

GOOD MORNING MR. CHAIRMAN AND MEMBERS OF THE COMMITTEE. I AM BOB HUNTER, DIRECTOR OF INSURANCE FOR CONSUMER FEDERATION OF AMERICA.

THE COMMITTEE ASKED FOR COMMENTS ON HOW TO MAKE POST-DISASTER CLAIMS MORE CONSUMER-FRIENDLY. I HAVE PREPARED WRITTEN TESTIMONY, WHICH STAFF HAS, AND I ASK THAT IT BE MADE PART OF THE HEARING RECORD.

MY REMARKS ARE BASED ON EXPERIENCE WITH CONSUMER CONCERNS IN MANY DISASTER SITUATIONS, AS FEDERAL INSURANCE ADMINISTRATOR RUNNING THE NATIONAL FLOOD INSURANCE PROGRAM, AS TEXAS INSURANCE COMMISSIONER HANDLING A LARGE FLOOD DISASTER IN DALLAS, IN THE PRIVATE SECTOR AS AN ACTUARY PRICING SUCH EVENTS AND AS A CONSUMER ADVOCATE TRYING TO HELP TRULY DEVASTATED PEOPLE WITH THEIR CLAIMS. MY COMMENTS SPAN EXPERIENCE FROM HURRICANE AGNES IN 1972, THROUGH ANDREW, KATRINA AND MANY OTHER DISASTERS, UP TO ISSUES CAUSING CONSUMER ANGUISH IN THE SANDY AFTERMATH. IT IS OBVIOUS THAT BOTH SHORT- AND LONGER-TERM REFORMS OF THE CAT SYSTEMS ARE NECESSARY.

SHORT TERM REFORMS

THE MOST IMPORTANT SHORT TERM REFORM IS FIXING THE CONFUSING AND DRACONIAN HOMEOWNERS INSURANCE POLICY. POST-CATASTROPHE CLAIMS ARE PAINFUL TO CONSUMERS BECAUSE THE HOMEOWNERS INSURANCE POLICY IS JAM-PACKED WITH LOOPHOLES AND CAPS AND LIMITS AND EXCLUSIONS THAT MOST CONSUMERS DO NOT UNDERSTAND. IN RECENT YEARS, INSURERS HAVE SUCCEEDED IN SHIFTING SIGNIFICANTLY MORE OF THE RISK OF LOSS ASSOCIATED WITH EXTREME RISKS TO POLICYHOLDERS LEAVING A SIGNIFICANT AND UNACCEPTABLE RISK EXPOSURE FOR CONSUMERS, WHICH HAS INCREASED TAXPAYER EXPOSURE. THE DATA SHOWING HOW INSURERS HAVE SHIFTED RISK AND COSTS ASSOCIATED WITH WEATHER CATASTROPHES TO CONSUMERS AND THE STATE AND FEDERAL GOVERNMENTS, IS DETAILED IN CFA'S FEBRUARY 2012 REPORT, "[THE INSURANCE INDUSTRIES INCREDIBLE DISAPPEARING WEATHER CATASTROPHE RISK](#)," AVAILABLE ON CFA'S WEBSITE.

IT IS HELPFUL TO LOOK AT CLAIMS/COVERAGE ISSUES IN RECENT CATASTROPHIC EVENTS TO DETERMINE WHAT PROBLEMS CONSUMERS FACE IN THE INSURANCE MARKET AND WHAT MIGHT BE DONE TO ENSURE THAT CONSUMERS HAVE BETTER ACCESS TO HOMEOWNERS INSURANCE THAT MEET THEIR NEEDS DURING CATASTROPHIC EVENTS. CFA HAS IDENTIFIED SEVERAL ISSUES THAT APPEAR TO BE MOST IMPORTANT:

1. CONSUMERS DO NOT HAVE SUFFICIENT FLOOD INSURANCE IN FORCE. IN THE SANDY IMPACTED AREA, IT IS ESTIMATED THAT ABOUT 70 PERCENT OF SANDY-FLOOD-DAMAGED HOMES DO NOT HAVE FLOOD INSURANCE.

