High Alert

Insurers are covering high-end vacation homes by stepping up their risk management techniques.

by Meg Green

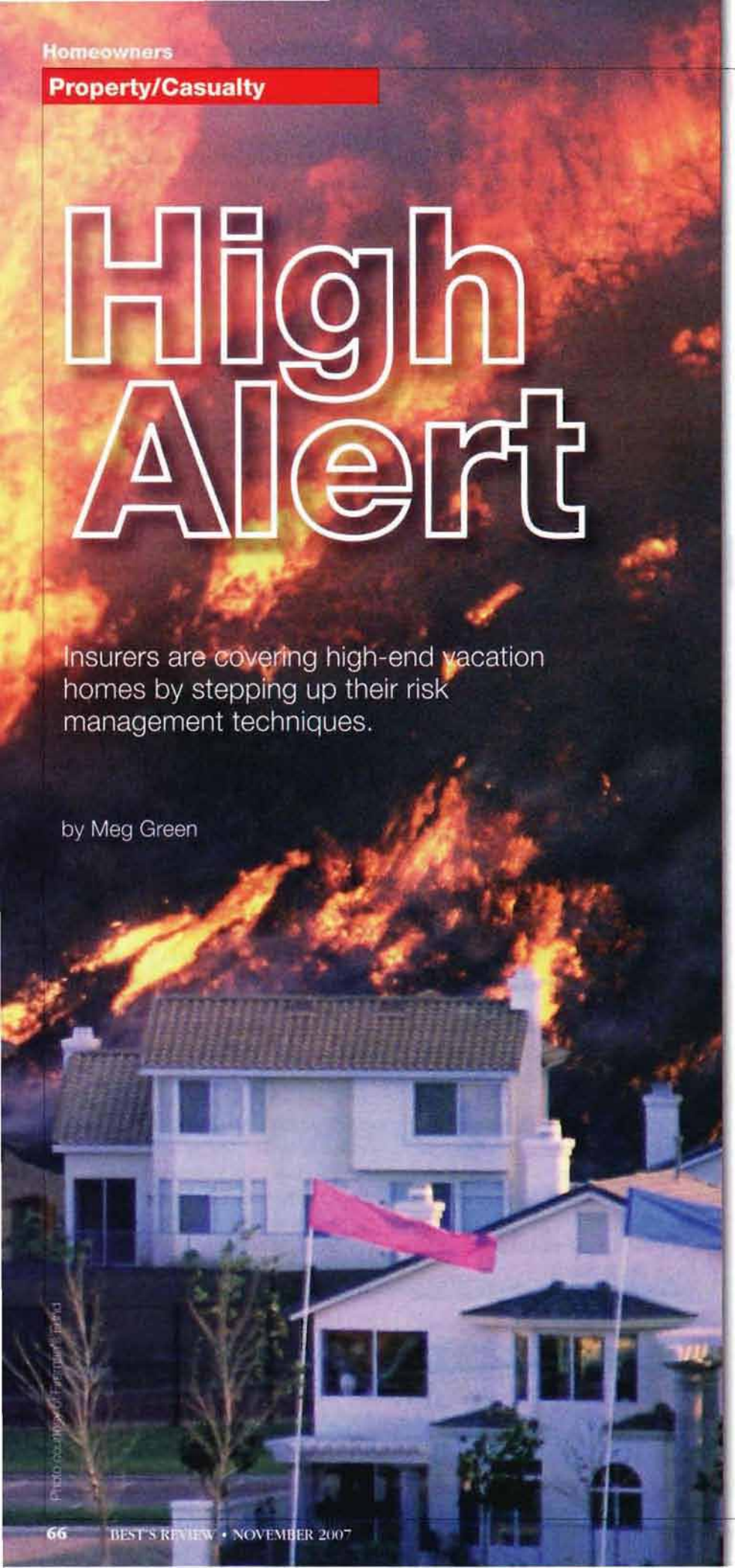

Photo courtesy of Fireman's Fund

Insurance companies are wooing vacation-home owners as part of an attempt to corner this high-end niche market.

Vacation homes can be a challenge to underwrite, because they often are located in high-risk areas and prone to perils such as hurricanes and wildfires, and many are left unoccupied for long periods of time. However, insurers are offering special risk-management services to help homeowners deal with those additional risks. Their goal is to write the vacation home as part of the homeowner's larger insurance portfolio, including homeowners insurance on primary residencies in addition to auto and umbrella liability coverage.

