


SAGE *Solutions*

Financial Independence.....Let's Not Ignore *Liability Risk*



At Sage Hill, we stress with our clients the importance of zealously protecting your financial independence. After all, think about all of the blood, sweat & tears it took to attain your financial independence. To this end, we assess and manage investment market risk, interest rate risk, inflation risk, and credit risk. Let's not ignore liability risk....any of you who have found out of this risk by being on the title of a child's auto may have experienced this risk. We asked an outside liability insurance specialist to address liability insurance gaps and risks of our clients and their various "instruments of harm". Following are their thoughts re high end homeowner's insurance as an example.

Think all insurance is the same? That's what some insurers want you to believe, and hence, they sell their wares on one thing, and one thing alone..... cheap price. But somewhere deep down, we all know, or suspect, that with insurance, like with most things in life.... you get what you pay for. Nowhere is this more true than in the purchase of insurance for what is, for most, their most valuable possession aside from family and good health.... their home.

The truth is "Saving 15% in 15 minutes" could cost you not thousands, but hundreds of thousands, when you need it most: when your house burns down, or is inundated by a water main break when you're away for the weekend! Sound scary? It is.... read on.

As a homeowner, it is important for you to know how much money you'll need to rebuild your home should you suffer a total loss. Why? Because, if you read the fine print in your policy, you'll quickly see it's your responsibility, not the insurer's, to set the value (a little known fact). Do it wrong, and it's your problem, not theirs. Compounding this concern, in the experience of many, is that most direct insurers (like AllState, State Farm, Liberty Mutual, and USAA) may do little to guide the client on choosing an appropriate limit, but instead, set an arbitrary dwelling value, and then add an additional 10-25% extension, known as a "cap." If the cost to rebuild exceeds the cap, then you will have to dive into your savings to cover the difference. Adding insult to injury, you will probably then need to rebuild at the same spot to avoid a depreciated settlement, and you'll likely have little or no freedom to choose your builder, or to simply "take the money and run" with a cash settlement, rather than rebuilding, if this is what you want to do. These just simply aren't options with such providers.

So what to do? How to get what you pay for in insurance, and feel protected and secure? A prudent alternative would be to insure with a company that provides true guaranteed dwelling replacement cost. There are a handful of companies in our region that do this, including Chubb, Fireman's Fund, Ace, AIG, and Middlesex. With guaranteed dwelling replacement cost, there are no percentage limits or caps, and the policy pays the actual cost of repairing or replacing a damaged or destroyed home, even if the cost to do so is above the policy limit. This is designed to protect you, particularly after a major disaster, when the demand for building contractors and materials can push up the normal cost of reconstruction.

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"Underinsurance" is, in fact, a rampant problem growing daily throughout the Country. Approximately 58% of U.S. homes are underinsured by an average of 21%, according to Marshall & Swift/Boeckh, a leading provider of building cost data, and another 20% may be underinsured by as much as 35 - 50%! Do the math on your own home, and you can see the problem you might face!

The reality is many direct insurers are more concerned with market share and writing lots of business than they are with insuring homes accurately.... because they know two things: by underinsuring, their premiums look good to the unsuspecting buyer, and most people will never suffer a significant (>50%) dwelling loss. Hence, they're rolling the dice (on you!) that most buyers will never know the risk they're self-insuring! Is this a problem? You bet....

Other top insurers like those mentioned above, on the other hand, will require you to insure to value (which costs more arithmetically), but they are there when you need them.... when the big loss occurs, and isn't that the reason for which you buy insurance in the first place? Furthermore, this type of insurer offers a complimentary in home appraisal to help estimate the cost to rebuild in the event of a loss. This appraisal enables the homeowner, together with the agent or broker, to select the appropriate amount of insurance. Other lesser insurers will typically, and quite simply, estimate replacement cost over the phone, or via a computer program, without a subsequent onsite visit, and this can leave one terribly exposed.

Finally, don't confuse "market value" with "replacement cost." Many homeowners don't realize that their insurance premium is based on the replacement cost to rebuild a home in the event of a major loss, not on market value, or what the house would sell for today. Surprising to some, homes including land, can frequently be purchased for far less than the cost to rebuild the home alone! How can this be? The fact is fluctuating energy costs, rising costs of skilled labor, less competition as some builders go out of business, difficult access to specialty items, and increased overseas demand for materials and building products frequently combine to make this just the case! This is even so in times of decreasing home sale prices, as has been the norm in the past 12-18 months!

Best advice? Do your homework, and choose well, when it comes to buying home insurance. Seek a quality insurer and the services of a trusted advisor, and, should the unthinkable happen, you'll be glad you did! The old adage, "You can pay the price now, or you can pay it later" is never more true than here!

If you would like Sage Hill's assistance, please feel free to contact Lisa Carson, Vice President – Client Relations at carson@sagehilladvisory.com.