SPECIAL REPORT

WHY THE GUARANTEED REPLACEMENT COST PROVISION ON YOUR HOMEOWNERS POLICY IS REALLY NOT A GUARANTEE

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Inasmuch as a home is our most valuable asset, typically, we need to be sure that if it is destroyed our homeowners policy will have an adequate limit in the event of a total loss.

As you will see in this Special Report, you really can't rely on the limit you have purchased, nor can you rely on the so-called guaranteed replacement cost provision with most insurance carriers.

Most homeowners policies have some form of guaranteed replacement cost coverage.

Depending on the insurance company, this can be called:

- Limited guaranteed replacement cost coverage
- Guaranteed home replacement cost
- Extended replacement cost
- Full replacement cost coverage
- Full replacement cost protection
- Dwelling expanded replacement cost
- Increased building limits coverage

The essence of this coverage is that if the dwelling limit on your homeowners policy for reconstruction of your home is not sufficient, the insurance carrier will pay 120%, 125%, 150% or an unlimited additional amount depending on the insurance carrier used.

This sounds really good because an insured may feel that they don't have to worry about the dwelling limit on their homeowners policy because of the automatic increased replacement cost endorsement.

As we will see, this is generally not true. However, before we get to this, let's see how this system works.

1. When you apply for a homeowners policy, the insurance carrier might use a replacement cost system based upon the square footage of your home to estimate what it feels it would cost to reconstruct your home just as it stands today without consideration of building code changes that might increase the reconstruction cost. (This is the subject of another Special Report on the impact of ordinance and law coverage.)

   This system uses a computer program based upon average values in your area and is really not specific to your own home. Short of paying for a contractor to do an exact cost analysis of what it would take to rebuild your home, there is no way an insured could know what the replacement cost limit should be on his or her homeowners policy.

   Even though the insurance company indicates that they require a certain limit at a minimum on your homeowners policy based upon their computer program, they do not guarantee that limit and you are really left to your own devices to determine whether or not the limit is adequate.

   This limit should be viewed as the minimum required limit and not the limit that should be insured.

   Most insureds do not pay attention to this minimum because they are looking for the lowest premium on their homeowners policy and thinking that the market value of their home is much lower than the replacement cost, they don't go out of their way to raise the homeowners dwelling limit.

Keep in mind that the reconstruction cost or replacement cost limit on your homeowners policy has nothing to do with market value. The market value of your home, in almost all cases, will be less than the reconstruction cost.

2. Why reconstruction usually costs more than new construction:

   a. **Economy of Scale** – When a contractor has many homes under construction at once, materials can be purchased in large quantities for delivery as needed – everything from framing lumber to plumbing fixtures. If you buy a large number of bathtubs, for example, suppliers will compete for your business and offer price discounts.

      When you buy just one bathtub, and it must be a match for one that has been destroyed, it will nearly always cost much more than if it had been part of a larger purchase. This holds true for almost everything that goes into a home and this factor alone can push the cost of rebuilding thousands of dollars higher than the cost for comparable new construction.

   b. **"Top-Down" vs. "Bottom-Up**" – New construction begins at the foundation and builds upward.

      Repairing a house that is not totally destroyed often means removing the roof and rebuilding from the top down, a far more time consuming and labor-intensive procedure.

   c. **Demolition and Debris Removal** – New home construction normally begins on open ground, perhaps with some brush removal and grading and other minor site preparation.

      Rebuilding begins with a partially or totally destroyed structure occupying the building site. Parts of the structure may still be standing but unusable, requiring demolition and removal. The site may have to be extensively cleaned after an intense fire, for example. The soil may be contaminated. The foundation may have been damaged beyond repair. A lot of work is usually required before the first cement can be poured or the first nail hammered in.

d. **Use of Labor** – When a new home builder has several houses under construction, even if they are not at all in the same area, work can be scheduled for the most efficient use of carpenters, plumbers, electricians, and other workers. If one house is not ready for wiring, the electrician can probably work on another.

