal Property Endorsement

In this chapter, we progress onto the additional coverages and endorsements homeowners may wish to include in their policy. Endorsements are amendments that can be added to your homeowners policy in order to cover excluded items or increase limits of coverage. Alabama law allows homeowners to create a contract to cover anything; as such, you will wish to find out if you are in need of any of these endorsements that are offered by your insurance company.

If you own expensive items like jewelry, furs, coin collections, stamp collections, or any other type of collection; you may wish to purchase Scheduled Personal Property Insurance, also known as Scheduled Personal Property Endorsement. While the standard homeowners insurance policy provides some coverage for personal property, it might fall short. The Scheduled Personal Property Endorsement allows individual items to have their own limit of coverage. The specified limit of coverage for these types of items would be on a separate endorsement page, called a Schedule, attached to your homeowners policy under General Conditions. This provides additional coverage specifically for the items on the schedule. If any of your items exceed the limited amount listed, that amount would not be insured. This additional coverage would typically have a lower deductible for the specified items on the schedule. The endorsement will also cover items that may be excluded on your homeowners policy.

3.7. Factors Affecting Homeowners' Insurance Premiums

Insurance companies often rely on statistical analysis to set premiums. They associate certain conditions with claims payouts and charge premiums according to the likelihood that your homeowners' insurance policy will generate a claim. The factors that most often affect the premiums you pay for homeowners' insurance are your house’s location, its characteristics, and your claims history. In the world of homeowners' insurance, your property’s location has the most significant effect on your premium amount. The closer you live to a coastline, the more likely you’ll pay higher premiums. Insurance carriers are especially wary of hurricane and tsunami risk. They also feel generous about charging you high premiums if you live in an area with a high incidence of homeowners' insurance claims, particularly for theft, glass breakage, and damages from falling trees. If you live in an area with a significant earthquake, tornado, hailstorm, wildfire, or flood risk, you'll pay more, too. All of these factors may affect your homeowners' premium because of your higher likelihood of making a claim. Another calculating factor is whether your house is an attractive target for thieves or is at risk of damage from natural disasters. An average home protected by an alarm system that's backed up by local police protection may generate significantly fewer claims than a large, isolated home without a monitored alarm system. Many people add extra locks to doors and windows, install security lighting and motion detectors, and purchase alarm systems after they've been burglarized, but by then it's too late. In cases of repeated losses in a given zone, an insurance provider may deny coverage entirely. Insurers are also likely to charge extra for unprotected homes or homes at risk of other types of loss. If protective measures are ineffective, your home coverage may not even cover you.

3.7.1. Location and Risk Assessment

The price you will pay for a homeowners' insurance policy is based on the risk that the insurance company has in insuring your home. The more risk the insurer takes on, the more you will pay for your coverage. One of the first things that an insurance company looks at when underwriting an insurance policy is the location of your home. It is safe to say that there are some homes that are in locations that are far more risky than others. If an insurance company can see that homes in your location burn down often or have frequent claims for some other covered loss, your premium is going to be high. This is especially true if your home is in a location that has a history of severe theft, burglaries, or any type of natural disaster, including hurricanes, floods, and earthquakes. Insurance companies typically price policies higher based on your risk level.

You cannot control the location of your home, so if you try to compare your homeowners' insurance rate with that of one of your friends on the other side of town, your quote could be significantly different simply because of where you live. Other factors in your home's location that could affect your homeowners' insurance pricing may include whether you live near a fire station or fire hydrant, or if you are near a boat dock, wildlife preserve, or volcano. When considering the risk of your home, insurance companies also consider the unlikeliness of another natural disaster affecting a wide area. For example, if you live in a tornado alley, your risk is higher, because a tornado can sweep out entire neighborhoods. Flooding alone can cause damage in several states and cities at once.

3.7.2. Home Characteristics

In addition to the risk level of a particular location, home characteristics also influence how fast a homeowner premium can rise, although these variables can also be used to vary policy premiums down. As a general rule, the greater the unduplicated exposure to physical risk, the higher the premium. Some of the physical characteristics that can verify and change premiums include: age of roof; presence of multiple roofs; roof slope; type of roof; type of siding; kind of construction; type of foundation; age of home; presence of fireplaces; age and type of electrical system; age and type of heating system; type of plumbing system; presence of pools; type of garage; type of floor; presence of mold.

