

# Money Mechanics

## Home Insurance

**W**HETHER YOU RENT an apartment or own a house, it's "home" to you and your family. In case of disaster, replacing that home—and your personal possessions—could be financially devastating. Buying home insurance is one way to protect yourself against that risk. But how do you choose the right policy? How much coverage is enough? What insurance do you need if you rent? This publication will help you answer these questions.



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### Defining Property

Generally, you can insure any property you own except land. For insurance purposes, the term "property" refers to two separate categories.

- **Real property or physical structures** such as your home and detached garage
- **Personal property or belongings** such as your furniture and clothing

To determine how much insurance you need, you'll have to figure out the value of both categories of property you own.

### Value of Real Property

Your home should be insured for its replacement cost—how much it would cost, at current prices, to rebuild the structure in the event of a total loss. It's estimated that two in three homeowners are underinsured. In today's market, homeowners must take responsibility for making sure they have adequate coverage. Insurance agents will estimate the cost of replacement, but it is a good idea to get a second opinion from a building contractor or an independent claims adjuster when buying coverage.

A policy that provides "extended replacement cost" coverage pays the amount stated on the policy plus, typically, an additional 20 to 25 percent. The additional percentage is intended to be a cushion in case coverage proves to be too low. But this buffer may not be enough if you fail to initially buy adequate coverage and fail to update it over time. Many policies will include an annual inflation adjustment, but even that may not be adequate during times of rapid increases in labor and materials costs. Home improvements—from kitchen remodeling to extra bedrooms—are another reason to update coverage.

**Figure 1** Personal property inventory sample form.

Room <i>Basement</i>		
Description of Item	Date of Purchase	Purchase Price
<i>Superior Brand Washing Machine Serial # J1234CVWS</i>	<i>3/1/2005</i>	<i>\$585</i>



If fire were to destroy your home, an inventory of your personal possessions could help you replace your belongings.

**Most policies insure personal property for its actual cash value at the time of damage or loss.**

### Value of Personal Property

How much are your possessions worth? Few people can estimate the value of furniture, clothing, sporting and hobby equipment, and appliances in their homes right now, let alone after fire destroys everything.

An inventory of your possessions is a good project for a rainy afternoon. Go through each room, including the garage, and list personal possessions with a date of purchase and purchase price. Inventory forms are available from insurance agencies or you can make your own “pencil and paper” or computer form by following the sample in **figure 1**. In addition to the written record, it is a good idea to take photographs or record a videotape. Once the inventory is complete, put copies in a safe deposit box or a fireproof container.

Most policies insure personal property for its actual cash value at the time of damage or loss. Actual cash value equals replacement cost minus depreciation. For example, if the television set you bought five years ago for \$450 were stolen, you would be paid the actual cash value of the stolen set, not the \$450 or the cost to replace the set at current prices. Some companies offer replacement cost coverage on personal property, eliminating the depreciation factor, but this adds 10 to 15 percent to your total premium.

Generally, the total amount of personal property coverage for household goods on the premises is 70 to 75 percent of the total real property coverage. If your house were covered for \$80,000, then, at 75 percent, its contents would be covered up to \$60,000. However, policies set limits on certain valuables such as cash on hand, jewelry, furs, collectibles, and artwork. Extra coverage, called floaters, may be purchased if you own such items and their value exceeds the basic coverage in your policy. When property is away from home such as when you are on vacation, coverage is up to 10 percent of insured property on the premises, or \$6,000 in this example.

### Policy Choices

Insurance companies provide six kinds or “forms” of homeowner’s insurance. If you own a house, you may choose from HO-1, HO-2, HO-3, and HO-8. Because of their limited coverage, HO-1 policies have become somewhat obsolete. The most popular form of homeowner’s insurance is HO-3. Too many renters lose all their belongings because they fail to carry renter’s coverage (HO-4). It is relatively inexpensive insurance and also includes some liability protection.

