

HOGAN LOVELLS US LLP

Vanessa Wells (Bar No. 121279)
855 Main Street, Suite 200
Redwood City, CA 94063
Telephone: (650) 463-4000
Facsimile: (650) 463-4199
vanessa.wells@hoganlovells.com

Michael M. Maddigan (Bar No. 163450)
Jordan D. Teti (Bar No. 284714)
1999 Avenue of the Stars, Suite 1400
Los Angeles, CA 90067
Telephone: (310) 785-4600
Facsimile: (310) 785-4601
michael.maddigan@hoganlovells.com
jordan.teti@hoganlovells.com

Katherine B. Wellington (Massachusetts
Bar No. 688577)
125 High Street, Suite 2010
Boston, MA 02110
Telephone: (617) 371-1000
Facsimile: (617) 371-1037
katherine.wellington@hoganlovells.com

Attorneys for Applicant
STATE FARM GENERAL INSURANCE
COMPANY

**BEFORE THE INSURANCE COMMISSIONER
OF THE STATE OF CALIFORNIA**

In the Matter of the Rate Applications of

STATE FARM GENERAL INSURANCE
COMPANY,

Applicant.

File Nos. PA-2024-00011, PA-2024-00012,
PA-2024-00013

**STATE FARM GENERAL'S BRIEF IN
SUPPORT OF INTERIM RATE
REQUEST AND RESPONSE TO
CONSUMER WATCHDOG'S PRE-
HEARING OBJECTIONS**

TABLE OF CONTENTS

TABLE OF AUTHORITIES ii

I. INTRODUCTION 1

II. UNDER LONGSTANDING PRECEDENT, THE COMMISSIONER HAS BROAD
AUTHORITY TO APPROVE AN INTERIM RATE INCREASE 4

A. The Commissioner Has Broad Authority To Grant An Interim Rate Increase 4

B. The ALJ Should Reject Consumer Watchdog’s “Plainly Invalid” Standard 6

III. STATE FARM GENERAL AND THE COMMISSIONER PROPERLY STIPULATED
TO INTERIM RATES 7

A. The Stipulated Rates Are Fundamentally Fair, Adequate, Reasonable, And In The
Interests Of Justice 7

1. *The requested interim rates are fundamentally fair, adequate, and reasonable* ... 8

2. *The requested interim rates are in the interests of justice* 10

B. Even If The “Plainly Invalid” Standard Applies, It Is Met Here 14

C. Consumer Watchdog’s Discussion Of Variances 6 And 10 Is Irrelevant 16

D. Consumer Watchdog’s Complaints About “Transparency” Are Really A Discovery
Dispute Properly Addressed As Part Of The Rate Hearing 16

E. Consumer Watchdog’s Remaining Objections Are Meritless 17

IV. CONSUMER WATCHDOG HAS A FULSOME OPPORTUNITY TO PRESENT
EVIDENCE AND ARGUMENT 24

V. CONCLUSION 24

TABLE OF AUTHORITIES

CASES:

<i>20th Cent. Ins. Co. v. Garamendi</i> (1994) 8 Cal.4th 216	3, 6, 16
<i>Barclay Hollander Corp. v. California Reg'l Water Quality Control Bd.</i> (2019) 38 Cal.App.5th 479	24
<i>Birkenfeld v. City of Berkeley</i> (1976) 17 Cal.3d 129	4
<i>Calfarm Ins. Co. v. Deukmejian</i> (1989) 48 Cal.3d 805	<i>passim</i>
<i>Pinnacle Armor, Inc. v. United States</i> (9th Cir. 2011) 648 F.3d 708	24
<i>State Farm General Ins. Co. v. Lara</i> (2021) 71 Cal.App.5th 148	6, 16, 17

STATUTES:

1988 Cal. Legis. Serv. Prop. 103, § 2	1
Cal. Code Regs., tit. 10, § 2656.1	
(a)	7
(c)	3, 7
(g)	2
Cal. Ins. Code § 1861.05	
subd. (a)	3-5

OTHER AUTHORITIES:

Cal Fire, Top 20 Largest California Wildfires (Oct. 2024), available at https://34c031f8-c9fd-4018-8c5a-4159cdff6b0d-cdn-endpoint.azureedge.net/-/media/calfire-website/our-impact/fire-statistics/top-20-largest-ca-wildfires.pdf?rev=097f901c128347149e2614f2fca4f546&hash=27DDE83DFEF9A69E67C73765892A2B75	23
Law & Alvarado, California homeowners insurance: Current state of the market and implications of the Los Angeles wildfires (Jan. 22, 2025), available at https://www.milliman.com/en/insight/california-homeowners-insurance-los-angeles-wildfires	21
Sullivan, <i>Setting The Record Straight: State Farm Didn't Burn California</i> (Mar. 6, 2025), available at https://df9fd9b6ab64495ad759-f14ba961ae89374e6d5a8ee602c09059.ssl.cf5.rackcdn.com/1919.pdf?i=817248	21

I. INTRODUCTION

State Farm General Insurance Company (“State Farm General”) has served the people of California for more than 60 years and shares the State’s goal of “ensur[ing] that insurance is fair, available, and affordable to all Californians.” (1988 Cal. Legis. Serv. Prop. 103, § 2.) But State Farm General cannot provide California homeowners with “fair, available, and affordable” insurance if its financial strength continues to deteriorate. State Farm General’s surplus—the money available to pay claims—has decreased from almost \$4 billion to around \$1 billion over the past decade, in significant part due to the increasing frequency and severity of California wildfires. (Declaration of David Appel ¶¶ 20, 43–45 [hereinafter “Appel Decl.”].) State Farm General has estimated that it will pay over \$7 billion in claims related to the Los Angeles wildfires. (SFG-VW-13, Letter from State Farm General to Commissioner Lara, dated Feb. 25, 2025 at p. 1 [hereinafter “Feb. 25 Letter”].) Although most of State Farm General’s losses will be covered by reinsurance, State Farm General expects its surplus to be further diminished by \$400 million following the wildfire claims. (*Id.*) State Farm General’s vastly depleted surplus, combined with the clear potential for future catastrophic loss in California demonstrated by the Los Angeles wildfires, has led to increasing concerns about State Farm General’s financial strength. (Appel Decl. ¶¶ 26–44;.) (Declaration of Bryon Ehrhart ¶¶ 13-14 [hereinafter “Ehrhart Decl.”].)

State Farm General’s financial strength matters because mortgage companies in California require policyholders to insure their homes with insurers that meet a particular financial strength rating from one of four credit rating agencies. (Appel Decl. ¶¶ 39-41). AM Best and S&P Global Ratings are the two credit rating agencies that large insurers most widely rely upon. (*Id.* at ¶ 40); (Ehrhart Decl. ¶¶ 13-14.) AM Best has already downgraded State Farm General, and S&P has now placed State Farm General on a “CreditWatch with negative implications,” a review process that “could lead to a rating downgrade by multiple notches.” (Appel Decl. ¶¶ 41, 44); *see* (SFG-VW-1, Letter from State Farm General to Commissioner Ricardo Lara , dated Mar. 20, 2024) at p. 3 [hereinafter “Mar. 2024 Letter”]; (SFG-VW-14, Letter from State Farm General to Commissioner Lara, dated Mar. 11, 2025 at p. 3 [hereinafter “Mar. 11 Letter”].)

1 If State Farm General’s financial strength does not improve and S&P downgrades State
2 Farm General, it “could jeopardize the stability of the entire California homeowners market.”
3 (Appel Decl. ¶ 41.) State Farm General policyholders with a home mortgage will need to find a
4 new insurer—affecting hundreds of thousands of people. (*Id.* ¶¶ 37, 40-42.) Whether such
5 policyholders will be able to find new insurance, apart from the FAIR Plan, following the recent
6 spate of insurers leaving California is in serious question. (*See id.* ¶ 38 [explaining that if SFG is
7 “unable to continue writing its share of the market (almost 20%) . . . [i]t is highly unlikely that
8 other insurers, or the FAIR plan, could absorb such a shock”]); (*Id.* ¶ 42 [similar].) State Farm
9 General wants to stay in the California market, but it needs an interim rate increase to improve its
10 financial strength and prevent a ratings downgrade that would be harmful to policyholders.

