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## Insurance: Mystery Solved

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The purpose of this paper is to help you—the media—understand insurance, and, in turn, we hope you will use this information to educate those who use you as a source of information.

Our hope is that by absorbing and analyzing this information that you will have a better understanding of the nature of insurance and how important it is for consumers to understand the contractual agreement they have with an insurance company.

It is also our hope that politicians considering regulatory changes in insurance will also have a better understanding of the basics of the business they believe needs regulatory changes. We believe this will help them in the decision-making process.

After reading this you will have questions. We have answers. Let us set up an interview with one of our community leaders or with the president of this association to help you educate others on how insurance really works.

PIA stands for Professional Insurance Agents. We are an association of independent insurance agents.

Independent insurance agents are Main Street America. They are the heart and soul of their communities and are plugged in as government leaders and community volunteers. The PIA Western Alliance is a nine-state alliance that represents several thousand PIA member agents in Alaska, Arizona, California, Idaho, Montana, Nevada, New Mexico, Oregon, and Washington.

To learn more about the PIA Western Alliance go to [www.piawest.com](http://www.piawest.com).

In addition to offering consumers more insurance choices which helps them get the best coverage at the lowest rates, one of our charges is to educate consumers on what insurance is and does. And that, too, is the purpose of this paper.

## ***An Introduction to Insurance***

A quick glance at the TV or daily paper on any given day of the week, or listening to stories in radio newscasts reminds us that we live in a disaster-prone world. The news is weighed down with information about a recent hurricane, high windstorm, the latest flood, wildfire or earthquake. Disasters like these often strike with the accompanying catastrophic loss of human life. Reports of millions—and in some cases, billions—of dollars in damage fill the nation's TV, radio and newspaper reports.

Disaster is a reality of everyday life.

Often mixed into the tragedy of disaster damage is another tragedy. People affected by natural disasters can find their claims denied by insurance companies. As we saw in the aftermath of the court decisions surrounding Hurricane Katrina, the insurance companies didn't mislead or mistreat claimants. It simply boiled down to the homeowner not having the right type of insurance. The reasons vary, but the primary culprit is the lack of understanding the nature of insurance, and what is and is not covered under the standard homeowners policy.

In short, insurance is a complex legal arrangement, and because of that fact, most people do not take the time to completely understand what their insurance dollars are actually buying. The result of this decision often has tragic consequences. Insurance is very complicated, and because of the complexity and because it is a legal document, the inclination of many insurance consumers is to divert to the only common denominator they understand—and that is price.

We say it now and we will say it often—where insurance is concerned—you get what you pay for!!! A true understanding of what the exposures are and the risk involved, and the insurance available to mitigate that exposure, and the consumer would immediately purchase the proper insurance.

### ***What is Insurance?***

Simply put, insurance is a transfer of risk mechanism. It is a contract between the consumer and the insurer to protect a given asset: a home, auto, business etc. The consumer, working with their professional independent insurance agent, determines how much insurance is needed to protect their "risk portfolio." To determine total exposure, the professional independent insurance agent and the consumer conduct a "risk analysis."

There is no insurance policy that will fit every insurance consumer. The basic forms used by most insurance carriers are similar, but there are no two insurance company policies that are exactly the same. This is where the education about the insurance purchase is critical. The



questions to ask are: what are my risks, what is available in the insurance industry to minimize those risks, and what is the cost for that insurance?

The consumer then makes the final decision on what coverage to purchase. This is where the transfer of risk begins. For a premium—which is usually a monthly, six month or yearly fee—the consumer “transfers” their risk of loss to the insurance company. The consumer generally retains some risk via the payment of a deductible or the understanding that some types of loss will not be covered under a specific policy or in some cases by a policy of any type. How much risk, exposure and retention they wish to pay for in the deductible and the decision whether to purchase insurance to cover the risk or not—if insurance is available—is totally up to the consumer.

It is important for the consumer to note there are causes of loss that are not insurable by anyone anywhere. This is an awareness and education issue that each insurance consumer absolutely needs to take the time to understand.

Another important fact consumers must understand is that insurance does not exist to provide them with a profit in the event of a claim. It is a mechanism to make them whole. In essence insurance restores them to where they were before the loss. Obviously insurance cannot replace a treasured family heirloom or invaluable family photos. Some of what a person owns cannot be measured with a dollar figure. Insurance can and does, however, put the victim on the road to recovery financially and gives them the ability to get back where they started.

The PIA Western Alliance, a nine-state association that is part of the National Professional Insurance Agents Association—the PIA—recommends that all consumers purchase the correct insurance at an appropriate level so when the worst-case scenario happens they can be made whole and put back where they were financially before the loss.

