OPPOSE AB 2167 (DALY)

Q & A: The Truth About AB 2167

The insurance industry is misleading legislators about AB 2167. The industry says this bill will solve California's wildfire problems by requiring insurance companies to sell and renew homeowners and renters' property insurance coverage in communities that it says are subject to wildfire risks. It also says that the bill "furthers the purposes of Proposition 103."

Both of these arguments are FALSE.

Q: What does AB 2167 actually do?

A: AB 2167 overrides the protections against price gouging and discrimination in homeowners' insurance enacted by the voters as part of Proposition 103. Making matters worse, AB 2167 specifically authorizes the pass-thru of unlimited reinsurance expenses, which is forbidden under current law and will lead to much higher premiums for Californians. AB 2167 flouts the purposes of Proposition 103.

Q: Will AB 2167 require insurance companies to sell and renew homeowners and renters' property insurance coverage in at-risk communities?

A: No. AB 2167 does not require insurance companies to sell or renew insurance coverage for all those who need to buy coverage in the communities the insurance industry has targeted. The legislation contains many loopholes that will permit insurance companies to renege on the "assurances" AB 2167 purports to require.

Q: Is AB 2167 the solution to problems in California's insurance market?

A: No. California voters enacted proposition 103 to protect themselves in insurance "crises" by preventing insurance companies from price gouging, unjustified refusal to sell and other forms of discrimination against neighborhoods, and other unlawful practices.

Proposition 103 was enacted after the insurance industry periodically imposed massive increases in the price of home, auto, business, municipal, health provider and non-profit insurance during the 1970s through the mid-1980s. In each wave of increases, the insurance companies claimed they were facing a "crisis" and could not cover claims unless they boosted their rates. The increases destabilized California's economy and led to insurance rates that were unaffordable. Many companies refused to sell insurance to communities at any price. At the time, California did not require insurance companies to disclose their profits or losses; regulate rates; or bar discriminatory practices.[1]

California voters passed Proposition 103 to address and prevent further crises in the insurance markets. It requires insurance companies doing business in California to open their books to public scrutiny and justify their need for rate changes; an insurance company must obtain the insurance commissioner's approval before it can raise insurance rates. The law also bars discriminatory practices by the industry. To make sure their reforms were fully implemented and enforced, voters made the office of insurance commissioner an elected post, and gave the commissioner very broad authority to protect the insurance marketplace *particularly when insurance companies destabilize the marketplace.*

Q: Will AB 2167 make homeowners' insurance more accessible and affordable?

A: No. AB 2167 will allow insurance companies to overcharge Californians, making problems in the marketplace worse, not better.

Q: Has Proposition 103 Kept Rate Artificially Low and are Insurance Companies Facing Insolvency?

A: No. The Insurance Commissioner has consistently approved applications for homeowners and renters rate changes, at the amount they have requested, since the first severe wildfire season a few years ago. Commissioner Lara recently estimated the number of those approvals to be in the hundreds. Proposition 103 requires the Commissioner to protect the solvency of the insurance companies.

Q: Is AB 2167 consistent with, and Incorporate, Proposition 103's Protections Against Excessive Rates and Discrimination?

A: No. Though the insurance lobby disingenuously says that AB 2167 is consistent with Proposition 103. That is FALSE.

AB 2167 explicitly creates a separate rate process, in a separate part of the Insurance Code, to which Proposition 103 – including its protections and detailed regulations – does not apply. These new provisions explicitly conflict with Proposition 103 and its implementing regulations, and would allow insurance companies to impose massive rate increases. (*Comparisons below*.)

---

[1]Independent analyses later concluded that the insurance industry "manufactured" the crises. (See, for example, *The Manufactured Crisis*, Consumer Reports 51 (August 1986); *Premium Increases and Refusals to Deal in the Property/Casualty Insurance Industry: Hearing Before the Judiciary Committee, U.S. Senate* (February 21, 1986) [Testimony of Jay Angoff, Counsel, National Insurance Consumer Organization at 5, *citing* Best's Insurance Management Reports, Release No. 31, December 30, 1985, at 9].