11 State Farm General requested a rate increase on June 27, 2024, for its homeowners non-
12 tenant HO-3 and renter/condo tenant, and on July 5, 2024, for its rental dwelling lines. (SFG-VW-
13 2, SFG’s Rate Application (No. 24-1271); SFG-VW-3, SFG’s Rate Application (No. 24-1273);
14 and SFG-VW-4, SFG’s Rate Application (No. 24-1330), respectively.) A hearing on State Farm
15 General’s rate applications is currently set to commence by June 1, 2025. (SFG-VW-19, CDI’s
16 Mar. 17, 2025 Notice of Hearing at p. 7:16–18 [hereinafter “Mar. 17 Notice of Hearing”].) In
17 order to help ensure its continuing financial strength and prevent a ratings downgrade prior to the
18 resolution of its rate applications, State Farm General requested an emergency interim rate of
19 21.8% for homeowners non-tenant HO-3 (File No. 24-1271), 15% for renter/condo tenant (File
20 No. 24-1273), and 38% for rental dwelling (File No. 24-1330). On March 14, 2025, the
21 Commissioner “provisionally granted” State Farm General’s request pursuant to a “two-way
22 stipulation between the Department and State Farm” under 10 CCR § 2656.1(g). (SFG-VW-5,
23 Commissioner’s Mar. 14, 2025 Emergency Interim Rate Order at p. 2.)

24 The Commissioner asked the ALJ to set a hearing on April 8, 2025, to “hear from State
25 Farm regarding its emergency rate requests,” including through “evidence and argument provided
26 at the hearing.” (*Id.* at p. 2.) State Farm General respectfully submits this brief to support its
27 request for an emergency interim rate and to respond to Consumer Watchdog’s objections.

1 The Commissioner’s broad authority to approve an interim rate is clear under longstanding
2 California Supreme Court precedent. (*See Calfarm Ins. Co. v. Deukmejian* (1989) 48 Cal.3d 805,
3 825); (Cal. Ins. Code § 1861.05, subd. (a).) The Commissioner may approve a stipulation to an
4 interim rate as long as the “stipulation is fundamentally fair, adequate, reasonable and in the
5 interests of justice.” (Cal. Code Regs., tit. 10, § 2656.1(c)) Those requirements are met here,
6 where a rate increase is plainly warranted following the Los Angeles wildfires. A rate increase
7 will improve State Farm General’s financial strength, help prevent a ratings downgrade that will
8 severely and negatively impact California homeowners, and allow State Farm General to continue
9 operating in California. “In light of [State Farm General’s] current financial condition, the
10 benefits to the market and the absence of risk to policyholders, it seems obvious that the interim
11 rate increase should be approved and implemented as soon as possible.” (Appel Decl. ¶ 60.)

12 It is important to note that an “interim” rate is just that—it is “subject to potential refunds
13 with interest” based on the outcome of the full rate hearing. (SFG-VW-5, Commissioner’s Order
14 Regarding State Farm General’s Request For An Emergency Interim Rate, dated March 14, 2025
15 at p. 3.) In other words, policyholders will get their premiums back from State Farm General
16 (with interest) if the rate determined at the full rate hearing is lower than the interim rate.
17 (*Calfarm Ins. Co.*, 48 Cal.3d at 825); (*20th Cent. Ins. Co. v. Garamendi* (1994) 8 Cal.4th 216,
18 246.) Indeed, this interim rate hearing should simply test whether the stipulation is
19 “fundamentally fair, adequate, reasonable and in the interests of justice” in the context of these
20 emergency conditions. (Cal. Code Regs., tit. 10, § 2656.1(c).)

21 Consumer Watchdog’s various objections should be overruled because they do not
22 undermine the propriety of an interim rate increase under the circumstances here. Consumer
23 Watchdog seeks to improperly expand this limited proceeding into an adjudication of the kind of
24 issues that will be fully assessed at the final rate hearing. For example, Consumer Watchdog’s in-
25 house actuary has attempted to find a handful of purported issues with State Farm General’s
26 interim rate template submitted on February 5, 2025 in support of the interim rates, and has
27 proposed his own rate indication. This kind of actuarial analysis is not necessary for the ALJ to
28

1 approve an interim rate pursuant to California Code of Regulations, title 10, section 2656.1(c).
2 Regardless, Consumer Watchdog’s actuary is wrong. As third-party expert actuary Nancy
3 Watkins explains in her declaration, Consumer Watchdog’s objections are unfounded, as the Rate
4 Template items criticized by Consumer Watchdog are actuarially sound. The ALJ should
5 accordingly approve the interim rate increase.

6 **II. UNDER LONGSTANDING PRECEDENT, THE COMMISSIONER HAS BROAD**
7 **AUTHORITY TO APPROVE AN INTERIM RATE INCREASE.**

8 **A. The Commissioner Has Broad Authority To Grant An Interim Rate Increase.**

9 The Commissioner has authority to grant an interim rate increase pending a full rate
10 hearing. (SFG-VW-6, Letter from Commissioner Lara, dated Feb. 14, 2025 at p. 4 [“The
11 Commissioner has the authority to approve an interim rate increase, as well as discretion in
12 administering the process”].)¹ The California Supreme Court expressly addressed this issue in
13 *Calfarm Insurance Co. v. Deukmejian* (1989) 48 Cal.3d 805, holding that “the commissioner can
14 approve an interim rate,” but if the rate is ultimately deemed too high, “the insurer must refund
15 express premiums collected with interest.” (*Id.* at p. 825.)² The California Supreme Court
16 reiterated that conclusion in *20th Century Insurance Co. v. Garamendi* (1994) 8 Cal.4th 216,
17 making clear that the Commissioner “can approve an interim rate pending” a “final decision” on a
18 rate application. (*Id.* at p. 246.)

19 The Commissioner’s authority to approve an interim rate derives from Proposition 103’s
20 command that “[n]o rate shall be approved *or remain in effect* which is excessive, inadequate,
21 unfairly discriminatory or otherwise in violation of this chapter.” (Cal. Ins. Code § 1861.05, subd.
22 (a) [emphasis added].) Based on this text, as well as the general proposition that administrative
23 officials “may exercise such additional powers as are necessary for the due and efficient

24 ¹ Available at <https://www.insurance.ca.gov/0400-news/0100-press-releases/2025/upload/nr018CommissionerLetterEmergencyInterimRateApproval.pdf>.

25 ² If the Commissioner lacked broad power to approve an interim rate, there would be no way to
26 obtain relief from a confiscatory rate prior to a full rate hearing—which would violate the
27 constitutional protections against confiscation. (*See Calfarm*, 48 Cal. 3d at 823–24 [discussing
28 *Birkenfeld v. City of Berkeley* (1976) 17 Cal.3d 129 and finding no confiscation problem due to
Commissioner’s authority to grant interim rate].)

1 administration of powers expressly granted by statute, or as may be fairly implied from the statute
2 granting the powers,” the California Supreme Court concluded that the Commissioner’s authority
3 to grant interim rate relief is both “necessary for the due and efficient administration of
4 Proposition 103” *and* “fairly ... implied” from Proposition 103’s “command that [n]o rate shall
5 ... remain in effect which is excessive, inadequate, unfairly discriminatory or otherwise in
6 violation of this chapter.” (*Calfarm*, 48 Cal.3d at p. 824-25) [internal quotation marks omitted]);
7 (*see also* Cal. Ins. Code § 1861.05, subd. (a).) The Commissioner thus has broad authority to
8 approve an interim rate.

