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The skyrocketing cost of insuring a home in Texas has captured the attention of consumers, lenders, real estate professionals and politicians. Many are wondering how we got in this predicament.

The short answer is that Texas homeowners insurance is unique. The state's comprehensive homeowners policy, Homeowners-B (HO-B; see "Texas Homeowners Policies"), offers Texans more protections than the standard national policy (HO-3) does. It also costs considerably more. Texas' homeowners insurance premiums have been the highest in the nation at least since the Insurance Information Institute began compiling comparative statistics in 1995 and probably longer.

Recent insurance rate hikes on top of already high homeowners insurance premiums are putting a squeeze on homeowners and making it harder for some first-time homebuyers to qualify for mortgage loans. Ultimately, high homeowners insurance premiums may negate the competitive advantage Texas' affordable home prices offer.

The difference between Wisconsin's average premium (the least expensive) and Texas' average premium was \$621 in 1998 (see "Homeowners Insurance Premiums — Highs and Lows"), meaning Texas' premiums were 240 percent more than Wisconsin's. With Texas insurers

raising rates in 2002, that difference will become even more striking.

Why the Disparity?

Why the difference in premiums? Insurance industry experts cite two reasons. Texas is at greater risk for catastrophic weather conditions. While some states are tornado hot spots and others have a seacoast vulnerable to hurricanes, Texas has both. Texas also has a large number of hail claims, which highlight a second reason homeowners insurance is pricier in the Lone Star state — Texas policies offer more coverage.

The Texas HO-B policy is more generous on hail damage, slab foundation damage and water damage coverage than the standard policy used by the rest of the nation. The Texas HO-B policy also allows mold claims, which other states either do not allow or strictly limit. Water damage covered by the national HO-3 form is clearly defined and limited to "sudden and accidental" damage, such as that caused by a burst pipe.

Although Texas' HO-B policy states, "We do not cover loss caused by . . . rust, rot, mold or other fungi," mold claims have been allowed in Texas because of a clause stating the policy covers ensuing losses resulting from covered water damage losses. The water damage can be gradual, such as that caused by a leak in a roof or a washing machine hose.

In the wake of heightened media focus on mold, claims have increased dramatically. From Jan. 1, 2000, to the middle of June 2001, the number of mold claims per thousand insured in Texas increased sixfold, from 1.6 to 10.8 claims per

Homeowners Insurance Premiums Highs and Lows

Most Expensive States

	Average Premium
Texas	\$879
Louisiana	\$692
Florida	\$650
District of Columbia	\$633
Alaska	\$595

Least Expensive States

Wisconsin	\$258
Ohio	\$303
Delaware	\$312
Idaho	\$322
Oregon	\$330

National Average (50 states and District of Columbia)	\$481
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Source: "Average Premiums for Renters and Homeowners Insurance, By State, 1998" published by the Insurance Information Institute. These are the most current data available as of this writing. Average insurance premiums were obtained by dividing the total dollar amount of premiums by the total number of policies.

Brick veneer home in Caldwell, Burleson County, in an urban area with good fire protection

Value of Home	\$80,000	
Down payment	\$8,000	
Mortgage rate	7%	
Monthly Mortgage Payment	\$479.02	
Property Taxes*	\$2,256/year (\$187.99/month)	If premiums double:
Insurance**	\$409/year (\$34.08/month)	\$818/year (\$68.16/month)
House Payment	\$701.09	\$735.17
Annual income needed to qualify:	\$30,047***	\$31,507

*Based on the total of property taxes for a resident of Caldwell.

**Based on State Farm Lloyds annual rates in Burleson County as of June 2001. State Farm Lloyds is the largest home insurer in the state. This rate includes \$80,000 coverage on the house, \$32,000 on its contents and a 1 percent (\$800) deductible.

***Based on requirements for loans purchased on the secondary market by Fannie Mae or Freddie Mac.

below a benchmark rate or else obtain prior approval from the Texas Department of Insurance. However, a loophole exempted certain types of companies. Today nearly 95 percent of homeowners policies are sold through companies exempt from rate regulation.

Rate regulation is not an ideal solution. In a free market, competition regulates rates. P.J. Crowley, vice president of public affairs at the Insurance Information

thousand. Farmers Insurance Group officials stated that the company's mold-related Texas claims grew from 12 in 1999 to about 8,000 in 2001.

In response to the mold crisis, Insurance Commissioner José Montemayor amended the HO-B policy in November 2001, retaining mold coverage under the ensuing loss provision, but limiting it to a sudden and accidental loss from an insured peril.

Montemayor allowed exclusion of the cost of testing, treating and disposing of mold beyond immediate damage, with the provision that homeowners could buy additional coverage for these expenses. The amended HO-B requires homeowners to report loss from water damage to their insurer within 30 days from the time it is discovered or should have been discovered.

Rate Inflation

Because the modified HO-B offers less coverage for mold and water damage, consumers expected lower premiums. However, the Texas Department of Insurance has received numerous complaints from consumers who say their premiums have doubled. Mark Minchew, whose Austin real estate firm closes about 1,000 transactions a year, says he is seeing policy costs double, resulting in a noticeable increase in house payments.

