

# HOMEOWNERS INSURANCE REVIEW

ALABAMA DEPT. OF INSURANCE

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# INDUSTRY HOMEOWNERS RESULTS

- Over the 7 years 2003-2009:
  - Insurance companies in Alabama have paid out approximately \$117 for Homeowners claims and operating expenses for every \$100 of premiums they have collected;
  - Insurance companies Countrywide paid out approximately \$97 for every \$100 they collected.

# INSURANCE INDUSTRY RESULTS

- Return on Net Worth for 1990-2009:
  - Property/Casualty Industry = 7.3%
  - Avg. of 227 other industries = 10.7%
  - P/C Industry ranked 163 out of 228\* industries
  - P/C Industry ROE was lower than the 227- industry average for 18 of the 20 years

\* # of industries in S&P's COMPUSTAT database for which 20 years of data was available.

# INSURANCE INDUSTRY RESULTS

- Return on Net Worth for 2000-2009:
  - Property/Casualty Industry = 6.3%
  - Avg. of 301 other industries = 9.4%
  - P/C Industry ranked 200 out of 302\* industries
  - P/C Industry ROE was lower than the 301- industry average for all 10 years

\* # of industries in S&P's COMPUSTAT database for which 10 years of data was available.

# INDUSTRY HOMEOWNERS RESULTS

## Homeowners Return on Net Worth: 2000-2009

|                |            |
|----------------|------------|
| Louisiana      | -32%       |
| Mississippi    | -29%       |
| Missouri       | -12%       |
| Kentucky       | -9%        |
| <b>Alabama</b> | <b>-8%</b> |
| Arkansas       | -7%        |
| Georgia        | -7%        |
| Nebraska       | -7%        |
| Tennessee      | -5%        |
| Texas          | -2%        |
| Oklahoma       | -2%        |
| Florida        | 0%         |
| W. Virginia    | +5%        |
| Virginia       | +10%       |
| N. Carolina    | +15%       |
| S. Carolina    | +21%       |
| Countrywide    | +5%        |

# INDUSTRY HOMEOWNERS RESULTS

- Alabama's **-8%** average ROE over the last 10 years means that if a company had started with \$1 billion in net worth 10 years ago, today the company would only have \$434 million net worth remaining.
- Companies must deploy their capital / net worth where they can achieve a reasonable return for their investors. Clearly a **-8%** average ROE does not make Alabama an attractive investment for companies.
- On the Coast, approximately 70% - 80% of the Homeowners policy premium is required to cover wind losses. Upstate it is only about 20% - 35%.
- A company's ROE can be improved in several ways:
  - Raise rates
  - Reduce the company's exposure to loss by raising deductibles or excluding wind coverage
  - Shift to writing more policies Upstate
  - Improve building codes to lower the damageability of houses; retrofit homes to higher building standards

# HOMEOWNERS AVAILABILITY

- Homeowners claims not related to wind are more predictable and profitable from year to year in Alabama, so some companies have chosen not to offer wind coverage near the coast, or at least to require higher wind deductibles so as to reduce their exposure to loss.

|   | <u>AL 2007</u> | <u>AL 2009</u> | <u>CW 2009</u> |
|---|----------------|----------------|----------------|
| • Market Share for the 4 Largest Groups*: | 68%            | 65%            | 44%            |
| • Market growth last 10 years:            | 111%           | 103%           | 96%            |
| • Surplus Lines Market Share:             | 1.6%           | 2.8%           | 1.9%           |

\* Comparing Alabama's 4 Largest Groups versus the 4 Largest Groups in the U.S.

# INDUSTRY HOMEOWNERS RESULTS

- Companies must feel confident that over the long run they can make a profit on Homeowners insurance in Alabama, or they will choose not to offer insurance in our state and utilize their capital to write more business in other states.
- The Dept. of Insurance permits companies to establish rates that over the long run should generate a profit margin on premiums of approximately 6% (which translates to less than 7% ROE, which is approximately the industry's 2009 countrywide average).
- If the Dept. of Insurance were to arbitrarily suppress rates that companies could charge, companies would further reduce their writings in Alabama, thus exacerbating the availability (and thus affordability) of Homeowners insurance.

# ALABAMA RATE STATUTES

- All Homeowners rate filings from admitted insurance companies require prior approval by the Department of Insurance.
- Non-admitted (Surplus Lines) companies are not required to file their rates with the Department and the Department has no regulatory authority over their rates.