9 Consumer Watchdog once *agreed* with this straightforward interpretation of Proposition
10 103, stating that “allowing for an interim rate” is “well within the Commissioner’s broad
11 authority.” (SFG-VW-7, Consumer Watchdog’s Opposition Brief at p. 19, *State Farm General*
12 *Ins. Co. v. Dave Jones*, San Diego Sup. Ct. Case No. 37-2016-00041469-CU-MC-CTL (Dec. 22,
13 2017).) Invoking the same authority that State Farm General now relies upon, Consumer
14 Watchdog acknowledged that “two unanimous decisions of the California Supreme Court
15 confirm” that Proposition 103 created a system where insurers may seek interim relief prior to a
16 full rate proceeding, and, if necessary, issue refunds with interest following the full rate
17 proceeding. (*Id.* at pp. 16–17.) Consumer Watchdog acknowledged, moreover, that policyholders
18 were adequately protected in the event that an interim rate proved too high, because they could
19 obtain refunds with interest. (*Id.* [discussing symmetry between insurers’ and insureds’ interests
20 under Proposition 103].) That conclusion is confirmed by the text of Proposition 103, which (1)
21 presupposes that an interim rate may later be proven improper, and (2) envisions that the
22 Commissioner may remedy any harm that comes from an excessive interim rate. (SFG-VW-8,
23 Consumer Watchdog’s Combined Appellants Reply Brief and Cross-Respondent’s Brief at pp. 43,
24 45, *State Farm General Ins. Co. v. Ricardo Lara*, D075529 (Nov. 20, 2020).)

25 The ALJ should hold—consistent with the Commissioner’s position as well as Consumer
26 Watchdog’s own prior position—that the Commissioner has broad discretion to approve an
27 interim rate.

1 **B. The ALJ Should Reject Consumer Watchdog’s “Plainly Invalid” Standard.**

2 Despite Consumer Watchdog’s prior agreement that the Commissioner has broad authority
3 to approve an interim rate, Consumer Watchdog has now changed its position, contending that
4 *Calfarm* permits the Commissioner to approve an interim rate only when the current rate is
5 “plainly invalid.” (See Consumer Watchdog’s Objections at pp. 6–8 fn.10 [hereinafter
6 “Objections”].) Consumer Watchdog claims this requires State Farm General to show that the rate
7 currently in effect is “excessive, inadequate, unfairly discriminatory, or otherwise in violation of”
8 Proposition 103. (*Id.* at p. 8.) That is the standard that State Farm General must meet *at the full*
9 *rate hearing*. (See, e.g., *State Farm General Ins. Co. v. Lara* (2021) 71 Cal.App.5th 148, 160.)
10 But applying that standard to an interim rate makes no sense; the purpose of an interim rate is to
11 allow an insurer to *temporarily* charge higher premiums while the parties litigate what the final
12 rate should be, subject to refunds if the interim rate turns out to be too high. (See *Calfarm*, 48
13 Ca.3d at p. 825.) The ALJ should reject Consumer Watchdog’s attempt to erect an interim rate
14 standard that is impossible to meet without a full rate hearing.

15 According to Consumer Watchdog, its preferred standard is mandated by *Calfarm* and *20th*
16 *Century*. But neither case holds that an interim rate may be granted *only* where the company’s
17 existing rates have been “shown” to be “plainly invalid.” To the contrary, both cases expressly
18 recognize that the Commissioner may approve an interim rate, and if that interim rate turns out to
19 be too high, require the insurer to issue refunds (with interest). (*Calfarm Ins. Co.*, 48 Cal.3d at p.
20 825); (*20th Cent. Ins. Co.*, 8 Cal.4th at p. 246.) *Calfarm* and *20th Century* thus both contemplate
21 that the Commissioner may approve an interim rate without the kind of proof needed to finally
22 determine whether the insurer’s existing rates are “plainly invalid.” This ALJ should instead hold,
23 consistent with the caselaw and the Commissioner’s position, that the Commissioner has broad
24 authority to issue an interim rate *without* requiring the kind of evidence and expert testimony
25 needed at a full rate hearing to finally determine the appropriate rate.

26 This conclusion is fully consistent with *20th Century*, which explains that “any insurer *who*
27 *believes* the rates set by” Proposition 103 “are confiscatory” may file an application “for approval
28

1 of a higher rate,” and the Commissioner “can approve an interim rate pending his or her final
2 decision.” (8 Cal.4th at p. 245-46 [emphasis added].) *20th Century* accordingly recognizes that
3 the Commissioner has broad discretion to approve an interim rate that an insurer believes is
4 necessary, pending a final rate determination, in order to ensure “the due and efficient
5 administration of Proposition 103” and the statutory command that “no rate shall ... *remain in*
6 *effect* which is excessive, inadequate, unfairly discriminatory or otherwise in violation of” law.
7 (*Id.*) The Commissioner is not required to make a determination that the current rate is “plainly
8 invalid” in order to grant interim relief; instead, the Commissioner can enter into a stipulation—
9 pursuant to California Code of Regulations, title 10, section 2656.1(c)—authorizing an interim
10 rate as long as he concludes the rate is “fundamentally fair, adequate, reasonable and in the
11 interests of justice.” This standard reflects the Commissioner’s broad authority to grant interim
12 relief that he believes is warranted under the circumstances. As State Farm General explains in
13 detail below, that standard is met here.

14 **III. STATE FARM GENERAL AND THE COMMISSIONER PROPERLY** 15 **STIPULATED TO INTERIM RATES.**

16 California law permits parties to “stipulate to the resolution of an issue of fact” or “agree to
17 settlement on a mutually acceptable outcome to a proceeding.” (Cal. Code Regs., tit. 10,
18 § 2656.1(a).) If the stipulation is proposed prior to the presentation of testimony, the parties need
19 only support the stipulation with “declarations indicating the reasons that the . . . stipulation is
20 fundamentally fair, adequate, reasonable and in the interests of justice.” (*Id.* § 2656.1(c).) The
21 attached declarations from David Appel, Bryon Ehrhart, and Nancy Watkins amply meet
22 Section 2656.1(c)’s requirements, supporting the conclusion that an interim rate increase is not
23 only warranted, but necessary for State Farm General’s continued operation within the State of
24 California.

25 **A. The Stipulated Rates Are Fundamentally Fair, Adequate, Reasonable, And In** 26 **The Interests Of Justice.**

27 State Farm General’s requested interim rates are fundamentally fair, adequate, reasonable,
28 and in the interests of justice, meeting Section 2656.1(c)’s requirements. State Farm General

1 requested interim rates to improve State Farm General’s financial stability and prevent a
2 downgrade of its financial strength rating, which could happen at any time and would negatively
3 and severely impact State Farm General’s policyholders as well as the broader California
4 insurance market. State Farm General has proposed interim rates that reflect the premium needed
5 to alleviate the current emergency. (*See* Appel Decl. ¶¶ 57–60).

6 *1. The requested interim rates are fundamentally fair, adequate, and reasonable.*

7 State Farm General “calculated an updated rate indication using the standard rate templates
8 included in the filings by changing two inputs: 1) using a 5/1/2025 effective date and 2) a new
9 catastrophe provision that incorporates wildfire loss estimates up through the most recent fires.”
10 (SFG-VW-9, State Farm General Feb. 3, 2025 Letter at p. 3 fn.6 [hereinafter “Feb. 3 Letter”].)
11 State Farm General requested an interim rate increase at or below the updated CDI template
12 indication, resulting in a requested 22% rate increase for non-tenant homeowners, a 15% rate
13 increase for renters and condominium unit owners, and a 38% increase for rental dwelling. (*See*
14 *id.*) The Commissioner provisionally approved these interim rates, which reflect a fair, adequate,
15 and reasonable estimate of the rate increases necessary to reflect the recent wildfire loss estimates.
16 (*See* SFG-VW-5, Commissioner’s Mar. 14, 2025 Emergency Interim Rate Order at p. 2.)

17 Consumer Watchdog seeks to nitpick these interim rate increases, but *this is not a full rate*
18 *hearing*. State Farm General need only show that its proposed rates are fundamentally fair,
19 adequate, and reasonable. State Farm General has met that standard here, where it has explained
20 that its rates are inadequate due to rapidly declining surplus, the new emergency created by the
21 Los Angeles wildfires and the more than \$7 billion in claims State Farm General has estimated it
22 must pay out, and the potential for an imminent downgrade of State Farm General’s financial
23 strength rating. *Infra* at pp. 10-14; (SFG-VW-15, Feb. 26, 2025 Tr. of the State Farm Interim Rate
24 Approval Hearing at pp. 35:20–36:10 [hereinafter “Feb. 26, 2025 Tr.”].) In these circumstances, it
25 is both fair and reasonable to allow State Farm General to charge a higher interim rate. That is
26 what is required for the Commissioner to approve a stipulated interim rate. The ALJ should reject
27 Consumer Watchdog’s attempt to raise the kind of technical challenge to the interim rates

1 provisionally approved by the Commissioner that would be appropriate in a full rate hearing.

