Review Your Current Insurance, Consider Whether You Need to Customize Policies

Personal Risk Management

by Alexandra Armstrong, CFP

Financial planning involves many components. One important but often overlooked part is protecting the assets you've accumulated with property and casualty insurance. For expertise on this kind of insurance, we consult specialists. So for this article we asked Mitch Freedman, regional vice president for NFP P&C Private Client Group, Reston, Va., for his insights.

For most people, risk management means proper asset allocation, balanced investment strategies and competent financial planning. An appropriate property and casualty insurance program can go a long way toward fulfilling another important element of risk management.

The unfortunate truth is that too many of us pay little attention to such a critical piece of our livelihood. Many of us tend to simply gloss over our homeowners, automobile, liability and other insurance contracts, making an annual premium payment and assuming coverage is adequate to protect us.

But is it? What would happen if an accidental kitchen fire or wire shortage led to a major or total loss to your home and contents? What if a slick, wet road causes you to temporarily lose control of your vehicle, resulting in an accident involving severe bodily injury to a third party? And what if that lovely diamond bracelet falls off your wrist unnoticed while you're enjoying an evening at the theater? Unfortunately, none of these scenarios is all that uncommon, yet we seem to take for granted that coverage is there to protect us. Maybe it's time for a closer look.

Homeowners

As house values have recovered over the past few years, the cost to rebuild in the event of a fire or other covered loss has also increased. This is particularly true if you live in a partly or fully custom-built home.

This brings us to two key aspects of homeowners insurance: insurance to value (ITV) and guaranteed replacement cost (GRC). Insurance to value means applying appropriate cost measures to establish an accurate dwelling-coverage amount.

Avoid relying on a direct correlation between market value and replacement cost; instead ask your agent to establish a per-square-foot cost based on factors such as size, year built, construction type, ZIP code and level of customization.

Most insurers have matrices to which they can apply such factors to determine approximate replacement cost. But even that may not be enough. The plain truth is that you never know what it costs to rebuild until, heaven forbid, it must be done.

This brings us to the second key element, GRC. Although many policies provide a cushion above the dwelling amount listed on the policy, this still may be insufficient. For medium to highly valued homes, it's important to secure a policy that provides GRC, meaning you're covered in full even if the amount to rebuild far exceeds the amount stated on the policy. To provide such coverage, insurers will likely complete a comprehensive on-site inspection to better approximate the cost to rebuild. In so doing, they'll also offer advice on loss control and mitigation techniques (alarms, waterflow control systems and so on) and comment on reasonable levels of contents coverage to make certain your personal property is fully insured as well.

A brief sidebar for those who enjoy condo living: It's important to understand what your association's master policy covers versus what your responsibility as a unit owner is. In some cases the master policy will cover your unit in full, in some cases it will cover only as it was conveyed to the original unit owner and in some cases it will cover only the bare bones of the building, meaning you're responsible from the "drywall in." Ask your association for a copy of the master policy and have your agent review it to determine whether you're covered adequately. Your home may be your most valuable asset, but it's by no means the only one worth protecting. Let's turn our attention now to your vehicle.

Autos

Whether you're operating a high-performance luxury auto, a fuel-efficient hybrid or something in between, proper auto coverage is another key element of your risk management program. Several elements of your auto coverage are worth considering.

The first is maintaining proper physical damage coverage for your vehicles at reasonable deductibles. For too long, many policyholders viewed their auto insurance contract as a means of recovering the premiums paid. That is, they maintained low deductibles ($50 to $250) and filed claims for every little dent or scratch under the sun. But carriers caught on, and the policyholders were penalized for filing frequent claims with higher renewal premiums or even nonrenewal. As with any other line of coverage, your auto policy should be there to protect against the more significant or catastrophic loss. Modify deductibles to $500 or even $1,000 or more for highly valued vehicles, saving premium charges and deterring you from filing a minimal claim that can be paid for out of pocket. Additionally, you might consider "agreed value" coverage for your vehicles. Agreed value locks in the value of your vehicle for the full policy period, guaranteeing you a specified amount in the event of a total loss from a covered peril. Most personal auto policies provide only the depreciated value of the vehicle at the time of loss. Today when vehicle values are plummeting as a glut of cars enters the preowned market, agreed value can mean a difference of thousands of dollars come claims time. Some carriers who provide agreed value also waive your deductible in the event of a total loss, another cash flow positive.

Even more critical than physical damage coverage to your vehicle is proper liability coverage for personal injury and property damage to others. For all the years and effort placed in building your asset base, one inadvertent turn or lane change can put that wealth at risk unless sufficient liability coverage is in place.

This is implemented on two levels: primary auto liability and umbrella liability, which we'll cover shortly. Although states regulate the minimum liability limits required by law, such limits are inadequate to cover a significant claim. Even modestly higher limits can be insufficient. With typical bodily injury limits of $100,000 per person and property damage limits of $50,000, one remains exposed if held liable for more significant injury or damage. With an increasing number of highly valued vehicles on the road today, $50,000 simply may not be enough to cover a total loss.

Becoming equally as important on the liability front is uninsured/underinsured motorist (UM/UIM) liability coverage. Despite state laws, many motorists operate without insurance or with very minimal limits. What happens if you're struck by such a driver and there are insufficient limits available? You become reliant on the UM/UIM coverage on your own policy. Unfortunately, too many of us don't bother to review the UM/UIM limits we carry, and in many cases they're far lower than the primary liability limits discussed above. So check your policy and make certain your UM/UIM limits match your primary liability limits. Additionally, as we'll discuss in a moment, consider excess UM/UIM coverage as part of an umbrella liability policy.

