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How to find the replacement cost of your home for insurance

Kathleen Pender

July 2, 2016 | Updated: Oct. 12, 2017 5:48 p.m.



Fires like this one in Kern County can offer a rude surprise for people who are underinsured.

Photo: Marcus Yam / Marcus Yam / Los Angeles times

When Herb Solomon changed his homeowners' insurance this year, he was surprised to see that his new company estimated the replacement cost of his 2,600-square-foot North Berkeley home at roughly one-third less than the old one.

Solomon's policy last year, from Fireman's Fund, had a limit for the dwelling of \$1,256,000, which was "based on an estimate of the cost to rebuild." His new insurer, AAA Insurance, had a limit of \$875,000.

That got him wondering: How can homeowners determine an appropriate replacement cost, to make sure they are not over- or underinsured?

"Do you have to hire and pay a contractor? This is by far our largest asset, and I can't afford to be wiped out," he said.

If you are a homeowner, the amount on your declarations page labeled "dwelling" is the most the company will pay to repair or rebuild your home if it is damaged by a covered peril, unless you have extended or guaranteed replacement cost coverage. Covered perils include fire, windstorm and hail. Earthquakes and floods require additional policies.

Dwelling coverage applies to the core structure of your home including floors, roof, doors and cabinets. You will have additional coverage, with separate limits, for personal property, detached structures and additional living expenses if your home becomes uninhabitable. The limit for these three categories of coverage is usually a percentage of your dwelling limit.

Your basic dwelling limit should be as close as possible to what it would cost to rebuild your home if it was destroyed, according to United Policyholders, a consumer group. But estimating that cost is not easy because it varies widely based on the type of construction, quality of finishes, ceiling height and other factors, such as the slope of the lot.

Some insurance companies "will grab year built and square footage, and put those numbers into a software program that will spit out a figure for rebuilding cost," said Kyle Cliff, an independent agent with Hub International Insurance Services in San Francisco. Others will send a person to inspect the home, which results in a more accurate estimate. This is more common with high-end homes.

Homeowners who are not sure whether their dwelling limit is accurate can ask their insurer for a physical inspection, or get quotes from multiple companies.

If the numbers seem off, “ask to review the property details the company has on file to calculate the reconstruction cost. Make sure the insurance company has all the right attributes,” including square footage, number of bedrooms and bathrooms, upgrades and “unique characteristics,” said Norrine Brydon, vice president of data and research with CoreLogic, which purchased Marshall & Swift, a company that provides replacement cost software for professionals.

Outside opinions

If homeowners want an independent opinion, here are some options:

- Ask a custom home builder. Robert Hunter, director of insurance for the Consumer Federation of America, said that when he wanted to estimate the rebuilding cost for his vacation home in Maine, “I looked at comparable buildings going up in my neighborhood. I went to the builder and asked how much it cost to build per square foot. I multiplied out by my square footage” and got an estimate.

Later, when he had to have the home nearly rebuilt after a burst pipe resulted in mold throughout the house, he found out that estimate was pretty accurate.

Palo Alto architect Roger Kohler, who works with many Peninsula builders, said that, “for quite a while, we were told you could do a nice home for \$250 to \$350 a square foot. You could do it for under \$250 with vinyl windows (and basic finishes). Recently that range has gone up with some contractors we work with. They are not sure they can do much for under \$400 a square foot.”

- Ask an appraiser. If you bought a home recently, you probably bought an appraisal for the lender. This appraisal will have a market value, which is what the home, in its current condition, and the land is worth. It should not be confused with replacement cost, which excludes the land value.

Some appraisals include a “cost approach,” which excludes the land value, but “it should say this should not be relied on for insurance purposes, said Alison Teeman, an appraiser with Yovino-Young in Berkeley. It is often no more than an “informed guesstimate.”

You could hire an appraiser who has the skills and software to do a replacement-cost estimate for insurance. The cost could range from a few hundred dollars if you have a floor plan and the appraiser doesn’t need to take measurements to more than \$1,000.

Teeman, who does insurance appraisals a few times a year, said that in the Bay Area, “we are now over \$300 a square foot for most construction from the ground up,” except for “basic stick construction on a flat lot,” which could be around \$200 per square foot, she said.

- Go online. For a ballpark estimate, try the free calculator at www.building-cost.net. This is designed for contractors to estimate new construction, but it could give you a “down and dirty” estimate for insurance purposes, said Denis DeSaix, an appraiser with Metrocal Appraisal in Livermore.

At www.e2value.com, you can get a replacement cost appraisal for most homes for \$25 each.

Negotiate the limit

If your estimate is different from your insurance company’s, ask it to reconsider. Doug Heller, a consultant to consumer groups, said his company reduced his coverage limit by \$32,000 after he showed his agent a lower estimate from a competing company.

Janet Ruiz, a spokeswoman for the Insurance Information Institute, which represents insurers, said the coverage limit “is ultimately the policyholder’s choice. They know their home best.”

Finally, make sure you know what kind of coverage and how much you actually have.

“Replacement cost” will pay to replace what you had new, at today’s prices. “Cash value” will pay only the depreciated value of what you lost. You could have replacement cost for all categories of coverage, or replacement cost for your dwelling and cash value for your personal property.

Many companies offer “extended replacement cost” coverage, which will pay an amount over the dwelling limit to cover cost overruns or price surges that follow natural disasters. “Most insurers offer 25 to 100 percent above the limits that appear on your declarations page,” said Amy Bach, executive director of United Policyholders. This could be included in your policy or offered at additional cost as an “endorsement.”

Some companies offer “full” or “guaranteed” replacement cost coverage, which will pay whatever it costs to rebuild your home without limit. This is not common except for high-end policies.

If your agent says you have extended or guaranteed replacement cost coverage, have him or her point it out in your policy and ask which coverages it applies to.

Also find out whether your policy will pay to bring your home up to current building codes. If not, you might need to purchase a building code upgrade. If you expand or substantially improve your home, be sure to notify your agent.

A rare need

Unless their home is destroyed by a fire, most homeowners will never exhaust their policy limit, Bach said. “It’s really important not to be underinsured if you are in a wildfire area.”

Although some insurance companies have been accused of overestimating replacement costs to increase profits, others have been accused of underestimating to sell more policies.

A Marshall & Swift study updated in 2014 found that 64 percent of U.S. homes are undervalued by an average of 19 percent, Brydon said.

“Competitive pressures” lead some companies to underestimate replacement costs because the vast majority of people “will never need every cent” of coverage, Bach said.

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