2. THE CONDITIONS UNDER WHICH HURRICANE DEDUCTIBLES APPLY ARE UNCLEAR AND RESULT IN CONSUMER CONFUSION. CONSUMERS DO NOT UNDERSTAND WHEN AND IF A HURRICANE DEDUCTIBLE KICKS IN AND WHEN AND IF A WIND DEDUCTIBLE APPLIES SINCE THE CONSUMERS HAD NO SAY IN THE SELECTION OF THESE DEDUCTIBLES. IT IS ALSO UNCLEAR TO CONSUMERS WHETHER IT IS THE INSURANCE COMPANY OR A STATE REGULATORY AGENCY THAT MAKES THE DETERMINATION THAT A SEVERE WEATHER EVENT TRIGGERS THESE DEDUCTIBLES. IT IS UNCLEAR WHETHER HURRICANE DEDUCTIBLES APPLY TO CLAIMS IN AN ENTIRE STATE IF A STORM IS CLASSIFIED AS A HURRICANE IN ONE PART OF A STATE BUT NOT IN ANOTHER PART OF A STATE. IT IS ALSO UNCLEAR IF THE WIND SPEED DEDUCTIBLE IS APPLIED BASED ON WIND SPEED IN THE SPECIFIC TOWN OR COUNTY OR WHETHER A TRIGGER APPLIES THE DEDUCTIBLE STATEWIDE.

3. CONSUMERS ARE EXTREMELY UNAWARE OF THE ANTI-CONCURRENT-CAUSATION (ACC) CLAUSE IN THEIR POLICIES. THE ACC STATES THAT, IF A STRUCTURE IS DAMAGED AT ABOUT THE SAME TIME BY TWO RISKS, ONE OF WHICH IS COVERED (LIKE FIRE OR WIND) AND THE OTHER NOT (LIKE FLOOD), THEN EITHER NO COVERAGE OR LIMITED COVERAGE WILL BE PROVIDED FOR THE "COVERED" PART OF THE CLAIM. PEOPLE SIMPLY DO NOT BELIEVE THAT THEIR OWN INSURANCE COMPANY WOULD DESIGN A TRAP DOOR IN THE BACK OF THEIR POLICY THROUGH WHICH THE COVERAGE THEY PURCHASED CAN FALL.

4. CONSUMERS ARE OFTEN UNAWARE THAT THEIR POLICY CONTAINS A CAP ON REPLACEMENT COSTS MAY RESULT IN SIGNIFICANT OUT-OF-POCKET COSTS. ALMOST NONE ARE AWARE OF THE RISK THEY TAKE IF A CATASTROPHIC EVENT OCCURS. AFTER A SEVERE WEATHER EVENT, THE PRICE OF MATERIALS AND LABOR TO REPAIR HOMES OFTEN INCREASE CONSIDERABLY, A PHENOMENON KNOWN AS “DEMAND SURGE.” IF REBUILDING PRICES SURGE, AS IS TYPICAL AFTER A LARGE EVENT WITH MANY DAMAGED HOMES, HOMEOWNERS FACE SIGNIFICANT OUT-OF-POCKET EXPENSES. **JUST YESTERDAY WE WERE TOLD BY XACTWARE THAT THESE COSTS ARE STARTING TO RISE IN THE SANDY AREA.** I HAVE SEEN SURGE GREATER THAN 50% IN SOME COUNTIES. SO, FOR EXAMPLE, IF A FAMILY BUYS REPLACEMENT COVERAGE WITH A \$500 DEDUCTIBLE ON \$200,000 HOME AND FILES A NORMAL TOTAL LOSS FIRE CLAIM, THEY WILL RECEIVE A CLAIMS CHECK FOR \$199,500 AND THEIR HOME WILL BE REBUILT. IF THE DAMAGE TO THEIR HOME IS THE RESULT OF A HURRICANE, AND BUILDING MATERIAL SCARCITY RESULTS IN A 50 PERCENT PRICE INCREASE IN BUILDING COSTS, THAT FAMILY WOULD NOW NEED \$300,000 TO RESTORE THEIR HOME. IF THE INSURER IMPOSES THE REPLACEMENT COST LIMIT, AND THEY RECEIVE A CLAIMS CHECK FOR \$199,500, THEY WILL BE FAR SHORT OF WHAT THEY WOULD NEED TO BE MADE WHOLE. TO RUB SALT IN THE WOUND, IF THEY LIVED ON THE BEACH AND THE HURRICANE DEDUCTIBLE OF 5 PERCENT OF VALUE IS APPLIED (IN THIS CASE \$10,000) THEY WOULD ONLY RECEIVE A CLAIMS CHECK FOR ONLY \$190,000.

