

March 11, 2025

The Honorable Ricardo Lara
Commissioner of Insurance
California Department of Insurance
300 Capitol Mall, 17th Floor
Sacramento, CA 95814
via email: commissionerlara@insurance.ca.gov

Re: State Farm General Insurance Company Request for Emergency Interim Rate Approval

Commissioner Lara,

Thank you for your time during our February 26 meeting as we answered your questions about State Farm General's Request for Emergency Interim Rate Approval. Throughout the pendency of these rate applications, and since our emergency request, we have been focused on providing you and your staff the information you need to safeguard the public's interests. We strongly believe this is best achieved by emergency approval of an interim rate, which indicates to providers of capital and rating agencies that there is a path for State Farm General (SFG) and the larger homeowners market toward a sustainable future even in the face of recent catastrophes.

Meanwhile, we have refrained from 'relitigating' before you our disagreements with intervenor Consumer Watchdog, as a public hearing is the place for a full and fair airing of relevant matters prior to a decision on a final rate. But as you continue to consider our request, we are compelled to correct the intervenor's ongoing mischaracterizations and misunderstandings. They propound an alternate reality where property insurers are making enormous profits in California but are inexplicably pulling back from the market. As we have said for many months, our aim is to create a path forward for SFG, its customers and the California market. We had hoped that given this crisis, all parties would work toward a solution, but evidently that is not the intervenor's goal.

- **The Commissioner has interim rate authority here.** Contrary to assertions, no one is suggesting there won't be a public hearing prior to a final rate approval absent settlement, fully consistent with Prop 103. And "plainly invalid rates" *under the regulations* is not the only legally recognized basis for an interim rate approval, as shown by past court decisions recognizing such authority to remedy unconstitutionally confiscatory rates, for example. The Commissioner has broad authority and discretion under Prop 103, and nothing in that law forbids him from taking emergency action to protect consumers from an approaching insolvency by granting the insurer an interim rate increase.
- **SFG has pursued needed rate with urgency and transparency.** Since these solvency-based rate applications were originally filed last summer, SFG has maintained continuous communications with the California Department of Insurance (CDI) as together we tried to work through the novel issues presented. We have publicly provided hundreds of pages of data and responded to every request from CDI in SERFF, including providing relevant data from confidential trade secret documents and inviting CDI to advise us what further information from those documents may be needed. And we have voluntarily responded to every Request for Information (RFI) from the intervenor. As counsel for

CDI noted at the February 26 meeting, “we have determined [that SFG has] made a preliminary showing that they can get the interim rates subject to refunds with interest, if necessary.”¹ SFG is prepared to further support its rate request in a public hearing, including through full first quarter 2025 data when it becomes available later in the spring.

- **SFG’s reinsurance program is structured to protect its own solvency for the benefit of its customers.** It is because of reinsurance that SFG hasn’t already been forced to massively reduce its book of business. And it is because of reinsurance that SFG still has a chance to retain much of that business, assuming an emergency rate is approved. The fact that SFG paid more for reinsurance over an arbitrary time period than it received back in recoveries isn’t evidence of a ‘bad deal’ any more than is a homeowner paying for insurance even in years their house didn’t burn down – because no one can know in advance when it will. Otherwise, no one would buy insurance at all. Catastrophe reinsurance, even more than primary insurance, is all about coverage for infrequent but very high severity events. SFG’s reinsurance premium payments to State Farm Mutual Automobile Insurance Company (its primary reinsurer) have provided SFG with an average of \$4.0 billion in annual coverage over the last 10 years, and \$8.8 billion in the most recent treaty year. Based on market insights from our reinsurance broker, placing this much coverage with third party reinsurers would be at a rate significantly higher than that charged by State Farm Mutual, if it could be placed at all under today’s difficult reinsurance market conditions in which many reinsurers are viewing CA wildfire as too volatile to allocate more capacity to the peril. In any case, the Los Angeles wildfires, for which SFG will retain roughly \$200 million while receiving billions of dollars of reinsurance recoveries from State Farm Mutual, illustrate with crystal clarity why SFG prudently administers a robust reinsurance program, and that it is designed to protect SFG’s solvency and not to maximize reinsurer profits.
- **Subrogation recoveries have been properly allocated between SFG and its reinsurers.** Another aspect of the intervenor’s confusion around reinsurance appears to stem from the treatment and timing of subrogation recoveries from the 2017 and 2018 wildfires. Subrogation recoveries received in 2020 and later years related to these earlier fires were contractually owed to internal and external reinsurers to the extent that the losses from the events exceeded losses SFG was required to retain under its reinsurance contracts. In essence, the reinsurers were reimbursed for their share of the losses that they absorbed in the first place. Without this contractual obligation to pass through subrogation recoveries to reinsurers, the availability and cost of reinsurance would be far more challenging for primary insurers than it is today.
- **Any allegation of “anticompetitive strategy” or “predatory pricing” by SFG is baseless.** The idea that SFG purposely kept its rates artificially low so that it could grab market share is so far from the truth that it’s hardly worth responding, but we direct you to a recently published piece² from a long-time industry observer who deftly summarizes its preposterous nature. He notes: “State Farm’s rapid growth ... was the result of being the last insurer standing. This is a common problem for State Farm. When everyone else leaves in a hurry, and they remain, suddenly all the business flows to them. They are guilty of being slow to turn off the spigot and join the others in a panic. If State Farm was a public company, as opposed to a mutual controlled by policyholders, investors would hate this behavior. As a

¹ See Transcript of February 26, 2025 meeting between the parties, at 28:7-9.