When only one home is being built, the same kind of efficient scheduling is rarely possible. Labor normally accounts for the largest share of homebuilding costs.

e. **Access to the Worksite** – When new houses are under construction, there is usually no landscaping which allows for easy access to the site. Materials can be driven directly up to any side of each structure as needed.

When a house is being rebuilt among existing homes, there are trees, shrubs, lawns, flowerbeds, fences and other obstructions limiting access. Materials often have to be off-loaded further away and hand carried to where they are needed. This factor is compounded if the building site is on sloping ground. The impact on labor costs can be significant.

f. **Special Features and Unusual Materials** – Older homes and homes that have been extensively remodeled often have customized features or include materials not commonly found in homes being built today. These features and materials can be very expensive, if not impossible, to duplicate. Examples include slate or tile roofs, lath and plaster walls, carved ceilings, wainscoting, solid (instead of hollow core) doors, custom ironwork, ornamented fireplaces, exposed beam ceilings, stained glass or other leaded windows, curved staircases, slate or tile floors, and other items.

g. **Building Code Changes** – Most older homes, and many newer homes, were built during times when building codes were less strict than they are today.

If you are rebuilding or restoring your home, you may need to meet the newer and more demanding building codes. Even undamaged parts of the structure may have to be rewired or re-plumbed to meet current codes. Building codes may also require you to replace windows with safety glass or replace roofs with fire-retardant materials. Building code changes can add thousands of dollars to the cost of restoring a damaged home.

h. **Construction Costs Rise After Natural Disasters** – In the wake of a disaster affecting a wide area – hurricanes, wildfires, etc., -- the costs of building materials and contractor fees nearly always rise sharply in response to the sudden surge in demand. Even without deliberate profiteering this would normally be true because when local supplies are quickly exhausted, materials have to be brought in on an emergency basis, often from mills or factories at great distance. This may require more expensive modes of transportation and a lot of overtime pay. When many homes have to be repaired or rebuilt at the same time, the cost for each will be higher than normal, sometimes much higher.

i. Undamaged Parts of the Home and the Contents Must be Protected – Once the fire is out or the windstorm has abated, all parts of the property that are not damaged must be protected from further damage or looting. This can involve covering a damaged roof, or missing window glass, and covering holes in the walls with plastic sheeting, for example, and, as soon as possible, surviving personal property items must be removed and placed in temporary storage for safekeeping.

The bottom line is that even if your home is brand new if it is destroyed <u>it is going to cost a great deal more to rebuild</u> it because of these factors and, <u>therefore, you cannot depend on what an insurance company determines is a minimum limit</u>.

We have seen case after case <u>where the limit provided by the insurance carrier is not sufficient to reconstruct that home</u>.

3. As we said, almost all insurance carriers offer an endorsement or a built-in coverage clause <u>that provides for an automatic increase in the dwelling limit on the policy</u> if it turns out after a total loss that the limit of insurance on the dwelling was not sufficient.

The lowest we have seen is 120% and the best is an unlimited endorsement that is provided by a number of carriers. This indicates that they will do whatever it takes to rebuild your home, or does it?

4. When the insurance company establishes a minimum limit for you to insure or even guarantees a limit via the automatic percentage increase endorsement, it is not really the limit to replace the home in accordance with current building codes. It is the limit required to replace your home as it was originally built under the building codes at the time.

   (Note: If you have an older home, you will not be able to build it as it originally was built and you will need coverage known as either ordinance or law coverage or building codes coverage where the insurance company will pay an additional amount to cover the difference in building codes. This is important but is the subject of another Special Report. What we are discussing here is reconstructing your home as it was just before the loss.)

5. Let's now look at the various guaranteed replacement cost endorsements that the following insurance carriers provide that purport to provide higher limits automatically: (Send us your homeowners policy and we will analyze this clause for you and add it to our list.)

   A. AAA
   B. Grange
   C. Citizens
   D. Frankenmuth
   E. Auto-Owners
   F. Encompass
   G. Allstate
   H. Fireman's Fund
   I. Ace
   J. Chubb
   K. Chartis

A. AAA FORM 6500-42132-MI-77 (7/22/07)

This provision provides up to 120% of the dwelling coverage limit if the amount actually and necessarily spent to repair or replace covered losses to building structures exceeds the applicable limit.