5. CONSUMERS ARE UNAWARE THAT THEIR POLICY PROBABLY DOES NOT COVER THE COST OF MOLD REMOVAL.

6. CONSUMERS ARE UNAWARE THAT MANY POLICIES DO NOT COVER ADDITIONAL COSTS IF CONSTRUCTION ORDINANCES OR BUILDING CODES REQUIRE CERTAIN UPGRADES. FOR INSTANCE, IF A STRUCTURE IS 50 PERCENT DAMAGED, FLOOD INSURANCE RULES REQUIRE ELEVATION OF THE FIRST FLOOR OF THE WHOLE HOME TO THE 100-YEAR FLOOD ELEVATION, OFTEN A VERY EXPENSIVE ADDITIONAL COST TO REBUILD A HOME.

WHAT SHOULD NAIC DO?

NAIC SHOULD REWRITE THE HOMEOWNERS INSURANCE POLICY TO MAKE IT FAIRER TO CONSUMERS WHEN FUTURE STORMS HIT AND STATES SHOULD REQUIRE THE NEW POLICY TO BE USED AS MINIMUM COVERAGE ACCEPTABLE IN THE STATE.

HERE ARE SOME SUGGESTIONS FOR THE NAIC TO CONSIDER TO ADDRESS THESE ISSUES:

FLOOD INSURANCE SHOULD BE OFFERED IN HIGH-RISK FLOOD AREAS THROUGH PRIVATE INSURERS. THERE ARE REASONABLY PRICED, PRIVATE-SECTOR SERVICE PROVIDERS WHO CAN MAKE THE FLOOD INSURANCE RATE MAP DETERMINATION OF RISK THAT COULD BE USED TO TRIGGER THE OFFER OF FLOOD INSURANCE WHEN A HOMEOWNERS INSURANCE POLICY IS SOLD (THEY DO IT TODAY FOR BANKS). IF A HOME IS IN A HIGH-RISK FLOOD AREA, THE INSURER SHOULD BE REQUIRED TO OFFER FLOOD INSURANCE WHEN SELLING ANY HOMEOWNERS INSURANCE POLICY. IF A HOMEOWNER WANTS THE FLOOD COVERAGE AND THE INSURANCE COMPANY IS AN NFIP WRITE YOUR OWN INSURER, THE COMPANY CAN SIMPLY ADD FLOOD INSURANCE TO THE HOMEOWNER'S INSURANCE POLICY. IF THE INSURER IS NOT A WYO INSURER, THE HOME INSURANCE CARRIER FOR THE CONSUMER CAN SECURE THE FLOOD POLICY FROM THE NFIP DIRECT SERVICING CONTRACTOR.

STATES SHOULD REQUIRE THAT A CONSUMER CHOOSE THE DEDUCTIBLES BASED ON WIND SPEED. NAIC'S MODERNIZATION OF THE HOMEOWNERS INSURANCE POLICY SHOULD REMOVE THE CURRENT, CONFUSING HURRICANE-RELATED DEDUCTIBLES AND ONLY ALLOW WIND SPEED DEDUCTIBLES TO BE USED. TO ATTACH THE WIND DEDUCTIBLE, THE INSURER WOULD BE REQUIRED TO GIVE, WHEN THE POLICY IS SOLD, THE POLICYHOLDER AN OPTION TO SELECT THE WIND SPEED DEDUCTIBLE FROM A TABLE OF DIFFERENT PRICES FOR DIFFERENT WIND SPEED DEDUCTIBLES. THE CONSUMER WOULD THEREFORE KNOW EXACTLY WHAT TO EXPECT IF A STORM HITS.

NAIC SHOULD REMOVE THE ANTI-CONCURRENT-CAUSATION CLAUSES FROM THE MODERNIZED POLICY. THIS DRACONIAN CLAUSE, HIDDEN IN THE FINE PRINT OF THE HOMEOWNERS INSURANCE POLICY, ACTS AS A TRAP DOOR THAT SNAPS OPEN REMOVING

COVERAGE TO THE SURPRISE OF CONSUMERS. THE ACC CLAUSE SHOULD BE PROHIBITED FROM USE FOR HOMEOWNERS INSURANCE POLICIES AND NAIC SHOULD DRAFT THE POLICY THAT WAY.