2 Consumer Watchdog claims, for instance, that State Farm General’s homeowner’s rate
3 “could be *decreased* by 11.5% without the rate becoming ‘inadequate,’” and that the maximum
4 permitted rate change is “-0.1%.” (Objections at pp. 9–10.) Consumer Watchdog likewise asserts
5 that smaller rate increases are warranted for renters and condo, and for rental dwelling. (*See id.*)
6 These figures were determined by Consumer Watchdog’s in-house actuary in reliance on
7 unfounded objections to State Farm General’s Rate Template. As third-party expert actuary
8 Nancy Watkins explains, Consumer Watchdog’s technical objections are flawed for various
9 reasons, including because they rely on the wrong regulation and adopt a glaringly problematic
10 apples-to-orange proposal for new “AIY trend factor” figures. [Watkins Decl. ¶¶ 31-35, 50-51.]
11 Ms. Watkins concludes: “CW has failed to show that State Farm’s proposed interim rate requests
12 are excessive. In various respects [Mr. Armstrong’s] selected assumptions are unsupported,
13 undocumented, and non-compliant with CCRs, and taken together they produce maximum
14 permitted rate indications that are not actuarially sound.” [*Id.* ¶¶ 74-75].

15 As another example, Consumer Watchdog contends that “State Farm’s interim rate
16 calculations from February 5 rely on an unsupported weighting scheme used in its catastrophe
17 load calculation, improperly giving excess weight to the 2025 data,” that State Farm General “uses
18 inconsistent time frames for its catastrophe and non-catastrophe loss data,” and that “State Farm’s
19 requested interim rate calculations use an unsupported AIY trend factor.” (Objections at p. 9.)
20 This is wrong, too. As Ms. Watkins explains, State Farm General used an actuarially sound
21 weighting approach that, in part, reflects a “rapidly growing catastrophe risk in California.”
22 (Watkins ¶¶ 48-54.) State Farm General similarly used actuarially sound time frames for
23 inclusion of its updated catastrophe data, which does not ignore the huge loss event of the Los
24 Angeles fires. (Watkins ¶¶ 20-24.) State Farm General likewise used an actuarially sound
25 approach to AIY trend based on the available data, while Consumer Watchdog’s expert appears to
26 have incorrectly relied on total AIY rather than average AIY per exposure. (Watkins ¶¶ 25-35.)

27 Consumer Watchdog’s objections are unfounded. But regardless of the technical specifics
28

1 of the interim Rate Template materials, this is precisely the kind of debate that the parties should
2 take up at the rate hearing—not before the ALJ in a hearing on an interim rate, where the
3 Commissioner and State Farm General have reached a fair, adequate, and reasonable stipulation to
4 address an imminent threat to State Farm General’s financial strength rating and financial stability,
5 and to the California insurance market more broadly. To the extent Consumer Watchdog’s real
6 complaint is that there is not yet perfect data to assess State Farm General’s rate request, or a full
7 hearing where experts may debate which weighting to use, that is precisely why an interim rate is
8 warranted—so the Commissioner can approve a reasonable estimate in light of the clear need for a
9 rate increase, which can then be confirmed at a full rate hearing, with refunds to consumers if the
10 interim rates turn out to be too high. And in any event, it simply defies belief for Consumer
11 Watchdog to take the position that a rate *decrease* is appropriate following the Los Angeles
12 wildfires and in face of undisputed evidence of State Farm General’s declining surplus, which
13 concretely demonstrates that the current rates are not fair, adequate, or reasonable. Leaving State
14 Farm General without any surplus to pay for catastrophic events—which appears to be Consumer
15 Watchdog’s proposed approach—is simply not fair, adequate, or reasonable, nor is it in the
16 interests of the consumers they purport to represent.

17 2. *The requested interim rates are in the interests of justice.*

18 As the Commissioner has recognized, the Governor’s Executive Order N-13-23 explains
19 the need for the Commissioner “to take *prompt regulatory action* to strengthen and stabilize
20 California’s marketplace for homeowner’s insurance and commercial property insurance, and to
21 consider whether the recent sudden deterioration of the private insurance market presents facts that
22 support emergency regulatory action.” (SFG-VW-10, Governor Gavin Newsom’s Executive
23 Order N-13-23 at p. 2 [emphasis added].) The state of emergency announced in the wake of the
24 Los Angeles wildfires, moreover, demonstrates that the need for prompt regulatory action is even
25 more pressing. (See SFG-VW-11, Governor Gavin Newsom’s Proclamation of a State of
26 Emergency (Sept. 21, 2023)); (SFG-VW-12, Commissioner Lara’s Declaration of Emergency
27 Situation (Jan. 7, 2025.)) The Commissioner’s decision to take prompt action and preliminarily

1 approve interim rates in light of the Los Angeles fires is plainly in the public interest, because it
2 will help stabilize State Farm General’s financial position pending a full rate proceeding, in turn
3 protecting homeowners in California who are insured by State Farm General.

4 Well before the Los Angeles wildfires, State Farm General warned that its “swift capital
5 depletion . . . is an alarm signaling the grave need for rapid and transformational action, including
6 the critical need for rapid review and approval of currently pending and future rate filings.” (Mar.
7 20 Letter at p. 3); (*see also* Appel Decl. ¶ 18.) Although State Farm General’s premium grew
8 from \$1.9 billion to \$3.1 billion over the past decade, the company experienced underwriting
9 losses of over \$5.2 billion over the same period. (Appel Decl. ¶ 18.) These losses led to year-
10 over-year decline in surplus totaling over \$2.8 billion. (*Id.* ¶ 20.) Concerted efforts to limit State
11 Farm General’s exposure in high-risk areas were unsuccessful, with catastrophe frequency and
12 increased construction costs far outpacing rate increases. (SFG-VW-1, Mar. 2024 Letter at p. 1.)
13 In March 2024, State Farm General’s policyholder surplus was less than 50 cents for every dollar
14 of risk. (*Id.*) State Farm General accordingly filed three applications for increased rates in the
15 summer of 2024. (*See* SFG-VW-2, SFG’s Rate Application (No. 24-1273) for +30.0% for Non-
16 Tenant (Homeowners);) (SFG-VW-3, SFG’s Rate Application (No. 24-1273) for +52.0% for
17 Tenants – Renters and +36.0% for Tenants – Condominium Unit owners;) and (SFG-VW-4,
18 SFG’s Rate Application (No. 24-1330) for +38.0% for Rental Dwelling (RDP).)³

19 State Farm General has estimated \$7.9 billion in direct losses due to the Los Angeles
20 wildfires. (SFG-VW-13, Feb. 25 Letter at p. 4.) And although robust reinsurance policies will
21 cover much of these losses, the remaining losses are expected to reduce State Farm General’s
22 surplus to approximately \$600 million. (*Id.*) If another catastrophic wildfire were to cause this
23 kind of loss, it would further deplete State Farm General’s surplus. And even without another

24 _____
25 ³ Those applications were based on Variance 6, a solvency-related adjustment to what is otherwise
26 the maximum permitted premium under the rate regulations. Because the Los Angeles fires will
27 undoubtedly increase the maximum permitted premium, it is highly likely that State Farm
28 General’s rate increases for some lines may be supported without requiring a variance. But it is
even more clear that the financial conditions that led to State Farm General’s Variance 6 filings
have only worsened given the impact of the Los Angeles wildfires. (SFG-VW-9, Feb. 3 Letter at
p. 1 fn.2.)

1 catastrophic wildfire, State Farm General expects its surplus to continue to deplete without a rate
2 increase due to inflationary trends (which increase the costs, for example, of the building materials
3 needed to rebuild houses). (Mar. 20 Letter at p. 1.)