➢ **What is required to receive this additional coverage?**

1. You must maintain coverage equal to 100% of the replacement cost of the dwelling.

2. You must notify AAA within 90 days of the start of any additions or changes, which either individually or collectively, increases the value of your building structure by $5,000 or more.

3. If you fail to notify AAA within 90 days the payment of loss will not exceed the limit of liability stated on the policy.

- **Comments on this language:**

1. This requirement does not indicate who determines 100% replacement cost. It should state "as determined by AAA." Taken literally, if you did not maintain coverage exactly equal to the replacement cost, you are already in violation and there is no reason to go any further.

2. We all know what an "addition" is, but what "changes" are they talking about?

   Does this mean paint color, new windows, new roof, new landscaping, etc., which undoubtedly will increase the market value of the home but not the reconstruction cost?

   Does the reference to "individually" or "collectively" apply from when you built or bought your home, or is it from the date you placed your coverage with AAA, or is it the last time you renewed your policy?

   In this same paragraph, they use the words "increase the value" by more than $5,000. The word "value" suggests market value and it is not a defined term in the policy.

   So, in Paragraph 1 they talk about "replacement cost" and in Paragraph 2 they use "value." What really is the test?

   Either way, individually or collectively, what we do over the years to our homes certainly will exceed $5,000 in replacement cost or market value.

- **Conclusion:** This clause is basically worthless because of its many ambiguities and the likelihood that almost all homeowners will be in violation of the requirement of this coverage.

What you are left with is what you started with; that is, a dwelling replacement cost limit determined by AAA but that is not guaranteed by them and, most likely, is not adequate to replace your home.

B. GRANGE 1K1046 (7-99) -- DWELLING EXPANDED REPLACEMENT COST COVERAGE PROVISION.

Grange agrees to settle covered losses to the dwelling at replacement cost up to a maximum of 150% of the specific policy limit.

➢ **What is required to receive this additional coverage?**

1. Adjust the limit of liability for the dwelling to equal 100% of the replacement cost of the dwelling and increases caused by inflation.

2. Notify Grange within sixty (60) days of the start of any alterations or additions that would increase the "value" of your dwelling.

3. If you fail to comply with these provisions, the coverage extension will not apply.

➢ **Comments on this language:**

1. You are required to adjust the limit to 100% of replacement cost.

   Does this mean you must increase this daily or at the policy anniversary date? Read, literally, it requires that you do this daily.

   Who determines this? It doesn't say the insurance company will do this, so this means the insured must do it.

   How is replacement cost defined? Is it a union contractor or non-union contractor, for example?

   You must also adjust the limit for increases caused by inflation.

   Does this mean daily, monthly, or annually?

   What is the inflation standard? Is it Ann Arbor, Detroit, etc.?

2. It is clear that you must notify Grange within sixty (60) days of the start of any alterations or additions. We know what an addition means, but what is an alteration?

   Is it new and improved windows?

   Is it new carpeting?

   Is it new aluminum siding?

   Note there is no dollar amount.

   Note it says "value," which is a market value standard.

   So, $1 in increased market value caused by better windows would kick out the 150% provision leaving you with the limit that the insurance company provided initially, which the insurance company will not guarantee.

- **Conclusion:** This form is so vague, ambiguous, and unrealistic that it is basically worthless.

C. CITIZENS FORM 231-5888-09-09

Citizens will provide full replacement cost for the dwelling regardless of the limits shown.

- **What is required to receive this additional coverage?**

1. Report to Citizens within sixty (60) days any improvements to the dwelling exceeding $5,000.

2. You must keep the dwelling limit at 100% of replacement cost.

- **Comments on this language:**

1. This says "report within sixty (60) days," but does not say "60 days from when."

Is it 60 days from the date the improvements started or is it the date finished?

Or, is it 60 days to report any improvements in prior years?

