

Consumer Counselor

Insurance Information for Michigan Consumers

Homeowners Insurance Replacement vs Repair Cost Policies

Homeowners insurance is a “package” policy which is made up of two basic parts:

1. **Property insurance** - Insurance that protects your dwelling and personal belongings in case of fire, theft, vandalism, etc.
2. **Liability coverage** – Covers losses for which an insured is legally liable. For homeowners insurance, liability coverage protects you against financial loss if you are sued and found legally responsible for someone else’s injury or property damage.

There are two types of homeowners insurance policies offering different kinds of property protection: **replacement cost policies** and **repair cost or market value policies**. Both types offer the same kind of liability protection. The two types differ in the amount and type of property protection coverage. Following is a description of the two types of homeowners policies.

Replacement Cost Policy

Replacement cost policies are what most people mean when they say “homeowners insurance.” This type of policy generally provides more complete coverage for your money. The amount of insurance you buy is based on what it would cost to replace your property.

A replacement cost policy will pay the amount needed to replace, rebuild or repair your damaged property to its original condition with materials of the same kind and quality. For example, if your hardwood floor is damaged, it can be replaced with the same type of wood. If you do not repair, rebuild, or replace the damaged property, the

insurance company is only required to pay you what the property was worth before the damage. This amount will be less than the replacement cost because it will subtract an allowance for depreciation.

By law, a company can refuse to sell you a replacement cost policy if your property is not worth at least \$35,000. You can also be turned down for this type of policy if you refuse to buy enough insurance to cover 80% of the replacement cost of your property.

Frequently, damage to property does not result in a total loss. Insuring at least 80% of the replacement cost of your home will cover most losses that may happen. Most companies require you to carry insurance equal to at least 80% of the replacement cost of your home or else they will not pay the full cost of repairing, rebuilding, or replacing a partial loss. If you do have a serious or total loss, you will not be paid more than the total amount of the policy.

When the cost of replacing your property is much higher than what it is currently worth, an insurance company may not want to sell you a replacement cost policy. If the company chooses not to offer you a replacement cost policy, it must offer you a repair cost policy instead.

Repair Cost (Market Value) Policy

This type of policy pays to replace, repair or rebuild your damaged property to a condition similar to what it was before the damage, using contemporary materials. For example, your damaged plaster walls may be replaced with drywall.



Like the replacement cost policy, the repair cost policy also requires that the property be repaired, rebuilt, or replaced. Otherwise, you will be paid only the depreciated value of the property before it was damaged. If you have a serious or total loss, you will receive no more than the maximum amount of the policy, which is the market value of the property. This will likely not be enough to repair, rebuild or replace the property to its original condition.

In order to qualify for a repair cost policy through a regular company, your property must be worth at least \$15,000 and you must buy an amount of insurance equal to the property's market value.

How to Decide What You Need

When you are deciding which type of policy suits your needs, consider what your house is worth, how much it would cost to replace it, and how much you can afford to spend for insurance.

For example, if you have a newer house, you probably would want to return it to its original condition if it were damaged. In this case, a replacement cost policy would be a good choice.

On the other hand, because older homes are often built with unusual, hard-to-get or expensive materials, they sometimes have a very high replacement cost. They sometimes do not have an equally high market value, however. If the market value is small when compared to the replacement cost, and it is not important to return the property to its original condition, you may wish to buy a repair cost policy.

In the case of a partial loss, for many people a repair cost policy will provide the same coverage as a replacement cost policy. If you have a total loss, a repair cost policy will pay you the market value of your home. This will probably not be enough to replace it.

Both the repair cost and the replacement cost policies protect you from a wide variety of possible losses and protect both buildings and their contents.

What to Do if You Cannot Get Homeowners Insurance From a Regular Company

The Essential Insurance Act provides these two choices so that homeowners insurance will be available to every eligible person in Michigan. The Insurance Counselor entitled "Homeowners Insurance: Are You Eligible?" explains who is "eligible" for homeowners insurance.

If you are unable to get homeowners insurance through the regular market, you may ask your agent to apply to the Michigan Basic Property Insurance Association (MBPIA). The MBPIA was created to provide property insurance to qualified persons who cannot get insurance in the regular market. If you are qualified, you can get insurance through the MBPIA, which is basically the same as insurance from regular companies, up to a specified maximum amount. The Insurance Counselor entitled "Michigan Basic Property Insurance Association" gives more information about the MBPIA.

REMEMBER, if one company or one agent does not offer you the type of policy you want and need, SHOP AROUND. Be sure to get the best combination of price, coverage and service for your money.

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