



United Policyholders
381 Bush Street, 8th Floor
San Francisco, CA 94104
415.393.9990
www.uphelp.org

June 24, 2013

Federal Insurance Office
Attention: Study on Natural Catastrophes and Insurance
Room 1319 MT, Department of the Treasury
1500 Pennsylvania Avenue NW.
Washington, DC 20220

Dear Commissioner McRaith and Staff;

We appreciate the opportunity to contribute to this important project. Your challenge is formidable and we hope to be of service. United Policyholders is a non-profit 501(c)3 organization that is an information resource and voice for insurance consumers in all 50 states. Through the three programs we run, we have extensive involvement in how catastrophe insurance matters are impacting consumers at the point of sale, during the claim process, and when policies come up for renewal after disasters.

Through our Roadmap to Recovery™ program we host workshops across the country in partnership with local governments and community and faith-based organizations after tornadoes, wildfires, earthquakes and floods. See www.uphelp.org. Property owners who attend these workshops share their stories, frustrations and confusion. They communicate to United Policyholders the ways in which their (increasingly various) insurance policies are not delivering the loss recovery funds they need and thought they had purchased. They communicate that the claim process feels very adversarial, and that following a loss – their premiums skyrocketed or they were dropped by their insurer. As a result, trust between property insurers and policyholders has been badly broken at a high cost to all of us.

Hard data on home insurance payouts in relation to actual damage sustained is hard to come by. The closed claim statistics that insurers provide to state regulators only reflect dollar amounts paid. They may look large and impressive, but they do not accurately reflect total amounts claimed or damages sustained. Homeowners who attended our recent workshops in New Jersey reported that their NFIP claim payouts after Superstorm Sandy were *far* below actual damage, and that they collected virtually *nothing* from their home insurers. “A few hundred dollars for spoiled food”, was the constant refrain. We urge FIO to review data from lenders and FEMA to grasp the extent to which property damage is increasingly not being covered by insurers after disasters that involve water, high winds and earthquakes.

While states and Congress have created entities that provide insurance for those who can't buy it in the private market, both the NFIP and state based plans need restructuring. They need better management, and more independence from private insurers and vendors including for-profit cat modelers. They need access to reasonably priced reinsurance and/or low interest loans to bolster claims paying capacity and solvency.

Board of Directors

Amy Bach
Executive Director

Alice J. Wolfson
Chair, Board of Directors

David Baria
Mississippi State Senator

Hon. Stanley G. Feldman
Chief Justice (RET)
Arizona Supreme Court

Larry P. Ginsburg, CFP®
Ginsburg Financial Advisors, Inc.

William H. Hedden
Consolidated Adjusting, Inc.

Jim Jones
Industry Ventures

Brian S. Kabateck
Kabateck Brown Kellner LLP

E. Gerard Mannion
Mannion & Lowe

Shirley Roberson
Non-Profit Consultant

Deborah Senn
Insurance Commissioner (1993-2001)
Washington State

William M. Shernoff
Shernoff Bidart Echeverria LLP
Ex Officio

Programs

Advocacy in Action

Roadmap to Preparedness™

Roadmap to Recovery™

1. The current condition of, as well as the outlook for, the availability and affordability of insurance for natural catastrophe perils in all regions of the United States, including whether a consensus definition of a “natural catastrophe” should be established and, if so, the terms of that definition

The current condition is excellent in most areas and fair to poor in repeat loss and coastal areas. Given current trends in the voluntary P/C market, solvency problems with quasi-public insurance entities, pending NFIP rate increases and climate change, the outlook if reforms are not implemented fair at best.