4 State Farm General’s financial situation is not “speculative,” as Consumer Watchdog
5 claims. (Objections at p. 6.) To the contrary, State Farm General’s annual statements betray the
6 severity of the insurer’s declining financial health. (Appel Decl. ¶¶ 28–36.) An insurer’s
7 “premium to surplus ratio” reflects the insurer’s exposure, as compared to the insurer’s capacity to
8 absorb that risk—the higher the number, the greater the risk of insolvency. (*Id.* ¶ 29.) In the past
9 decade, State Farm General’s ratio has soared from 0.48 to 3.03. The results of State Farm
10 General’s Risk Based Capital tests paint an even bleaker picture. State Farm General’s Risk
11 Based Capital ratio dropped from 644% in 2017 to 150% at the end of 2024. (*Id.* ¶ 34.) This
12 nearly placed State Farm General into a “regulatory action level”—the second of four levels set by
13 the National Association of Insurance Commissioners (NAIC) for potential control over insurers.
14 (*Id.* ¶¶ 31–34.)

15 Credit rating agencies took notice. AM Best had a negative ratings outlook for State Farm
16 General *before* the Los Angeles wildfires. (*Id.* ¶ 41.) S&P Global Ratings is poised to follow suit.
17 It placed State Farm General on a “CreditWatch with negative implications”—a review process
18 that “could lead to a rating downgrade by multiple notches” and prevent Californians from using
19 State Farm General insurance to insure mortgage collateral. (*Id.* ¶¶ 41–42, 44); *see* (SFG-VW-1,
20 Mar. 2024 Letter at p. 3); (SFG-VW-14, Mar. 11 Letter at p. 3.) If this were to occur, any State
21 Farm General insured with a mortgage that requires the homeowner to obtain insurance from an
22 insurer with a higher financial risk rating would have to obtain new insurance, hugely disrupting
23 hundreds of thousands of California citizens. (Appel Decl. ¶ 42.)

24 The reason for an interim rate is to alleviate this crisis. As the Commissioner explained,
25 State Farm General’s financials are not just “significant . . . for the company, but for the entire
26 California market.” (SFG-VW-15, Feb. 26, 2025 Tr. at p. 9:9-14.) State Farm General holds
27 more homeowners’ insurance policies than any other insurer in the State. (*Id.*) The remaining
28

1 insurers are unlikely to absorb all of those policies if State Farm General stops doing business in
2 California. (Appel Decl. ¶¶ 38, 59); (SFG-VW-15, Feb. 26, 2025 Tr. at p. 9:20–9:48.) The only
3 option for many Californians will be the FAIR Plan—an alternative which provides lower
4 coverage at higher rates and was not designed to withstand the amount of risk it would have to
5 shoulder if State Farm General stopped operating in California. (Appel Decl. ¶ 38); (SFG-VW-13,
6 Feb. 25 Letter at pp. 4–5); (SFG-VW-15, Feb. 26, 2025 Tr. at p. 41:6–19); (SFG-VW-16, Tr. of
7 Mar. 11, 2025 Follow-up Meeting at p. 9:20–48 [hereinafter “Mar. 11, 2025 Tr.”].) Forcing
8 Californians to the FAIR Plan will separately jeopardize other insurers’ abilities to remain in
9 California. An increase in FAIR Plan policies will likely yield an increase in FAIR Plan losses—
10 costs shared by admitted carriers according to their market share. (SFG-VW-13, Feb. 25 Letter at
11 pp. 4–5.)

12 In the event of a financial strength rating downgrade of sufficient magnitude, many
13 mortgage lenders *will not accept* State Farm General insurance to insure mortgage collateral—
14 including for policies that are *currently* insured by State Farm General. (Appel Decl. ¶ 39);
15 (Ehrhart Decl. ¶¶ 13–14); (SFG-VW-9, Feb. 3 Letter at p. 3 fn. 5.) The limited impact of AM
16 Best’s downgrade will increase exponentially if another credit ratings company follows suit.
17 (Appel Decl. ¶¶ 41–42.) If that were to happen, homeowners with a mortgage would be forced to
18 find other insurance, without any action on State Farm General’s part. Disqualifying State Farm
19 General insurance policies from insuring mortgage collateral in California could compel the loss
20 of coverage for nearly 700,000 current State Farm General policyholders—who would need to
21 find coverage with another insurance company, or more likely, the FAIR plan. (*Id.* ¶ 42); (Ehrhart
22 Decl. ¶ 14.)

23 An interim rate, by contrast, will help safeguard State Farm General’s solvency and
24 accordingly help prevent a ratings agency downgrade. Rate levels, and the premiums they
25 produce, are generally “the primary means of generating surplus growth in insurance,” particularly
26 in the homeowners line. (Appel Decl. ¶ 12); *see also* (*id.* ¶¶ 15–16.) An immediate rate increase
27 is therefore critical to help prevent further decline of State Farm General’s financial health and
28

1 help millions of Californians to retain comprehensive, reliable coverage that could otherwise be in
2 jeopardy based on lender requirements in the event of a downgrade. By taking a crucial step to
3 ensure State Farm General’s financial stability, the Commissioner also inspires confidence in
4 California’s insurance market by insurers and policyholders. Market confidence drives continued
5 investment and competition, increasing the availability of insurance across the State. The
6 requested interim rates plainly serve the interests of justice.

7 **B. Even If The “Plainly Invalid” Standard Applies, It Is Met Here.**

8 Even if State Farm General is required to meet Consumer Watchdog’s “plainly invalid”
9 standard, however, State Farm General has made a sufficient showing for emergency interim relief
10 under that standard—for all of the same reasons described above. State Farm General’s rates are
11 plainly invalid. There can be no real dispute on this point: As State Farm General explained to
12 the Commissioner, “[o]ver the nine-year period ending with 2024,” State Farm General “will pay
13 \$1.26 in claims and expenses for every \$1.00 collected in premium, resulting in over \$5 billion in
14 cumulative underwriting losses.” (SFG-VW-9, Feb. 3 Letter at p. 2.) State Farm General’s
15 surplus has deteriorated from almost \$4 billion to around \$1 billion over the course of a decade.
16 That is *before* the Los Angeles wildfires, where State Farm General has estimated that it will pay
17 over \$7 billion in claims, leading its surplus to further decline to \$600 million. *Supra* pp. 10-12.

18 Meanwhile, State Farm General’s “risk exposure grew tremendously in the last few years,
19 with construction cost inflation being a major driver,” resulting in a “surplus of less than 50 cents
20 for every dollar of risk (as measured by net written premium).” (SFG-VW-1, March 2024 Letter
21 at p. 1.) The Commissioner has recognized these serious concerns, which are only exacerbated by
22 the unprecedented Los Angeles wildfires. (SFG-VW-15, Feb. 26, 2025 Tr. at pp. 7:24–8:3);
23 (SFG-VW-16, Mar. 11, 2025 Tr. at pp. 1:37–2:55, 6:00–7:19.) These factors already led one
24 rating agency to downgrade State Farm General, and another to threaten an imminent downgrade
25 that would mean State Farm General does not meet basic requirements for serving as an insurer for
26 policyholders with mortgages. In these circumstances, State Farm General’s rates are invalid, and
27 State Farm General is entitled to an emergency interim rate.

1 Notably, Consumer Watchdog’s own expert in the litigation over State Farm General’s
2 2015 rate request concluded that State Farm General had a “high level of financial integrity”—
3 which Consumer Watchdog’s expert relied on to conclude that State Farm General’s current rates
4 were not confiscatory—based on several metrics that *are no longer true*. [SFG-VW-18, Pre-Filed
5 Direct Testimony of Allan I. Schwartz, File no. PA-2015-00004 at pp. 29 *et seq.* (Oct. 15, 2015)
6 [hereinafter “Schwartz Decl.”].) Consumer Watchdog’s expert in 2015 cited evidence that State
7 Farm General “has received an A. M. Best Financial Strength rating of A (Excellent) from at least
8 2011 to the present,” (SFG-VW-18, Schwartz Decl. at p. 30:1–2), but State Farm General has now
9 been downgraded to a “B” rating. (Appel Decl. ¶ 41.) Consumer Watchdog’s expert in 2015 cited
10 evidence that State Farm General “falls within the normal range of results on all thirteen of the
11 NAIC’s Insurance Regulatory Information System (IRIS) Ratios,” (SFG-VW-18, Schwartz Decl.
12 at p. 30:3–5), but State Farm General’s “premium to surplus ratio in excess of 3.0” now “causes it
13 to fail the first IRIS ratio test,” (Appel Decl. ¶ 10b.) And Consumer Watchdog’s expert in 2015
14 cited evidence that “State Farm’s Total Adjusted Capital of \$3.821 billion is almost 26 times as
15 large as its Authorized Control Level Risk-Based Capital level of \$148.5 million.” (SFG-VW-18,
16 Schwartz Decl. at p. 31:4–5.) Today, in contrast, State Farm General’s RBC ratio has fallen to
17 150%, which “places it in the Company Action Level under the NAIC’s RBC rules” and right on
18 the cusp of the regulatory action level. (Appel Decl. ¶¶ 10a, 10b, 34.) Consumer Watchdog
19 ignores that the very factors its expert emphasized in 2015 as indicators of State Farm General’s
20 financial strength now show State Farm General’s financial weakness, further demonstrating that
21 State Farm General’s current rates are “plainly invalid.”