CAPS ON REPLACEMENT COST: CFA PROPOSES THAT THE STATES REQUIRE INSURERS TO OFFER DIFFERENT RC CAPS AT THE TIME OF SALE WITH THE PRICE IMPACT OF EACH OPTION BEING DISCLOSED CLEARLY TO THE CONSUMER. SECONDLY, IN A DEMAND SURGE SITUATION, INSURERS SHOULD BE THE RISK-TAKERS, NOT THE POLICYHOLDERS. NAIC'S MODERN POLICY SHOULD REMOVE DEMAND SURGE PRICE CHANGES FROM ANY CALCULATION OF THE RC CAP IN A CLAIM DURING A DISASTER SITUATION.

MOLD EXCLUSION: CFA BELIEVES THAT STATES SHOULD REQUIRE THAT MOLD COVERAGE BE A YES/NO CHOICE AT THE TIME OF THE POLICY SALE WITH THE COST IMPLICATIONS FULLY DISCLOSED TO CONSUMERS.

LAW AND ORDINANCE COVERAGE: CFA PROPOSES THAT STATES REQUIRE, AT TIME OF SALE, A YES/NO DECISION ON SUCH COVERAGE BE OFFERED TO THE CONSUMER, ALONG WITH THE PREMIUM IMPLICATIONS DISCLOSED CLEARLY.

THE NEW HOMEOWNER POLICY SHOULD REQUIRE A CONSUMER BILL OF RIGHTS ACCOMPANY EVERY HOMEOWNERS INSURANCE POLICY SOLD AND EVERY CLAIM FILE OPENED USING THE BILL OF RIGHTS ADOPTED IN TEXAS AS A MODEL.

BESIDES FIXING THE HOMEOWNERS POLICY, THE NAIC SHOULD ENCOURAGE CATASTROPHE CLAIM REFORMS INCLUDING:

CLAIMS TRANSPARENCY

CONSUMERS SHOULD BE ENTITLED TO A COMPLETE COPY OF ALL DOCUMENTS IN THEIR CLAIM FILE. CONSUMERS SHOULD BE INFORMED THEY HAVE A RIGHT TO HIRE THEIR OWN

PUBLIC ADJUSTER BUT THAT THEY SHOULD BE WARNED TO CHECK REFERENCES, LICENSE STATUS AND EXPERIENCE BEFORE DOING SO. IN CASES OF A DECLARED NATURAL DISASTER, APPRAISALS SHOULD BE OPTIONAL, NOT MANDATORY. INFORMATION ON WHEN TO CONSIDER THE NEED TO HIRE AN ATTORNEY SHOULD ALSO BE INCLUDED.

CLAIMS SCORE CARD

THE NAIC SHOULD CREATE AND FACILITATE FOR ALL STATES A SCORECARD ON HOW EACH INSURER IS DOING IN SPEED OF CLAIM PAYMENT, NUMBER OF CLAIMS, NUMBER CLOSED WITH PAYMENT, NUMBER CLOSED WITHOUT PAYMENT AND OTHER INFORMATION. THE SCORECARD CREATED BY THE GOVERNOR OF NEW YORK JUST A FEW DAYS AGO IS A MODEL FOR SUCH REFORM.

CLAIMS ADJUSTER LICENSING AND ACCOUNTABILITY

THE NAIC SHOULD PROPOSE A SYSTEM OF NATIONAL LICENSING OF CLAIMS ADJUSTERS FOR CATASTROPHE SITUATIONS AND ESTABLISH MINIMUM STANDARDS FOR TRAINING AND COMPETENCY AMONG ADJUSTERS.