Exposed Risks

Vacation homes are a growing market. About 14% of all homes purchased in 2006—up from 12% in 2005 and 11% in 2004—were vacation properties, according to the National Association of Realtors. An additional 22% of homes purchased in 2006 were investment properties, so a total of 36%—more than a third of homes purchased in 2006—are not occupied full time by the owner, a fact that makes some insurers hesitant to enter this market.

FIRE POWER: More than 2,000 homes and businesses were destroyed by wildfires in San Diego County, Calif., in 2003. Vacation homes are often located in scenic areas prone to wildfires, hurricanes and other perils.

▶ **At Issue:** Vacation homes, since they're often unoccupied for long periods and exposed to nature's wrath, are tricky to underwrite.

▶ **The Situation:** Insurers now offer customized risk management services that protect high-end vacation homes and minimize risk.

▶ **The Payoff:** Insurers underwrite vacation homes as part of homeowners' larger insurance portfolios, including coverage for primary residences, autos and umbrella liabilities.

Of those vacation homes purchased last year, 29% were in rural areas, 24% were in resort areas and 15% were in small towns, according to the NAR.

"It's a tricky market because vacation homes tend to be in high-risk areas," said Bruce Callander, president of Sweet & Baker, a San Francisco insurance agency that specializes in high-net-worth clients. "I can't think of any of my clients who aren't in high-risk places. In the Lake Tahoe area, there are huge brush fire issues. On beaches, we have waterfront issues. In the Napa Valley, we have big properties on a lot of land with beautiful views, where fire services aren't close by."

A secondary issue is that vacation homes, by their very nature, are often empty.

"Most homeowners policies have a vacancy policy of 30 days," said Bill McCord, vice president of marketing and underwriting for Tapco Underwriters, an excess and surplus lines-managing general agency. "If the house is vacant more than 30 days and something happens, you do not have coverage."

Having an unoccupied home means a higher risk of vandalism and burglaries. A serious loss also can arise if a water pipe breaks or leaks and water runs unchecked for weeks at a time. Owners of seasonal homes often have to pay a surcharge and buy an endorsement to a standard policy so the home is covered even when it's vacant for extended periods.

Some insurers have offered coverage to secondary or vacation homes with a dwelling fire policy, a less robust policy than a standard home-owners insurance policy, McCord said.

"A lot of companies will offer less coverage than a normal policy. They will cover the structure to the same level, but they will limit theft or offer no theft at all, because the vacancy is the primary underwriting issue," he said.

The dwelling fire form is the original homeowners policy, dating back to before the 1960s, but is still used today for secondary dwellings, said Peter Wells of Marshall & Swift, a company that specializes in calculating replacement costs.

"It's just basic coverage for a few perils, like fire, wind and lightning," Wells said. "You can expand it to include another 17 perils, including vandalism, theft and mischief, but you'd have to buy each individual coverage. There's no liability coverage."

Wells said that oftentimes a policy is written on market value, not for replacements costs. So the market value on a home, if it wasn't in a great location, might be $100,000 but the cost to rebuild the home, if necessary, could be 10 times that.

What's more, dwelling fire policies often are based on actual cash value, not the replacement value. Wells explained the difference: Standard homeowners policies pay to put a new roof on your house if it blows off, whereas ACV policies take depreciation into account. So, if your roof was three years old, the ACV policy would pay to replace the roof, minus three years' worth of value.

"The best thing to do is assess whether the structure is a fully encapsulated building, then get a homeowners policy," Wells said.

For high-end vacation homes, companies are moving away from dwelling fire policies and are eager to offer traditional homeowners coverage—if it is part of a larger portfolio, Callander said.