# ALABAMA RATE STATUTES

- Alabama statute says that rates must not be:
  - \* Excessive
  - \* Inadequate
  - \* Unfairly discriminatory

# ALABAMA RATE STATUTES

- Not excessive: We require that rates are actuarially justified, meaning the rates do not exceed those rates statistically justified by the insurance company's claim history or models.
- Not inadequate: We do permit insurance companies to utilize rates below their actuarially justified rates in order to be competitive, as long as it does not endanger the company's financial solvency.

# ALABAMA RATE STATUTES

- Not unfairly discriminatory: We review each company's rate structure to ensure that rates are not excessive for any individual territory, policy type, policy limit, deductible level, etc., separately for wind versus non-wind coverage.

# HOMEOWNERS RATE COMPONENTS

- Most Companies publish a single combined Homeowners rate to cover all perils insured against. However, in providing justification for those rates, their data is segregated into non-wind and wind components by territory, and the Department of Insurance scrutinizes that justification.

# HOMEOWNERS RATE COMPONENTS

- The non-wind portion of a company's Homeowners rates must be justified by the company's Alabama non-wind claims experience statewide and by territory over the past 5 years.
- For competitive reasons, for some or all territories, companies may choose to file for lower non-wind rates than those justified actuarially, and we generally permit this.

# HOMEOWNERS RATE COMPONENTS

- The wind portion of a company's Homeowners rates consists of three components:
  - The hurricane rate
  - The non-hurricane wind rate
  - The cost of reinsurance

# HOMEOWNERS RATE COMPONENTS

- The hurricane rate is almost always developed from independent vendors' computer models that predict the frequency and severity of hurricanes. The models estimate the average annual claims that the company will experience based on the policies they currently write in the state. These claim estimates are developed at the zip code level and then averaged over each rating territory used by the company.

# HOMEOWNERS RATE COMPONENTS

- The hurricane computer models are reviewed by a national industry expert panel every time they are revised to ensure that their statistical methodologies are valid.
- These models are being regularly updated to include new analyses and data (such as climate change and recent storms) that affect the frequency and severity of hurricanes.

# HOMEOWNERS RATE COMPONENTS

- The non-hurricane wind rate is developed from either the individual company's 20- or 30-year historical claims data for Alabama or from industry claims data for Alabama.
- In the case of the April, 2011 Alabama tornadoes, which may be considered a 1-in-250 year event, the ALDOI anticipates that it will greatly restrict the inclusion of these losses in future rate filings.

# HOMEOWNERS RATE COMPONENTS

- The cost of reinsurance. Companies cannot risk having to pay the entire loss from a large hurricane or tornado outbreak, so they must purchase reinsurance.
- Reinsurers use the same hurricane models as the companies, though they may utilize different assumptions. The rates for reinsurance that are charged to the companies are not regulated by the Dept. of Insurance, and the companies pass this cost on to their insureds in the premiums they charge.
- Reinsurance is a global industry, so the cost of hurricane reinsurance for most companies is unfortunately impacted by large catastrophes experienced around the world and by the current financial crisis. Over the past 5 years the cost of this wind reinsurance had been rising, but recently it has stabilized and in some cases declined.

# HOMEOWNERS RATE COMPONENTS

- Companies almost never file wind rates below the actuarially justified rates since there is a high risk that the actual wind/hurricane losses could be greater than those predicted by the models.
- History has shown that the hurricane models generally under-predict the amount of losses when the actual storm occurs.
- Companies are typically justifying rate increases in the 10% - 20% range (due to higher losses, inflation and upgrades in hurricane model estimates), and we have not been permitting any individual insured to receive more than a 35% increase at renewal.

# HOMEOWNERS RATE FILING REVIEWS

- Though Alabama Homeowners rates are very high on the coast, the Department of Insurance is scrutinizing every admitted company's rates to make certain that they are statistically justified and that they will not generate excessive profits for the companies.