### ***Who Chooses What Insurance Is Needed?***

The decision as to how to insure an asset is completely up to the buyer/consumer. It is their choice. A professional independent insurance agent can only suggest types of insurance coverage, limits, pricing, and can only recommend how a person should insure themselves, their family and their assets. The PIA Western Alliance recommends that insurance consumers spend time with a trained, professional, insurance agent to determine what coverage is available and at what cost. As has already been mentioned, insurance decisions are important because they are financial decisions. If the wrong decision is made, the consumer suffers severe financial consequences.



## ***Defining Homeowners Insurance***

The definition of homeowners insurance and what it covers can easily be the most misunderstood. Rejection of claims filed under homeowners policies also generate the most complaints and gets the most negative coverage by media.

Here is what your homeowner's policy does not cover:

- Flood
- Landslide / mudslide
- Earthquakes
- Limited coverage for guns, jewelry and art
- Other specific items listed in the exclusion section of the homeowners policy

Coverage for those events requires a separate policy. Remember—no two policies are the same, and—with insurance you get what you pay for!!!

## ***Why Flood, Earthquake, and Landslide / Mudslide are Not Part of the Standard Homeowners Policy?***

To a certain extent fire and other potential disasters on property covered by the homeowner's policy can be controlled. Flood, quake and slides are different. It is critical to understand the difference.

For everything you purchase there is a price. Do you need to purchase everything that is available? The answer is no. For example, a person living in Spokane, Washington does not need earthquake insurance as much as a person living in San Francisco, California. A consumer purchasing earthquake coverage in Spokane is probably not a good buying decision. That same person in San Francisco failing to purchase earthquake coverage is very foolish.

Again, think of it this way: the consumers should only buy the insurance really needed based on a proper analysis of their risks and the risks in the area.

Another reason these policies are separate has to do with what human beings can control. Loss control mechanisms to minimize or "mitigate" damages to the home can make them less of a risk for the insurance company.

For example, brush can be cleared from around a building and things can be done to keep the home safe from fire. In most areas a fire department is within easy reach. Fire extinguishers or sprinkler systems can be located in strategic places inside and outside of the dwelling to control a fire before it gets out of control. Stairs can be kept clear and slip-proof and so on.



A consumer cannot do anything to prevent or mitigate a flood, an earthquake or a slide. That is why flood, earthquake, and Difference in Conditions Coverage are special coverage—and are not part of the standard homeowners policy. Each can be purchased through a PIA member professional independent insurance agent.

### **Flood Coverage**

A flood can be so destructive that the only coverage available to those in a flood plain or a designated flood area is coverage subsidized by the U.S. government. Insurance agents write flood insurance but the only source of that coverage is the federal government. Federal dollars—money from taxes combined with premiums from flood insurance policies—are set aside in a fund and when a flood event happens, consumers with the good sense to purchase a flood policy, will be covered.

Someone owning a home along a river or one of the many coastal areas in this nation will want flood insurance. Again—an informed decision with the proper education is critical. Knowing where you live and the risk factors of living there is crucial to making an insurance decision. Unless an area is prone to flash floods, a homeowner living in the middle of a desert probably doesn't need this type of insurance.

Fire—for example—may never happen. In fact, it is more likely that fire will never happen to a consumer than happen. For those dwelling wetlands, along rivers or along the coast, a flood will happen. No matter how high a levee is built or how deeply a river is dredged, or how carefully seashore is shored up, Mother Nature will at one point or another beat the best humans can do and the property will flood. That is a fact.

So a consumer living in those conditions will definitely need flood insurance.

### **Earthquake Coverage**

Earthquake insurance works the same way. A person in California's San Francisco Bay area will absolutely want to carry a policy to cover damages in case of an earthshaking event. People in the nation's mid-section may not need earthquake protection.

### **Difference In Conditions Coverage**

A Difference in Conditions Coverage (DIC) policy is specific to an uncovered peril to a standard property or homeowners policy. They are for property coverage only and stretch from easily understood conditions like land and mudslides to lesser known risks like living underneath power lines or close to an airport.



Here's an example of why this separate policy is necessary. A landslide or a mudslide is not covered in a homeowners policy. It is also not the result of flooding so a flood insurance policy won't cover damage. In some cases you may not even be able to buy flood insurance if you live on a hillside but getting a DIC policy is likely.

Rain causes slides. And like flood and earthquake, rain cannot be controlled. A homeowner can shore up the hill with concrete and rip wrap but eventually the weight will wear that hill down and it will fall. It may take 10 years, 100 years, 1,000 years, or 1 million years but eventually the hill is going to come down.

**The bottom-line:** The difference between the just discussed policies and a standard homeowners policy is the control loss mechanism. There is no switch to turn off a flood, landslide or a mudslide, or an earthquake. No matter what you do there is really nothing you can do to minimize loss with these types of disaster. We live at the mercy of Mother Nature until the crisis is over.

And the crisis is over when it's over.