Insurers have raised premiums for a number of reasons, including losses resulting from mold claims. A less lucrative investment climate is another reason. To survive, insurance companies must have large cash reserves available to meet claims. Companies invest this cash, and in the '90s, they earned high

returns on their investments. In 1998, for example, thanks to investment income of 12 percent, insurance companies made a 2 percent profit despite the fact that claims and other expenses exceeded premiums collected in the United States.

But the past two years have been a different story. The Dow Jones Industrial Average dropped nearly 1,500 points from the end of 1999 to the end of 2001, and insurers had to rely more heavily on premiums for income.

Rob Schneider, attorney with the Consumers Union's southwest regional office, blames high Texas insurance premiums partly on the lack of rate regulation. In 1991, a rate regulation system was adopted for homeowners insurance that required companies to set rates within a range 30 percent above or

Institute, says lack of rate regulation is not the reason insurance is higher in Texas.

"When major insurers are reluctant to write more business in a competitive market, more regulation is not going to solve the problem," Crowley says.

It would instead lead to artificial rate caps without addressing the basic problem with the HO-B policy that is driving up costs, he says. "In a rate-regulated environment, companies would either write less coverage in Texas or, in a worst-case scenario, drop out of the market."

Premiums and Housing Affordability

The Texas Department of Housing and Community Affairs (TDHCA) defines

It Pays to Do Your Homework

Comparison shop. The Texas Department of Insurance website (http://www.tdi.state.tx.us/apps/perlroot/u_cp_homerate/rghome.html) lists many licensed insurance companies by county, compares premiums and financial soundness ratings, and provides each company's complaint index and contact information.

Know what you are buying. Some companies now are selling the modified version of the HO-B policy, and some are selling the "old" version (see Texas Policies). The modified HO-B limits mold coverage, but homeowners have the right to add additional mold coverage in increments at an additional cost.

Some insurers have discontinued HO-B renewals or new HO-B policies and are selling an expanded HO-A instead. Homeowners switching to an HO-A form should be aware that the coverage might be considerably less. See "Texas Homeowners Policies." For a list of companies selling HO-B policies, see <http://www.tdi.state.tx.us/company/pccphob.html>.

Research discounts. Some companies offer discounts for deadlock bolts, hail-resistant roofs, burglar alarms or sprinkler systems. Ask about other discounts.

Check out the company. New insurer in town? Call the Texas Department of Insurance (800-252-3439) to be sure it is licensed. If it is not, your property may not be protected.

affordable housing as housing for which the homeowner is paying no more than 30 percent of his or her gross income for all housing costs, including mortgage principal, mortgage interest, taxes, homeowners insurance and utilities.

Sarah Anderson, director of the Housing Resource Center at TDHCA, says that insurance premiums are certainly a factor in the affordability equation.

"I think a rise in homeowners insurance premiums may affect the afford-

ability of homes in Texas," she says. "For low-income households, \$50 more per month can mean the difference in whether or not they can afford a home."

The table (next page) illustrates how doubling insurance premiums affects qualifying income and monthly payments for a home in one Texas community.

The insurance rate issue clearly is important to the Texas real estate industry. Finding affordable insurance is difficult. Minchew says his firm used to run into insurance-related problems

about once a year. Now he is running into some type of insurance problem about once a week. Coupled with Texas' extraordinarily high property taxes, rapidly rising insurance premiums will make it more difficult for Texans to afford a home. ■

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Forty-nine states and the District of Columbia use national homeowner's insurance policies identified as HO-1, HO-2 and so on. But true to its independent spirit, Texas created its own policies, which have historically covered more than the national policies and are lettered rather than numbered (HO-A, HO-B, HO-C).

Homeowners A (HO-A). This policy covers only **named perils** — fire, lightning, wind, hail, explosions, aircraft and vehicles, vandalism, smoke, theft, riot and civil commotion.

HO-A is an **actual cash value** policy. Homeowners are reimbursed for the replacement cost minus the deductible and depreciation (in other words, what the covered items are worth today). For a higher premium, some companies offer an upgraded HO-A policy with replacement cost coverage for the dwelling.

Homeowners B (HO-B). This policy protects the house and other structures on the property against all perils **except those specifically named**. Covered perils include fire, lightning, hail, falling objects, windstorms, explosions, vandalism, theft, freezing pipes and damage from out-of-control vehicles. It also covers accidental water damage and damage caused by a water leak under a slab foundation. Floods and earthquakes are among the perils not covered.

The standard HO-B policy covers the **replacement cost** of the home only. Homeowners are reimbursed for the full cost of replacing the loss, minus the deductible. The actual cash value of personal property is covered for named perils only. Homeowners can add an endorsement to their HO-B policy that will cover the replacement cost of personal property.

Beginning Jan. 1, 2003, only the modified version of the HO-B policy will be sold. The modified HO-B policy limits water damage losses and excludes testing, treating and disposing of mold, although additional coverage may be purchased.

Homeowners C (HO-C). This policy is similar to HO-B but covers personal property for all perils. Because of its higher cost, fewer consumers purchase HO-C.



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