Prop 103:	AB 2167:
Ins. Code Division 2, Part 1, Chapter 9.	Ins. Code Division 2, Part 1, Chapter 12

AB 2167 would enact new standards for setting rates that conflict with those the voters established in Proposition 103. Section 10109.1 of AB 2167 authorizes an insurance company to submit an "Insurance Market Action Plan (IMAP)" that allows the company to seek "adequate rates" and contains a plan to "maintain the insurer's solvency." *What do these terms mean?* Section 10109.3 states that rates must be "actuarially sound": *this is industry jargon for deregulation*, since it would allow insurance company actuaries to substitute their judgment for the Insurance Commissioner's. That is how California insurance law was interpreted prior to the passage of Proposition 103. The phrase "adequate to cover expected losses" does not appear in Proposition 103, and would give insurance companies far more latitude to inflate risk and loss projections then Proposition 103 regulations permit.

Prop 103	AB 2167
Section 1861.05 (a): No rate shall be approved or remain in effect which is excessive, inadequate, unfairly discriminatory or otherwise in violation of this chapter. In considering whether a rate is excessive, inadequate or unfairly discriminatory, no consideration shall be given to the degree of competition and the commissioner shall consider whether the rate mathematically reflects the insurance company's investment income.	Section 10109.1 (a): (1) A request for adequate rates, as described in Section 10109.3. (2) A plan for maintaining the insurer's solvency as policy count grows in IMAP counties, taking into account, among other things, risks related to overconcentration in high-risk communities. Section 10109.3 (a): A rate proposed … shall not be excessive, inadequate, or unfairly discriminatory, and shall be actuarially sound so that premiums are adequate to cover expected losses, expenses, and taxes, and shall reflect investment income of the insurer.

AB 2167 explicitly overrides Proposition 103's protections against common insurance industry accounting tricks that inflate rates and premiums. For example, section 10109.5 (a)(1) dictates the assumptions that insurance companies can use to project future losses that conflict with the highly detailed Proposition 103 regulations now in place.

Prop 103:	AB 2167:
§ 2644.7. Loss and Premium Trend. (a) "Loss trend" and "premium trend" is the process by which forces not reflected in historical loss and premium data are expected to affect losses and premiums in the rating period.	10109.5 (a) An insurer that submits an IMAP filing pursuant to this chapter shall receive an expedited review of its rate filing if either of the following conditions are met:

(b) Trend factors shall be based on the exponential curve of best fit. Companies shall file the most recent 8, 12, 16, 20, and 24 quarters of rolling calendar year data excluding catastrophes. The premium and loss trend factors shall be developed using the insurer's most actuarially sound company-specific rolling calendar year data excluding catastrophes, for the most recent 8, 12, 16, 20, or 24 quarters. The insurer shall file its rate change application using the single data period that it determines to be the most actuarially sound. The Commissioner may require the use of an alternative data period if the Commissioner determines that use of the alternative is the most actuarially sound. Frequency trend shall be calculated as reported or closed claims divided by exposures. Severity trend shall be calculated on paid losses divided by closed claims or total paid losses, including partial payments in previous calendar years, on closed claims divided by closed claims. The insurer shall submit the frequency and severity calculations on all bases, and shall demonstrate that its selection is the most actuarially sound. Premium trend factors shall be developed using company-specific premium per exposure data. (c) Where the trend factor within a given line significantly varies by subline, by policy limits, by region of the state, or by coverage, separate trend factors shall be calculated in accordance with that evidence. § 2644.6. Loss Development. "Loss development" is the process by which reported losses are adjusted for anticipated payout patterns. Loss development shall be presented as a loss-development triangle, based on the dollar-weighted average of the ratios of losses for the three most recent accident-years, policy-years or report-years available for a reporting interval. Filings shall contain both paid losses and case-specific reserves, stated separately. Loss development shall employ either paid losses or the sum of paid losses and case-specific reserves. The insurer shall submit both the factors and ultimate losses or claims for the paid and incurred loss and the reported and the paid claims development calculations, and shall demonstrate that its selection is the most actuarially sound. Loss development data shall exclude catastrophes. Where the loss development factors within a given line significantly vary by subline, by size of loss, or by coverage, separate loss development factors shall be calculated in accordance with that evidence.	(1) The insurer uses an actuarial assumption for trend and loss development that is at the midpoint or less of rate impacts, and does not otherwise change any other aspect of its rate filing from its previous department approved rate.