Availability

Other than in the Outer Banks and areas that have been hit repeatedly by natural disasters, some level of coverage for catastrophe perils is still *readily available* throughout the U.S. In some regions and for some perils, available policies may not cover full or replacement cost value of properties, and high deductibles may apply. In some regions and for some items, (e.g. roofs and foundations) and for specific perils, coverage is only available on an Actual Cash Value (ACV) basis, or only through an insurer of last resort/ residual market mechanism or a non-admitted carrier. It may involve a package of policies and endorsements, but coverage for natural catastrophes can still be procured. In most areas, there is still ample competition among private insurers, even after there’s been a disaster. In repeat loss areas and for certain perils, (flood and earthquake) State and Federal lawmakers have responded to private marketplace failures by creating insurers of last resort. In areas that have been hit repeatedly by wildfires, hurricanes and other weather events, there is a consistent pattern of residents being non-renewed by the insurers they’ve been with for many years. But with diligence and assistance from independent agents and brokers, state insurance departments, and occasionally, United Policyholders, people seem to be able to replace their non-renewed policies.

Affordability

Affordability is another matter. From coastal Massachusetts all along the coast south to Florida and west through Texas, property owners have been experiencing acute rate shock. So acute that a grass roots consortium of faith based and homeowner associations, consumer advocate groups and realtors have become engaged in challenging rates, rate models, risk assumptions, underwriting and “file and use” regulatory regimes. [See “South Carolina Realtors push for property insurance reform”, The Post and Courier, Page 1, April 20, 2013, and comments to FIO in support of a Coast Band Reinsurance Entity filed by the Consumer Federation of America, Hurricane Homeowners Insurance Initiative, and the Gulf Coast East Coast Homeowners Insurance Reform Coalition].

Louisiana residents who had been paying \$800 per year for insurance on their modest homes before Hurricane Katrina got hit with premiums in the \$3,000-\$8,000 range. After the 1994 Northridge earthquake, when the cost of insuring against just that one peril jumped into the thousands (on top of basic home insurance), most people deemed the protection unaffordable. Rumors are that when federal flood insurance rates increase for non-elevated homes in coastal and river areas as required by the Biggert-Waters Act of 2012, (BW12) home owners will be looking at premiums of into the five figure

June 24, 2013

Page 3 of 9

range. Most people United Policyholders has heard from have been paying \$350-\$700 annually for flood insurance.

Post disaster property insurance rate shock has led to 90% of Californians having no earthquake insurance. An increasing number of homeowners are “going bare” if their mortgages are paid off, and property insurance has become a very hot political issue in Florida, Texas, Alabama and the Carolinas.

Condition of the cat insurance marketplace

United Policyholders’ website, including our published survey results, offers ample evidence of the affordability and availability problems people in many parts of the country are now having when trying to comply with lender’s insurance requirements and protect their assets by buying adequate insurance. We also offer ample evidence of the shrinking amount of protection contained in home policies, and chronic problems in claim adjusting and payouts when people need their home insurance to recover after natural disasters. [See www.uphelp.org/surveyresults] We have previously provided your office with the results of a recent survey on affordability that we did in coordination with non-profits based in South and North Carolina, Alabama, Florida and Louisiana.

A consensus definition of “Natural Catastrophe”

The federal government and states currently have standards that are applied after weather and/or other types of events that damage or destroy property as to whether the event merits a disaster declaration. If an event causes a certain level of damage, it qualifies as a state and/or federal disaster. The declaration(s) have financial significance with regard to funds that will flow into the area through FEMA or a state office of emergency management. Property losses that reach a certain level of dollar damage and scope are deemed a disaster regardless of whether they are caused by a fire, flood or explosion. A consensus definition of Natural Catastrophe could arguably follow similar standards.

If a standardized all-perils home policy is developed for sale nationwide, either as a stand-alone comprehensive product or as Natural Catastrophe protection add-on to a basic home policy – it should not distinguish between the causes of the catastrophic loss. We need to return to a simpler form of property insurance where people know how much money their insurance will provide for repairing and rebuilding after a disaster – regardless of what caused it.

2. The current ability of States, communities, and individuals to mitigate their natural catastrophe risks, including the affordability and feasibility of such mitigation activities;

Florida, South and North Carolina have considerable experience in mitigation approaches that have proven effective in reducing property damage from hurricanes, high winds and storm surges. These steps include building code enforcement, construction techniques, and the installation of roof tie

downs, storm shutters and other features that make structures better able to resist the forces of wind and water.