### ***Educating the Consumer—and politicians and the media***

Everyone has insurance. Whether it's Joe Average Consumer or a politician or a member of the media, most people likely have an auto insurance policy, homeowners or renter's policy, health insurance, and maybe even a life insurance policy.

As discussed earlier, one trap most of us fall into when purchasing insurance is not taking the time to understand the contract. We comprehend the deductible amounts and the basics just fine but fail to ask key questions on the fine points of a policy. And I will say it again—you get what you pay for!!!

Your PIA professional independent insurance agent orders the policy from the company that writes the policy. That same professional insurance agent explains the basics and asks if there are questions. This is where the consumer choice explained in the opening paragraphs of this document comes into play.

Questions should be asked all along. And those questions start when first considering the purchase of an insurance policy:

- What are my assets and how much would it cost to replace them?
- What exposures do my assets have?
- What is available to mitigate potential loss of these assets in the insurance market
- What do I choose to purchase insurance to protect and what am I protecting myself



To get the proper insurance the consumer must understand their asset inside and out. What poses a danger to that asset? In the case of a homeowner living on a hillside it is the hillside. On a river or the coast, the danger is flood. In a wooded area it is fire and surrounding trees. Questions like these lead to obtaining the proper insurance to make the person whole in the event of a disaster.

This is where your PIA member professional independent insurance agent is so valuable. The more information given to them and the more time the consumer takes to help them understand their insurance needs and the better off they will be in the event of a disaster.

A PIA professional independent insurance agent will assist in the process to understand what a person has, how it can be protected, and what that protection will cost. Failure to have the correct insurance or the understanding of what is and what is not insured in any situation is a recipe for disaster.

### ***Key Points to get Properly Insured***

- Spend time with a PIA professional independent insurance agent to make sure property is insured to proper limits and to replacement value.
- As the cost to rebuild goes up, so should limits.
- Understand replacement costs and the cost of getting an asset up to code if codes have changed.
- Do not fail to evaluate those limits at renewal.

Of all of those points the most important is the time spent communicating needs and changes with a PIA professional independent insurance agent at renewal.

### ***But it's so expensive***

It doesn't take a rocket scientist to understand that the greater the risk to an asset, the higher the cost of insurance. Once prices start to be calculated, affording the proper insurance can seem overwhelming. This is another place where the advice of a highly trained, skilled professional independent insurance agent is invaluable.

A trained professional independent insurance agent won't advise that a person cut corners. They will, however, know how to minimize the impact on the wallet. Here are just a few things an agent will tell a consumer to do to minimize cost:

- Deductibles are the out-of-pocket expenses when there is a loss. Assume some of the risk and raise those deductibles.
- Don't claim the small stuff. A \$250 broken window a few times a year can hurt rates.



- Make sure a home is up to code (here are some examples):
  - Make sure it is up to fire standards
  - Make sure assets and property are valued to a level where there is enough insurance to pay for replacement in the event of a loss
  - That brush has been cleared from the property
  - The roof is in good condition and has fire retardant on it
  - Wiring is set to standard and the breaker box is not overloaded
  - The dwelling has earthquake protections
  - Potential floodwaters have been diverted and there is an action plan in place in case of a flood.
  - Understand completely what you DO NOT have protected by insurance

The more that is done to minimize risk, the lower the premiums (price of the insurance policy).

Whenever possible use one company for all of insurance needs. That gets additional credits with the company for using them for more than one policy.

### ***No matter what—Stay Safe***

Disasters are going to happen. They are a part of life. Should a situation develop like some described here, please keep a number of things in mind:

- Keep calm
- The top priority for a person is to keep themselves and their family safe
- Possessions can be replaced—a life can't
- It's hard to lose an heirloom but heirlooms don't measure up to the value of a life
- If it's a fire—once out of the house, stay out of the house
- In a flood—sandbagging won't help while the water is pouring in
- Earthquake—when the shaking stops, get out of the house
- Pets—everyone loves their pets but once out of the house, stay out of the house

When it is safe to return, immediately contact a professional independent insurance agent and start the claims process.

It is also important to stave off future loss. A good example is a tree falling on a house. If possible, safely remove the encroaching tree and cover the hole with a tarp. This will keep the loss meter from climbing and save money.



## ***The Bottom-Line***

Here is the best advice we can give. Find a PIA member professional independent insurance agent and discuss insurance needs with them. Go over exposures with the proverbial fine tooth comb to get the proper coverage for all of needs: homeowners, auto, commercial and more.

It is the right coverage for the right needs that stand between individuals and their family and disaster.

“People complain about paying for the high cost of insurance. Some don’t think they get anything in return for the expense. Then they get hit with a disaster and they first thing they think is, ‘Thank God I have insurance.’” Kevin O’Connell, President, PIA Western Alliance board of directors.

