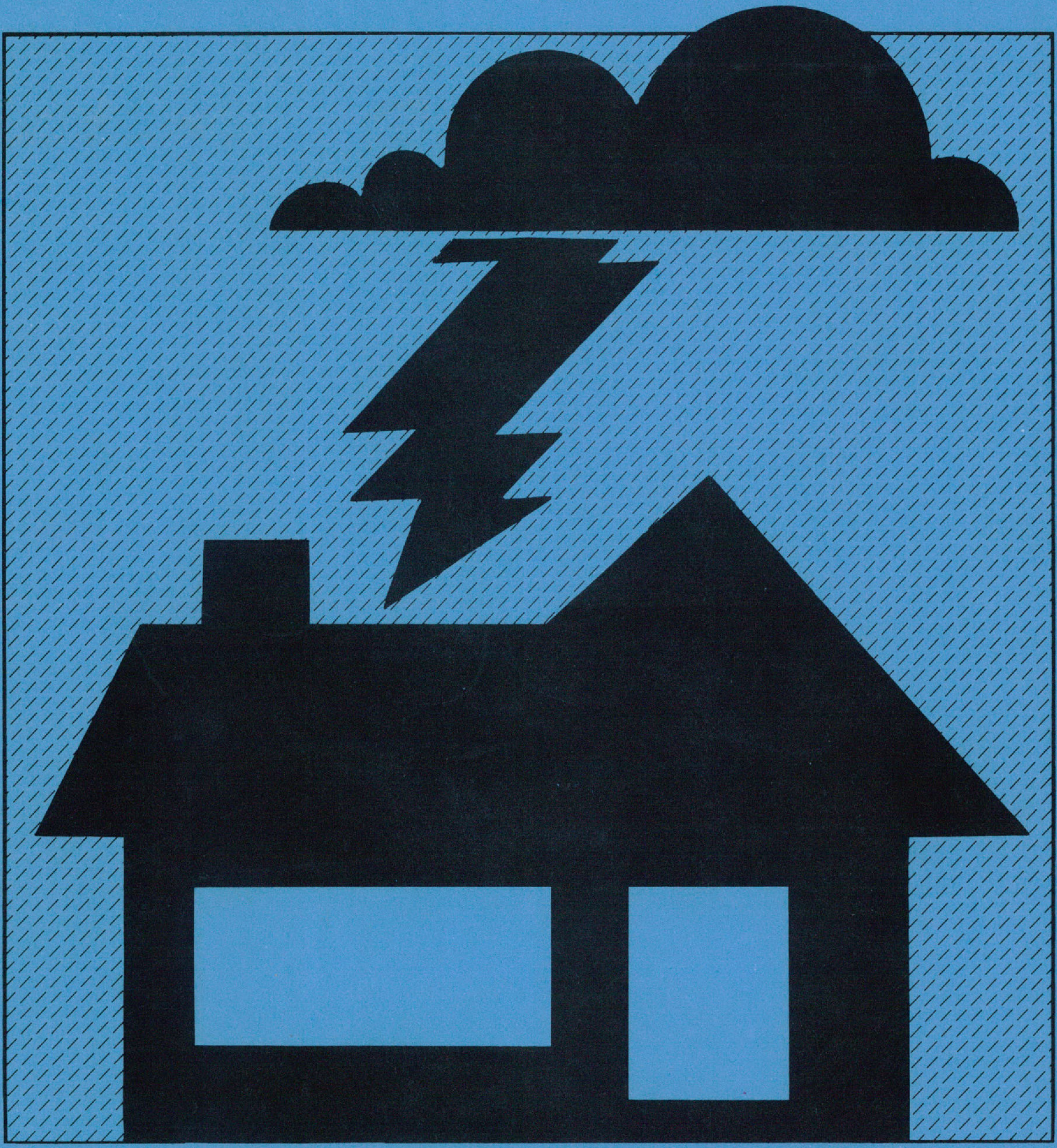
REAL ESTATE CENTER
Technical Report

Understanding Texas Homeowners Insurance



UNDERSTANDING TEXAS HOMEOWNERS INSURANCE

Judon Fambrough
Senior Lecturer

Real Estate Center
Texas A&M University
College Station, Texas 77843-2115

687-750-587

June 1987

REAL ESTATE CENTER

DIRECTOR

Dr. Richard L. Floyd

The Real Estate Center was created in 1971 by the Texas Legislature and placed at Texas A&M University.

The Center conducts a comprehensive program of research and education to meet the needs of many audiences, including the real estate industry, instructors, researchers and the general public.

A catalog describing hundreds of publications, audiovisuals and computer programs is free for the asking. Write the Real Estate Center, Texas A&M University, College Station, Texas 77843-2115 or telephone 409-845-2031.

ADVISORY COMMITTEE

Solutions Through Research

CONTENTS

Most people have a homeowners insurance policy, but few understand its coverage, conditions and exclusions. Often, it is only after a casualty occurs that the homeowner learns about specific coverage. To avoid such a situation and because insurance costs are rising, homeowners may wish to re-examine their policies. Because the insurance contract--the policy--is complex, the layperson may need some assistance in interpreting and understanding its provisions. This report provides such assistance.

