

The Homeowner's Insurance Crisis

by K. Michelle Lind, AAR Legal Counsel

The Problem

Homeowner's insurance is generally required to obtain a loan and close escrow on a home purchase. Most loan documents require homeowners to maintain homeowner's insurance for the term of the loan. However, homeowner's insurance in Arizona, as in other states, is less available and more expensive than in years past. The Consumer Federation of America reports that homeowner's insurance rates in Arizona rose 13.25 percent in 2001 and 14.82 percent in 2002. Some homes may be virtually uninsurable.

The Cause

The insurance industry cites some of the following reasons for the increased cost and reduced availability of homeowner's insurance:

- Number of recent catastrophes
- Mold claims
- Stock market losses
- Repair cost increases
- Past use of these policies as a "loss leader" to secure auto and other coverages

People and property most likely to be affected

Those most likely to be affected are:

- People who have made an insurance claim or claims inquiry in the last five years.
- People with adverse credit issues.
- A home on which an insurance claim has been made, especially if the claim involved mold

and conditions conducive to mold, such as water damage.

The Arizona Department of Insurance reports that in 2002, consumers reported difficulty in obtaining insurance for "vacant dwellings, dwellings in unprotected areas, low-valued dwellings, old dwellings, high-priced dwellings and dwellings that have had any losses within the last three years." (*Press Release, April 2, 2003*).

Reports from the Comprehensive Loss Underwriting Exchange ("CLUE")

CLUE tracks both the person making an insurance claim and the property on which the claim was made. This repository of information purportedly contains 95 percent of all insurance claims or claim inquiries made in the United States for a five year period. The report includes information on the cause of loss and the amount paid by the insurance company on the claim, if any. The report also contains personal information on the homeowner, such as the owner's social security number and date of birth.

Obtaining a claims history report

A homeowner may be able to obtain a five-year claim history at no cost by simply requesting the report from their insurance agent. In the alternative, homeowners may purchase a CLUE report on their own property. Buyers may request a

copy of the CLUE or claims history report from the seller, but do not have the right to order a report on a home they do not own.

The CLUE report is sold by a company called ChoicePoint and currently costs \$12.99. The report may be obtained [online](#) or by calling 866-527-2600. Individuals may also obtain their personal insurance history from the same company.

Insurance cancellations after close of escrow

Some insurance companies that use information from CLUE or other insurance reporting agencies in their underwriting practices obtain a report only after a binder (contract for temporary insurance) is issued or after escrow has closed and the policy is to be issued. Thus, there have been numerous reports of homebuyers having their homeowner's insurance cancelled after closing escrow on a home purchase.

An insurer can generally cancel a homeowner's insurance policy for any reason in the first sixty days after issuance. See *A.R.S. §20-1652*. And, once a policy is cancelled, the cost of replacement coverage can be two to three times higher than the original cost, depending on the reason for the cancellation.

Simply obtaining the CLUE report or claims history does not solve the problem. The underwriting practices of individual insurance companies vary and not all insurance companies use CLUE reports on both the person and the property. The companies that do use CLUE or other claims history reports evaluate the

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Buyer's Initials Buyer's Initials

information in different ways. Therefore, simply obtaining a copy of the report will not tell a buyer how an individual insurance company will evaluate the risk of insuring that particular buyer in that particular home.

AAR's response to this concern

AAR has been proactive in responding to this homeowner's insurance crisis. AAR has undertaken to educate buyers about this issue and encourage them to apply for homeowner's insurance as soon as a purchase contract is executed. The AAR [Residential Resale Purchase Contract](#) advises buyers to make inquiries and consult insurance agents during the contract inspection period (lines 222-226). A buyer may give written notice of reasonable disapproval and elect to cancel the contract based on that inquiry. AAR's [Seller's Property Disclosure Statement](#) now prompts the seller to disclose any known homeowner's insurance claims regarding the home. The [Buyer Advisory](#) was revised to inform buyers about how claims history may affect their homeowner's insurance.

AAR also initiated a legislative response to address these problems. Senator Barbara Leff agreed to sponsor Senate Bills 1265 and 1266, both of which have been passed by the legislature.

SB 1265 requires that if an insurer uses information from an insurance support organization, such as CLUE, or information from a consumer reporting agency for underwriting purposes, the insurer must obtain that information as soon as practicable and before the issuance of a binder of insurance coverage. The failure of the insurer to timely obtain the information precludes the insurer from declining insurance coverage or terminating a binder of insurance coverage based on the information. Finally, thirty days after the application for insurance coverage, no declination or termination of

Residential Resale Purchase Contract (lines 222-226)

Buyer Responsibility Regarding Inspections and Investigations: *Buyer is advised by Broker to obtain inspections and investigations of the Premises. Buyer acknowledges that Buyer should make inquiries and consult government agencies, lenders, insurance agents, architects, and other appropriate persons and entities concerning the use of the Premises and the surrounding areas under applicable building, zoning, fire, health, and safety codes, and for evaluation of potential hazards. Buyer acknowledges that more than one inspection may be required.*

insurance coverage may be based on information from an insurance support organization or consumer reporting agency.

SB 1265 should reduce the possibility that the homebuyer's insurance policy will be cancelled after close of escrow. However, an insurer still may decline or terminate insurance coverage based on the condition of the premises as determined through a physical inspection of the premises. This legislation will become effective on December 31, 2003.

SB 1266 addresses premium increases when the insurance company has suffered no loss. Homeowners have complained that their premiums were increased based upon property damage or loss when the insurer made no payments under the policy. AAR believes that a claim that results in no payment by an insurance company should not result in increased premiums to the homeowner. However, in a compromise with the insurance industry, AAR accepted the following language: "[a]n insurer shall not charge more for homeowner's insurance coverage with a single below-deductible claim, not exceeding five hundred dollars in the previous three years, than it would charge for like coverage on the same property if the property had no below-deductible claims." "Below-deductible claim" means a claim was closed without any payment because the amount of the loss was less than the amount of the deductible provided

by the policy. This legislation will become effective 90 days after the end of the current legislative session.

To obtain additional information on homeowner's insurance

The Arizona Department of Insurance has developed a [comparison of homeowner's insurance rates](#) to encourage consumers to comparison shop for their insurance. The Department also developed a [Consumers Guide to Homeowner's Insurance](#).

Advice to homebuyers

AAR is considering other possible actions to address these concerns and further legislation may be necessary. In the meantime, buyers should educate themselves about their insurance company's underwriting practices and shop around for a company that will best suit the buyer's needs. Further, a buyer may want to request that the seller provide the buyer with a five year claims history on the home, so any claims issues are identified early in the transaction. Finally, buyers should apply for homeowner's insurance as soon as possible after entering a contract to purchase a home. ▲

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