22 Consumer Watchdog’s real complaint appears to be that if the Commissioner approves an
23 interim rate—and the rate later proves too high—it will hurt policyholders. (*See* Objections at pp.
24 22–23.) The Legislature, however, has addressed this issue, prescribing that if an interim rate is
25 too high, the remedy is a refund with interest. (*See* Cal. Ins. Code § 1861.16(g).) Consumer
26 Watchdog’s grievance with the statutory scheme, which the Legislature has determined is the
27 appropriate way to protect consumers, is not a basis for denying State Farm General emergency

1 relief. The California Supreme Court has likewise repeatedly recognized that if an interim rate
2 proves too high, policyholders are entitled to a refund with interest. (*See Calfarm*, 48 Cal.3d at p.
3 825); (*20th Cent. Ins. Co.*, 8 Cal.4th at p. 254.) State Farm General’s policyholders will suffer
4 severe injury if State Farm General’s financial strength rating is downgraded and they are forced
5 to find a new insurer, which is directly contrary to Proposition 103’s purpose to keep insurance
6 “available” in California. (*See State Farm*, 71 Cal.App.5th at 176 [recognizing “the objective” of
7 Proposition 103 “is not just to keep insurance rates fair to consumers, but to keep insurance
8 available—which requires that rates be fair to the insurers as well.”].) Granting an interim rate in
9 these circumstances thus protects policyholders, rather than injures them, given that they will be
10 entitled to a refund with interest if warranted.

11 **C. Consumer Watchdog’s Discussion Of Variances 6 And 10 Is Irrelevant.**

12 Consumer Watchdog asserts that an interim rate is not appropriate, because State Farm
13 General is not seeking an interim rate based on either Variance 6 or Variance 10. (*See Objections*
14 at pp. 11–12.) State Farm General agrees that it did not seek an interim rate based on either of
15 these variances, although it preserves the right to raise both variances in the full rate proceeding (if
16 appropriate). State Farm General was not required to invoke either Variance 6 or Variance 10 in
17 order to obtain an interim rate. It is clear given State Farm General’s financial situation that its
18 current rates are not sufficient to maintain the company’s financial strength in light of the
19 enormous losses from the Los Angeles wildfires, or to protect State Farm General from an
20 imminent financial strength rating downgrade. That is more than sufficient to justify an interim
21 rate without relying on Variances 6 or 10.

22 **D. Consumer Watchdog’s Complaints About “Transparency” Are Really A**
23 **Discovery Dispute Properly Addressed As Part Of The Rate Hearing.**

24 Consumer Watchdog claims that State Farm General is not entitled to an interim rate
25 because it has “consistently resisted providing essential financial documentation necessary to
26 evaluate the legitimacy of its original rate requests.” (*Objections* at pp. 12–13.) This is really a
27 dispute between the parties over the proper scope of discovery for the full rate hearing, and in
28 particular around whether State Farm General should be required to disclose confidential financial

1 information related to its Variance 6 request as part of that rate hearing. State Farm General’s
2 position is that it should not be required to disclose confidential information, *particularly* where
3 there is publicly available information about State Farm General’s declining surplus, payouts due
4 to the Los Angeles wildfires, and probable maximum loss (PML), among other publicly available
5 financial indicators. (See SFG,VW-17, Letter from Nikki McKennedy, dated Aug. 16, 2024 at p.
6 1.) Regardless, this is not an issue that the ALJ needs to address (or should address) in this interim
7 rate proceeding, where State Farm General has not invoked Variance 6, and where the
8 Commissioner asked the ALJ to evaluate the evidence before it when evaluating whether an
9 interim rate is warranted.

10 **E. Consumer Watchdog’s Remaining Objections Are Meritless.**

11 Consumer Watchdog’s remaining objections are meritless, and the ALJ should reject them.

12 *First*, Consumer Watchdog claims that “the uncertainty creating the risk of a ratings
13 downgrade is entirely within State Farm’s control,” because State Farm Mutual could simply give
14 State Farm General more money. (Objections at pp. 15–16.) To be clear, S&P explained that its
15 “rating action” was based on State Farm General’s “weak underwriting performance over the past
16 five years (2019–2023), continued underperformance in 2024, and the potential earnings pressure
17 in 2025, largely from the recent wildfires which lead to deteriorating capital near the regulatory
18 authorized control level,” “uncertainties related to capital support from the State Farm group,” and
19 “the California Insurance Department’s ambiguity around rate approval.” (Appel Decl. ¶ 44.)
20 State Farm General’s inability to obtain rate increases, coupled with its declining surplus and the
21 Los Angeles wildfires, are crucial reasons why S&P is considering a downgrade.

22 As for Consumer Watchdog’s position that State Farm Mutual should just give State Farm
23 General money, State Farm General and State Farm Mutual are separate companies, a point the
24 California Court of Appeals recognized in *State Farm*, 71 Cal.App.5th at p. 172. State Farm
25 General has policies almost exclusively in California, whereas State Farm Mutual has policies in
26 many other states. State Farm Mutual is under no obligation to give State Farm General an
27 unlimited amount of money to replenish its surplus or ensure its solvency. Indeed, that would be
28

1 tantamount to policyholders in *other states* subsidizing the cost of insurance in California.
2 Refusing to approve an interim rate increase on the ground that policyholders in other states
3 should be funding State Farm General’s surplus to the benefit of State Farm General’s California
4 policyholders is not fair, reasonable, or in the interests of justice. The core reason State Farm
5 General is facing a financial strength rating downgrade is that it cannot collect enough premium
6 under current insurance rates in California to replenish its surplus and pay out in the event of
7 another catastrophic loss. (*See* Appel Decl. ¶ 12.) The purpose of the interim rate is to address
8 that serious problem. This is a structural issue that cannot be fixed by a one-time capital
9 contribution from State Farm Mutual to State Farm General, but can instead be addressed only by
10 a sustainable insurance market in California, which includes rates that reflect the cost of selling
11 insurance. It is Consumer Watchdog—and not State Farm General—who is engaged in
12 “gamesmanship” by failing to recognize this serious issue and the real steps both State Farm
13 General and the Commissioner are taking to solve it. Comparing State Farm Mutual’s response to
14 other catastrophes is inapt. (*See* Opposition at pp. 18–19.) State Farm General’s declining surplus
15 in California is the result of a long-term problem that needs to be addressed.

16 *Second*, according to Consumer Watchdog, State Farm Mutual has been overcharging State
17 Farm General for reinsurance, which Consumer Watchdog claims is the source of State Farm
18 General’s financial instability. (Objections at pp. 17–22.) In State Farm General’s view, the
19 question whether it is overpaying for reinsurance is a technical question that is far outside the
20 scope of the hearing on the stipulation and more appropriately addressed in the full rate hearing.
21 However, to the extent the ALJ intends to address it, State Farm General has submitted a
22 declaration demonstrating that it is not overpaying for reinsurance, and that Consumer Watchdog’s
23 position on this issue is baseless.