**Table 1**

**Coverages Under Standard Policies**

*(Figures are for main features of standard policies. However, policies of some companies may differ.)*

Forms	House	Detached Buildings	Trees, Shrubs, Plants	House Contents	Personal Property off Premises	Temporary Living Expenses
<b>Basic HO-1</b> (Perils 1–10)*	100% of policy value	10% of policy value	5% of policy value, \$500 maximum per unit	50% of policy value	10% of insured value of property on premises	10% of policy value
<b>Broad HO-2</b> (Perils 1–16)*	100% of policy value	10% of policy value	5% of policy value, \$500 maximum per unit	50% of policy value	10% of insured value of property on premises	20% of policy value
<b>Special HO-3</b> (All risks covered except those excluded by name.)	100% of policy value	10% of policy value	5% of policy value, \$500 maximum per unit	50% of policy value	10% of insured value of property on premises	20% of policy value
<b>Renter's HO-4</b> (Perils 1–16)*	10% of policy value on renter's additions to unit	Not applicable	Not applicable	100% of policy value	10% of policy value	20% of policy value
<b>Condominium HO-6</b> (Perils 1–16)*	\$1,000 on owner's additions to unit	Not applicable	10% of policy value	100% of policy value	10% of policy value	40% of policy value
<b>Older Home HO-8</b> (Perils 1–10)*	100% of policy (actual cash value)	10% of policy value	5% of policy value, \$500 maximum per unit	50% of policy value	10% of insured value of property on premises	20% of policy value

\*Perils covered

1. Fire, lightning
2. Windstorm, hail
3. Explosion
4. Riots
5. Damage by aircraft
6. Damage by vehicles (not your own)
7. Damage from smoke
8. Vandalism
9. Theft
10. Window breakage
11. Falling objects
12. Weight of snow, ice, sleet
13. Damage from steam heating or water heating system/appliances
14. Leakage or overflow of water or steam
15. Freezing of plumbing, heating, air conditioning
16. Short-circuit damage to electrical appliances

HO-6 is designed for condominium owners. Like the renter's policy (HO-4), its main coverage is for personal property. Generally, coverage of the condominium structure itself is included in one overall policy for the condominium community.

HO-8 policies provide actual cash value coverage designed to pay for returning the property to serviceable condition, rather than replacement of the same kind and quality of the original materials in older homes.

As indicated in **table 1**, coverage varies with each form. Generally, the more protection offered—or perils insured against—the higher the premiums. Rates vary with building materials and location of property. Also, some companies consider your credit history in setting premiums—charging consumers with credit problems higher rates. However, credit scores cannot be used solely as the basis for accepting applications or not renewing homeowner's insurance. The summary of coverage in table 1 omits many details, and coverage will vary from company to company. Keep in mind that insurance typically won't cover damages due to mold, termite or other pest infestations, or a lack of maintenance.

## Additional Coverage

In addition to coverage for your real and personal property, most homeowner's policies provide for living expenses while your home is being repaired or rebuilt. The amount is a percentage, generally 10 to 20 percent, of the total amount of coverage on the home.

A homeowner's policy also protects against liability claims against the policyholder and all members of the family who live at home. Personal liability pays the legal costs of lawsuits involving bodily injury on or off your property as a result of your family's activities. It also covers injury caused by an animal you own. Basic coverage is \$100,000 per occurrence, but higher limits are available.

## Insurance Buying Tips

Finding affordable home insurance can be a challenge. Many insurance companies have raised rates, lowered coverages, denied claims, and canceled policies. Shop carefully to find a low-cost insurer with a good reputation for claims service. Ask about rate discounts for property in low-risk areas.

Some insurance companies offer special rates to homeowners who are nonsmokers or whose property is equipped with burglar alarms, smoke detectors, and fire extinguishers. You also may get a special discount if your house is constructed with fire-resistant materials. The same discounts can apply to rental structures.

If you are buying a home, shop for insurance before closing the deal. Previous insurance claims on the property may hinder your ability to get coverage. Iowa allows insurance companies to back out of a home insurance contract for any reason during the first 60 days of a new policy.

Comparing coverage can save you money on homeowner's insurance premiums. Another way to save is to have a higher deductible placed on your policy. Deductibles—or the amount you pay for damages before the insurance policy pays—usually are \$500 to \$1,000 but can go as high as 1 to 5 percent of the coverage. The higher the deductible, the lower the premiums. It may be to your advantage to cover big risks with insurance and smaller risks with personal cash reserves.

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If you have any questions or complaints about insurance, contact:

**Iowa Insurance Division**  
330 Maple Street  
Des Moines, Iowa 50319-0065  
<http://www.iid.state.ia.us>  
Toll-free: (877) 955-1212

For more information, visit [www.extension.iastate.edu/finances](http://www.extension.iastate.edu/finances) or the Iowa State University Extension office in your county.

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