California and Colorado have experience in what it takes to “harden” a structure against a wildfire and how brush clearance, vent screens and certain roofing materials can make all the difference for a firefighter working to save a home. After the Loma Prieta and Northridge earthquakes, cities, counties and the State of California invested considerable resources into establishing stronger seismic safety standards and promoting quake damage mitigation through structural improvements and preparedness education and outreach. Mitigating flood damage has at least two very simple solutions: Don’t allow new construction close to a river or ocean or below sea level, and elevate existing homes in those areas. Easier said than done.

Theoretically, states and individuals have the ability to mitigate natural catastrophe risks. In practical reality, significant barriers exist:

- A lack of consensus among experts as to the effectiveness of various mitigation techniques.
- Political and economic power wielded by real estate developers.
- Reluctance by insurers and their actuaries to adjust rates or offer discounts for mitigation.
- Private property rights.
- Property owners’ resistance to building code enforcement and forced mitigation.
- The cost of mitigation expenditures.
- A lack of financial incentives to make those expenditures, insufficient insurance discounts.
- There are multiple sources but no “official” agency, place or website where one can go to find out:
 - 1) What exposure their home has to the risk of severe to total loss in a disaster
 - 2) What specific, recommended action steps they should take, given their local risks and type of home that will reduce that exposure
 - 3) What kind of professional they should hire to make the improvements
 - 4) How much the most effective improvements should cost
 - 5) How to find the right person to do the work
 - 6) How to finance the work if they can’t afford it on their own.

Monroe County Florida is a community that strictly enforces their building codes. Through the good work of a non-profit called Fair Insurance Rates in Monroe, (FIRM), Monroe County residents are pressing insurers to recognize their hard work by giving residents a break on their property insurance.

a. The current and potential future effects of land use policies and building codes on the costs of natural catastrophes in the United States;

People who work and own primary residences in coastal areas but who have outstanding home loans need financial assistance to contend with mandated home and flood insurance that is unaffordable to them. With regard to new construction, there has to be stricter enforcement of building codes to prevent new development in areas that are at risk for flooding and storm surges. Because banks in

quake-prone regions don't mandate that borrowers buy earthquake insurance, the vast majority of residents don't carry it.

b. The percentage of residential properties that are insured for earthquake or flood damage in high-risk geographic areas of the United States, and the reasons why many such properties lack insurance coverage;

Somewhere between 88-90% of California homeowners do **not** carry earthquake insurance. While we don't know how many people in A or V flood zones currently carry flood insurance, we find that typically less than half those who attend our workshops in flooded areas carried insurance at the time of the event. A commonly held (erroneous) belief is that if a person's home has not flooded in the past, it is not at risk to flood in the future.

c. The role of insurers in providing incentives for risk mitigation efforts;

Without question, insurers need to be much more pro-active in helping customers know which home improvements will protect their homes against natural disasters. Insurers also need to incentivize their customers to make recommended home improvements by offering substantial enough discounts upon proof of completion, as well as financial and technical assistance.

3. The current state of catastrophic insurance and reinsurance markets and the current approaches in providing insurance protection to different sectors of the population of the United States;

Catastrophe insurance coverage and claim deficiencies

With the exception of a select few insurers (Chubb, Ace, and AIG) that sell all-risk policies to high net worth individuals, **all** property policies that are currently being sold throughout the U.S. have deficiencies in coverage and claim handling that manifest after natural disasters. This goes for policies that are being sold by private insurers as well as those being sold by residual market insurers, surplus lines insurers and quasi-public entities such as Florida and Louisiana Citizens, the Texas Windstorm Association (TWIA), the California Earthquake Authority, and the National Flood Insurance program (NFIP). Property owners don't necessarily expect that every single dollar of cat damage to their homes will be covered by insurance. But they are increasingly experiencing true shock at what many describe as a "second nightmare" of confronting major gaps in coverage and a claim process that for many is adversarial from the get-go.

Property insurance coverage deficiencies that emerge after natural catastrophes include caps and exclusions that cause holes people were not aware of so had no chance to plug in advance: Flood, anti-concurrent causation, earth movement, earthquake, building code compliance, water damage originating off-site, etc. Property insurance claim handling deficiencies include adjuster overload (which leads to over-reliance on estimating software) and independent adjuster compensation schemes that

reward haste and lowballing. These deficiencies also include serious conflicts between the financial interests of cat victims/claimants and the shareholders of publicly traded insurers.