24 Reinsurance “is a critical component of the insurance industry and an important part of the
25 financial health of insurance companies.” (Ehrhart Decl. ¶ 7.) The *amount* of reinsurance an
26 insurer holds is critical to the insurer’s continued financial well-being, as reinsurance “helps
27 ensure that the insurance company has sufficient assets available to pay policyholder claims” and
28

1 allows the company “to write additional policies because it has the available capital to do so.” (*Id.*
2 at ¶ 8.) Insurance companies regularly retain multiple reinsurers, who assume different “layers” of
3 the insurance company’s risk. (*See id.* at ¶ 12.) In general, reinsurance at lower layers is more
4 expensive than reinsurance at higher layers for the same risk because the lower layers (which kick
5 in at a lower level of loss) are more likely to pay claims in the event of a catastrophic loss. (*Id.*)
6 State Farm General, like many other insurers, layers its reinsurance coverage. (*See* Ehrhart Decl.
7 ¶ 30-32.) Twenty percent of its reinsurance is placed with unaffiliated reinsurers, while the
8 remaining 80% is placed with State Farm Mutual or other affiliated reinsurers. (*Id.* at ¶ 20-21.)

9 State Farm General’s net reinsurance costs neither explain the insurer’s surplus decline nor
10 negate the value of reinsurance. (Appel Decl. ¶ 23.) Consumer Watchdog contends that State
11 Farm General paid State Farm Mutual \$3 billion for reinsurance. (*Id.* ¶ 22.) But even cutting that
12 cost *in half* would not come close to remedying the \$2.7 billion in operating losses that State Farm
13 General suffered over the past ten years. (*Id.* ¶ 24.) Indeed, State Farm’s worsening financial
14 condition *is the reason why* it has had to increase its reinsurance coverage. (Ehrhart Decl. ¶ 27).
15 If State Farm General had purchased *less* reinsurance, it “would be insolvent” as a result of the
16 Los Angeles wildfires—where State Farm General has estimated that its reinsurance from State
17 Farm Mutual will cover \$5 billion in losses. (SFG-VW-13, Feb. 25 Letter at p. 6); (SFG-VW-15,
18 Feb. 26, 2025 Tr. at p. 58:12–23.) Taking into account the Los Angeles wildfires, State Farm
19 General has estimated that it “will have recovered \$5.5 billion more” in reinsurance “recoveries
20 than they paid in premium.” (*Id.* at p. 57:13–18.) Reinsurance also played a vital role after the
21 2017 fires by allowing “State Farm General to stay viable” until it received a “subrogation
22 recovery from PG&E.” (*Id.* at pp. 56:25–57:5.)

23 State Farm General’s reinsurance policies are thus a significant boon to its policyholders,
24 not a burden. (Appel Decl. ¶ 10e); (Ehrhart Decl. ¶ 21, 34-39.) By maintaining robust
25 reinsurance, State Farm General has ensured that its policyholders remained covered even as State
26 Farm General’s financial condition has continued to worsen—and played a key role in protecting
27 State Farm General’s policyholders after the 2017 and 2025 wildfires. (Ehrhart Decl. ¶¶ 28-29,

36-39.) Consumer Watchdog claims that State Farm General improperly paid State Farm Mutual \$3 billion for reinsurance—while ignoring that it is precisely this reinsurance that will enable State Farm General to pay many billions of dollars in losses caused by the Los Angeles wildfires without becoming insolvent. The fact that State Farm General purchases reinsurance to protect against precisely what happened is not “fundamentally unfair” to policyholders, and it certainly does not undermine the propriety of the stipulated interim rate.

Consumer Watchdog contends that State Farm General overpays for reinsurance, but this is baseless. Most of State Farm General’s reinsurance comes from State Farm Mutual, which provides reinsurance at a competitive price at risk levels that State Farm General likely could not obtain in the traditional reinsurance market. (Appel Decl. ¶ 10c); (Ehrhart Decl. ¶ 31.) The “price that State Farm pays for the coverage provided” by State Farm Mutual “is less” than it “can otherwise get in the external market, and the amount of coverage provide is *also simply not available*” on the external market. (SFG-VW-15, Feb. 26, 2025 Tr. at 56:7–16 [emphasis added]); (Ehrhart Decl. ¶¶ 30-32.) The traditional reinsurance market has “no appetite” for offering increased California reinsurance capacity “anywhere near” the prices State Farm pays for the coverage that its parent company and other State Farm affiliates provides. (Ehrhart Decl. ¶ 31); (*see also id.* at ¶ 32.) State Farm General’s reinsurance policies deeply benefit its policyholders, as demonstrated by the large payout following the Los Angeles wildfires.

Consumer Watchdog’s view that State Farm General receives a “bad deal” on reinsurance arises from improper comparisons, a too-small dataset, and a flawed belief that State Farm General should never pay more in reinsurance premiums than it receives in recoveries. (Appel Decl. ¶¶ 10c, 13, 53-56.) For starters, “it is impossible to validly compare the ceded loss ratios across different insurers” without considering the comparative structure of each company’s reinsurance program. (*Id.* ¶ 55); (*see also id.* ¶¶ 53-54.) Nor can the value of reinsurance—a product designed to protect against rare, high severity events—be assessed by only looking to 10 years of data. (*Id.* ¶¶ 10c, 55.) Consumer Watchdog’s cherrypicked sample size shows why: Had the intervenor extended its data period by three months, it would have encompassed the 2025 Los Angeles

1 wildfires, painting a much different picture of State Farm General’s reinsurance costs. (*Id.* ¶ 56.)

2 Moreover, Consumer Watchdog misapprehends how reinsurance works, suggesting that
3 net reinsurance costs somehow show financial mismanagement. Reinsurance recoveries may in
4 some years exceed reinsurance costs, but for reinsurers to remain profitable, reinsurance costs
5 must in the long run exceed recoveries. (Appel Decl. ¶ 13.) Reinsurance involves primary
6 insurers transferring risk to reinsurers—a service that reinsurers provide at a cost. (*Id.*) As a
7 result, “the price of reinsurance must not only include expected reinsurer losses (i.e., recoveries),
8 but also . . . reinsurer expenses and the cost of reinsurer capital.” (*Id.*) If there were not a positive
9 net cost of reinsurance, reinsurers could not pay for the latter two expenses. (*See id.*)

10 Consumer Watchdog’s accusation of predatory pricing by State Farm Mutual turns almost
11 entirely on a Wall Street Journal article that was recently rebuked for its many misrepresentations.
12 (*See* Objections at pp. 20–21); (Sullivan, *Setting The Record Straight: State Farm Didn’t Burn*
13 *California* (Mar. 6, 2025)).⁴ Rightly so. Contrary to the article’s and Consumer Watchdog’s
14 contentions, State Farm General has *not* increased its market share over the past decade—even as
15 other insurance companies have left California en masse. (*Compare* Objections at pp. 21–22 with
16 Appel Decl. ¶ 50-51; Sullivan at p. 1); (*see also* Law & Alvarado, *California homeowners*
17 *insurance: Current state of the market and implications of the Los Angeles wildfires* (Jan. 22,
18 2025) [identifying over a dozen insurers announcing an intent to substantially withdraw from
19 homeowners insurance lines]).⁵ What is more, Consumer Watchdog lacks any actual evidence
20 that State Farm General’s lower than indicated rate requests were part of an attempt to dominate
21 the market. To the contrary, the evidence shows that State Farm General has fought vigorously
22 (and publicly) for increased rates, which it finally received in 2022—but was unable to obtain the
23 higher rate it was entitled to for years as a result of protracted litigation. (Appel Decl. ¶¶ 47-48.)

24 Consumer Watchdog’s attempts to rewrite history are particularly disingenuous given the

25
26 ⁴ Available at <https://df9fd9b6ab64495ad759-f14ba961ae89374e6d5a8ee602c09059.ssl.cf5.rackcdn.com/1919.pdf?i=817248>.

27 ⁵ Available at <https://www.milliman.com/en/insight/california-homeowners-insurance-los-angeles-wildfires>.
28

1 role that intervenors play in disincentivizing insurers from seeking rate increases above 6.9%.
2 (*See id.* ¶¶ 46–48.) The threat of intervenor involvement in rate proceedings has made filing for
3 6.9% rate increases a common practice amongst California insurers. (*Id.* ¶¶ 47-49.) Rate hearings
4 are unavoidably costly and time consuming, particularly where an intervenor is involved. (*Id.*)
5 They frequently involve multiple rounds of (disputed) discovery, days long hearings spread across
6 weeks or months, and hefty price tags, with insurers frequently having to pay for the intervenors’
7 fees. (*Id.* ¶¶ 47-48.) State Farm General, for example, filed one rate application exceeding 6.9%
8 in 2014; the ultimate decision was not issued in that case until 2022, depriving State Farm General
9 of hundreds of millions of dollars in needed rate level while the proceedings were pending. (*Id.* ¶
10 48.) This delay and expense—not attempted antitrust violations—deters a wide range of insurers
11 from seeking the rates needed to be self-sufficient in the California market. (*See id.* ¶¶ 47-52.)

