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What Coverage Limits Do You Need for Homeowner's and Auto Insurance?

Most people avoid thinking about scenarios that would cause an insurance claim - our homes damaged by fire or tornado, someone injured on our property, or family members hurt in an auto accident. However, it is necessary to give some thought to these upsetting possibilities to ensure that you are adequately prepared and protected in the event of a catastrophe. Reviewing your insurance coverage will also clarify if there's a need for an additional umbrella policy for extra protection. So, let's try to summarize some of the basics on coverage limits.

Homeowner's Insurance

Homeowner's insurance covers three areas: damage to the home, damage to the contents of the home (personal property), and your liability for injuries to others.

Prior to obtaining homeowner's insurance, it's a good idea to stop and consider exactly what you want the insurance to cover. You may want coverage just to pay off the mortgage in the event you can no longer occupy your home. It's more likely you'll want to continue living in your home after a claim or sell it at market value, so you will want your insurance to pay for repairs caused by wind, fire or some other covered peril. In most cases, reconstruction means you will need insurance that actually covers more than the home's market value.

Replacement value, which is the cost to reconstruct a damaged home, is typically higher than the cost of buying a similar home on the market due to the specialized nature of reconstruction as opposed to new construction. For example, in reconstruction there is an initial cost of debris cleanup. New construction starts at the bottom and builds up, but with reconstruction it is often necessary to take off the roof and build down, which is more expensive. Additionally, after a natural disaster, construction costs may rise due to increased demand. Keep in mind that your insurance can cover not only the costs to rebuild, but also the costs for you to live elsewhere, if necessary, while the home reconstruction is completed. An experienced insurance agent can help you assess your coverage needs as well as determine available coverage based on the age and condition of your home.

Also, you will need to consider whether you want replacement coverage for clothing, furniture, appliances, and other personal property inside your home. Without replacement coverage, your coverage for personal property is depreciated by the age and wear of the items lost. Due to depreciation, the computer you paid \$500 for three years ago may be valued at only \$150 or \$200, which is all the insurance company would pay if you don't have replacement coverage.

Some insureds will need more coverage for personal property (contents) than their policy provides. The amount of personal property coverage is usually limited to 70% of the coverage limit for the structure. For instance, if you have an art collection, antique furniture, jewelry, or other valuable possessions, talk to your agent about supplemental coverages, such as fine arts or scheduled property endorsements, to adequately protect your investment in these items. The cost is modest for the extra protection.

Liability limits generally start at about \$100,000; however, some experts recommend that you purchase at least \$300,000 worth of protection, which covers personal liability for damage to property or personal injury caused to others. The additional coverage also help to protect your assets in the event you are found liable in a personal injury lawsuit. Additionally, you may want to consider purchasing a separate liability umbrella policy (discussed below).

Auto Insurance

There are six different types of auto insurance coverage. Three relate to liability, two for damage to your vehicle, and one provides specific coverage for accidents involving you and an uninsured or underinsured driver.

Collision coverage covers the costs of damage to your vehicle caused by collisions with other cars or objects; comprehensive coverage covers theft or damage to the vehicle caused by events other than a collision with another car or object. The amount of coverage you need depends on the value of your vehicle.

Auto liability insurance is required in most, if not all, states, but the liability limits that drivers are required may not be enough to protect your assets. Even one serious injury caused by an accident for which you are liable could cost into the six figures, or more in extreme cases, just for medical expenses. And the amount only increases if there are more injured people. It's easy to see that the \$50,000 of per accident liability coverage required in many states would not be enough to pay all the costs of property damage and bodily injury. Auto insurance companies recommend that you have \$100,000 of bodily injury protection per person and \$300,000 per accident. If your personal net worth is more than \$300,000, consider buying additional liability auto insurance.

What About an Umbrella Policy?

Unfortunately, even with our best intentions and efforts, accidents may happen for which we are legally at fault. Medical costs can skyrocket. If someone were permanently disabled by an accident, the expenses of lifetime care could be astronomical. If someone killed left behind survivors who were depending on that person for support, you could be liable for damages to the survivors. Be aware that any costs not covered by insurance will come out of your pocket. Hence, you could be forced to sell property or to turn over part of your earnings for years to come, perhaps the rest of your working life, to an injured party.

There are limits on the amount of liability coverage available as part of your homeowner's and auto insurance policies. If you have total assets valued at more than these limits - including, say, your vacation home, investments, rental property, boats and vehicles -- or if you have a high income, an umbrella policy offers a great deal of protection for a relatively low premium.

In addition to the assets you want to protect, you may want to consider your risk of being sued. Do you live in a state that is particularly friendly to plaintiffs? Do you have frequent guests on your property? Do you have a swimming pool, trampoline, swing set, or other sports equipment in your yard? Do you have a dog that is overly protective of your property? Are you or any of your household members aggressive, fast, or careless drivers? If so, your risk is greater that someone may be injured, perhaps very seriously, and you would be legally at fault. In fact, any situation that could result in serious injury, long-term physical impairment, psychological damage or death could put your financial well-being at risk.

Once the liability limits are exhausted on your home or auto policy, your umbrella policy takes over and provides another layer of liability protection. Policies typically start at \$1 million with coverage available up to \$10 million. Premiums start at around \$300 a year - less than a dollar a day for a great deal of protection.

The best way to determine whether you need an umbrella policy is to discuss your financial status,

lifestyle, and current and future assets with your insurance agent. Ask him or her to review the liability limits in your current policies and suggest the best strategy to ensure protection of your assets in the event of an injury for which you are legally liable.