Deficiencies in the catastrophe insurance currently being sold by private market insurer are:

- Placing untenable financial strain on FEMA and county governments.
- Causing local and state governments to lose property tax revenues when disaster survivors don't collect insurance funds to finance rebuilding.
- Overtaxing the resources of charitable aid organizations that now must serve middle income *in addition* to lower income disaster survivors.
- Defeating the expectations and preparedness efforts of home and business owners who reasonably believed their insurance would provide funds to repair and rebuild.
- Wasteful and inefficient.
- Eroding the public's confidence in the insurance system – particularly young people.

Reinsurance markets

While UP does not claim to be expert in the reinsurance market, we can competently make two observations about its current state:

- 1) Dennis Burke who lobbies state insurance regulators on behalf of reinsurers, has repeatedly and very publicly stated that the reinsurance industry has “lots and lots of capacity” and very much wants to insure catastrophic risk.
- 2) Fluctuations in reinsurance pricing and the generally high cost of reinsurance are perhaps the most significant reason why the policies that are being sold through the California Earthquake Authority are unaffordable for many homeowners.

Post cat marketplace changes and disturbances

Following many natural catastrophes, some insurers – typically those with the largest market share in the impacted region – reduce their exposure in the area by non-renewing policies when they come up for renewal.

In wildfire areas where all the trees have been destroyed, the reduction doesn't seem logical, but this pattern by insurers has been consistent. After the 1991 Oakland-Berkeley firestorm, many homeowners in the impacted and surrounding areas were distraught at being dropped when their policies came up for renewal after the disaster. Not only did residents feel betrayed (“I've been paying premiums to this company for 20+ years, and now this...”) but those who had a “loss in progress” couldn't find replacement coverage. To assist the homeowners, United Policyholders created a simple and successful

program called “Match-UP” through which we connected those who’d been dropped with independent agents/brokers who self-identified as having access to insurers willing to take on new customers in the area. That approach was less successful after a subsequent series of wildfires in Southern California, so the legislature enacted a statutory consumer protection. Property Insurers in California must now give disaster victims at least one renewal option when their policy comes up renewal after a disaster.

The State of Florida experienced a complete transformation of their home insurance market after State Farm and other major insurers pulled out of writing home policies after a series of hurricanes. The quasi-public Citizens Insurance Company became the top insurer in the state. The Florida Office of Insurance Regulators and elected officials are still working on depopulating Citizens. A similar situation exists in Louisiana, though far less severe.

4. The current financial condition of State residual markets and catastrophe funds in high-risk regions, including the likelihood of insolvency following a natural catastrophe, the concentration of risks within such funds, the reliance on post event assessments and State funding, and the adequacy of rates;

Many of the quasi-public entities – the NFIP, TWIA and others – need restructuring and are deep in debt for various reasons. Reform efforts by states and state regulators primarily focus on implementing rate increases and reducing subsidies, not on fundamental restructuring that will create cost savings through improved efficiencies in operations. We submit that reforms such as reducing program expenses, agent commissions, and participating carrier servicing fees, as well as giving them alternatives to expensive reinsurance are imperative approaches to making State residual markets and Cat funds more sustainable. Given that most are “take all comers”, they need and deserve financial advantages that private insurers who can cherry pick their customers, should not enjoy.

UP has repeatedly proposed better coordination among residual market mechanisms in the various states, (“FAIR”/Joint Underwriting Associations, quasi-public/pools/association entities). We recommend that these entities work together to create shared (public) cat models and pool their limited resources. At numerous NAIC meetings and at the 2011 Windstorm Network conference in Houston, Texas, United Policyholders proposed that the top executives of Louisiana and Florida Citizens, AIUA, TWIA and the MWUA stay in close contact and help each other make efficiency and productivity improvements to their operations. FIO clearly can have an important role in this regard.