"What is interesting about this market is we have always found the primary carrier will write the secondary home," he said. "Even if the risk of the secondary is so ugly, a carrier will say they will only write the vacation home if they can write the primary residency, the cars and the umbrella policy. They want to write the entire portfolio. I don't

Homeowners Insurance Losses by Cause, 2001-2005

(Percent of losses incurred)

Cause of loss	2001	2002	2003	2004	2005
Property damage					
Wind and hail	21.7	20.7	25.5	51.2	45.0
Fire, lightning and debris removal	30.8	32.6	31.8	20.5	25.1
Water damage and freezing	22.3	21.5	21.9	15.7	16.8
Theft	4.7	4.5	3.3	2.2	2.6
All other property damage	13.2	12.3	10.7	6.1	6.5
Liability					
Bodily injury and property damage	6.5	7.3	5.8	3.7	3.3
Medical payments and other	0.7	0.8	0.8	0.7	0.7
Credit card and other	0.2	0.3	0.2	0.1	0.1

Sources: Insurance Information Institute; ISO

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Sweet Spot

Don Soss, vice president of personal insurance and chief underwriting officer for Fireman's Fund, said Fireman's is "very interested" in writing business on secondary or vacation homes for affluent and high-net-worth clients.

"It's right up our alley," Soss said.

Fireman's Fund considers high-net worth clients to be those with net assets of $5 million or more and who pay annual premiums of $25,000 or more.

Fireman's Fund, American International Group and Chubb "want to write all the personal lines they can in the luxury home market, for homes worth $1 million or above," said McCord. "All three are big players in that arena and are big into those homes. They are happy to write vacation homes if they have the other house."

AIG Private Client Group, which also specializes in high-net-worth individuals, defines its target client as having a home worth $1 million or greater, or paying a minimum of $10,000 in annual premiums.

Fireman's Fund and AIG both said they'd write a vacation home as part of a larger insured portfolio, including insurance on the primary home, automobile insurance, umbrella liability coverage and any additional insurance, such as coverage for fine art and jewelry.

"In my view, I don't see a difference in profitability between insuring a primary residence and a secondary home," Soss said. "But there is a difference between a secondary home and a seasonal home."

He said a secondary home is one that is visited frequently, maybe every weekend. "It's occupied frequently, and is a better exposure," Soss said.

A seasonal home, such as a winter home used during ski season or a summer home at the seashore, is boarded up when not in use. "We have to take certain precautions there," Soss said. "We'll give a premium credit if there is a full-time caretaker at the residency, for instance."

Homeowners are likely to face still higher premiums if their vacation homes include "attractive nuisances," such as swimming pools, swing sets, trampolines or boats, Callander said. However, loss mitigation techniques such as fences to keep trespassers away can help reduce risks.

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Home Alone

More than 16.4 million homes were vacant in 2006, and another 4 million were only used seasonally, according to the U.S. Census Bureau. Here are ways to prevent losses in your vacant vacation home:

1. **Adjust Thermostat:** In colder climates, do not turn the heat lower than 55 degrees. A frozen pipe that cracks one-eighth of an inch can leak up to 250 gallons of water a day, wrecking furnishings. In warmer climates, don't turn your air conditioner below 85 degrees, because high temperatures and humidity can damage furniture.

2. **Protect Plumbing:** Both plastic and copper pipes can burst. For extended vacancies, the best protection is to shut off the water and drain the water lines. However, if your house is protected from fire by a sprinkler system, shutting off the water will deactivate it. Instead, leave the water on and insulate pipes; turn off water to appliances, sinks and baths; consider installing an electronic leak detection system; and make sure the sump pump is working.

3. **Plan for Wind:** Trim dead limbs from trees and put away outdoor furniture. Close and lock all doors, windows and skylights. Install storm windows or hurricane shutters.

4. **Make Your House Look Lived In:** Put interior and exterior lights on timers and/or motion sensors. Hire someone to maintain your property by removing snow and mowing the lawn. Suspend mail and newspaper delivery. Install a monitored security system. Inform the local police that your house will be empty.

Source: Institute for Business & Home Safety

Insurers covering expensive vacation homes have stepped up their loss-prevention services as a way of reducing claims and attracting more clients.

Preventing Losses

"Risk management was not part of the personal insurance landscape until five or 10 years ago, when insurers began to focus on the high-end market," said Gary Raphael, assistant vice president of Risk Management Advisory Services for Fireman's Fund. "With the right amount of time and forethought, people can do a lot to protect themselves from these events. One of our missions is to inspire them to take action."

Fireman's Fund used to provide an engineer who would visit a policyholder to make sure the property was insured to the right coverage level. Now, companies such as Fireman's Fund and AIG are offering extensive services to help policyholders protect their properties from future losses.