Q: Is the section of AB 2167 allowing insurance companies to pass through to consumers the costs of expenses like reinsurance a good idea?

A: No. Another egregious provision that conflicts with Proposition 103 is section 10109.5 (a)(2), which allows insurance companies to pass through the cost of "reinsurance" to California homeowners.

Prop 103:	AB 2167:
10 CCR § 2644.25. Reinsurance (a) For all lines and sublines except for those listed in	10109.5 (2) The insurer files for a rate increase based solely on increased reinsurance costs,

the next subparagraph [earthquake and medical malpractice], ratemaking shall be on a direct basis, with no consideration for the cost or benefits of reinsurance.	subject to the requirements of Section 10109.6, and does not otherwise change any other aspect of its rate filing from its previous department approved rate.
	10109.6. If a rate requested as part of an IMAP filing includes the net costs of reinsurance, including internal or external reinsurance, the reinsurance agreement shall be entered into in good faith in an arm's length transaction and at fair market value for the coverage provided. The reinsurance shall meet the department's statement credit requirements.

Q: What is reinsurance?

A: Reinsurance is coverage that insurance companies buy from other insurance companies to cover future claims. For example, State Farm General, which sells homeowners insurance in California, buys reinsurance from its parent company, State Farm Mutual.

Reinsurance rates are not regulated, and reinsurance policies are often inside deals negotiated between subsidiaries and affiliates of the same company. As a result, the price that insurance companies pay to buy reinsurance is often grossly inflated. Fraudulent inter-affiliate reinsurance transactions designed to artificially boost the insurance company's financials were at the heart of the infamous AIG Insurance criminal scandal that came to light in 2006.

Since AB 2167 would allow reinsurance expenses to be incorporated in rates and passed through to consumers, insurance companies would have every incentive to maximize reinsurance premiums in order to generate more investment income. For these reasons, Proposition 103 regulations in place since the early 1990s expressly block pass-thru of reinsurance expenses.

AB 2167's reinsurance pass-thru requirement would by itself cause immediate and calamitous rate increases.

Similarly, the blanket authority in AB 2167 to include "expected expenses" in rates would allow insurance companies to raise premiums to cover political contributions and excessive executive salaries, both of which are expressly excluded from rates under Proposition 103 rules. (See 10 CCR § 2644.10 - Excluded Expenses.)

Q: Is the expedited review mandated in AB 2167 as good for consumers as the insurance industry says it is?

A: No. Like much of AB 2167, it makes matters worse. Under AB 2167, companies that take advantage of these improper giveaways are granted "expedited review" by the Commissioner. Instead of a 180-day review process, AB 2167 would require the Commissioner to fast-track review within 120 days. This "fast-track" authority would undermine the Commissioner's ability to carefully review proposed rate increases – and conflicts with the current, consumer friendly process.