Fire is considered the most costly physical risk for a residence. It can generate the most claims and require the most expenditures for insurers throughout the United States. Other risks are also of concern to insurers, such as those from windstorm, earthquakes, and floods for coastal properties; sinking, flooding, or settling for a vacation or seasonal property or a residential property located in an area with sand or mixed sand and clay; termites or other pests. Whatever the risks involved, they can be supplemented by poor maintenance on the part of the homeowner. Home and water damage from faulty plumbing and appliances tends to result in high losses, as do claims for stolen jewelry and art that are not properly kept in safe, insured, or documented condition.

The effective management of fire risk has long been the central focus of national and local insurers with regard to policy pricing and coverage. Insurers develop and use risk assessment models that include various geographic, demographic, and structural variables, mainly to gauge the risk of loss from fire. Underwriting decisions concerning policies or endorsements of small and mid-market personal lines property accounts are based on some form of predictive risk analysis. In addition to statistical data, the home portrait is also derived from historical underwriting guidelines. These guidelines examine an entire home's landscape and architecture.

3.7.3. Claims History

If you are just buying a new home, you may not have a previous history for your new home. However, the previous homeowner’s claims history is something to investigate while you are buying or before you shift. If a buyer has had previous claims, then the new homeowners’ insurance may be significantly higher, as the new insurance companies may feel that the buyers would be more likely to make similar claims.

How do you check the previous homeowner’s claims history? The database that insurance companies use is called the Comprehensive Loss Underwriting Exchange or CLUE for short. Unlike credit reports, consumers can’t get a free report from CLUE; consumers must pay a fee and can only get a report by mail. You may need to be prepared to provide personal info to prove your identity. The data in CLUE is only as good as the insurance companies that report it, and mistakes happen. If you’re going to ask the current homeowners for a claims history, at least you’ll have backup to validate the history that you are being given.

What kinds of claims will make insurance companies run fast the other way? Here is a list of claims or problems that could cause extreme reluctance from an insurance company: A recent fire in the house or on the property; Multiple theft claims – especially if items such as things you would have to strap down, like a tractor or lawnmower; A claim for vandalism to the house or property; Frequent claims for the same type of issue, like water damage; Even claims for “acts of God,” like falling trees, may make insurance companies reluctant to help you out.

What else will make an insurance company hesitate to insure, or significantly increase the premium price? Shareholders or board members who do business in the same city, county, or state; Previous “high risk” history for that same area, like a high incidence of mortgage fraud; Previous claims to the same house, if being used as a rental or for a vacation home; If you’re buying in a neighborhood with a lot of foreclosures.

3.7.4. Credit Score Impact

Insurers factor in your credit score in part because they are anxious to avoid customers who are high risk. A credit score does not measure only consumers' tendency to repay debt. It also has to do with consumers' ability to manage their affairs well. People with low credit scores tend to be more careless in their general lives. They are, for example, more likely to be negligent and fail to report a fire, theft, or some other insured loss. They also tend to be more careless when reviewing their bills and are therefore more likely to overlook a small error on a bill that, if corrected, would prevent a larger loss in the case of an insurable event. In other words, a bad credit score is an indicator that consumers might be more careless about money-related matters. This could raise the chances of an insurer suffering a loss, regardless of whether the loss stems from a claim for an accident resulting in an injury, a claim for property damage, or a claim for theft.

Having a bad credit score isn't the only negative sign to insurers wanting to provide insurance. There are other factors used by insurers that signal greater susceptibility to filing a claim. You might be an applicant with poor credit, but there are other data points equally relevant to prospective claims flagging. Other risk factors that insurers might consider include personal or family income, whether outstanding debts are greater than net worth or family income, family size, married vs. single status, and whether you live on the premises or not. These other factors are perhaps not as public, however: there are many reasons why they could be used to help determine the insurance premium, given that this information is gleaned from a credit report, and the other family-related and income-based data points are relatively easy to obtain.

