Small insurers are growing in Louisiana. Will more go insolvent after the next big storm?

NOLA

The dozen insurers that failed after two busy hurricane seasons left hundreds of thousands of Louisiana homeowners scrambling for new insurance policies at a time when premiums were soaring.

A review of new state market share data and financial filings shows the void left by the failed companies has largely been filled in two ways. Some of the market has been gobbled up by new firms that structurally resemble the ones that failed. And the rest has mostly gone to Louisiana Citizens, the state-backed insurer of last resort, which by law charges policyholders above-market rates.

All of it raises further concerns about the health of Louisiana's insurance marketplace.

Most of the fastest-growing private companies are rated by Demotech, the firm that rated all 12 of the companies that went belly-up after the storms of 2020 and 2021. In the insurance world, the gold standard is A.M. Best, which rates larger firms like State Farm and Allstate. Researchers have recently raised red flags about Demotech's ratings, suggesting the companies it rates tend to be of "significantly lower quality," are often undercapitalized and have a riskier book of business than other insurers.

Those attributes were common among the insurers that collapsed here, many after rapidly gaining market share in the years leading up to 2020. Several of the new companies share another similarity with the failed firms: They use an affiliate model that allows them to farm out many functions – and premium dollars – to less-regulated affiliates, an arrangement that has raised concerns among some regulators and some observers of the industry.

Louisiana lawmakers are considering a bill that would require those affiliates to report more information to the state, legislation filed after The Times-Picayune | The Advocate highlighted the practice.

The 12 failed companies together held about one-sixth of Louisiana's market.

Of the 10 companies that have gained the most in market share from 2019 to 2023, five are smaller regional firms rated by Demotech. Four of them use the affiliate model. Four of the biggest gainers, meanwhile, are larger national insurers, although one of them, AllState, simultaneously shrank some of its subsidiaries, offsetting the gains.

The last company is Citizens, which gained more market share during the period than all but one company.

Differing opinions

Insurance Commissioner Tim Temple, a Republican who is pushing a sweeping package of bills to make Louisiana's laws easier on insurance companies, has vowed to bring more carriers to the state, a dynamic he says will stabilize the market and make rates as affordable as possible.

Temple has criticized the rise of companies that write what he calls "cheap insurance." Such firms are part of what he called a "false economy" of undercapitalized insurers that grew fast by taking state grant money and huge batches of Citizens policies before going bankrupt.

Insurance Department spokesperson John Ford said the agency is confident that its new efforts to bolster review of reinsurance contracts and to ensure risk among insurers is diversified will prevent another cascade of collapses.

But Ford also said the smaller firms have grown in part because Louisiana has an unappealing "environment" that Temple is seeking to fix, by making it easier for insurers to drop policyholders and raise rates, among other things.

"That's one of the reasons you've seen all these Demotech firms move in," Ford said. "We need insurance coverage. We're not attractive enough for these larger companies. So we are relying more on these Demotech companies."

To be sure, some bigger companies have also grown their presence here, and, unlike in Florida, most of Louisiana's homeowners market is still controlled by large carriers like State Farm and AllState.

But the continued rise of smaller insurers with less capital has drawn concerns from consumer advocates, who say it underscores the folly of Louisiana's long-held approach of propping up the private market at all costs.

Amy Bach, executive director of the consumer rights group United Policyholders, said some small firms that move into risky areas view premium dollars as "free money," and get into trouble when it comes time to pay claims. And she pushed back against Temple's strategy of making it easier on insurers, saying the state needs to embrace a strong "hybrid" government and private-sector solution.

She said the private market has failed badly at providing affordable and reliable insurance in storm-prone areas like Louisiana's coast.

"It's screaming for a government solution," Bach said. "Not throwing people at questionably financially strong entities."

Echoes of post-Katrina landscape
The rise of smaller companies – and the retreat of bigger ones – in some ways recalls what happened to the insurance landscape after Katrina.