To understand a policy's provisions, the homeowner needs some knowledge of the general principles of property insurance.

First, insurance may be purchased to cover two basic risks: casualty and liability. A casualty risk (or loss) occurs to the property from a sudden, unexpected or unusual event such as fire, lightning, windstorm or theft. A liability risk (or loss), on the other hand, is an injury occurring to a person or damage to the property of another that the property owner is legally obligated to protect. An insurance policy may be solely a casualty policy or a liability policy or the two combined. This report deals only with casualty (or property) insurance.

Second, to obtain either a casualty or liability insurance policy, the purchaser must have an insurable interest in the property. The purchaser has an insurable interest if he or she would suffer financial loss in case the property was lost or damaged or if he or she is legally liable for an injury to a third party or to the property of another.

Insurable interest is quite evident when insured property is leased to a third party. Here the owner's (or lessor's) insurance policy limits its coverage solely to the owner's property. None is extended to the renter's (or lessee's) property because the owner has no insurable interest in it.

Third, in Texas, all homeowner's policies are promulgated by the State Board of Insurance. There can be no difference between policies issued by different carriers; **they are all alike.** Even the available policy endorsements are alike.

Fourth, the maximum rates the carrier can charge for issuing a policy are set by the State Board of Insurance. Within the prescribed rate schedules, **the premiums will vary depending on the amount of insurance purchased, the level of deductibles chosen and the types of endorsements added to the policy.**

Fifth, because Texas homeowners' policies are alike, the purchaser must individualize the policy by choosing and purchasing the desired endorsements from the ones offered by the carrier.

Casualty insurance policies are issued in one of two forms: **specified-peril** or **all-risk.** Sometimes these are referred to respectively as limited or basic form and broad form policies.

A specified-peril (also known as named-peril) policy lists or designates the types of perils (causes of loss) **insured** to the exclusion of all others. With this type of policy, the purchaser must pay particular attention to the perils insured to determine if the necessary protection is provided. As a general rule, specified-peril policies provide less coverage at a lower premium than do all-risk policies.

For example, suppose a property owner wishes to purchase fire protection only. This would be a specified-peril policy. However, endorsements for other types of specified perils may be purchased and attached to the policy from time to time. The additional endorsements are sometimes referred to as **additional extended coverage.** In addition to windstorm and hail, extended coverage may be available for such perils as explosions, smoke, aircraft, accidental discharge of water or steam, theft, vandalism and malicious mischief to name a few. In Texas, additional extended coverage can be added only to a specified-peril policy.

The all-risk (sometimes called the multiperil) policy lists or describes the types of perils **excluded**--not insured--to the inclusion of all others. Here the purchaser must pay close attention to perils excluded to see if adequate protection is provided.

The actual insurance contract consists generally of six basic parts: declarations, endorsements, perils insured against, exclusions, conditions and recovery. The policy does not package the parts neatly in such individual sections, however.

DECLARATIONS

The declarations, set forth on the front page of the policy, describe the types of property insured, the parties covered (the insured), the issuing company (the insurer), the limits of liability for the different types of property insured, the policy period, the deductibles, the premium costs and the types of endorsements.

PROPERTY INSURED

Three types of property may be insured: the dwelling, unscheduled personal property and scheduled personal property. The limit of liability (maximum amount of dollar coverage) for each property type and the respective deductibles are specified on the declaration page.

Dwelling (Coverage A)

By the policy's definition, the dwelling is the residence described on the declaration page, occupied by the insured and used principally for dwelling purposes. The dwelling does not include property rented to others or used for commercial purposes. Wall-to-wall carpeting attached to the building is classified as part of the dwelling.

A portion of the coverage extended to the dwelling (usually 10 percent) may be applied to detached structures on the premises. The detached structures must be used in connection with the dwelling and for non-commercial purposes. In Texas, this coverage is called **additional insurance.** For example, a homeowner has a $100,000 policy for the dwelling with a 10 percent coverage as **additional insurance** for detachments. In the event of a total loss of both the dwelling and the detachments, the homeowner could recover a total of $110,000 less the deductible.

A portion of the coverage extended to the dwelling (usually 5 percent) also may be applied to the loss of trees, shrubs, plants and lawns on the premises. The loss, however, must have been caused by a peril specified in the policy. Generally losses caused by fire, lightning, explosion, aircraft, vehicles, vandalism, riots and theft are insured. Losses caused by wind are not. This coverage excludes trees, shrubs, plants and lawns grown for commercial purposes and losses caused by a vehicle owned or operated by an occupant of the dwelling. Any loss in excess of $250 for any tree, shrub or plant, including the cost of its removal, is excluded from the policy. No deductible applies to this coverage. Otherwise, the limitation on the coverage might be more than offset by the deductible.

Unscheduled Personal Property (Coverage B)

By the policy's broad definition, unscheduled personal property is the non-commercial personal property owned, worn or used by the insured, including family members of the same household. The insured may opt for the unscheduled personal property to include the personal property of others, except for that of roomers and tenants, while their property is on the premises of the described dwelling. Window or wall air-conditioning units are classified as personal property and not part of the dwelling.

