

Insurance Times: Behind the rising cost of homeowners insurance
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The following is an edited version of a broader essay by Hartwig on the costs behind both auto and homeowners insurance. For more information, visit the Insurance Information Institute's web site at www.iii.org.

Many policyholders have seen the price they pay for homeowners insurance increase over the past year. In 2002, the average cost of insuring cars is expected to increase by 8 percent. In 2003, the cost of insuring both cars and homes is expected to rise by 9 percent. The increases may have taken some policyholders by surprise given that they came after several years of relatively flat to decreasing prices. While these increases translate into a relatively modest \$40 for the average homeowner, many policyholders are understandably concerned about higher insurance costs and have been left wondering why their premium rose and what they can do to keep costs down in the future. This article will address the major cost drivers in auto and homeowners insurance today and offer customers money saving tips that can help them offset these costs.

Why is the Cost Increasing?

Homeowners know that the price they pay for insurance depends on factors like type of construction, age of the home and the quality of local fire protection services. Nevertheless, it is the extraordinary number of catastrophes, the high cost of home repairs, the aging of the U.S. housing stock and the emergence of mold claims (yes, I said mold) that are pushing homeowners insurance rates upward. Mold claims—which were virtually unheard of just a few years ago—cost homeowners insurers more than \$1 billion dollars last year, approximately five times the cost in 2000.

During the 1990s, the frequency and severity of catastrophes began to increase dramatically. Over the past 12 years, insurers paid out more than \$100 billion in catastrophe-related losses—about \$700 million per month—many times more than in previous decades. (Excludes the impact of the September 11, 2001 terrorist attacks.)

Catastrophes include well-known events such as Hurricane Andrew and the Northridge earthquake, but also hundreds of smaller disasters associated with tropical storms, tornados, wildfires, hail, ice and snow. (Insurers define a catastrophe as any single event that produces insured losses of \$25 million or more.)

Homeowners insurance rates in many parts of the country continue to rise because of the extraordinary costs associated with paying these claims. In fact, virtually every part of the country is now at risk for billion dollar disasters.

In dollar terms the numbers are sobering. Homeowners insurers over the past decade paid out \$1.18 in losses and expenses for every \$1 they earned in premiums. In 2001 alone, homeowners insurers paid out \$8.9 billion more in losses and expenses than they received in premiums, the second worst year on record (1992, the year of Hurricane Andrew, produced losses of \$11.5 billion). Losses in the homeowners insurance line over the past three years (2000 through 2002) are estimated at \$19 billion, rivaling the \$20.3 billion in insured property losses from the September 11 terrorist attack.

Every homeowner knows that home repairs don't come cheap and that home repair and rebuilding costs continue to rise. This phenomenon is a major driver of behind rising homeowners insurance rates today.

Mold has recently emerged as the dominant cost driver in some states. Mold is certainly not new—it's been around for hundreds of millions of years—but the sharp rise in mold claims is definitely a 21st -century phenomenon. Multi-million dollar jury awards, sensationalized reporting in the media and profiteering by some individuals have led to an explosion in mold claims and costs.

In Texas, for example, mold claims in 2001 cost insurers more than \$850 million compared to virtually nothing just a few years earlier. The number of mold claims in the state increased by 1,300% between the first quarter of 2000 and the fourth quarter of 2001 while insurer payouts through the third quarter of last year increased 1,200%. Runaway costs associated with mold claims are having an adverse affect on the availability and affordability of homeowners insurance in Texas, and increasingly in other states. California, for example, has seen a large spike in water damage claims—which often give rise to mold claims. Water claims accounted for 32% of all claims in 2001, up from 24% in 1997. Over the same period, the average cost of these claims surged by 86% from, \$2,537 to \$4,730.

Saving Money

Although the cost of insuring homes is rising, there are many ways that policyholders can hold down and even lower what they pay for insurance. They should take advantage of every discount for which they are eligible. Insurance companies offer many discounts, including discounts to loyal customers and to customers who insure multiple cars or their home and vehicles with them. Homeowners can save money if their residence is equipped with smoke detectors and if they have installed certain home security devices. Raising deductibles is another way to save money.

AVERAGE EXPENDITURES ON HOMEOWNERS INSURANCE

1994	\$420
1995	\$418
1996	\$440
1997	\$455
1998	\$481
1999	\$488*
2000	\$500*
2001	\$512*
2002	\$553*
2003	\$603*

* III estimates

Sources: NAIC, Insurance Information Institute