Prop 103:	AB 2167:
1861.05 (c) … a rate change application shall be deemed approved 180 days after the rate application is received by the commissioner (A) unless that application has been disapproved by a final order of the commissioner subsequent to a hearing, or (B) extraordinary circumstances exist. For purposes of this section, "received" means the date delivered to the department. (d) For purposes of this section, extraordinary circumstances include the following: (1) Rate change application hearings commenced during the 180-day period provided by subdivision (c). If a hearing is commenced during the 180-day period, the rate change application shall be deemed approved upon expiration of the 180-day period or 60 days after the close of the record of the hearing, whichever is later, unless disapproved prior to that date. (2) Rate change applications that are not approved or disapproved within the 180-day period provided by subdivision (c) as a result of a judicial proceeding directly involving the application and initiated by the applicant or an intervenor. During the pendency of the judicial proceedings, the 180-day period is tolled, except that in no event shall the commissioner have less than 30 days after conclusion of the judicial proceedings to approve or disapprove the application. Notwithstanding any other provision of law, nothing shall preclude the commissioner from disapproving an application without a hearing if a stay is in effect barring the commissioner from holding a hearing within the 180-day period. (3) The hearing has been continued pursuant to Section 11524 of the Government Code . The 180-day period provided by subdivision (c) shall be tolled during any period in which a hearing is continued pursuant to Section 11524 of the Government Code . A continuance pursuant to Section 11524 of the Government Code shall be decided on a case by case basis. If the hearing is commenced or continued during the 180-day period, the rate change application shall be deemed approved upon the expiration of the	10109.5 (b) The time period for the expedited rate review shall not exceed 120 days, and the department shall not request that the insurer waive the 120-day requirement.

180-day period or 100 days after the case is submitted, whichever is later, unless disapproved prior to that date.	

Q: Does AB 2167 protect California communities against insurance discrimination?

A: No. Insurance companies have long sought to penalize entire communities for arbitrary and unjustified reasons. The redlining and territorial rating that insurance companies are engaged in across California, as they arbitrarily refuse to sell or renew coverage in areas they deem to be "too risky," is a form of the same discriminatory practices that the industry engaged in decades ago, when insurance companies were exempt from California's civil rights laws.

As part of Proposition 103, the voters for the first time made insurance companies subject to state civil rights, consumer protection and fair competition laws.

Under AB 2167, Proposition 103's protections do not apply, as noted above. In particular, the changes made by Section 10109.3 require an insurance company's rate increases be approved even if the rate would violate other state law protections against discrimination (See Proposition 103's section 1861.05(a), above, giving the Commission the authority to block rate increases if the rate is "otherwise in violation of" Proposition 103.") Indeed, Section 10109.7 of AB 2167 explicitly forces the Commissioner to set aside any "contested issue" – such as unfair discrimination – "other than a rate calculation." (Section 10109.7).

The insurance industry is pressing for this exemption from Proposition 103's anti-discrimination provisions because it wants carte blanche to continue to arbitrarily discriminate against an expanding list of California communities it deems "too risky." Instead of having to prove that their redlining of these communities is justified, AB 2167 is a get out of jail free card for the insurance industry. AB 2167 undermines the Commissioner's ability to prevent insurance companies from engaging in exactly the kind of underwriting and other insurance company abuses that are plaguing Californian homeowners.

Q: Will AB 2167 make homeowners insurance more affordable?

A: No. To the contrary, deregulating insurance rates means premiums will skyrocket.

Q: Will AB 2167 make homeowners insurance more available?

A: No. The insurance industry argues that if AB 2167 is passed, it will resume selling and renewing insurance for people and communities from which the insurance companies have withdrawn. In its preamble, which is not enforceable law, AB 2167 says "The Legislature finds these measures are necessary to limit the number of insurer-initiated non-renewals that occur in response to changes in the understanding of wildfire risk." (Section 1 (c)(3)(A).) The preamble further asserts that the companies will make such "assurances." (Section 1(b)(3).) But nothing in the text of AB 2167 actually requires any insurance company to sell or renew a policy to all Californians who want one.

In fact, AB 2167 says only that "An insurer shall commit …to offer new and renewal residential property insurance policies…." (Section 10109.1(b)(1).) But this vague language requires no more than a *pledge*; it does not impose an obligation that is *enforceable* and there is no penalty if an insurance company violates its "commitment." Moreover, AB 2167 expressly allows an insurer to escape its "commitment" to "avoid overconcentration in any one particular area… in order to prevent a catastrophic loss that could impair its solvency." These vague terms have no definition or meaning – they are "escape clauses" that the insurance lobby has written to escape any true legal obligation.