NAIC SHOULD DRAFT A MODEL BILL FOR THE REGULATION OF VENDORS WHOSE PRODUCTS IMPACT THE CATASTROPHE CLAIMS AND PRICING DECISIONS OF INSURERS

UNDER THE MODEL, STATES SHOULD BE EMPOWERED TO REGULATE VENDORS WHOSE COMPUTERIZED PRODUCTS HAVE MAJOR IMPACTS ON CLAIMS SETTLEMENT OFFERS AND ON HURRICANE AND OTHER STORM PRICES CHARGED BY INSURERS IN THE STATE. PRODUCTS SUCH AS "XACTIMATE" IMPACT THE VALUATIONS OF HOMES FOR CLAIMS PAYOUT PURPOSES. PRODUCTS LIKE CAT MODELS IMPACT THE PRICE OF INSURANCE FOR HOMEOWNERS. YET THESE MODELS AND COMPUTERIZED 'BLACK BOXES' ARE OFTEN NOT REGULATED. PROVIDERS OF SUCH PRODUCTS SHOULD BE REGULATED AS ADVISORY

ORGANIZATIONS IN THE SAME WAY THAT OTHER SUCH ENTITIES, LIKE THE INSURANCE SERVICES OFFICE, ARE REGULATED.

LONG-TERM REFORMS

THE NAIC TAKE A LEAD IN RATIONALIZING OUR TOPSY-TURVY NATIONAL CATASTROPHE INSURANCE SYSTEM

JUST TO SEE HOW IRRATIONAL OUR CURRENT SYSTEM IS, IMAGINE THIS FICTIONAL SCENARIO, MR. CHAIRMAN. IMAGINE THAT, A YEAR AGO, THE NATION HAD NO INSURANCE OR MITIGATION PROGRAMS FOR NATURAL CATASTROPHES AT ALL. YOU AND THE COMMITTEE WERE TASKED TO DEVELOP SUCH SYSTEMS USING YOUR BEST IDEAS. YOU CONTRACTED WITH THE GREATEST EXPERT IN THE SOLAR SYSTEM ON NAT CATS, MR. MORK FROM MARS. HE IS NOW PRESENTING HIS IDEAS. MAKE BELIEVE, AND THE INDUSTRY SHOULD LIKE THIS, THAT I AM A LITTLE GREEN MARTIAN ACTUARY.

“MR. CHAIRMAN, I AM MORK, PRESIDENT OF MAA (MARS ACADEMY OF ACTUARIES). I HAVE DEVELOPED A PLAN. THE UNITED STATES HAS 3 MAJOR NATURAL CATASTROPHE POTENTIALS ALL OF WHICH HAVE VARYING DEGREES OF RISK IN EACH STATE. THEY ARE FLOOD, EARTHQUAKE AND WIND. THE FLOOD RISK IS MOST EXTREME ALONG YOUR LARGER RIVERS AND ON THE EAST COAST FROM THE STATE YOU CALL MAINE TO THE ONE CALLED TEXAS. EARTHQUAKE RISK IS EXTREME ON THE WEST COAST FROM ALASKA TO CALIFORNIA. WIND RISK IS GREATEST WHERE TORNADOES ARE FREQUENT AND ON THE SAME PARTS OF THE EAST AND GULF COASTS. IN THIS AREA WIND AND FLOOD RISK OFTEN HAPPEN AT THE SAME TIME WHEN HURRICANES HIT.

“NOW HERE IS MY PLAN. FOR FLOOD, THE FEDERAL GOVERNMENT WILL BE THE SOLE PROVIDER OF COVERAGE. I EXPECT THAT THEY WILL ACHIEVE MARKET PENETRATION OF A HIGH IN NEW ORLEANS OF 60%, 30% ON THE EAST COAST AND UNDER 20% MOST ELSEWHERE. FOR EARTHQUAKE, I PROPOSE THE PRIVATE SECTOR HANDLE ALL STATES EXCEPT CALIFORNIA WHERE A STATE PLAN WILL BE CREATED. THE MARKET PENETRATION WILL BE 15% IN CALIFORNIA,

UNDER 5% ELSEWHERE. FOR WIND, I PROPOSE A SORT OF PRIVATE PLAN, WITH THE PRIVATE SECTOR SELLING INSURANCE IN MOST PLACES BUT WITH A FEW STATE PLANS IN THE STATES WITH BIGGER HURRICANES. THIS WILL GET ALMOST FULL MARKET PARTICIPATION. I PROPOSE TAX-FREE RESERVE BUILD UP FOR THE CALIFORNIA PLAN AND THE FLORIDA PLAN BUT NOWHERE ELSE. I PROPOSE THAT MITIGATION BE SCATTERED AMONG MANY AGENCIES AND NOT TIED INTO THE INSURANCE PROGRAM DIRECTLY. I ALSO EXPECT MY PLAN TO MAXIMIZE TAXPAYER EXPOSURE AND MINIMIZE EFFECTIVE LAND USE AND BUILDING CODE PROVISIONS. I EXPECT THAT AFTER DISASTERS, THE WIND INSURERS WILL RETRENH ,SHARPLY RAISING PRICES AND DROPPING RISKS INTO THE POOLS.

