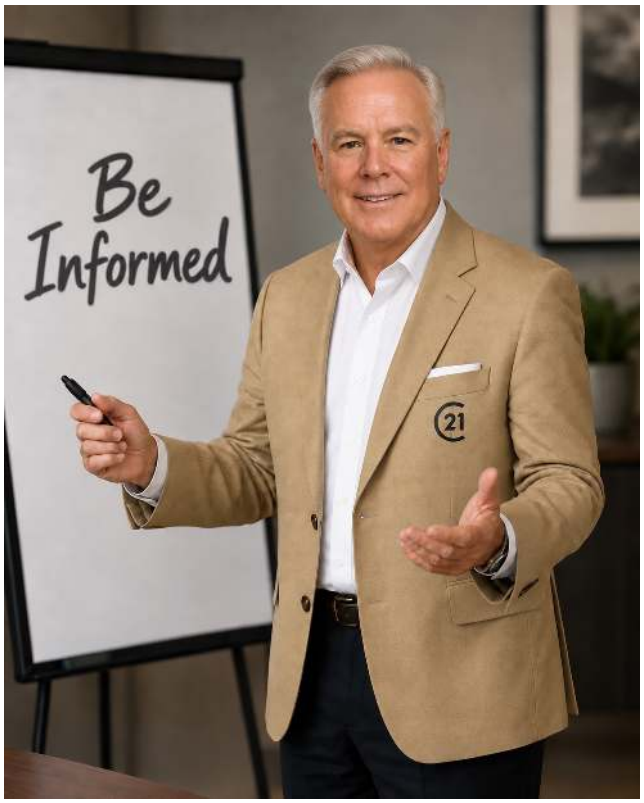
MISC

Homeowners Insurance



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NATIONAL ASSOCIATION OF REALTORS®

CONSUMER GUIDE: HOMEOWNERS INSURANCE

Understanding homeowners insurance is essential for anyone looking to purchase a home. Start looking at policies early and ask an agent who is a REALTOR® to connect you with a licensed insurance agent for assistance. A detailed industry overview of available coverage is here, and below are some of the basics:

What is homeowners insurance? Homeowners insurance covers you for unexpected losses at your home or property. It can include provisions to repair or rebuild the property or other structures not attached to your house (e.g., fences or detached garages), replace assets within the home, cover legal and/or medical fees for accidents that happen to you or someone else on the property, or even pay for living expenses if a covered incident forces you to live elsewhere temporarily.

What are perils, and which are covered? "Peril" is an insurance term for a specific risk or reason for a loss. Your insurance will cover a loss only if it is caused by a peril that your policy covers. Policies can vary in which perils are covered, but the most common policy type, HO-3 or the "Special Form," covers the home structure and personal belongings for disasters including fire, hail, lightning, freezing, theft, and vandalism. Most policies exclude floods and earthquakes.

Is homeowners insurance required? If you are taking out a mortgage on your new home, your lender will require you to have a homeowners insurance policy for the duration of your mortgage. If your mortgage is paid off, or if you've paid for the home in cash, no laws require you to maintain insurance. However, having insurance is generally a good idea to ensure your assets are protected.

How much does homeowners insurance cost, and how do I pay it? The cost of homeowners insurance depends on several factors, such as the house's age, square footage, condition of the property, and location. You may have the option to pay your premium on a monthly, quarterly, or annual basis. Some lenders collect the insurance premium as part of your monthly mortgage payment, place it in an escrow account, and pay the insurer on your behalf.

How much will my insurer pay me? In the event of a loss, there are two common types of reimbursement:

- **Replacement cost value** is the amount needed to buy a new, similar version of something you own. Insurers often cover this for your dwelling or property up to the limit of the insurance policy. If your home is insured for at least 80% of its replacement cost, and it gets damaged or destroyed, the insurer will reimburse you to have it repaired or replaced with similar materials of like kind and quality. Replacement cost is not the same as market value. For example, if you bought a $500,000 home five years ago, it is destroyed by a fire, and the actual cost today to restore it using similar materials is $375,000, you may be paid $300,000 after the deductible.

- **Actual cash value** is the current value of an item that loses value over time due to use and/or age (depreciation). The insurer pays out the cost to make repairs, minus any depreciation. This reimbursement type is most often used for replacing personal property but could also be applied to your dwelling if your property is significantly underinsured (less than 80% of replacement cost). In this case, if you bought a new table five years ago for $1,500, but due to normal wear and tear, it's only worth $750 at the time of the covered incident, then your insurer will only pay out up to $750. You can, however, purchase replacement cost coverage for your personal property for an additional charge.

In addition, some insurers may offer add-on options to extend your dwelling coverage. For example, an **extended replacement cost policy option** gives extra coverage above the policy limit up to a set percentage. For example, if a home insured for $500,000 takes $750,000 to rebuild, an extended coverage policy at 20% would mean the insurer pays 120% ($600,000), or $100,000 above the limit.

Are homeowners insurance premiums tax deductible? If the property in question is your main home, then your home insurance is generally not deductible. However, people who run a business from their home or those intending to rent out their property may be able to claim a deduction. Additionally, if you suffered a loss to your property caused by a presidentially declared disaster, you may be able to claim a casualty loss deduction. Discuss your unique needs with a tax professional.

Practices may vary based on state and local law. Consult your real estate professional and/or an attorney for details about state law where you are purchasing a home. Please visit facts.realtor for more information and resources.

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