Valuable Articles

Let's turn our attention back to personal property for a moment. In particular, consider those highly valued items such as jewelry, fine art, silverware and other collectibles that carry not only intrinsic but also real pecuniary value. You can certainly look to rely on the contents coverage on your homeowners policy, but more than likely you'll find yourself disappointed to learn there are special sublimits for certain categories of valuables, including but not limited to those mentioned above. A separate valuable-articles rider can adequately protect these items, either with an identified limit for specific items or under blanket coverage that provides an aggregate amount for a particular category with a per-item limit. Either way, you have broader coverage with fewer exclusions and "first dollar coverage," meaning no deductible applies.

In many instances, if your valuables make up a significant portion of your contents, you may be able to offset some of the premium by reducing the contents limit on your homeowners policy. Not all carriers allow such flexibility, so it's important to ask your agent whether this makes sense and whether it's feasible. Now that we've protected your heirlooms and other collections, let's turn to protecting your asset base from the potential catastrophe of personal injury liability.

Umbrella Liability

We've already talked a bit about having appropriate liability limits in place on your homeowners and automobile policies. But even these limits may not be adequate to protect you from a major liability claim. The most cost-effective means of protecting you from third-party personal injury claims is by securing a personal umbrella liability policy. For about $150 to $200 per million, you can secure additional limits to protect your current assets and possibly future wages.

Price, of course, can vary depending on the number of homes and vehicles owned, youthful drivers, watercraft usage, etc. A severe auto accident, injury to a house guest or other personal injury can lead to settlements in the millions of dollars.

For a modest premium, often reallocated from the savings reaped from a higher deductible on your homeowners policy, you can protect yourself from such an assault. Furthermore, your insurer has a duty to defend you even if the claim is baseless, with defense costs picked up by the carrier.

Another important element of an umbrella liability policy is the definition of personal injury. In this litigious society, liability claims aren't limited to bodily injury and property damage. A broad definition of personal injury that includes libel, slander, defamation of character and so on is important to maintain, especially in this era of social media in which someone's disparaging words, written or spoken, can lead to legal action very quickly.

Review your policy language with your agent and make sure the contract either includes this broad definition by default or can be added by endorsement.

There's no set answer to how much coverage to secure. An open dialogue with your agent and other advisers should include issues such as price, risk tolerance and exposure to potential loss. One rule of thumb often used is to obtain coverage equal to your net worth, but other factors often also need to be considered. Whether it be $2 million, $5 million or more, we think the premium asso-

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Award Honors Those Furthering Our Mission

Nominations Sought for Nicholson Award

BetterInvesting's board of directors is calling for nominations for the George A. Nicholson Jr. Distinguished Service Award in Investment Education to honor individuals who have furthered the association's mission.

The award, named after a co-founder of BetterInvesting and creator of its principles and Stock Selection Guide, recognizes those both inside and outside the BetterInvesting community who have introduced individuals to the ownership of business through stocks as well as provided investment information and education that enables individuals to be successful lifetime investors.

Anybody who helps promote investment education or creates educational programs, tools and resources that help individual investors apply common-sense investing practices is eligible for the award. Past Nicholson Award winners aren't eligible, however.

The board of directors may present the award annually and to more than one person. To nominate someone for the Nicholson Award, email the name to:

nicholsonaward@betterinvesting.org

Nominations need to include the nominee's name and contact information, as well as a letter of support explaining this person's or group's outstanding contributions in promoting investment education or advancing the organization's mission of empowering individual investors.

Nominations are due by Feb. 28.

The board of directors will present the Nicholson Award at the 2017 BetterInvesting National Convention in May in Cincinnati *(see p. 44)*.

Don Danko, former chief editor of *BetterInvesting Magazine* and current member of the magazine's Editorial Advisory and Securities Review Committee, was the inaugural recipient of the Nicholson Award.

In 2014 the board honored Ralph Seger, an educator and champion of BetterInvesting's principles through much of its history; and the Beardstown Ladies, the rural Illinois club that popularized investment clubs in the early and mid-1990s.

In 2015 the award was given to Gretchen Hurt, a longtime volunteer known for her dedication to service and support of BetterInvesting's mission. And last year Avi Horwitz, a BetterInvesting volunteer working with four chapters across the country, was recognized.

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ciated with such coverage is arguably the best-allocated money in your entire risk management portfolio.

Sound Program, Sound Sleep

We've covered a lot here, but that's not to say we've been comprehensive and that other issues don't persist. The elements and variables of a property and casualty risk management program are unique to each household. Additional issues to consider may include watercraft, second homes rented to others, rental properties, young drivers, assets owned in trust/limited liability company, domestic staff, wine collections and any number of other items.

The important takeaway is that in managing risk, it's critical not to overlook the importance of a sound P&C program to help you sleep at night. Although we continue to watch the financial markets gyrate day by day, you should at least rest easy knowing that if something catastrophic occurs in your daily routine, you have appropriate coverage in place.

In many cases, maintaining continuity with a single agent and carrier not only solidifies a program and simplifies its administration, but also can often lead to premium savings, too. So ask your agent the questions that matter in determining whether your existing program is right for you and how it can be enhanced to better protect you, your family and the assets you've worked so hard to obtain.

Our thanks to Mitch Freedman for providing us with the expertise for this article.

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