Colorado fire victims face high building costs exceeding insurance coverage

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Losses expected to reach $1 billion in fire that swept through suburbs between Denver and Boulder

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Rising construction costs will push the price tag for rebuilding after Colorado's most destructive wildfire beyond the insurance coverage of some homeowners, according to construction, insurance-industry and government officials.

Losses are expected to reach $1 billion in last week's Marshall Fire, which swept through the suburbs between Denver and Boulder, Colo. Rebuilding the roughly 1,000 homes destroyed and repairing damage to hundreds of others will strain already stretched builders and supply chains.

The majority of homeowners in the burned neighborhoods are thought by insurers to have enough coverage for most rebuilding costs. That is in contrast to rural areas in Kentucky hit by tornadoes last month, where some working-class homeowners had little to no insurance.

In both places, labor shortages and the magnitude of the damage will make it more difficult to rebuild, said Erin Collins, a senior vice president at the National Association of Mutual Insurance Cos., a trade group. "There are individuals in both impacted areas that are either uninsured or did not have adequate coverage in place to compensate for their losses," she said.

Some two-thirds of fire victims typically are underinsured, according to surveys by United Policyholders, a national nonprofit consumer-advocacy group based in California. A survey of people affected by wildfire in 2020 in Colorado's Grand and Larimer counties revealed shortages often amounting to hundreds of thousands of dollars.

A major cause is the difficulty for homeowners in determining how much coverage they need, said Daniel Schwarcz, a professor at the University of Minnesota Law School who has studied homeowners insurance. Part of the problem is that consumers have wide choice, and many opt for cheaper policies to hold down their annual premiums.

For buyers, “there is incredibly limited transparency” in figuring out what a limit should be, he said. Many consumers assume that an agent or insurer has a financial incentive to sell them more coverage than they need, he said. But some agents promote cheaper policies because they don’t want to lose a sale to a rival.

In some catastrophe-prone areas, insurers are trying to limit their potential losses, said Amy Bach, executive director of United Policyholders. “We know of many situations where consumers ask for higher limits and are turned down,” she said.

Last week’s blaze was the most destructive wildfire in Colorado history in terms of numbers of structures destroyed, according to disaster-modeling firm Karen Clark & Co. Its $1 billion estimate of insured damage includes homes in the areas of Louisville and Superior and unincorporated Boulder County as well as a large commercial area with a destroyed shopping center and hotel.

Colorado Insurance Commissioner Michael Conway said that “there is likely going to be an issue about underinsurance,” stemming from both inadequate coverage amounts to start with and a continuation of inflation. That said, over the next two years as construction gets under way, “there is so much that will be in flux about inflation, building costs, labor costs that when we get to the point we are rebuilding these homes, the world will likely look much different.”

He noted that the Federal Emergency Management Agency provides some financial assistance for underinsurance, though the agency typically doesn’t act on a consumer’s request until after a carrier has wrapped up its total payouts.

Insurers acknowledge that their policies’ proceeds won’t always be sufficient to cover the damage, but they say their agents have worked hard in recent years, in the face of other high-profile disasters, to promote purchase of policies with the most-generous terms.

As in many cities across the country, the Denver-area housing market has been red-hot in the past year.

Low mortgage rates drove robust home-buying demand that vastly outpaced the number of properties for sale, pushing up housing prices.

Builders increased activity in response, with housing starts in the Denver metro area up 30% in the third quarter from a year earlier, according to housing-market research firm Zonda. But they have been slowed by labor shortages and supply-chain issues. Nationally, the cost of home-building materials rose 21% in November from a year earlier, while residential construction wages rose 8.1% in October from a year earlier, according to a National Association of Home Builders analysis of government data.

Boulder County is the most difficult and expensive area to build new homes in the Denver metro area, due to limited land supply and higher regulatory costs, said John Covert, principal of advisory at Zonda. As homes in the city of Boulder have become more expensive, demand has risen in the neighboring suburbs, including Louisville and Superior, he said.

Building costs in the current market are especially volatile due to supply-chain disruptions, said David Sinkey, chief executive of Boulder Creek Neighborhoods, a builder based in Louisville.

“Predictability around cost is just almost impossible right now,” he said. “I think what’s starting to dawn on a lot of people is the insurance coverage is going to be a lot lower than the current cost to build.”

Underinsurance can lead to delays in reconstruction, and some people whose homes were destroyed in Boulder-area wildfires in 2020 have yet to rebuild. “My wounds were ripped back open last Thursday, and I relived every moment of the trauma” of the blaze that burned down his Boulder house in October 2020, said Kevin Mott, a dermatologist who is living in a recreational vehicle for now.

His insurance came up short, and his rebuilding was delayed while he lined up financing. He had a $900,000 limit for the dwelling itself, plus $700,000 for contents. His new home will cost about $2 million, including upgrades to meet new local building regulations, he said.

With the exception of insurers selling to rich homeowners, most carriers have eliminated once-common and relatively generous guarantees to pay the full cost of rebuilding. Instead, in the event of a shortfall, some policies offer to pay a fixed amount, such as 20%, above a dwelling’s insured value.

Many insurers, including State Farm and USAA, also include some type of inflation protection. But they still rely on homeowners to update their policies to account for remodeling or expansion.

Source: https://uphelp.org/colorado-fire-victims-face-high-building-costs-exceeding-insurance-coverage/ Date: April 26, 2024