Generally, personal property is the property of the insured consisting neither of land nor structures affixed to the land. This includes things such as wearing apparel, furniture, tools, appliances, books and household items such as televisions, stereo systems and radios.

Unscheduled personal property receives broad coverage. All the insured's personal property meeting the policy's definition and not explicitly excluded is automatically insured up to the extent of the policy's limit of liability. There is no itemized list.

The policy includes also **Off-Premises Coverage** as additional insurance for the unscheduled personal property owned, worn or used by the insured or members of the insured's family of the same household anywhere in the world. The **Off-Premises Coverage** is limited to $1,000 or 10 percent of the policy's limit of liability for unscheduled personal property, whichever is greater, less the deductible. The **Off-Premises Coverage** is limited to the personal property of the insured and members of the insured's family of the same household. No **Off-Premises Coverage** is extended to the property of others.

However, it is important to review the property **not considered** unscheduled personal property by the policy such as:

- Animals and birds

- Aircraft and highway motor vehicles

- Outboard motors and watercraft not located on the premises

- Money or coin collections in excess of $100 per loss

- Documents such as notes, manuscripts, securities, gold or silver bullion, stamps, deeds, letters of credit, passports and tickets in excess of $500 per loss

- Gems, watches, jewelry or furs in excess of $500 per loss by certain specified perils

- Personal property pertaining to a ranch, farm, business, trade, profession or occupation in excess of $2,500 per loss while on the premises; all coverage excluded while off the premises

- Scheduled personal property

A specific endorsement, number 339, is available for insuring jewelry, furs and watches for more than $500 per loss. The endorsement raises the limit of the liability for jewelry, furs and watches to $5,000 for any one loss.

Scheduled Personal Property (Coverage C)

The purchase of a homeowners insurance policy grants automatic protection to the insured's personal property under Coverage B (discussed on p. 3). Each item of the insured's personal property is not listed in the policy along with its insured value.

However, the insured may wish to purchase individual coverage for certain unique or expensive articles. To do so under the homeowners policy, the insured must invoke, with the agent's assistance, Coverage C of the policy.

Coverage C, the scheduled personal property section, lists the articles receiving individual coverage along with each item's insured value. In the event of a loss, the recovery is the article's insured value less the deductible and any depreciation.

There is no automatic protection extended under Coverage C with the purchase of policy. In fact, the scheduled personal property portion of a homeowners policy is rarely used. A more effective and efficient means of securing protection for unique or expensive items of personal property is available under an all-risk Personal Article Floater Policy.

PARTIES INSURED

The policy covers only the person or persons declared as the named insured. As a general rule, the named individuals must have an insurable interest in the property, both when the policy is issued and when the loss occurs, to recover for a loss.

As noted earlier, the insured party for purposes of the dwelling is the named insured only. However, the insured parties for purposes of unscheduled personal property include:

- The named insured

- The members of the insured's family of the same household while on the premises

- At the option of the insured, the personal property of others while on the premises except for the property of roomers and renters

If a mortgage exists against the real estate, the mortgagee (lender) becomes an insured party. The lienholder is noted on the declaration page. A standard mortgage clause is attached to the policy to cover the mortgagee's interest. This clause provides separate and distinct agreements between the insurer and the mortgagee. The contract applies only to items of real property (not personal property) insured by the policy. In the event of a casualty loss, the payment is made jointly to the insured and the mortgagee. The two must decide how to divide the proceeds.

The standard mortgage clause also gives the mortgagee unique provisions but only to the extent of the mortgagee's security interest in the property. For instance, any negligent act of the owner shall not invalidate the policy as to the lender's interest. A foreclosure by the lender shall not terminate the policy. Any change of ownership or increase of hazard shall not cancel the policy as to the mortgagee's interest as long as the lender notifies the insured of such changes as soon as they are known.

Also, the mortgagee is given additional time to file a claim. Generally, the owner must file a claim within 91 days **after a loss occurs.** The mortgagee, in the standard mortgage clause, must file a claim within 91 days **after being notified** by the insurer.

Finally, as mentioned earlier, roomers, renters and persons using the property for commercial purposes are explicitly excluded from being insured parties.

With the exception of endorsements, the rest of the items contained on the declaration page are self-explanatory. These include the issuing company (insurer), the limit of liability for the different types of property insured, the policy period (generally one year) and the premium costs.

ENDORSEMENTS

An endorsement is an attachment added to an insurance policy that clarifies, extends or restricts the policy's coverage of perils, locations, insured parties or exposure. It may be used to amend the policy period or premiums. As mentioned earlier, an endorsement may be used to add coverage for additional perils or to raise the limit of liability for certain items of unscheduled personal property.

The declaration page lists the endorsements by a designated number such as "365" with the additional premium costs, if any, for including the endorsement to the policy. The purchaser should find out from the issuing insurance broker what each endorsement covers and why it is needed. Generally, the coverage for an endorsement commences when it is noted on the declaration page, executed by an authorized agent of the insurer and any additional premium has been paid. The endorsement should be attached physically to the policy.