If so, is it prior years with Citizens or years subsequent to when the dwelling was built?

What does the word "improvement" mean? Is it additions, or is it improvements to the structure such as painting, a replacement roof, or replacement windows?

Is it landscaping improvements that are unrelated to the dwelling?

2. The second paragraph says you must keep the dwelling insured at 100% of replacement cost, but does not say who determines this.

   If it means the insured, what is the purpose of the automatic increase clause because for it to apply you must not have insured at 100%.

   Does this mean as of the inception date or every day of the policy?

   What is the standard to be used? Is it replacement with a union contractor, non-union contractor, etc.?

- **Conclusion:** This form is basically worthless because it is vague, ambiguous, and unrealistic.

D. FRANKENMUTH LIMITED GUARANTEED REPLACEMENT COST COVERAGE

If there is a loss to the dwelling that exceeds the dwelling limit shown on the policy Frankenmuth agrees to provide an additional amount "as displayed under description of additional coverages on the Declarations." This typically would be 125% or 150% increase.

- **What is required to receive this additional coverage?**

You must notify the insurance company within ninety (90) days of the completion of any alterations to the dwelling, which increase the replacement cost of the dwelling by more than $5,000.

➢ **Comments on this language:**

1. The word “alterations” is not defined. For example, did you change the banister on your stairway with something different? Did you add a bathroom in your basement?

2. There is no indication as to what policy period applies.

   For example, if you were with Frankenmuth for 5 years and make an alteration within the first year and forgot to inform the insurance carrier and a loss occurs in the fifth year, does this negate this coverage even though Frankenmuth may have automatically increased your limit each year because of inflation or other factors?

➢ **Conclusion:** This form is basically worthless because it is vague, ambiguous, and unrealistic.

E. AUTO-OWNERS GUARANTEED HOME REPLACEMENT COST, #57160

Under this form the dwelling limit is increased to equal the current replacement cost of your dwelling and shall apply to the cost of repairing or replacing your dwelling at the residence premises.

➢ **What is required to receive this additional coverage?**

You must notify the insurance company of any additions, alterations or improvements to your dwelling which individually or cumulatively increased your dwelling replacement cost by $10,000 or more and pay an additional premium for the increase.

➢ **Comments on this language:**

1. This applies retroactive but it does not say to when:

   - Is it from when you first purchased a policy from Auto-Owners?
   - Is it from when you purchased your home?

2. What is an "alteration" or "improvement," which increases your dwelling replacement cost?

    - Is it new windows, a new furnace, a new roof, a swimming policy, etc.?
    - It is very likely that we all make small change that over the years will have increased the replacement cost of our dwelling.
    - Auto-Owners has indicated that it applies this endorsement <u>over the life of the time Auto-Owners had the policy in force</u>.
    - In a recent Auto-Owners case, a 17-year policyholder had a $300,000 coverage gap because an insured <u>had not reported the fact that cumulative improvements and alterations were in excess of $10,000</u>.

- ➢ **<u>Conclusion</u>:** This form is basically <u>worthless</u>. The longer you are with this carrier, the more likely it is that you will not receive the benefit of this endorsement.

F. <u>ENCOMPASS, G1-72263-A, 01-07</u>

This policy has a built-in provision that pays whatever it takes to repair or replace the residence premises up to the aggregate limit which, with Encompass, <u>is a limit that combines the dwelling, other structures, and contents</u>. This is one of very few insurance carriers that have this blanket limit.

Then, if the residence value is not sufficient, Encompass will adjust it to equal current replacement cost. <u>There is no percentage limitation</u>.

- ➢ **<u>What is required to receive this additional coverage?</u>**

1. Insure the dwelling for full replacement cost as <u>determined by Encompass</u>.

2. Notify Encompass within ninety (90) days of the <u>start</u> of any <u>alterations</u> to the real property, which increase the <u>replacement cost</u> of the real property by 5% or more.

- ➢ **<u>Comments on this language:</u>**

This policy is very well written in that it has <u>clarity</u> regarding the dwelling value. Here is why:

1. Even without the replacement cost extension which, as we said, has no percentage limitation, which is a good thing, Encompass provides an additional safety net by having a blanket limit for the dwelling, other structures and personal property.

