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United Policyholders' Comments on REG-2023-00010, Catastrophe Modeling and Ratemaking

As an organization that dialogues regularly with the full spectrum of stakeholders this proposal will impact and that regularly coordinates with your agency to problem-solve for insurance consumers, United Policyholders acknowledges the hard work, brainstorming, negotiating and time the Commissioner and CDI staff are putting in solving the conditions underlying this proposal, and we appreciate this follow up opportunity to provide input.

Like your agency, United Policyholders has been processing distressed emails and phone calls and working hard to help people, businesses and communities since competition among property insurers in California began to slow dramatically (first in WUI regions) starting in 2017. But each time we've prepared to host a shopping help webinar and checked in with agents and brokers across the state, there have been fewer and fewer admitted company options, and more and more people having to go with lightly regulated non-CIGA backed surplus lines insurers or the bare-bones (still) no liability coverage California Fair Plan.

United Policyholders has been surveying[1] California homeowners and gathering data on non-renewals, jaw-dropping premium increases, Fair Plan frustration and the number of people going bare because they can't afford the quotes they're getting and don't have a mortgage company forcing them to buy a lender-placed policy (which only covers the amount of the mortgage anyway…not their assets).

[1] https://tinyurl.com/mrffu8tx

We are clearly at a crisis point today. Even if insurers are orchestrating the crisis in order to be able to fast track rate increases, as it does appear, one need only look at similar marketplace problems in states that allow CAT modeling and file and use and recent ratings downgrades to recognize there's more going on than just that.

While the causes of our crisis are complex and include high, unregulated reinsurance rates, underwriting decisions based on extreme events associated with climate change, the use of drone/aerial images AI, risk scoring and modeling, plus inflation and interest rates, we don't have the option of doing nothing and hoping it will all go away. People and small businesses are really hurting, property values are declining and other economic ripple effects are manifesting.

Is UP "in favor of" of allowing rating plans based on opaque CAT models that are likely to raise rates across the board and that will compel CDI staff to fight trade secret battles in order to understand the underlying assumptions in those models? Of course not. But given the Department's expertise and toolbox, they fact they're in use in several lines of business already, given that every other state allows insurers to use them, and given that the proposed reg requires models to include mitigation credits, we understand why the Department is advancing this approach.

We believe the CDI team is sophisticated enough to recognize the risks of allowing rate filings to be based on commercially-derived "forward-looking" CAT model projections and we know your agency does not want to see California policyholders get charged more than a fair rate. We know your team is proud of being among the most respected insurance regulatory agencies in the country with a solid track record of protecting consumers and deservedly so.

We believe that *most* stakeholders share the goal of restoring affordable, available insurance options for Californians, healthy competition among well-capitalized, admitted insurers and a Fair Plan policy count well below its current level. The consumers we assist and advocate for generally understand that risk is higher due to drought and extreme weather conditions and premiums must increase accordingly. But "accordingly," not excessively – is the key to our shared goal.

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The proposed regulation seeks to strike a balance by retaining a system where rates are based on actual events, claim data, historical payouts and projections tied to those data points, but adding a new rule that allows insurers to base their rates in part on CAT models (upon approval by a Model Advisor) as those who sell outside California can do in other states.

<u>The Model Advisor's imperative</u>

We understand why insurers want to incorporate cutting edge data science on how climate change is impacting their risk exposure and capital needs. But there is no getting around the fact that *projections are subjective and open to being manipulated for the profit objectives of the entity that commissions them.*

The Model Advisor and CDI's Rate Regulation Bureau obviously need to take that into account. They also must take into account that the dollar amounts insurers have been paying out on past catastrophe loss claims were based on lower deductibles and more generous policy language than what's in policies today. Coverage is shrinking – make no mistake. Payouts will be smaller going forward. *CAT models must be required to take that into consideration.*

Such models must also be required to take into account subrogation recoveries from utilities and other parties found to be at fault for catastrophic events, wide scale mitigation actions undertaken to reduce wildfire exposure including shaded fuel breaks, controlled burns, enhaned fire-fighting capacity home mitigation actions at the community level and risk mitigation undertaken by local and regional utility companies such as undergrounding and covered conductor lines.

<u>The Public Model Imperative</u>

Numerous public and private California Universities are already highly engaged in studying and modeling wildfire risk from an academic, not for-profit perspective. Their work can be incorporated in the design of a public wildfire risk model that will serve as a benchmark for privately designed models, similar to the approach that Florida has taken with its Commission on Hurricane Loss Projection Methodology.[2]

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[2] https://fchlpm.sbafla.com/

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Alternative approaches

We have previously proposed, and will restate here, that a safer alternative to allowing the use of opaque CAT models would be to collect the industry wide catastrophe loss data, trend it by wildfire score to implement a forward looking result, and then allow insurers to use those projections based on their mix of business by score. Insurers already have all this data - in fact, it is included in the rate filings submitted over the last 20+ years.

Even if the Department believes it is necessary to allow the industry a greater concession, then that transparent result based on historic losses could be entered as a heavily weighted component in an average that also includes the results of two or more wildfire model loss projections. Another approach would be to amend the proposed regulations to not just "allow" for but to require that insurers to submit the results of more than one model - the ideal in this scenario would be to require the insurer to submit the output of three models with the lowest loss projections of the three getting the highest weighting in the rate calculation.

In conclusion…

We have no choice but to expedite wildfire risk reduction on the widest possible scale and acknowledge that we need private insurers in our marketplace and must make adjustments (with appropriate safeguards) but also be pursuing long term solutions including the establishment of publicly-supported risk pools and CAT risk financing innovation to lessen reinsurer's control over pricing and availability here in California.

Sincerely,

Amy Bach
Executive Director

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