Appendix A lists some of the more common endorsements purchased and added to a homeowners insurance policy. References are made to particular endorsements throughout this article.

PERILS INSURED AGAINST AND DEDUCTIBLES

As noted earlier, two types of casualty insurance cover property--specified-peril and multirisk. Depending on the type of policy the owner purchases, it is quite possible for the dwelling to be covered by multirisk insurance and the personal property (either scheduled or unscheduled or both) to be covered by specified-peril insurance. In Texas, unscheduled personal property receives specified-peril coverage. These perils are listed in Appendix B.

Regardless of the type of coverage the homebuyer selects, the deductibles are based on the peril causing the damage or loss to the property. A deductible is the amount of the loss the purchaser is willing to absorb before the insurer is asked to pay. The higher the deductible, the lower the premium because the insurer assumes less risk and has lower administrative costs of processing small claims.

There are two deductibles. The first deductible, generally referred to as **Clause No. 1**, is for each loss to either the dwelling or unscheduled personal property resulting from windstorm, hurricane, hail or wind-driven rain. The second deductible, commonly referred to as **Clause No. 2**, is for each loss to either the dwelling or unscheduled personal property <u>not resulting</u> from windstorm, hurricane, hail or wind-driven rain.

EXCLUSIONS

Exclusions are limitations, restrictions and denials of coverage by the policy. Some policies have a section entitled "Exclusions," but particular exclusions may be found throughout the contract.

Appendix C lists some of the more frequently used exclusions. Exclusions apply both to the coverage of the dwelling and personal property. Before purchasing the policy, the insured should be familiar with any exclusion to avoid receiving inadequate coverage.

The purchaser should note that each exclusion relates primarily to the cause of a loss and not to the property damaged. For instance, losses resulting from freezing, flooding, deterioration, earth movement, machinery failures and animals kept by the insured usually are excluded by the policy. Flood insurance can be acquired only from the federal government.

CONDITIONS

When an insurance policy is issued, a jacket or pocket part is given to the insured, stipulating the basic policy conditions. The conditions specify the rights, duties and responsibilities of both the insured and insurer. It is imperative that the insured review and understand the various conditions. The insured's failure to comply with a condition may void the policy.

Some of the more important conditions contained in the policy jacket are listed below.

CONCEALMENT OR FRAUD

The willful concealment or misrepresentation of any material fact or circumstance concerning the insurance or any fraud or false swearing by the insured either before or after a loss shall void the policy.

Certain misrepresentations could be made by the insured on the declaration page. For instance, under the section entitled **Declarations of the Insured**, it states:

- The premises are not occupied by more than two families or two roomers or boarders per family
- The premises are the only place the insured or spouse resides
- No business is conducted on the premises.

If these statements are not correct, the coverage may be affected.

Fraud or false swearing could be made by the insured when a Proof of Loss Form is filed.

VACANCY

If the insured should cease to reside in the dwelling, and if all or a substantial amount of the insured's unscheduled personal property is removed from the dwelling's premises, the policy shall be suspended 60 days after the removal of the unscheduled personal property.

REMOVAL CLAUSE

If it should become expedient to remove property from the premises because of impending peril, the policy will cover both the expense and damage occasioned by the move. However, the impending peril must be one insured against by the policy. Limited coverage is extended for up to 30 days at each place to which the property is relocated. For example, if furniture is damaged while removing it from a burning house, the policy would cover the damage to the furniture and any cost in having it removed.

CANCELLATION OF POLICY

Either the insured or insurer may cancel the policy at any time. The insured may cancel by notifying and surrendering the policy to the insurer. All unused premiums will be refunded. The insurer may cancel by giving the insured a ten-day written notice. Again unused premiums will be refunded.

OTHER INSURANCE

The insured may have more than one insurance policy covering the same loss. The policy has specific directions for calculating the limit of the insurer's liability when other insurance is carried.

Basically the policy provides that the insurer shall not be liable for more than the ratio of the policy's limit of liability bears to the total amount of insurable coverage under all applicable insurance policies. For example, an insured has two policies covering the dwelling for fire. The limit of liability for Policy A is $80,000 and $90,000 for Policy B. Fire breaks out, causing $50,000 damage to the dwelling. Under these circumstances, Policy A would cover $23,530 of the loss (less any deductible). This figure is derived by dividing the limit of liability under Policy A ($80,000) by the total coverage under all policies ($170,000). The resulting fraction is multiplied by the amount of the damage ($50,000). Because this formula is used by the insurer, the policyholder can never overinsure the property. The insured receives no greater **total** recovery from two or more insurance policies covering one casualty than would have been received from one policy. In fact, if both policies have a deductible clause, the insured may be a net loser because the deductibles are not prorated as is the recovery.

REQUIREMENTS IN CASE OF LOSS

Within 91 days after a casualty loss, the insured must swear to and file with the insurer a Proof of Loss Form. The claim must contain, to the best knowledge and belief of the insured:

- The time and cause of loss
- The interest of the insured and others in the property,

- Any encumbrances (liens) on the property

- Other insurance covering the property

- The cash value of each item and the amount of loss

- The replacement cost of the property if a replacement cost endorsement is attached to the policy

- The cost of repair or replacement of loss without considering depreciation

Also, if the loss results from a violation of the law, the insured must notify the proper police authority.