² See Brian Sullivan, “Setting the Record Straight: State Farm Didn’t Burn California,” Property Insurance Report, March 6, 2025 (<https://df9fd9b6ab64495ad759-f14ba961ae89374e6d5a8ee602c09059.ssl.cf5.rackcdn.com/1919.pdf?i=817248>).

regulator, or as a consumer, or a consumer group, this market-stabilizing activity is exactly the kind of thing you hope for out of your market leader.” He says that SFG warned of rate inadequacy “very publicly” and “over and over as they requested substantial rate increases.” Continuing: “Verifying these claims were financial statements ... showing enormous underwriting losses that were draining available capital. ... State Farm was not lowballing the market. They were charging the maximum [the historical regulatory approach] would allow. To suggest that State Farm was intentionally charging too little is to ignore the available facts.” Finally, it’s important to remember that during much of the last decade, the rating regulations were applied (over SFG’s objection) to reduce SFG’s allowable rate by the imputed investment income of its parent company. That issue was not resolved until litigation upholding SFG’s objection finally concluded in 2022, which then allowed SFG additional rate in CDI’s rating formula.

- **Any allegation of SFG “manipulating” regulators or the public through its emergency request is likewise baseless.** The intervenor points to recent social media coverage of unofficial comments in a personal setting from an individual no longer associated with any State Farm company. This person was never an officer of SFG, never supervised any officers of SFG and was never involved in or had any responsibility for business decisions relating to SFG or its California operations, including anything to do with our pending rate requests or exposure reduction measures. SFG’s actions and communications have been grounded in our attempts to be forthright with you and with the public about the economic realities we face and the difficult choices before us.
- **Writing new policies doesn’t make any sense at this time.** Having blamed SFG’s problems on growing too much without securing sufficient rate increases, the intervenor suggests the remedy is more of the same. This fails to understand basic economic realities of the business of insurance. Increasing our risk exposure wouldn’t be responsible for an insurer that’s already struggling to maintain statutorily-required levels of surplus for the exposure it already has.
- **Our rate request isn’t about SFG’s so-called “Wall Street credit rating.”** As the intervenor well knows, SFG is not listed on any stock exchange, nor is its parent, which is a mutual company with no shareholders. SFG does not use any external financing such that its “credit rating” would matter. Rather, we’re seeking to prevent an additional downgrade to SFG’s “financial strength rating,” as determined by independent rating agencies, which is a metric used by mortgage lenders to determine whether policyholders can use SFG insurance to meet the mortgage lenders’ insurance requirements. In addition to AM Best’s downgrade of SFG’s financial strength rating last year, S&P Global Ratings recently announced that it has placed SFG on what it calls a “CreditWatch with negative implications,” a review process that “could lead to a rating downgrade by multiple notches.”³ As explained previously, a downgrade of sufficient magnitude could mean mortgage lenders might not accept SFG insurance as adequate protection for their mortgage collateral (i.e. the insured structure). If that were to happen, homeowners with a mortgage might be forced to find other insurance – likely the FAIR Plan - without any action at all on SFG’s part. That is, the primary concern here is *for our policyholders*, as SFG has explained to the intervenor from the day it requested an interim rate. This potential impact on consumers is what drives the urgency behind our emergency request.

³ See <https://disclosure.spglobal.com/ratings/en/regulatory/article/-/view/type/HTML/id/3328722> (“State Farm General Insurance Co. ‘AA’ Ratings Placed On CreditWatch Negative On Weakening Capital Position,” published February 25, 2025).

- **Consideration of parental support depends on emergency rate approval.** As we explained on February 26th, “the State Farm Mutual Board is comprised of all external, independent directors except for the State Farm Mutual CEO” and “their fiduciary duties require them to exercise reasonable care, judgment, and diligence [around] what is in State Farm Mutual’s best interest as an entity and its policyholder group as a whole.” State Farm Mutual has policyholders in all 50 states, including California residents who may not own a home or have any SFG products. It would be imprudent to ask State Farm Mutual’s Board of Directors to consider injecting capital into a company whose prospects for repayment are grim without emergency rate approval and continuing transformational reforms to the market. It has been noted that State Farm Mutual has offered capital support to an affiliate in the past, such as in the case of Texas. That example is actually instructive, as the rating environment there has in fact allowed that particular surplus note to be entirely repaid, with interest. Without realistic prospects for an affiliate to be able to stand on its own, parental support would merely temporarily mask whatever is contributing to its financial distress and the affiliate would before too long revert to where SFG is today. That said, we reiterate our assertion at the meeting that an emergency rate approval would be a positive sign in support of a request from SFG to the State Farm Mutual Board of Directors for financial assistance.

In conclusion, Commissioner, in the interest of our customers and the entire California insurance market, we respectfully urge you to grant our emergency interim rate request with immediacy, while leaving any remaining issues to be resolved at a full public hearing if the parties are unable to first reach a settlement.

Sincerely,



Dan Krause
President and Chief Executive Officer
State Farm General Insurance Company



Mark Schwamberger
Vice President and Treasurer
State Farm General Insurance Company



Keesha-Lu Mitra
Vice President and General Counsel
State Farm General Insurance Company

CC: Michael Martinez, Chief Deputy Commissioner, California Department of Insurance
Nikki McKennedy, Assistant Chief Counsel, California Department of Insurance
Pamela Pressley, Senior Staff Attorney, Consumer Watchdog
Vanessa Wells, Esq., Hogan Lovells