UP strongly supports the California Earthquake Authority’s efforts to enact federal legislation that would give them an alternative to reinsurance capital, which in turn would allow them to sell an affordable product.

Some view reduced subsidies, strict elevation requirements, revised flood maps and the pending flood insurance rate increases due to enactment of Biggert-Waters 2012 as essential to keeping the program viable and reducing its huge debt. Others view these reforms with dread and staunch opposition. [See www.stopfemanow.com]. CFA Insurance Director Robert Hunter has publicly stated that flood

insurance premiums are far below what they need to be, and one resident of a Jersey Shore community that was very hard hit by Superstorm Sandy recently opined that perhaps its best that BW12's increases take effect so people know the real cost of living by the ocean. That view is not shared by the vast majority of coastal home owners and realtors.

5. The current role of the Federal Government and State and local governments in providing incentives for feasible risk mitigation efforts and the cost of providing post-natural catastrophe aid in the absence of insurance;

The federal government should be working with states to require private insurers to take a much more active role in helping homeowners know what mitigation steps will make their homes more resistant to damage and qualify them for insurance discounts. Private insurers should be helping homeowners finance mitigation.

We strongly support allowing homeowners to create tax-free Catastrophe Savings Accounts to cover losses below their deductibles. We strongly **oppose** granting tax breaks to cover homeowners' insurance premiums (as proposed by the Property Casualty Insurers Association). This approach would give a direct taxpayer subsidy to insurance companies, many of whom are paying their CEOs multi-million dollar bonuses each year.

6. Current approaches to insuring natural catastrophe risks in the United States;

Each state is currently taking its own approach to ensuring that its property-owning citizens can insure their homes against natural catastrophes. Most are letting the private market run its course with minimal regulatory intervention (Oklahoma). Others are taking a very pro-active approach. (California and Colorado) Others are experimenting with various solutions, (Texas, Louisiana, Florida, Mississippi, Alabama). A push for "rating transparency" is taking hold in a number of states, the idea being that people deserve to know how their insurer is calculating the rate they're being charged.

a. Current and potential future Federal, State, and regional partnerships that support private, direct insurance coverage;

b. The potential privatization of flood insurance in the United States; and,

Insurers are free to sell private flood insurance today but most choose not to. We don't see how flood insurance can be privatized unless perhaps every state agrees to force the insurers that want to sell auto insurance to also sell home insurance that covers the peril of flood.

June 24, 2013

Page 9 of 9

Conclusion

For many, many years prior to the last decade – private insurers were happy to insure homes in coastal areas, urban wild land interface zones, and areas prone to tornadoes and hail storms. Obviously that situation has changed dramatically. As leading insurers increasingly move away from selling all-risk policies to named perils policies, raise deductibles, depart from ISO forms and rates, and react to catastrophes by reducing their local market share and otherwise responding to climate change, we are seeing substantial challenges ahead for property owners, realtors, the construction industry, local, state and the federal government, and ultimately, all Americans.

It is crystal clear that the home and flood insurance markets need to be reformed and that FIO has an important role to play. Among the many stakeholders that will assist in implementing the needed reforms are: state regulators, insurers, reinsurers, producers (agents/brokers), commercial and residential policyholders, grass roots activists, construction and claim professionals, structural engineers, lenders, actuaries, risk modelers and other experts.

The fact that international reinsurers have tremendous control over natural catastrophe insurance pricing and availability, yet there is little regulation of their rates is a significant challenge. Short term, we believe that a better-coordinated state-based system of rate regulation can **help, not harm** the private insurance market by maintaining fair competition and stability and by preventing panic-based actions by insurers. Every state needs to provide:

- Public filings of property insurance rates and policy forms
- Actuarial review/Adequate state regulator resources
- A process for intervener participation/compensation to supplement state regulator resources
- Automatic hearings on rate increase requests over 10%
- Limit use of catastrophe modeling (no near/short term)

FIO has an important role to play in helping meet our nation's critical need for risk spreading, sharing/pooling, and pre-disaster financial planning. We trust these and other comments will assist your office.

Sincerely,



Amy Bach, Esq. Executive Director