

CO-INSURANCE

“What You Don't Know Could Hurt You”

The term "coinsurance" when used in the context of **property** (commercial building – your home) insurance has an altogether different meaning than in other coverage like health insurance. Here, coinsurance is the percentage of value that the policyholder is required to insure. A building with a value of \$1,000,000 and a policy with a 90% coinsurance clause must be insured for at least \$900,000 or if it is a 80% coinsurance clause it must be \$800,000.

To make life more complicated, "value" is determined at the time of the loss. If the amount of insurance is found to be under the coinsurance percentage then a penalty is applied reducing the claim payment. This hurts the policyholder.

Using our building and policy mentioned above, as an example, illustrates the point. If the policyholder decides to buy \$500,000 of insurance and a \$200,000 fire occurs the claim is calculated by dividing what was purchased (\$500,000) by what should have been bought (\$800,000). The result in this case is 62.5%. The factor is multiplied by the amount of the loss. The calculation works out:

Building valued	\$1,000,000
Building insured for	\$ 500,000 with 80% co-insurance

At time of loss, the insurance looked at the real building value (\$1,000,000) time your co-insurance of 80%. Then the minimum value should have been \$800,000. Since you insured it for \$500,000, your penalty will be $\$500,000/\$800,000 = 62.5\%$. This penalty factor is going to be used to pay your total claim of \$200,000 or a payment of \$150,000.

$$\$200,000 \times 62.5\% = \$125,000.$$

Thus the policyholder, you, will receive \$125,000 (less any deductible) for the \$200,000 claim.

Almost all property insurance policies contain a coinsurance clause. Building insurance, contents coverage, computer coverage, inland marine policies, business personal property floaters all contain the penalty clause mentioned above. Some require 100% of the value!

In property insurance, coinsurance could only reduce the settlement or have no impact. In some policies you could elect to eliminate the coinsurance clause for almost no premium. If the insurance company charges you to eliminate the coinsurance it could be worth the extra premium.

If you have any questions don't hesitate to contact me.

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