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JOURNAL REPORTS: WEALTH MANAGEMENT

Insurers Aim to Fill In the Disaster Gap

As natural disasters increase, homeowners look for more ways to cover more expenses

Catastrophic parametric insurance is increasingly being marketed in areas with natural disasters and fires such as the Camp Fire in Paradise, Calif., in 2018. PHOTO: HECTOR AMEZCUA/SACRAMENTO BEE/ZUMA PRESS

By Lisa Ward

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One of a homeowner's worst nightmares is learning that major expenses resulting from a natural disaster aren't covered by their insurance policy.

As hurricanes, wildfires and other natural disasters have increased in recent years, so has marketing of insurance products designed to offer policyholders more coverage than typical homeowners policies give.

With some policies, there is no deductible and policyholders can spend the money on any disaster-related expense, say, on plywood or finding emergency accommodations. Payouts for such policies tend to be small and linked to the severity of the disaster itself, not actual damages, which is partly why they are not seen as a substitute for a standard homeowners policy.

Other insurers selling more standard homeowners policies, meanwhile, are making efforts to bridge gaps in coverage that result from high hurricane deductibles and from outdated estimates of what it costs to rebuild.

“It’s great that the market is experimenting,” says Benjamin Collier, an assistant professor at Temple University’s Fox School of Business. “Insurance typically covers property, but households have a variety of additional challenges following a disaster.”

One type of policy consumers are seeing more of is catastrophic parametric insurance. Unlike traditional indemnity insurance, parametric policies pay a predetermined amount of money when a trigger is met—such as a named storm, certain wind speeds, geological readings, waterlines, flood depths or burned acreage. No claim needs to be filed to receive the payout. And while such payouts tend to be small, they can be helpful when disaster-related deductibles, like those for hurricanes and earthquakes, leave homeowners responsible for tens of thousands of dollars before any payout begins.

The parametric model is not new. Low-income farmers in developing countries have also used parametric policies for catastrophic coverage. Companies and municipalities have used them to recoup loses, like drops in sales or tax revenues, after natural disasters.

One reason parametric insurance may be of growing interest to homeowners in areas particularly vulnerable to hurricanes, earthquakes and floods is that there are frequently large gaps in their catastrophic insurance coverage; supplemental insurance for flood or earthquake policies tends to be expensive, or their homeowners policies feature very high deductibles that pertain specifically to disasters like hurricanes.

Assured Risk Cover is a five-year-old company that sells a parametric-hurricane-insurance policy in Florida. Founder and CEO Alok Jha says his company can help pay for damage to a home, but also out-of-pocket costs, evacuation costs, food spoilage and generator rentals. The policy, marketed under the name “Storm Peace,” has no deductible. It provides coverage up to $60,000 and bases payouts on a hurricane’s strength and the home’s distance from the storm. The company sends a text message to customers within 24 hours of the storm and makes payment within a day of receiving their response, provided that it already has the customer’s payment information.

While his product is often used along with traditional home or renters insurance, Mr. Jha says, it can be a stand-alone product, say, for residents of mobile homes who may have a hard time finding hurricane insurance elsewhere. The policy costs about 7% of the total coverage, he says.

Industry experts say there are some drawbacks to these types of policies. The amount of a payout, for example, is determined by the policy, not the specific amount of destruction. “The payment could be lower or higher than the actual damages,” says Carolyn Kousky, executive director at the University of Pennsylvania’s Wharton Risk Management and Decision Processes Center, a research institute focusing on risk.

For example, a tropical storm with a lot of rain and flooding but not enough wind speed to count as a name hurricane could fail to trigger a payout if the insurer used a gauge like wind speed to determine reimbursements, Ms. Kousky says.

Another parametric product is Jumpstart, which provides coverage for earthquakes in California and is underwritten by Lloyd's of London. The company, founded in 2015, provides coverage up to $10,000 for each adult in a household. If the earthquake reaches a certain threshold measured by the U.S. Geological Survey, funds will be distributed, usually via direct deposit, within one to three days and can be used for any expenses the policyholder chooses.

The cost of Jumpstart policies varies by ZIP Code, but the population-weighted average cost is about $20 a month or $240 a year, says CEO Kate Stillwell. Only about 10% of California residents have earthquake insurance, according to the California Earthquake Authority.

In some cases, homeowners might be better off making sure that the value of their current insurance policy reflects the true value of their home, especially if they have updated or upgraded, or if property values in the area have appreciated.

"The price you paid for your home—or the current market price—may be more or less than the cost to rebuild; and if the limit of your insurance policy is based on your mortgage (as some banks require), it may not adequately cover the cost of rebuilding," says Loretta Worters, a spokeswomen for the Insurance Information Institute, an industry organization that seeks to improve public understanding of insurance.

CoreLogic, a research firm in Irvine, Calif., estimates that roughly 60% of homeowners in the U.S. have less coverage than it would cost to completely rebuild their homes if destroyed in a natural disaster. If policyholders lack savings to fill this coverage gap, they may be in a particularly perilous position because it can also be difficult to borrow money after a natural disaster.

The California Department of Insurance found that owners of many homes damaged by fires in recent years were underinsured. It wasn't "because people were trying to lower their premium or pay less for coverage," spokeswoman Nancy Goldberg says; it was because they had underestimated the value of their belongings and the cost to rebuild their home. Some, she says, had not checked on their homeowners coverage for a decade or more to add more coverage to reflect increased value from improvements and renovations.

Meanwhile, some insurers are working on reducing deductibles. In Florida, typical hurricane deductibles tend to range from 2%, 5% or 10% of the home's insured value or replacement cost. And many homeowners don't realize their hurricane deductible is separate from and much higher than the deductible for other kinds of damage.

During hurricanes Irma and Michael, a lot of customers did not understand that their hurricane deductible was far larger than their standard deductible, says Barry Gilway, president and chief executive of Citizens Property Insurance Corp.

To bridge that gap, some insurers now offer lower hurricane deductibles or separate hurricane-deductible insurance, which helps cover amounts not covered by another policy due to a hurricane deductible, Mr. Gilway says.

Zurich American Insurance Co.'s Cat4Home policy offers Florida homeowners coverage for hurricane deductibles up to $100,000. Any damage caused by incidents that are covered under the primary policy would be covered, which typically excludes flooding. The cost of such coverage generally depends on the home's overall value and location, the company says.

Will Kastroll, founder of the Naples, Fla.-based insurance agency Harbour Insurance, suggests to customers shopping for home insurance another way to reduce hurricane deductibles: a policy with a step-down deductible credit. If the deductible goes untouched, Mr. Kastroll says, it shrinks over time, usually several years.

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