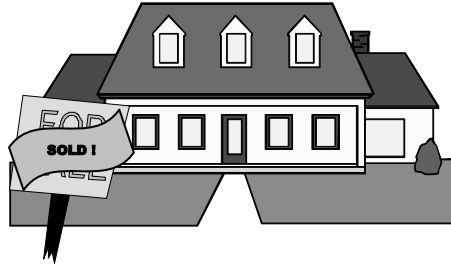


# The New Reality of Property Insurance

## What You Should Know



### **Q. How can insurance availability or affordability affect the real estate transaction?**

A. The affordability and availability of insurance affects both buyers and sellers. Buyers will typically be obtaining mortgage financing to pay the purchase price of the property. The lender will require that there be property insurance to cover their interest in the property. If proof of insurance is not available at closing the lender will likely refuse to release the funds and therefore delay or even derail the transaction, either of which can impose both inconvenience and cost to both the buyer and seller. Even in a “cash” transaction the buyer may be hesitant to complete a transaction where insurance is not available to cover the buyer’s equity in the property.

### **Q. When should a buyer apply to obtain an insurance policy to cover the property being purchased?**

A. The interest of both buyers and the sellers now suggests that the buyers should begin their search for insurance no later than the time of the contract to purchase is signed. This helps to assure a firm commitment for the issuance of a policy well in advance of the settlement of the transaction. Waiting until the last days or even weeks before the closing can limit the opportunities of the buyers and sellers to address the affordability and availability issue and, if needed, to find alternatives for difficult to insure properties. There have been many examples of transactions which have been adversely affected in some manner because of problems associated with insurance availability/affordability.

### **Q. What kinds of events/records can affect the ability to obtain insurance on a property being purchased?**

A. A number of factors can affect the availability and cost of homeowner insurance on a property being purchased. For example, they include:

- a. past claims filed on the property (up to previous five years)
- b. poor insurance credit score of the prospective purchaser
- c. past claims filed by the property purchaser on other properties
- d. physical characteristics of property (e.g., leaky roof)
- e. characteristics of the property's location (e.g., proximity to fire station, regional weather conditions)

**Q. How does the insurance company know what claims have been filed in connection with the property?**

A. Approximately 90% of all insurance companies contribute information regarding claims to an insurance industry database. When underwriting a new policy the insurance company may obtain a report from this system from one of a couple different sources to determine the property's claims history. This report is most often identified as a *Comprehensive Loss Underwriting Exchange* report or a "C.L.U.E. Report." The report contains information regarding property claims filed in connection with a particular property and claims filed by a particular insured person. The current owner of the property may obtain a free report through ChoicePoint, Inc., by writing to:

ChoicePoint, Inc.  
PO Box 105295  
Atlanta, Georgia 30348

or by visiting their website, [www.ChoiceTrust.com](http://www.ChoiceTrust.com), or by calling 866-312-8076. Another firm known as ISO, furnishes similar reports called A-PLUS. ISO can be reached at 800-709-8842.

**Q. Should I get a copy of the C.L.U.E. Report?**

A. While this decision is up to the property owner, it is important to understand the limitations of the report. The report contains only raw information and how that information will affect the insurability of a property isn't explained as a part of the report. Moreover, not all insurance companies use the report and those that do use it don't all use the information in the same way. As a result having the report may not enable you to predict whether a particular company will insure the property. If you want information on how a C.L.U.E. Report or other similar report may affect your ability to obtain insurance contact your insurance agent.

**Q. Are there factors unique to a buyer that can affect their ability to obtain insurance?**

A. Yes, although not used by all insurance companies in determining eligibility for insurance, some companies do review the claims filed by the buyer on properties owned by the buyer during the preceding five years. This is another aspect of the C.L.U.E. Report database that focuses upon the insured individual rather than the insured property.

Another more controversial factor is the use of Insurance Scores. Insurance Scores, which are formulas developed by insurance companies in an effort to predict the likelihood of an individual filing claims, are sometimes used to determine to whom or at what price an insurance policy will be issued. Insurance scores are not standardized within the insurance industry and both how they are calculated and how they are used is generally not known outside of individual insurance companies. If you want additional information on how insurance scoring may affect your ability to obtain insurance contact your insurance agent.

**Q. Can a seller include a requirement that the buyers demonstrate their insurability as a condition of the sales contract?**

A. Yes, although not common, such a requirement could be included in an agreement. However, the specific language of such a condition should be carefully considered. Check with your real estate agent to find out if any standardized language has been developed in your community and/or consult with your attorney. As discussed herein the factors used to determine a particular buyer's insurability will vary from one insurance company to another and can leave questions regarding whether and when such a condition had been satisfied.

**Q. Can a buyer include a requirement that property be insurable and/or the insurance be affordable as a condition of the sales contract?**

A. Yes, but the specifics of such a condition should be carefully considered. Check with your real estate agent to find out if any standardized language has been developed in your community and/or consult with your attorney. There are multiple factors which might be used to determine a property's insurability or the "affordability" of the insurance in such a clause. The factors used in a contract clause could include, but are certainly not limited to:

- a. acceptable C.L.U.E. report
- b. purchaser is satisfied of the insurability of property
- c. secure binder of property insurance on property
- d. cost of insurance doesn't exceed specified threshold

Both buyers and sellers should be aware that there are advantages and disadvantages to such a clause that should be considered. The advantage of such a contingency is that it may allow the buyer to cancel the transaction if the property proves uninsurable or insurance is unaffordable. This avoids reliance on a financing contingency and any question regarding its application where the property and borrower would otherwise qualify for a loan. On the other hand, the inclusion of such a clause may affect the acceptability of an offer, particularly if the offer is being made in a competitive environment.

### **Transaction Checklist - Insurance Issues**

- Discuss current insurance market conditions with your insurance agent and any problems you may have in obtaining insurance on the home you are purchasing
- Review offer to purchase to identify insurance issues/contingencies or need for such contingencies with your attorney
- Contact one or more insurance agents immediately following acceptance of purchase contract by both parties to begin process of obtaining necessary insurance.
- Obtain commitments to issue an insurance policy from an insurance company in writing and carefully review it with your attorney or insurance agent to determine scope of that commitment.
- Be aware of alternative insurance sources that may be available if a problem develops:
  - Know available sources of insurance (i.e., what other insurance companies are in market by calling different insurance agencies in the community)
  - Check with Seller's current insurer to determine if that insurer will continue to insure property with new owner
  - Check with Buyer's current insurer to determine if that insurer will continue to insure buyer in a new property
  - Alternative forms of coverage that may allow transaction to proceed (FAIR Plans, Fire & E.C., etc.)

*Prepared by the Risk Management Committee of the National Association of REALTORS®*



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