12 Indeed, Consumer Watchdog continues to argue that State Farm General should *decrease*
13 its rates despite declining surplus and enormous payouts following the Los Angeles wildfires.
14 State Farm General believes that the market cost of reinsurance is a complex topic beyond the
15 scope of this interim rate proceeding, but even if the ALJ addresses it, a single Wall Street Journal
16 article is not sufficient evidence to deny State Farm General’s interim rate request.

17 *Third*, Consumer Watchdog claims that it would be unfair for the ALJ to permit an interim
18 rate, when State Farm General has announced its intent to non-renew a small percentage of
19 policies. (Objections at pp. 19-20.) State Farm General takes seriously the coverage
20 commitments that it provides its policyholders. But the company’s ability to honor those policies
21 is at risk any time its PML, which is the value of the largest loss that could result from a disaster,
22 exceeds the recovery that State Farm General can provide. (SFG-VW-15, Feb. 26, 2025 Tr. at pp.
23 19:17-20:1, 20:12-19, 39:11-18) [explaining that State Farm General “simply can’t handle this
24 much exposure”]. Restoring State Farm General’s stability requires improving both sides of the
25 ledger: increasing the amount of coverage that State Farm General can provide by increasing rates
26 and decreasing the company’s PML by reducing its book of business. Far from being “unfair,”
27 non-renewals are a necessary component of any strategy to ensure that State Farm General

1 remains a viable insurer for as many Californians as possible.

2 State Farm General does not make non-renewal decisions lightly. The company worked
3 hard to maximize its PML reduction while minimizing the number of non-renewals, impacting the
4 smallest possible number of California policyholders. Indeed, State Farm General is “striving to
5 minimize the impact of the necessary actions that must be taken” in narrowly tailoring non-
6 renewals. (SFG-VW-1, March 2024 Letter at p. 2). This means State Farm General maintained
7 coverage for nearly all of its customers, while significantly decreasing its PML through non-
8 renewals of a small percentage of customers.

9 State Farm General must be able to complete these non-renewals. These non-renewals are
10 in the public interest because they allow State Farm General to continue to insure other customers,
11 and they are essential for State Farm General to continue providing reliable, comprehensive
12 coverage to homeowners across the State. The effects of climate change mean that natural
13 disasters in California (and elsewhere) have become increasingly unpredictable and severe. (*See*
14 *Ehrhart Decl.* ¶¶ 26-27); (*see also* SFG-VW-15, Feb. 26, 2025 Tr. at p. 6:18–21 [Commissioner
15 discussing effects of climate change on California insurance market]); (Mar. 11, 2025 Tr. at p.
16 2:56–3:37 [similar].) Even before the Los Angeles wildfires, 18 of the largest 20 wildfires in
17 California history occurred in the past 20 years, with 13 of those fires occurring after 2017. (*Cal*
18 *Fire, Top 20 Largest California Wildfires* (Oct. 2024).)⁶ The current risk of another severe natural
19 disaster is untenable: were the Los Angeles wildfires to occur again today, State Farm General
20 *would not be able to cover the resulting losses because its surplus will have been depleted.* This
21 outcome benefits no one. State Farm General reasonably seeks to tackle this problem both
22 through an interim rate increase and by non-renewing a small percentage of policies.

23 *Fourth*, Consumer Watchdog briefly complains that State Farm General’s “final rate might
24 be calculated under new regulations” that would allow “the inclusion of reinsurance costs and

25
26 ⁶ Available at <https://34c031f8-c9fd-4018-8c5a-4159cdff6b0d-cdn-endpoint.azureedge.net/-/media/calfire-website/our-impact/fire-statistics/top-20-largest-ca-wildfires.pdf?rev=097f901c128347149e2614f2fca4f546&hash=27DDE83DFEF9A69E67C73765892A2B75>.
27
28

1 reliance on catastrophe modeling rather than historical loss data.” (Objections at p. 23.) In other
2 words, Consumer Watchdog is concerned that the ALJ may approve the stipulation to an interim
3 rate, which might *ultimately prove justified* under new regulations that are intended to better
4 reflect the cost of insurance in California. This argument makes no sense. If the interim rate is
5 ultimately upheld in a rate hearing based on an approach that the Commissioner has determined is
6 best suited to determining the cost of insurance in California, that is a good outcome, not a bad
7 outcome. It would mean that the interim rate provided State Farm General with the appropriate
8 relief prior to the rate hearing, and it would serve Proposition 103’s goal of ensuring that insurance
9 remains available in California. In any event, Consumer Watchdog is merely speculating about
10 what may happen in a future rate hearing; this is not a basis to deny the interim rate.

11 **IV. CONSUMER WATCHDOG HAS A FULSOME OPPORTUNITY TO PRESENT**
12 **EVIDENCE AND ARGUMENT.**

13 Consumer Watchdog contends that the ALJ cannot approve the stipulation because State
14 Farm General did not submit declarations in support of the stipulation. (Opposition at pp. 16–17.)
15 Consumer Watchdog’s complaint is premature, as State Farm General was not required to submit
16 its declarations with the stipulation because a notice of hearing had not yet been set. (*Compare*
17 *SFG-VW-17*, Letter from Nikki McKennedy, dated Aug. 16, 2024 at p. 1 [explaining “Consumer
18 Watchdog’s First and Second Sets of Discovery Requests . . . are premature at this time” because
19 the “[Rate Enforcement Bureau] has not yet filed a notice of hearing in this matter”] *with* *SFG-*
20 *VW-19*, Mar. 17 Notice of Hearing at p. 7:16–18 [issued on March 8, 2025, setting hearing date
21 on April 8, 2025].) State Farm General submitted both this brief and the accompanying
22 declarations in advance of the interim rate hearing, with an opportunity for Consumer Watchdog
23 to respond both in writing and at the hearing. There is no prejudice to Consumer Watchdog,
24 which has had—and will have—multiple opportunities to respond to State Farm General’s
25 position. (*See Barclay Hollander Corp. v. California Reg’l Water Quality Control Bd.* (2019) 38
26 Cal.App.5th 479, 511 [finding no due process violation where agency gave party “several
27 opportunities . . . to address the entire range of issues presented in the proceeding before it”]);
28

1 (*Pinnacle Armor, Inc. v. United States* (9th Cir. 2011) 648 F.3d 708, 717 [similar].)

2 **V. CONCLUSION**

3 In the interest of its policyholders and the entire California insurance market, State Farm
4 General respectfully requests the ALJ to recommend that the Commissioner imminently adopt the
5 stipulation, leaving any remaining issues to be resolved at a full public rate hearing if the parties
6 are unable to first reach a settlement.

7
8 Dated: April 2, 2025

9
10 Respectfully submitted,

11 **HOGAN LOVELLS US LLP**

12 /s/ Jordan D. Teti

13 Michael M. Maddigan (Bar No. 163450)

14 Jordan D. Teti (Bar No. 284714)

15 1999 Avenue of the Stars, Suite 1400

Los Angeles, CA 90067

Telephone: (310) 785-4600

Facsimile: (310) 785-4601

michael.maddigan@hoganlovells.com

jordan.teti@hoganlovells.com

18 Vanessa Wells (Bar No. 121279)

19 855 Main Street, Suite 200

Redwood City, CA 94063

Telephone: (650) 463-4000

Facsimile: (650) 463-4199

vanessa.wells@hoganlovells.com

22 Katherine B. Wellington (admitted in

23 Massachusetts, Bar No. 688577)

24 125 High Street, Suite 2010

Boston, MA 02110

Telephone: (617) 371-1000

Facsimile: (617) 371-1037

katherine.wellington@hoganlovells.com

27 *Attorneys for State Farm General Insurance*
28 *Company*