Even if the insurance industry decided to sell or renew policies in so-called "risky" communities, once insurance rates are deregulated, most people will be unable to afford to purchase them.

Thus, AB 2167 is a no-lose deal for the insurance industry**.**

Q: Is it true, as the insurance companies argue, that AB 2167 is necessary because it permits the establishment of Insurance Marketing and Assistance Plans (IMAP) as the key to accessible and affordable homeowners' insurance?

A: No: AB 2167 is not necessary to establish Insurance Marketing and Assistance Plans (IMAPs) for risky geographic regions. *The Insurance Commissioner already has the power to establish IMAPs under Proposition 103*. Proposition 103 reads:

> Emergency Authority
> 1861.11. In the event that the commissioner finds that (a) insurers have substantially withdrawn from any insurance market covered by this article, including insurance described by Section 660, and (b) a market assistance plan would not be sufficient to make insurance available, the commissioner shall establish a joint underwriting authority in the manner set forth by Section 11891, without the prior creation of a market assistance plan.

Q: Does AB 2167 further the purposes of Proposition 103?

A: No. Like many ballot measures, Proposition 103 contained the following limitation on the power of the Legislature: "The provisions of this act shall not be amended by the Legislature except to further its purposes by a statute passed in each house by roll call vote entered in the journal, two-thirds of the membership concurring[.]"

As the California Supreme Court explained in invalidating another industry sponsored bill to exempt certain insurance companies from Proposition 103:

> [T]he voters have the power to decide whether or not the Legislature can amend or repeal initiative statutes. This power is **absolute** and includes the power to enable legislative amendment *subject to conditions attached by the voters.* (*Amwest Surety Ins. Co. v. Wilson*, 11 Cal.4th 1243, 1251 (1995) (italics in original)).

The Supreme Court made clear that it would not simply defer to the Legislature's determination that an amendment to Proposition 103 "furthered its purposes." The analysis must look at the measure's purposes and each of its provisions.

The voters stated that the purpose of Proposition 103 "is to protect consumers from arbitrary insurance rates and practices, to encourage a competitive insurance marketplace, to provide for an accountable Insurance Commissioner, and to ensure that insurance is fair, available, and affordable for all Californians."

AB 2167 explicitly conflicts with and undermines these purposes and provisions of Proposition 103.

AB 2167 also conflicts with Proposition 103 by usurping and overriding the authority the voters explicitly bestowed upon the Insurance Commissioner to regulate insurance companies. In *The Foundation for Taxpayer and Consumer Rights v. Garamendi* (2005) 132 Cal.App.4th 1354, the Court of Appeal reviewed a legislative amendment sponsored by Mercury Insurance to modify the Commissioner's authority to regulate auto insurance premiums. The Court said:

> In enacting Sen. Bill 841, the Legislature sought to override the Insurance Commissioner's authority to set rates and premiums for automobile insurance. … In providing for an elected rather than appointed commissioner, the voters made the Insurance Commissioner responsive to the voters, not the Legislature. Under Proposition 103, therefore, it is the Insurance Commissioner rather than the Legislature that is vested with ratemaking authority subject to the appropriate ratemaking process. (*Id*. at 1372.)

Therefore, AB 2167 is also an unconstitutional amendment to Proposition 103.

Q: Does AB 2167 address climate change?

A: No. AB 2167 claims it is needed to address the impact of "climate change." But nothing in the bill does so.

Q: Does AB 2167 do anything to require insurance companies to pay wildfire claims?

A: No. Insurance companies are refusing to pay many of the claims arising out of previous wildfires. Reneging on their legal obligations, they have forced Californians to accept low-ball settlements or bring lawsuits that will take years to resolve. Nothing in AB 2167 addresses the insurance industry's appalling claims practices