3.8. Conclusion

Homeowners' insurance can be a daunting and confusing subject, but this book serves as a practical guide to help make sense of many aspects of this important form of insurance. In Chapter 1, we discussed what homeowners' insurance is, what it covers, and why it is important. Additionally, we examined the following major points of interest regarding homeowners' insurance: the cost of homeowners' insurance; how to shop for coverage; the difference between a homeowner's policy and a dwelling fire policy; actual cash value vs. replacement cost; special limits of liability; additional living expenses; endorsements to standard policies; and high-risk, vacant, seasonal, and short-term rental properties. In the earlier chapters, we also discussed the many specifics of homeowners' insurance: structural coverage; homeowners' policy four coverage categories; personal property and personal liability protection; coverage for an owner-occupied residence; coverage for a tenant-occupied residence; coverage for a part-time rental property; and coverage for a seasonal and short-term rental property.

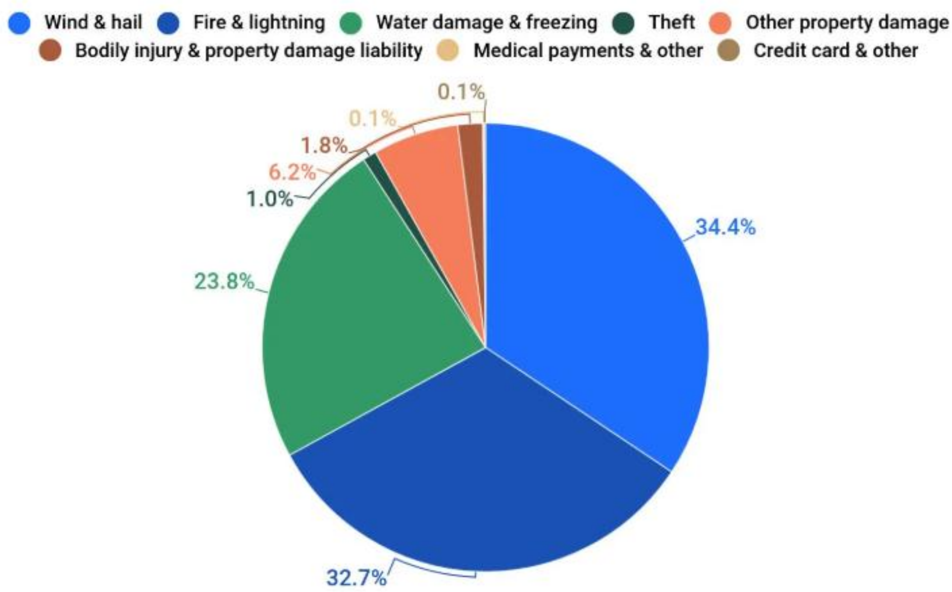

Fig 3 . 3 : Home Insurance Facts and Statistics

In summary, although navigating the world of homeowners' insurance can be an overwhelming challenge at times, understanding its basic structure can lessen the pain involved in the process. Additionally, having this knowledge can help homeowners understand their own specific insurance needs and help find a qualified insurance agent to take care of the homeowners' coverage. Homeowners can also participate more actively and knowledgeably in the process of selecting coverage that best fits their needs and budget. It is important to remember the old adage: caveat emptor, or let the buyer beware. Although this adage does refer to the buyer of real estate and not the buyer of insurance, the same philosophy can be applied to the insurance purchasing process. Many factors come into play when determining your coverage needs, and no two homeowners have identical needs.

3.8.1. Summary and Final Thoughts on Homeowners' Insurance

In conclusion, the purchase of homeowners insurance provides the owner with peace of mind and protection. Every homeowner should review their policy carefully before any loss occurs. They should understand what coverage applies, what deductible and limit apply, and when the coverage commences and terminates. The person should walk from room to room and examine what would be covered in the event of a catastrophic loss and what limit of insurance would apply. They may want to consider investing in pictures, videotapes, and audio tapes of their possessions to make any claims that might occur easier to process. Homeowners insurance is a very important financial tool that protects the homeowner from a huge financial loss due to disaster, theft, liability, or disaster that arises from their ownership of property.

Homeowners' insurance and the coverage that it provides are generally available only to owner-occupied dwellings. It is intended to protect the owner and their family members from loss and/or liability arising from their ownership, occupancy, and use of the structure. In comparing coverage, the homeowner should be familiar with what the current homeownership policy includes and excludes. Once this is done, the person can consider the coverage of other policies to see if the broader or narrower homeownership policy better fits their needs and wants. In the end, the person can select one or the other or even decide to go without homeowners insurance.

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