   This limit is determined by a dwelling cost estimating system and the value is multiplied by 2. This is the aggregate limit referred to.

   In the unlikely event this is not sufficient, Encompass will increase this limit to cover the difference between the actual replacement cost as determined after the loss and the original limit on the policy.

2. We also like the reporting provision because it does not use the words "modifications, improvements," etc. It uses the word "alteration" which would suggest a significant change. It also has a more generous ninety (90)-day provision from the start of the alterations.

   They also have a generous provision that requires that the alterations be reported if they increase the replacement cost of the real property by 5% or more. So:

Original Replacement Cost Limit on the Dwelling		5% Increase
$1,000,000	=	$50,000 or more
$ 500,000	=	$25,000 or more
$ 250,000	=	$12,500 or more

- **Conclusion:** We like the blanket limit, the clarity of the language, the "unlimited" provision, the 90 days, and the high improvements threshold of 5%.

G. ALLSTATE: BUILDING STRUCTURE REIMBURSEMENT EXTENDED LIMITS ENDORSEMENT #AP357

This endorsement will pay up to 120% of the limit of liability applicable to the dwelling structure.

- **What is required to receive this additional coverage?**

1. Insure your dwelling and attached structures and detached building structures to 100% of replacement cost as determined by Allstate and based on the accuracy of information furnished by the insured, or

   The Allstate inspection of your residence premises, and

2. You have accepted an annual limit adjustment and to pay the additional premium, and

3. You notify Allstate within sixty (60) days of the start of any modifications that increase the aggregate value of your dwelling, attached structures and detached building structures by $5,000 or more.

- **Comments on this language:**

1. The language of the first paragraph is clear that 100% of replacement cost will be determined by Allstate. At the same time, they do not guarantee the limit if it is not sufficient, in which case the 120% extension endorsement fails.

2. You must notify Allstate within sixty (60) days of the start of any modifications; however, this is not defined and could mean a new roof, energy-efficient windows, a swimming pool, etc., and could be minor in nature.

   It goes on to say that if the modifications (they don't say to what) increase the value of the dwelling and structures, then the extension will not apply if the aggregate value (note, it does not say "replacement cost") is in the amount of $5,000 or more.

   So, here they utilize, apparently, market value as the standard.

   This standard would appear to apply during the life of the policy.

- **Conclusion:** This form cannot be relied upon to provide any protection if the policy limit is not adequate in the event of a major loss. If you can't rely on it, the form is worthless.

H. FIREMAN'S FUND: FULL REPLACEMENT COST COVERAGE, # 5250, 11-02

Fireman's Fund agrees to pay the amount needed to replace a dwelling after an occurrence even if the limit shown on the declarations is less than the cost of repairs (as long as the dwelling is not being newly constructed or is vacant or has been unoccupied for more than thirty (30) consecutive days while undergoing renovation but even, in these instances, they will pay up to 125% of the limit.)

➢ **What is required to receive this additional coverage?**

1. Insure the dwelling at 100% of its replacement cost as determined by Fireman's Fund.

2. Notify the insurance company prior to the start of a renovation that will cause your dwelling to be vacant or not occupied (for more than 30 days).
3. "Promptly notify us of a renovation (defined) that increases the replacement cost of a dwelling or other structure by $25,000 or more."

4. If you fail to report renovations prior to an occurrence, you will have no coverage for the replacement cost of these renovations.

➢ **Comments on this language:**

1. We like this language better than many other policies because it at least defines "renovation," although this is quite expansive and includes: updating, repairs, remodeling, and restoration.

2. It also includes increased costs due to enforcement of ordinances that increase the cost of reconstruction.

3. We do not like the undefined word, "promptly."

4. We like the higher threshold limit of $25,000.

➢ **Conclusion**: We like this form because of the higher threshold of $25,000 and its defined terms except for the word "promptly."