“WHAT DO YOU THINK, MR. CHAIRMAN?”

AND YOU WOULD ANSWER, “GET OFF OF OUR PLANET YOU CRAZY MARTIAN ACTUARY!”

A CRAZY MARTIAN APPARENTLY DEVELOPED THE CATASTROPHE INSURANCE AND RISK MANAGEMENT PLAN IN PLACE IN OUR NATION. IT IS PAST TIME THAT STEPS WERE TAKEN TO MOVE TOWARD A MORE RATIONAL SYSTEM. OBVIOUSLY, AS SOON AS CONGRESS AND THE ADMINISTRATION END THE ATTEMPTS TO PUSH EACH OTHER OVER THE FISCAL CLIFF, THEY WILL HAVE A KEY ROLE TO PLAY IN DEVELOPING A SYSTEM WITH VISION AND LOGIC. (I HAVE A NOTE HERE THAT SAYS ‘PAUSE FOR LAUGHTER’ – BUT HOPE SPRINGS ETERNAL) ON THE INSURANCE FRONT, THE NAIC SHOULD TAKE THE LEAD AND INVOLVE STATES, THE FEDS AND ALL INTERESTED PARTIES. YOU REALY SHOULD START THINKING ABOUT YOUR CONTRIBUTION TO A BETTER SYSTEM.

DEVELOPING THE VISION IS ESSENTIAL. ON THE INSURANCE FRONT, HERE ARE A FEW IDEAS THAT MIGHT BE VISION-WORTHY:

- DEVELOPING TRUE ALL-RISK INSURANCE POLICIES SUCH AS A HOMEOWNERS INSURANCE POLICY INCLUDING FLOOD AND EARTHQUAKE AND WITH NO SURPRISES FOR UNSUSPECTING HOMEOWNERS AFTER A DISASTER.

- DETERMINING HOW BEST TO SPREAD THE RISK AMONG POLICYHOLDERS, INSURERS, PRIVATE REINSURERS, CAT BOND AND OTHER MARKET MECHANISMS, STATE REINSURANCE AND FEDERAL REINSURANCE.
- DETERMINING HOW TO GET THE BEST MITIGATION SYSTEM IN PLACE. THIS ITEM WOULD INCLUDE INSURANCE PRICING MECHANISMS THAT ARE ACTUARIALLY SOUND AND
- Z THAT REWARD MITIGATION EFFORTS BOTH AT THE INDIVIDUAL LEVEL AND THE COMMUNITY LEVEL. BUILDING CODES AND LAND USE STRATEGIES WOULD BE PART OF THE PLAN, WITH STRONG ENFORCEMENT REQUIRED IN HIGH-RISK AREAS.
- THE BASIC INSURANCE MODEL -- A RISK POOL DIVERSIFYING AND SPREADING THE RISK OF MANY CONSUMERS -- MUST GIVE WAY TO INSURANCE AS BOTH RISK TRANSFER AND A MECHANISM TO FINANCE AND IMPLEMENT LOSS MITIGATION AND LOSS PREVENTION. PART OF THIS IS ACCURATE PRICING OF THE INSURANCE -- THIS IS ESSENTIAL TO GIVE CONSUMERS AND BUSINESSES THE APPROPRIATE PRICE SIGNALS TO MAKE INFORMED AND RATIONAL DECISIONS ABOUT THEIR INVESTMENTS IN PROPERTY AND STRUCTURES. BUT THE MOST IMPORTANT PART OF THIS IS ENGAGING INSURERS AND THE PUBLIC SECTOR TO PARTNER WITH POLICYHOLDERS TO FINANCE THE ESSENTIAL INVESTMENTS IN LOSS MITIGATION -- BE THAT CAT-RESISTANT-STRUCTURES OR OTHER LOSS PREVENTION MEASURES.

THANK YOU. I'D BE HAPPY TO TAKE QUESTIONS.