WHEN LOSS PAYABLE

The amount owed by the insurer for a property loss is payable within 60 days after the Proof of Loss Form is received and an ascertainment of a loss has been made. The "ascertainment of a loss" can be made either by agreement with the insured or by the filing of an appraisal award by an appraiser (see Appraisal, p. 9).

EFFECT OF LOSS ON LIMIT OF LIABILITY

For certain types of insurance, such as title insurance, a payment to the insurer under the policy reduces the limit of liability remaining under the policy. For example, if a person purchases a $100,000 title insurance policy for land and receives a $30,000 payment for a loss resulting from a title defect, only $70,000 of effective coverage remains under the policy.

Casualty coverage under a homeowner's policy is not so structured except in limited cases for fire insurance. For instance, the policy states that any recovery paid for a fire loss reduces the remaining limit of liability for fire coverage by the amount of the payment. However, the coverage is reinstated as the repairs increase the value of the dwelling up to the original limit of liability but not in excess of the amount.

APPRAISAL

If the insurer and the insured cannot agree on the value of a casualty loss, the dispute will be settled by each side selecting a disinterested appraiser. The two appraisers shall then determine the amount of loss. If the two appraisers cannot agree, an umpire shall be picked by the two appraisers to settle the matter.

Each party shall pay the cost of his or her selected appraiser. The cost of the umpire shall be shared equally by the insured and the insurer.

COMPANY OPTIONS--ABANDONMENT

In the event of casualty loss, the insurer is given the option of taking all or any part of the damaged property at the agreed or appraised value; likewise the company can repair, rebuild or replace the property destroyed or damaged with other of like kind and quality within a reasonable time.

If the company should select any of the above options, it must communicate its intent to do so within 30 days after the receipt of Proof of Loss Form is filed. However, the insurer cannot be forced to accept any destroyed or damaged property. The acceptance of this option is solely at the insurer's discretion.

ACTION AGAINST THE COMPANY

This provision provides that no action against the insurer in a court of law shall be sustained until the insured has complied with all the policy's prerequisites for recovery. Time limits are also stipulated for bringing a cause of action. They are two years for a casualty loss.

CHANGES

No changes can be made or perils added except by endorsements properly executed by an authorized agent and attached to the policy. No provisions may be waived except by the terms of the policy subject to such changes.

PAIR AND SET CLAUSE

If a lost article is part of a pair or set, the measure of loss shall be a reasonable and fair proportion of the total value of the set. However, in no event shall the loss of a part of a pair or set be construed as a total loss of the pair or set.

BENEFIT TO BAILEE

To understand the contractual condition contained in the insurance policy entitled **"Benefit to Bailee"**, the purchaser needs to understand the law of bailment. A bailment is the delivery of personal property to another (known as the bailee), in trust, for the execution of a particular purpose. When the specified purpose has been accomplished, the personal property must be redelivered to the owner (bailor) or to another specified individual. Bailments arise in a number of ways. For instance, letting a friend borrow a car, leaving a watch for repair at a jeweler, boarding a pet or even sending items through the mail may constitute a bailment arrangement.

The bailee in possession of the personal property is charged with its care. The bailee may be liable to the bailor for the property's loss or destruction. The standard of care the bailee must exercise in protecting

YOUR

OPINION

Please

Thank you for ordering this publication from the Real Estate Center. To better serve you in the future, we would appreciate hearing from you. Please take a few minutes to complete the following questions and return this card to the research Center.

1. **Please evaluate each characteristic of this publication:**
(check all applicable blanks)

	Excellent	Good	Fair	Poor	No Opinion
overall content	____	____	____	____	____
amount of detail	____	____	____	____	____
technical clarity (readability)	____	____	____	____	____
organization of material	____	____	____	____	____

2. **To what degree did this publication meet your needs?**
(circle the number that best indicates your opinion)

very useful 5 4 3 2 1 not useful at all

3. **How did you learn of this publication?** ____________________

4. **What magazines or periodicals do you read most regularly to stay abreast of real estate topics?**

a) ____________ b) ____________
c) ____________ d) ____________

5. **What other topics or information would you like to know more about?**
____
____

6. **What is your principal occupation?** ____________________

7. **What real estate license do you hold?** ____ **broker** ____ **salesman** ____ **none**

COMMENTS: ____________________
____
____

No. 587

NO POSTAGE
NECESSARY
IF MAILED
IN THE
UNITED STATES

BUSINESS REPLY CARD

FIRST CLASS PERMIT NO. 148 COLLEGE STATION, TEXAS 77843

POSTAGE WILL BE PAID BY ADDRESSEE

Real Estate Center
Texas A&M University
College Station, Texas 77843-9990

the property depends on whether or not the bailee is getting paid for the bailment, i.e., a bailee for hire.

