Leveraging ITV and Replacement Cost Tools in Structural Claims

Xactware User Conference 2011

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Agenda

- The value of insurance to value (ITV) in a claims environment
- Best practices for insuring to value
  - 360Value - Underwriting
  - Xactimate - Claims
- Summary
- Question and discussion
Insurance to Value: Defined

Insurance to value is achieved when the coverage limit on a building equals the cost to rebuild the structure in the event of a total loss.

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<tr>
<th>Replacement Cost Estimate</th>
<th>$100,000</th>
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<td>Coverage A Limit</td>
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**Insured to Value**

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15% Underinsured*

*$100,000 - $85,000 = $15,000 underinsured;
$15,000 / $100,000 = 15% underinsured.
Underinsurance is an Issue. Why?

Assume coverage is $100K, but replacement is $135K. How do you bridge the gap?

• Add 5% debris removal
• Add an additional 20-25% for expanded (but not full) replacement cost protection
• Add a few percentage points for inflation.
• Conclusion: you’re probably at the $135K you need.

BUT…

• You collected premium for a $100K risk but paid $135K (assuming/structure payments only).
• Then add contents, loss of use, etc., to the payment stream…

It’s easy to see how underinsurance begins to become a problem.
Impacts of Underinsurance

- **Homeowner:**
  - Inadequate protection at time of loss.
  - Policy “safety nets” (debris removal, inflation factoring, conditional replacement cost provisions) may help, but not always.
  - Customer satisfaction and policy retention are impacted.

- **Insurer:**
  - Collected inadequate premium for loss.
  - Loss ratios increase resulting in possible policy rate increases.
  - Customer retention suffers.
  - Growth and expansion efforts suffer.

- **Conclusion:**

  *Underinsurance can lead to premium leakage and enterprise wide underperformance.*
Impacts: claims environment

- Insufficient coverage:
  - Homeowners pay out of pocket
  - Customer dissatisfaction

- Homeowner is not fully indemnified

- Larger payments for partial losses than appropriate for the premium
Insuring to value helps ensure adequate protection for the homeowner in the event of a total loss.
Impacts: Underwriting & Product Environments

- Inadequate premium collection
- Customer dissatisfaction
- Inadequate reserves
- Reduced satisfaction and retention
- Reduced growth
- Reduced profitability
ITV Benefits Insurers by via Adequate Premium, Reserves & Profitability

Annual rate hikes

Increased base deductibles

Excluded coverage

Reduced or eliminated discounts & credits

ITV lessens the likelihood for:
Best Practices for ITV Throughout the Life of the Policy

- Starts with education:
  - *What ITV is*
  - *Why ITV is important*
  - *How to achieve ITV*
  - *Who benefits from ITV*

- ITV & Replacement Cost ≠ Market Value

- Gather accurate property information

- Involve the homeowner: verify details at the start, monitor updates, additions, etc.

- Maintain ITV: annual recalculation or inflation factors
ITV is a Moving Target

Out-of-date property characteristics impact costs

Improved construction techniques impact costs

New and better materials are introduced

Labor and materials costs are constantly changing

Energy prices fluctuate with changes in demand
Achieving ITV: RC Estimates Based on Current, Reliable & Localized Cost Data

- 360Value’s cost database uses the latest building materials & techniques at the **component level**
- Costs are localized at the **5-digit zip** code level
- Replacement costs are **reconstruction costs**, not new construction costs
- **Monthly cost updates** provide current cost information
Component-Based Estimates Help Determine Proper Coverage for Specific Structures

Buildings vary in labor, materials & equipment components needed to rebuild.

