



# Insurance to Value: Taking Aim at a Moving Target



# Rerunning in-force property portfolios at renewal can yield a clear advantage

Maintaining insurance to value (ITV) on a homeowners book of business has become more challenging in recent decades. Some of the driving factors are the growing size, intricacy, and customization of the U.S. housing stock. While insurers are well aware of these trends, gravitating to more precise ITV tools is their best option for both fully protecting their customers from a total loss and ensuring that premium is adequate for the risk.

There was a time years ago when the average home was relatively easy to mock up on paper. Typical new homes around 1975 were roughly 1,600 square feet of simple, uniform construction, with a modest menu of features and materials distinguishing one house from another. Deviations were generally smaller and less widespread than they are today.

Since the 1990s, homes have become larger, more complex, and more individualized, with available high-end materials, finishes, and features no longer limited to the most exclusive developments. Verisk data points to ever-expanding U.S. homes, with the average square footage of a home 13 percent larger now than in the mid'90s.

Year built	Average square feet
1975	1,764
1985	1,851
1995	2,135
2005	2,407
2015	2,460
2017–2018	2,418

Logically, if homes are larger, more unique, and more complex, replacement cost values will not follow a linear trend. It's become more difficult to simply apply portfolio-wide ITV solutions and maintain estimated replacement cost (ERC) close to reality. For example, a certain style of home may use more lumber than another home of similar size and quality. If, in a given year, the increase in the cost of lumber is an outlier, an insurer's ITV solution should be able to account for that factor to maintain accurate ERCs on homes across a range of sizes and styles.



## The optimal approach to protect clients and your bottom line

You may take the most common approach to ITV at renewal: apply a factor or a percentage increase to an existing policy to update the replacement costs when policy renewal is due. However, this approach can gradually erode the ITV of the policy. Our ongoing research of properties that sustain total losses shows that deviations tend to compound year after year. Valuations can be off an average of nearly 4 percent just three years from the original calculation, with the gap growing to approximately 7 percent by the fourth year and approaching 11 percent at five years. This may leave homeowners with an underinsurance exposure and you with premium leakage.

Rerunning a property's replacement cost estimate at renewal may seem daunting to implement. However, the cost of not updating the individual building costs of each property at renewal could mean that the property is not fully protected in the event of a total loss for the next policy term—a claim and reputational risk exposure.

Taking the initial inputs used to calculate replacement cost when the policy was bound, and updating with any known changes to the component-level costs with refreshed replacement cost data, yields a granular, address-level updated replacement cost.

This is a win-win for you and your customers.

## If you must index, make it regional

Regional replacement cost indexes measure the change in reconstruction costs over time across various U.S. regions and a wide variety of structures, accounting for materials and labor costs. Indexing is based on the law of large numbers: aggregated, averaged numbers calculated to account for all sizes, styles, and makeups of today's housing stock. But insurers that are rerunning their books of business at renewal may see greater impact than when using indexes.

Verisk's Regional Replacement Cost Indexes are divided into 19 regions across the United States and aggregate the cost to rebuild 30 different structures representing a range of size, style, and quality in each economic market. The calculation is based on price changes for materials and labor compiled from Verisk's market analysis. This process enables publishing an index value of unparalleled accuracy.



## Solutions that scale to your resources

To validate the reliability of residential replacement cost estimates regularly, Verisk compares valuations produced for specific structures to actual reconstruction estimates written by claims and construction professionals and submitted to Xactware's claims management system, XactAnalysis®. Verisk's 360Value® solution shares the same building cost data as the claims loss estimation system Xactimate®, providing highly reliable replacement cost estimates based partially on recent claims loss experience.

Verisk offers multiple options to meet the needs of any book of business, including web services to automatically build renewal processing into current workflows.

It's typically not challenging for IT teams to program systems for renewal reprocessing with 360Value. Today's web services technology easily passes data between insurers and Verisk's systems. Rerunning is essentially programmed during the 360Value implementation process, after which no further resources are required.

But no two insurers are alike: priorities and resources may point some toward a less granular approach to ITV. Whatever the need or preference, data-rich ITV solutions can help keep valuations aligned with current construction costs—and help protect insurers and customers alike.



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