I. ACE: FULL REPLACEMENT COST PROTECTION, ACE-0612

Ace will pay the current replacement cost of the dwelling or other structure after a covered loss even if this is greater than the policy limit.

➢ **What is required to receive this additional coverage?**

1. "Insure an amount agreed to by you and Ace."

2. The automatic increase does not apply if you construct additions or make renovations that are equal to 10% of the dwelling limit or $500,000, whichever is less.

Example:	Original Replacement Cost Limit on Policy	Automatic Increase Fails If Renovations are Equal to or More Than
	$1,000,000	$100,000
	$ 500,000	$ 50,000
	$ 250,000	$ 25,000

3. There is no reporting requirement but, presumably, the policy can be endorsed to provide higher limits.

➢ **Comments on this language:**

In this form, you are out of luck if you construct an addition or make a renovation (undefined) that is higher than the threshold amount indicated. This applies during the policy period when the loss occurs.

➢ **Conclusion:** We like this language because of the higher renovation threshold, but do not like the fact that the word, "renovation" is not defined. We like the fact that this provision is limited to the policy period.

J. CHUBB DELUXE HOUSE COVERAGE, 10/14/13, EXTENDED REPLACEMENT COST

Chubb will pay the reconstruction cost even if greater than the policy amount and even if building ordinances have changed increasing the reconstruction costs.

- **<u>What is required to receive this additional coverage?</u>**

1. You insure the amount established by Chubb and agree to it.

2. If at any time during any policy period you construct <u>additions</u>, <u>alterations</u> or <u>renovations</u> (not defined) to your house or any permanent structure which exceeds the lesser of 10% of the amount of coverage for the house or $500,000, the automatic increase <u>will not apply</u> and you will be subject to the "<u>conditional replacement cost</u>" clause until construction is complete.

   If coverage reverts to <u>conditional replacement cost,</u> you will be paid the <u>greater of</u>:

   a. Reconstruction cost <u>less depreciation</u> (not defined), or

   b. The proportion of the covered loss to your house or other permanent structure determined by dividing the amount of coverage for your house by 80% of the amount to rebuild your entire house.

      Example of "b": You insured $1,000,000.

      You should have insured $1,500,000 x 80% = $1,200,000.

      If you did insure $1,000,000, and you should have insured $1,200,000; then you will collect .833 of $1,500,000 which is $1,249,500 or .833 of any partial loss.

      Note: If conditional replacement cost applies, <u>there is no reporting provision to make this go away</u> during additions, alterations, or renovations. Conditional Replacement Cost remains the payment basis until construction is complete.

      You must increase your coverage in an effort to avoid being underinsured.

- **Comments on this language:**

1. On the one hand, this form is quite generous in that it provides the lesser of 10% of the amount of coverage on the house or $500,000. A $1,000,000 house would have to undergo $100,000 in additions, alterations, or renovations before this clause would apply.

2. On the other hand, it appears to be cumulative by indicating “any policy period.”

   So, if you do exceed the 10% clause throughout the years you have been with Chubb in a long-term uncompleted alteration or renovation program, the automatic conditional replacement cost coverage applies which, in essence, applies a depreciation penalty which is undefined, or a coinsurance clause.

3. The policy also has no definition of “alterations or renovations.” (The word, “additions,” really doesn’t require a definition.)

   Looking at Webster’s II Dictionary:

   Alterations: “The process of making something different; modify.”

   Renovations: “To make new; to restore to a previous condition as by remodeling; to give new vigor; to revive.”

4. As we said, the problem is that the conditional replacement cost provision applies whenever you exceed 10% of the dwelling value for additions, alterations or renovations.

   “Additions” are easy to pin down, and if you add square footage to your home it needs to be reported if it exceeds the 10% threshold described above.

   However, looking at “alterations,” does this mean new and improved windows, new wood floors, upgraded cabinets, etc.?

   “Renovations” suggest repainting, sanding of floors, a new roof, new furnace, etc.

5. Here is the problem. On a long-term basis you could do alterations and renovations (whatever this means) that exceed the threshold which invokes the conditional replacement cost clause which is not a good thing.