Back then, Louisiana welcomed smaller companies that concentrated on coastal areas, offering them taxpayer-funded grants and handing over huge batches of policies from Citizens. One such company, Maison, told investors in 2014 that the Bayou State offered a unique opportunity to make money in years without major storms. By 2022, Maison had failed, along with 11 others, several of which had assumed policies from Citizens "depopulation" or gotten grants from state incentive programs.

More recently, a new round of smaller companies focused on coastal areas has materialized. Five smaller companies have rapidly gained Louisiana market share in the past five years: SureChoice, CURE, Allied Trust, Safepoint and Gulf States. The oldest was founded in 2013; the newest, CURE, sprang up in 2022.

All five have struggled to turn a profit in recent years, according to a review of financial statements. Collectively, the companies have posted net losses of $117 million since 2021, when Hurricane Ida caused billions in damages. All five companies posted losses in 2023, according to data from AM Best. However, it is difficult to tell whether investors are making money anyhow, because most of the companies send millions of dollars every year to affiliates that often serve as the profit centers for the companies but are less regulated by the state.

Brian Keefer, CEO of Allied Trust, said not all smaller companies are at risk of collapse when a big storm hits. He said his company doesn't participate in Citizens depopulation, noting many of the failed companies did. And he defended the use of affiliates, saying that while they can be abused, the regulator should be able to monitor them.

"It's not necessarily the structure, it's about how you operate in that structure," Keefer said. "It's about how responsible you are in managing your business."

As small firms grow, some behemoths are choosing to shrink their footprint. State Farm, for instance, lost the most market share of any company over the time period. A spokesperson said the company, which retains the largest share of the state's homeowners market, is "committed to our Louisiana customers."

Benjamin Albright, CEO of the Independent Brokers & Agents of Louisiana, said there's nothing "inherently wrong" with a Demotech-rated carrier, and that small companies can play a role in the market. Their fate will depend on whether they are buying enough reinsurance – protection for catastrophes – and whether the state Department of Insurance is regulating them properly, he said.

Most agents would prefer to write business with big carriers rated by A.M. Best, Albright said.

"Unfortunately, most of the large, national carriers choose not to write business in our state because of the combination of our catastrophic wind exposure with the many years of oppressive legislation, litigation and regulation," he said.

Paper raises concerns
The rise of the smaller companies coincides with growing worries about their financial strength.

At a Citizens board meeting last year, Albright's group raised concerns that Citizens was continuing to let Demotech-rated companies take vast numbers of policies, even though state law calls for a B+ rating from A.M. Best.

Still, the board approved the transfer of thousands of policies to Safepoint and CURE.

In December, researchers at Columbia, Harvard and the Federal Reserve Board published a paper that found Demotech-rated insurers are of “significantly lower quality” than traditional insurers.

Demotech insurers have a “much higher likelihood of insolvency,” the researchers wrote, noting that in the past decade, 19% of Demotech insurers entered rehabilitation, a state supervision process that can end in liquidation. Zero traditional insurers did, the paper noted.

Demotech has pushed back on the paper, which has not been peer-reviewed, saying the findings are hypothetical.

Joe Patrelli, CEO of Demotech, said in an interview that the real reason the companies failed is because of a huge wave of litigation made easier by technology. He said that hit larger companies too, but the Demotech companies were smaller and couldn’t survive.

“Our guys went down because they were smaller and they were litigated to death,” he said.

Patrelli said his company has created a way of tracking such litigation risk and is putting it to use to better understand the litigation risk and prevent a future wave of collapses.

The month after the paper was published, Citizens gave away another batch of policies, part of its ongoing effort to trim its rolls. The board approved three Demotech-rated companies – Safepoint, CURE and Ocean Harbor – to participate. The board voted to exclude one brand-new Demotech insurer, Lilypad, from the process, over concerns it was too new to the market.

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