THE EFFECTS OF BEING OVER OR UNDER-INSURED

Hard insurance market conditions continue to influence high-net-worth individuals and family offices, requiring them to be extremely discerning with their risk management strategies to avoid being under or over-insured.

The effects of both circumstances equate to a potential loss of wealth. In the event of a catastrophic event, the underinsured can experience financial consequences beyond just the loss of property; for the overinsured, too much coverage means dollars spent on unnecessary premiums.

Because inflation remains high and a threat of a recession exists, the cost of insurance is likely to go even higher. Market valuations and actual replacement values are subject to change. The hard insurance market positions high-net-worth individuals and family offices to greater vulnerabilities—regardless of the amount of wealth owned. The immediate first step is to perform a proactive review of all insurance policies to ensure no gaps occur.

DISCOVERING THE RISKS — **UNDER**INSURED

An oversight that can lead to the underinsuring of property is assuming it is in a catastrophic safe zone. With the number of natural disasters increasing over the last decade, some insureds now lack proper coverage. Often, they reconcile paying out of pocket for any possible losses to save money on insurance premiums, thinking their homes are safe from impact.

The NOAA National Centers for Environmental Information cites that in the U.S. in 2022, droughts, heat waves, flooding, hail, hurricanes, tornadoes, wildfires, and winter storms impacted the country to create several billion-dollar weather-related disasters. No U.S. state has been untouched by the physical and economic impact of a natural disaster (1). While Federal Aid availability may be provided in the event of a disaster, high-net-worth individuals should take precautions against solely relying on these funds to rebuild or replace property.

3 out of 5 homes are underinsured by **Average 20%** below full value (2)

Actual Insured for = $300,000
Actual Replacement Cost = $450,000

80% Replacement Cost = $360,000
least amount property should be insured for

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Larger, more expensive homes or multiple residences will require a thorough look to avoid underinsuring properties. To figure out the true replacement cost, what would it cost to rebuild each property today?

Several types of homeowners insurance policies offer coverage—from replacement coverage to extended replacement coverage to guaranteed replacement coverage. An experienced insurance broker will guide individuals to ensure they have adequate coverage based on replacement value, not market value. Receiving this type of guidance protects high-net-worth families from unexpected cash outlays that could create tax consequences in the event other assets need to be sold to care for property losses.

DISCOVERING THE RISKS — **OVER-**INSURED

High-net-worth individuals tend to become overinsured because atypical insurance brokers focus on a client's wealth as the reason to pay more for or hold too much insurance. An insured will buy too much coverage beyond the actual value or replacement cost of the asset.

Another culprit to over-insurance is when insureds offer a 'best guess' of the asset's value to their insurance broker. A poor valuation creates a multitude of problems, including a higher quote from the insurer. In many cases, high-net-worth individuals could work with an appraiser and their insurance broker to obtain proper coverage, take the dollars spent on higher premiums, and allocate the funds toward home improvements or upgrades.

The effects of overinsuring with excessive policies pose a moral hazard. If an insured overinsures a property and a loss occurs, the individual may end up profiting from the loss, potentially creating a motivation to cause a loss to realize a profit; this scenario perpetuates damage to the insurance industry in the form of fraud.

Ways to prevent being under or over-insured:

- Comb your insurance policies to determine what is and is not automatically covered. At times, your homeowner's insurance will not cover the inside contents—only the property.
- For the contents of your home, you can purchase additional coverage to protect high-value assets, such as artwork, collectibles, or electronics.
- Be sure to make a list and document all contents.
- As you work with your insurance broker, consider combining all policies to pay less in premiums and minimize under-insuring your assets.
- Find a professional who will perform a thorough risk assessment to determine the exact coverage needed.
- Provide proper valuations or, at a minimum, use an inflation factor as part of the overall valuation of assets—material and labor costs are steadily increasing, and property values can be a sticking point for quoting the most appropriate coverage.
- Sometimes when individuals are over-insured, duplicate or redundant policies are to blame. Review all insurance policies to determine how to adjust your coverage.

Connect with our Private Client team to help ensure you're properly covered to protect your assets and your family.

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