6. One good thing is that the provision <u>applies only until construction is complete</u> even if you have not reported it to the insurance company. The question is when are alterations and renovations completed, or are they ever completed?

7. There is a clause that is entitled "Your Duty" which indicates that <u>you must notify</u> your agent or broker at the <u>beginning of</u>, <u>throughout</u>, and at the <u>completion of construction</u> so that the amount of coverage can be adjusted.

   Does "throughout" mean, daily?

   This "Your Duty" provision seems to remove the 10% threshold provision by imposing a duty to report at the <u>beginning</u>, <u>throughout</u>, and at the <u>completion</u> of construction.

- **<u>Conclusion</u>:** We would like to see the threshold apply for the current policy year only.

  We would like to see definitions for alteration and renovation.

  We would like to see the "Your Duty" paragraph removed.

K. <u>CHARTIS PCHO (09/06) GUARANTEED REBUILDING COST COVERAGE</u>

This provision is indicated as applying to the policy <u>if there is an indication on the Declarations page</u>. If so, it will pay the reconstruction cost of your house or other permanent structures even if the amount is greater than the policy limit.

- **<u>What is required for the clause to apply?</u>**

If you are newly constructing your house or other permanent structure, constructing additions, or undergoing renovations:

- equal to or in excess of the lesser of 10% of the house coverage limit or $500,000, and/or

- it results in your moving out of the house for any period of time,

the payment basis will be reconstruction cost less depreciation unless Chartis gives its prior consent.

➢ **Comments on this language:**

There are two key elements here that will remove the guaranteed rebuilding cost limit.

1. The first is 10% or less of the house coverage limit.

House Limit on the Policy	Threshold
$1,000,000	$100,000
$ 500,000	$ 50,000
$ 250,000	$ 25,000

   If you do additions or renovations in excess of the threshold, the guarantee clause does not apply.

2. The second element is:

   ". . . or it results in your moving out of the house for any period of time." Many of us do short-term renovations of low cost that require us to stay at a hotel.

   One example is re-sanding and refinishing wood floors and, because of noise, dust, and bumps, we move out for a one-night stay in a hotel. You could argue that "moving out" means moving all of your furniture out as well, but it doesn't say this.

   If so, this kicks out the coverage and the penalty is quite severe. You receive a maximum of replacement cost less depreciation, and this could be a major reduction in coverage.

- **Conclusion:** Primarily because of the provision that removes full replacement cost if you move out of your house for any period of time, this clause is of value only to insureds that will not have occasion to move out of their home during a renovation.

HERE IS WHAT IS IMPORTANT

1. Do not rely on the replacement cost estimate provided by your insurance carrier or agent.

2. Understand that there are many factors that will significantly increase reconstruction cost way above purchase price, market value, or recent cost new.

3. What is helpful is a detailed construction cost on-site appraisal done by many insurance carriers and almost always by Encompass, Fireman's Fund, Chubb, and Chartis.

   The reason for this is that they are specific to your home and are based on detailed factors that are different for living areas, basements, garages, etc.

4. Report to your agent or to the insurance carrier, in writing, before you do anything to your home that could negate the so-called "guaranteed replacement cost" provision of your home, regardless of the time and dollar amount threshold indicated in the policy and regardless of whether you move out of your house or not.

5. In your insurance placement considerations, favor insurance carriers that have clarity of language regarding how you will be paid in the event of a major loss.

   Only the words of the insurance policy matter at the time of loss. Statements by an insurance agent such as:

   > "We have never had a problem with this."
   >
   > "This insurance company would never do that"!

"The Claims Department says they don't apply this clause."

. . . are worthless.

6. Be aware of the impact of building code changes that also increase the replacement cost of your home. Some insurance carriers include this in the replacement cost extension endorsement and some require a separate endorsement.

7. This discussion is general in nature and is meant to alert you to these issues. Our emphasis has been on renovations to existing homes as opposed to new construction.

   The same insurance carrier could use different forms in different states, so look at the specific form that you, as an insured, have purchased.