The insurance policy provides that if a loss is caused by a carrier or other bailee for hire, no coverage under the policy shall benefit such bailees. For example, an insured takes winter clothes to the cleaners before storing them for the summer. A fire, caused by the negligence of the owner, destroys not only the cleaners but all the winter clothes. There are two parties liable for the loss. The insurance company is liable for the **Off-Premises Coverage** for unscheduled personal property. The cleaners (bailee for hire) also is liable for its negligence.

Because the policy provides that its coverage shall not benefit a bailee for hire, a payment by the insurance company to the insured shall not relieve the cleaner's obligation to repay the insurance company for the loss. (See Subrogation for more details.)

SUBROGATION

If an insurer is liable for a property loss, the company may require the insured to assign all rights of recovery against a third party responsible for the cause of the loss. The insured shall do nothing to prejudice the rights of the company to recover from the third party. The assignment to the company shall be only to the extent payments are made by the company on behalf of the insured.

This provision would require the insured, in the prior example, to assign to the insurance company the insured's rights to recover from the cleaners for the winter clothes. The assignment would be only for the amount the insurance company had paid the insured for the clothes.

The insured may waive the right of recovery from a third party for a casualty loss but only as long as the waiver is given **before** the loss occurs.

LIBERALIZATION CLAUSE

If the State Board of Insurance prescribes a policy form more favorable to the insured or more favorable endorsements, rules or regulations during the term the insurance policy is in force or within 45 days prior to the policy's inception date, the more favorable rules shall apply automatically if the company can do so without additional premium charges.

STANDARD MORTGAGE CLAUSE

As stated earlier, the Standard Mortgage Clause extends automatic coverage to the mortgagee's interest, if any, in the real estate insured. (See earlier discussion of Parties Insured, p. 4, for more details concerning the Standard Mortgage Clause.)

ASSIGNMENT

The insured may not assign (or transfer) the policy to a third party without the insurance company's consent. Assignments occur generally when the owner sells the dwelling to another person during the policy period.

RECOVERY

If an insured should incur a casualty loss, the policy provides specific means for calculating the recovery. The determination is different for each of the three types of property insured: the dwelling, unscheduled personal property and scheduled personal property.

RECOVERY FOR DWELLING

The dwelling, described as Coverage A in the policy, includes the insured's residential structure as described on the declaration page of the policy. By the policy's definition, the dwelling includes also the building's wall-to-wall carpeting.

As mentioned earlier, up to 10 percent of the coverage extended to the dwelling may apply to detached structures located on the premises. The insured also may apply up to 5 percent of the limit of liability for the dwelling to trees, shrubs, plants and lawns located on the property.

If the dwelling is totally or partially destroyed or damaged by an insured cause, the policyholder has two choices of recovery. The insured may either recover up to the limit of liability stated on the declaration page (depending on the severity of the damage) less the applicable deductible, or have the dwelling repaired or replaced on the same premises with like kind and quality of material. Again, a deductible will be charged. The insured must make the choice of recovery when filing the Proof of Loss Form.

The insured's monetary recovery, regardless of the option chosen, depends on the level of insurance purchased for the dwelling. If the dwelling is fully insured, i.e., the limit of liability equals its full replacement cost as defined by the policy, the insured will recover 100 percent of the loss or cost of repair regardless of whether it was a total or partial loss.

If, on the other hand, the dwelling was less than fully insured, the insured must consult the coinsurance provisions of the policy. The coinsurance provisions were developed to encourage the insured to purchase insurance up to a certain percentage of the property's replacement cost. Primarily, the insured must determine whether 80 percent or more of the dwelling's replacement cost was insured at the time of the loss.

If the dwelling is 80 percent or more insured, the insured may recover 100 percent of a partial loss as long as the cost of the repair or loss does not exceed the policy's limit of liability. For example, the full replacement cost of a dwelling is $100,000. It is insured for $80,000 or 80 percent. A fire inflicts $65,000 worth of damages. The insured would recover the full amount of the loss or $65,000. However, if the loss had been in excess of $80,000, the recovery would be limited to $80,000.

If the dwelling is less than 80 percent insured, the insured's recovery is figured by the following formula. The value insured by the policy (the policy's limit of liability) is divided by 80 percent of the full replacement cost of the dwelling. The resulting fraction is multiplied by the amount of loss to determine the recovery which cannot exceed the policy's limit of liability as demonstrated in the next example.

The full replacement cost of a dwelling is $100,000. It is insured for $60,000, or 60 percent. A fire inflicts $40,000 worth of damages. The recovery would be $30,000, i.e., $60,000/$80,000 x $40,000. However, if the loss had been $90,000, the recovery would be limited to $60,000, even though the formula results in $67,500 ($60,000/$80,000 x $90,000). In no instance may the recovery exceed the policy's limit of liability which, in this case, is $60,000.

The phrase "full replacement cost" as used in the policy for purposes of coinsurance does not include:

- The value of any depreciation to the dwelling
- The value of any excavations
- The value of underground pipes, wiring and foundation
- The cost of wall-to-wall carpeting attached to the building
- The costs of cloth awnings and fences

If the insured elects to have the damaged property repaired or replaced, the repair or replacement must be finished within 180 days after the loss but may be extended to 360 days upon written request by the insured. The insurer is not liable until the actual repair or replacement has been completed with like kind and quality of material on the same premises.