"The high-net worth individual has unique issues and vulnerabilities that the general population generally is not exposed to," Raphael said. "We'd rather prevent a loss than adjust one."

Fireman's Fund has a staff of 60 risk management advisers doing precautionary on-site inspections of 20,000 to 25,000 properties every year and documenting what they see from structural and security standpoints. They craft a comprehensive program of pre-loss service for customers to help identify where they might be vulnerable to loss, and propose solutions to reduce their risks.

When it comes to vacation homes, the biggest issues are vacancy and location of the property.

As it develops individualized policies to help its policyholders prevent losses, Fireman's Fund relies on a network of recommended third-party experts, called the Prestige Advisories Service Network.

"We direct people to services and systems that will help protect and even monitor their property," Raphael said.

For instance, when dealing with the potential risk of a windstorm, Fireman's Fund will recommend companies that specialize in fortifying windows and exterior doors. If a home is vacant, the company recommends protection systems such as fire alarms, sprinklers and water-detection services.

"We may even recommend setting up cameras inside and outside the property, so they can monitor it whenever they want," Raphael said. "We try to recreate what it's like to have someone present there. Ideally, we like to have caretakers and arrangements made so someone is monitoring the property itself. But with cameras, we can have the same effect without the need for someone to be there."

To minimize the risk from forest fires, Fireman's Fund recommends a buffer space around the house that's void of combustible brush or material. Brush clearing and wildfire protection consultation and services—provided by firefighting professionals—are available to Fireman's Fund policyholders at a 10% discount; a complimentary wildfire home protection review is included. The service also is offered to anyone in California for a fee, Raphael said.

For homes where hurricanes are a threat, Fireman's Fund might identify a safe place in the house—say a second floor room without windows—where valuables can be stored when the home isn't in use.

"We could even have a plan to remove valuables from the house, and can recommend movers and storage facilities that are hurricane-rated," Raphael said. "However, in the process of moving things out, there can be a greater risk than leaving them inside. It's not a one-size-fits-all approach."

AIG Private Client Group created a loss prevention service office three years ago to tackle the major

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perils of hurricanes, wildfires and mechanical fires.

The residential engineering program, which is available to homes valued at $10 million or more, involves taking infrared images of mechanical systems to recognize hot spots that could cause potential fires, said Todd Triano, vice president of loss prevention services for AIG Private Client Group. The group also examines plumbing to look for potential weaknesses and vulnerabilities where leaks might occur.

AIG's hurricane prevention program is available to policyholders in parts of Florida and Long Island, NY. The program works with clients and brokers to establish preparedness plans.

After a storm, with a policyholder's permission, AIG will enter a property and provide post-storm emergency response to mitigate further damage. If, say, a hurricane blows out a window or part of a room, AIG will seal up the house to prevent further loss. Such action can keep a $150,000 claim from ballooning into a $500,000 claim, Triano said.

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Fighting Fire With Prevention

AIG has taken an aggressive stance on preventing wildfire losses.

Before the wildfire season starts, AIG sends out its team of fire mitigation experts to assess brush exposure at its high-value clients' homes in wildfire-prone areas. If necessary, the team sprays the native brush around the home with a long-term fire retardant. The treatment is water soluble but will last until the next good rain, said Stan Rivera, director of wildfire protection for AIG Private Client Group.

During this survey, the team also gathers critical information, such as contact information and access codes, which can help during an emergency response.

Once a wildfire is three to five miles from a covered property, AIG's emergency response team arrives to spray not only native brush, but also landscaping or potential fuel next to the home, as well as the wood components of the home itself including wood decking, siding and roofing.

Rivera said the retardant is environmentally friendly, safe around people and pets and does not harm or stain long-term structures. It's the same retardant that the U.S. Fire Administration drops on wildfires but without the red dye, he said.

While the program is available in 150 ZIP codes in California and Colorado, AIG has responded to wildfires in Montana, Idaho, Texas, Arizona, Oregon, Washington and Nevada. "If we have resources available, we will mobilize that fire truck to offer free protection to policyholders," Rivera said.

Policyholders don't even need to be at the property.

"We'll call a policyholder's agent to tell them what we've done," Rivera said. "People are so impressed. They can't believe their insurance company would provide this level of service."

Triano said AIG's emergency response team has "helped us avoid what potentially could have been a catastrophic event for us." BR

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