**Component-based** replacement cost estimates are a critical component of insuring to value.
Reliable Component-Based Estimates: 3 Key Variables

- Address
- Year Built
- SQ FT
- Number of Stories
- Roof Shape
- Quality of Construction

Localized, current, and detailed labor and materials reconstruction costs
True Component-Based Replacement Cost Estimates

- Residential, commercial, and agricultural properties all in one tool
- Includes all material and labor costs needed to re-build the structure
- Generated using a detailed component driven cost database

Sample of components used in an estimate
Xactware uses a Proprietary Process to Research Reconstruction Cost Pricing

Real-Time Feedback
(Field-estimator feedback based on usage)

Bottom-Up Method
(Independent material and labor surveys)

Top-Down Method
(Installed Unit Cost Surveys)

Cluster Analysis Engine

~ 50,000 Contractor Users
~ 18,000 Independent Adjuster Users
~ 24,000 Insurance Carrier Users
~ 40,000 Material, Equip. & Labor Suppliers

More than 60,000 contractor surveys annually
More than 22 million claims estimates to date

Detailed Pricing
• Material
• Labor
• Equipment
• Assembly items
• Market conditions
Underwriting: Estimate Replacement Cost at Point of Sale

- Address
- Year built
- Square footage
- Quality of construction
- Number stories
- Foundation type
- Foundation shape
- Exterior wall construction
- Roof shape
- Roof cover
- Garage/carport
- Number of baths
- Etc.
Underwriting: Update Replacement Cost at Renewal

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![360Value](image)
Underwriting: Update During the Claims Process

- Is coverage sufficient?
  - If not, why?
  - Is loss settlement impacted?
  - Is homeowner satisfaction impacted?

- Verify property characteristics; revise if necessary.
- Update the replacement cost estimate.
Claims: Support Underwriting During the Claims Process

Inform Underwriting of property aspects that may impact premium and risk:

- Is there a pool, trampoline, or other hazardous structure?
- Did the homeowner add an addition or garage?
- Is there an unknown business operating on site?
- Did a new dog join the family?
- Is the property in disrepair?
Claims: Insuring to Value in a Claims Environment using Xactimate

- Quickly and efficiently verify property characteristics on site.
- Complete a “valuation” assignment in Xactimate.
- Consider completing an “Underwriting Checklist” to advise underwriters of risks, hazards, condition deficiencies.
- Helps reduce Underwriting inspections.
Bridging the Gap Between Claims & Underwriting

360Value & Xactimate share the same building cost data.

- Used by 80% of insurance repair contractors
- Used to write more than 60% of homeowner claims
- Used for remodeling & contents estimation

- Used by 4 of the top 10 U.S. insurers
- Used to write approximately 40% of replacement cost estimates

Estimating replacement costs in 360Value and claims losses in Xactimate will better align Underwriting with Claims and improve profitability.
Decision: Which Tool? Valuation or Estimate?

Choosing to determine ITV (via 360Value or Xactimate) is more important than choosing which tool:

- Why? *ITV is important*
- 360 Value & Xactimate *can both do the job*
- 360Value & Xactimate:
  - Share the *same pricing data*
  - Share the *same costing engine*
  - Share the *same valuation analytics*
Claims: Valuation Tool in Xactimate

- Answer *a few questions* to generate a residential valuation
- **Save time** when creating an estimate for large loss
- **Generate a valuation** as an ITV tool in the claims process.
Be as granular as you want regarding structure details (if they are known)

A few minutes invested in the valuation translates into a lot of time saved later adding line items to an estimate
Xactimate Valuation Reports Add Value

Valuation reports:

- Contain a wealth of information
- May be used as stand-alone documents
- May be used in conjunction with an estimate
Xactimate: Create an Estimate from the Valuation

- The rooms, systems, components, and structures that were created in the valuation are available to the user as common Xactimate items in the created estimate.

- Let the valuation do the ‘heavy lifting’ when creating an estimate for a large or total loss.
Summary: Insuring to Value with Xactware

- Client-Focused Customer Service
- Intuitive and Easy to Use
- Leading-Edge Technology
- Superior Building Cost Information
- Component Based Estimates
- Supports Insurance Value Chain
Questions & Discussion