Additional Living Expense and Rental Value

If a loss to the dwelling renders it wholly or partially untenantable (incapable of being occupied or lived in), the insured may receive up to 20 percent of the limit of liability for the dwelling as additional insurance for:

- The necessary and reasonable increase in living expenses to continue the insured's normal standard of living because of being displaced

- The loss of fair rental value because of a loss of a portion of the structure rented to others

Additional living expenses and loss of rental value become payable on the date of loss and continue until the repair or replacement is completed. The period may extend beyond the expiration of the policy. However, it will not extend beyond the time required to make the repair or replacement with the exercise of due diligence, or the time it takes for the insured's household to become settled in permanent quarters.

RECOVERY FOR UNSCHEDULED PERSONAL PROPERTY

In the event of an insured loss to unscheduled personal property, the recovery for Coverage B property will depend on the limit of liability contained in the policy, the presence or absence of the Replacement Cost Endorsement and the size of the deductible. If the Replacement Cost Endorsement has been purchased, the recovery will be the replacement cost of the article(s) stolen or destroyed less the deductible. If not, the recovery will be the replacement cost less both the depreciation for each item and the deductible.

Unlike the recovery for an insured loss to the dwelling, there is no coinsurance provisions establishing a minimum amount of required insurance for unscheduled personal property. For instance, the insured owns $50,000 of insurable unscheduled personal property. It is insured for its full replacement cost, and the Replacement Cost Endorsement is purchased and attached to the policy. If the insured should experience a total loss, recovery would be the full replacement cost of the unscheduled personal property (assuming its value does not exceed the policy's limit of liability of $50,000) less the applicable deductible. No deductions would be made for the depreciation of the items.

Exceptions to the Replacement Cost Endorsement are:

- Property that, by its nature, cannot be replaced

- Property not maintained in good workable condition

- Property that, at the time of the loss, is either obsolete or useless to the insured

For example, the insured owns $50,000 of insurable unscheduled personal property that is insured for $30,000. No Replacement Cost Endorsement is purchased. A fire destroys $30,000 of the personal property valued at $20,000 after depreciation. The insured's recovery would be $20,000.

Consequential (or Indirect) Loss Coverage

The insured's unscheduled personal property is subject to two Consequential Loss Coverages. Both coverages deal with the personal property located inside a building on the insured premises that is damaged as a result of a change in temperature. The difference in the two provisions lies in the causation of the temperature change.

If the temperature change was a direct result of physical damage to the building, the ensuing consequential damages to the personal property are covered up to the limit of liability of the policy. This is true as long as the original physical damage to the building was caused by an insured event.

On the other hand, if the temperature change was a direct result of damage to an apparatus for power, heating or cooling equipment or to the connections or supply pipes thereto, the consequential damage to the personal property is covered up to $500. Again, this is true only if the original damage to the apparatus, connections or supply pipes was caused by an insured event.

Automatic Removal

The Automatic Removal provisions apply if the insured should move to a new principal residence anywhere within the continental United States or Hawaii. The coverage for the unscheduled personal property shall continue at the new location for a period of 30 days from the date the removal commenced.

There are two limitations to this coverage. First, while the property is in transit, the maximum recovery for a loss shall be limited to the policy's **Off-Premises Coverage.** This is the greater of $1,000 or 10 percent of the limit of liability for Coverage B property. Second, if all the property is not moved to the same location, the recovery for a loss during the 30-day period at any one site is prorated. The amount of recovery is determined by dividing the value of the property at the location where the loss occurred by the total value of all the insured's unscheduled personal property. The resulting fraction is multiplied by the policy's limit of liability for Coverage B property. This is the maximum amount the insured could recover if all the property is destroyed at one specific location.

RECOVERY FOR SCHEDULED PERSONAL PROPERTY

The scheduled personal property, described earlier, includes articles of the insured's personal property individually listed and insured for a stated value. If a loss occurs, the owner recovers the value insured less both the depreciation of the item and the deductible. There is no Replacement Cost Endorsement, no **Off-Premises Coverage** or Consequential Loss Coverage for scheduled personal property.

CONCLUSION

Many homeowners have some type of property insurance for their dwelling and personal effects. Some purchase the insurance because they cannot sustain a financial loss. Others purchase it because it is required by the lender in the deed of trust.

Regardless of the reason for buying insurance, most homeowners do not comprehend fully the policy's coverage nor grasp the meaning of its conditions and exclusions. Typically, the purchaser relies on the advice of the issuing insurance broker or the procuring agent, both to establish insurance needs and to acquire the necessary protection. The arrangement has obvious drawbacks where the needs of the purchaser are not communicated clearly and accurately to the issuing broker or where the needs of the purchaser change after a policy is issued.

The Texas State Board of Insurance has standardized the homeowners insurance forms. Even so, the language of the policy can be quite difficult to understand. Consequently, the homebuyer and homeowner frequently need assistance in understanding and interpreting the insurance policy. Real estate brokers who advise them in its acquisition should be knowledgeable about the subject also.

This article is an attempt to help laypersons understand the homeowners policy issued in Texas. However, it is not a substitute for competent legal counsel nor advice from an expert in the field.

APPENDIX A

APPENDIX A

STANDARD ENDORSEMENTS FOR CASUALTY INSURANCE POLICIES

Number	Type
224	Windstorm, Hurricane and Hail Exclusion Agreement Endorsement
301	Additional Insured Endorsement
309	Television and Radio Antenna
315	Additional Amounts on Money and Securities, Etc.
317	Other Private Structures on the Premises
325	Additional Premises Endorsement
331	Secondary Residence Endorsement
335	Change Endorsement
339	Additional Limits on Jewelry, Watches and Furs
349	Residence Glass Breakage Endorsement
351	Assignment, Transfer or Change of Mortgage
355	Scheduled Personal Property--Coverage C Endorsement
361	Homeowners Secondary Residence Windstorm, Hurricane and Hail Exclusion Agreement Endorsement
365	Replacement Cost Endorsement
390	Home Computer Coverage Endorsement

APPENDIX B

APPENDIX B

INSURED PERILS FOR UNSCHEDULED PERSONAL PROPERTY

1. Fire and lightning

2. Sudden and accidental damage from smoke

3. Windstorm, hurricane and hail

4. Explosion

5. Aircraft and vehicles

6. Willful and malicious damage or destruction to property

7. Direct loss from pillage and looting occurring during and at the immediate location of a riot or civil commotion

8. Partial or complete collapse of building

9. Freezing of domestic appliances

10. Any act of stealing or attempted theft

11. Accidental discharge, leaking or overflow of water or steam used within a plumbing, heating or air-conditioning system or domestic appliance

12. Falling objects as long as the building containing the property first sustains actual damage to its exterior by the falling object.

APPENDIX C

APPENDIX C

EXCLUSIONS

1. Loss to electrical appliances, devices or wiring caused by electricity, other than lightning

2. Loss caused by smog or by smoke from industrial or agricultural operations

3. Loss caused by windstorm, hurricane and hail to:

    a. cloth awnings

    b. greenhouses and their contents

    c. buildings or structures and their contents located either wholly or partially over water

    d. radio and television towers, masts, antennas, wind chargers and windmills

    e. personal property within a building caused by rain, snow, sand or dust unless wind or hail shall first make an opening in the walls or roof

4. Loss caused by or resulting from floods, surface water, waves, tidal water or tidal wave, overflow of streams or other bodies of water or spray from any of the foregoing, whether driven by wind or not

5. Loss caused by or resulting from freezing while building is unoccupied unless:

    a. due diligence had been exercised to maintain heat in the building or

    b. the plumbing, heating and air-conditioning systems had been drained and the water supply shut off during the unoccupancy

6. Loss caused by theft from other than the insured's described dwelling unless the insured temporarily resides there

7. Loss caused by earthquakes, landslides or other earth movements

8. Loss to machinery, appliances and other mechanical devices caused by mechanical breakdown

9. Loss caused by inherent wear and tear, deterioration, rust, rot, mold or other fungi, dampness, extreme temperature, contamination, termites, moths or other insects

10. Loss caused by animals or birds owned or kept by the insured, members of his household or any other occupant on the premises

11. Loss to the dwelling caused by settling, cracking, bulging, shrinkage, or expansion of foundations, walls, floors, ceilings, roof structures, walks, drives, curbs, fences, retaining walls or swimming pools

Note: Any of the above exclusions shall not apply to any ensuing loss caused by fire, smoke or explosions.

Also note: Exclusions (9), (10) and (11) do not apply to an ensuing loss caused by a total or partial collapse of a building, by water damage or by breakage of glass provided the initial collapse of the building, water damage or breakage of glass was covered by the policy.

12. Loss caused by sonic booms or other forces resulting from shock waves created by the movement above the surface by aircraft, missiles or other objects

13. Loss caused directly or indirectly by nuclear reaction, nuclear radiation or radioactive contamination; however, loss due to fire resulting from nuclear reactions, nuclear radiation or radioactive contamination is insured

14. Loss of property or bodily injury caused by or resulting from hostile or warlike action in time of peace or war by the government forces or by insurrection, rebellion, revolution or civil war or the government actions used to hinder, combat or defend against insurrections, rebellions, revolutions or civil wars

15. Loss caused by an order of any civil authority except acts of destruction for the prevention of the spread of fire provided the fire did not originate from a peril excluded by the policy and

16. Loss caused by the enforcement of laws regulating local or state ordinances or laws regulating the construction, repair or demolition of a building or structure.

REPRINT POLICY

This publication was funded by appropriations to the Real Estate Center by the Texas Legislature.

ADDITIONAL COPIES

Requests for additional copies of this publication should be directed to the Publications Room at the address listed above.

QUANTITY DISCOUNTS

Discounts may be granted for quantity orders. Requests for such discounts should be made in writing to the Director, Real Estate Center. Such requests should state the quantity desired, purpose for which the item will be used and any other pertinent information that may assist in price determination. Instructors with special projects or unique requirements for multiple copies may receive special consideration. Such requests should be submitted in writing on college or university letterhead to the Center director.