# ALABAMA HOMEOWNERS RATES

- **2007 NAIC DATA – AVG. PREMIUM PER POLICY BY STATE**
  - HO-3
  - COV. A = \$175,000-199,000
  - DATA EXCLUDES WIND POOLS, CITIZENS OF FL AND LA
  - DATA INCLUDES PRIVATE MARKET POLICIES BOTH INCLUDING AND EXCLUDING WIND

# ALABAMA HOMEOWNERS RATES

## STATE PREMIUM INDEX TO AL

|           |              |             |
|-----------|--------------|-------------|
| <b>CW</b> | <b>\$718</b> | <b>76%</b>  |
| <b>AL</b> | <b>946</b>   | <b>100%</b> |
| AK        | 730          | 77%         |
| AZ        | 573          | 61%         |
| <b>AR</b> | <b>832</b>   | <b>88%</b>  |
| CA        | 656          | 69%         |
| CO        | 693          | 73%         |
| CT        | 653          | 69%         |
| DE        | 466          | 49%         |
| DC        | 768          | 81%         |
| <b>FL</b> | <b>1,365</b> | <b>144%</b> |
| <b>GA</b> | <b>661</b>   | <b>70%</b>  |
| HI        | 534          | 56%         |

## STATE PREMIUM INDEX TO AL

|           |              |             |
|-----------|--------------|-------------|
| ID        | \$397        | 42%         |
| IL        | 597          | 63%         |
| IN        | 650          | 69%         |
| IA        | 640          | 68%         |
| <b>KS</b> | <b>957</b>   | <b>101%</b> |
| KY        | 590          | 62%         |
| <b>LA</b> | <b>1,468</b> | <b>155%</b> |
| ME        | 562          | 59%         |
| MD        | 586          | 62%         |
| MA        | 737          | 78%         |
| MI        | 695          | 73%         |
| MN        | 732          | 77%         |
| <b>MS</b> | <b>1,133</b> | <b>120%</b> |

**Gulf Coast – Averages 41% above AL**

**Tornado Alley – Averages 5% below AL**

**Eastern Seaboard – Averages 29% below AL**

# ALABAMA HOMEOWNERS RATES

STATE PREMIUM INDEX TO AL

|    |       |      |
|----|-------|------|
| MO | \$716 | 76%  |
| MT | 686   | 73%  |
| NE | 826   | 87%  |
| NV | 586   | 62%  |
| NH | 612   | 65%  |
| NJ | 576   | 61%  |
| NM | 641   | 68%  |
| NY | 624   | 66%  |
| NC | 635   | 67%  |
| ND | 854   | 90%  |
| OH | 529   | 56%  |
| OK | 1,162 | 123% |
| OR | 440   | 47%  |

STATE PREMIUM INDEX TO AL

|    |       |      |
|----|-------|------|
| PA | \$607 | 64%  |
| RI | 737   | 78%  |
| SC | 779   | 82%  |
| SD | 691   | 73%  |
| TN | 726   | 77%  |
| TX | 1,369 | 145% |
| UT | 467   | 49%  |
| VT | 600   | 63%  |
| VA | 603   | 64%  |
| WA | 421   | 45%  |
| WV | 678   | 72%  |
| WI | 470   | 50%  |
| WY | 629   | 66%  |

Gulf Coast

Tornado Alley

Eastern Seaboard

# ALABAMA HOMEOWNERS RATES

Average premium relativity for 3 large companies for a \$200,000 home compared to Muscle Shoals, AL:

|                          |          |             |
|--------------------------|----------|-------------|
| Rome, GA                 | =        | 78%         |
| Pittsburg, KS            | =        | 98%         |
| Russellville, AR         | =        | 99%         |
| <b>Muscle Shoals, AL</b> | <b>=</b> | <b>100%</b> |
| Beatrice, NE             | =        | 105%        |
| Farmersville, LA         | =        | 116%        |
| Walls, MS                | =        | 127%        |
| Joplin, MO               | =        | 129%        |
| Brownsville, TN          | =        | 135%        |
| Mt. Pleasant, TX         | =        | 164%        |
| Miami, OK                | =        | 171%        |
| Ft. Walton Beach, FL     | =        | 214%        |

# ALABAMA HOMEOWNERS RATES

Average Premium Relativity (with Wind) by City for a \$200,000 Home:

|                           |               |
|---------------------------|---------------|
| <b>Birmingham (35242)</b> | <b>= 100%</b> |
| Huntsville (35801)        | = 110%        |
| Montgomery (36117)        | = 111%        |
| Tuscaloosa (35401)        | = 120%        |
| Camden (36726)            | = 135%        |
| Gadsden (35901)           | = 136%        |
| Dothan (36301)            | = 139%        |
| Saraland (36571)          | = 263%        |
| Mobile (36608)            | = 294%        |
| Bay Minette (36507)       | = 300%        |
| Fairhope (36532)          | = 311%        |
| Gulf Shores (36542)       | = 328%        |

# STEPS UNDER CONSIDERATION BY THE DEPT. OF INSURANCE

- Require Companies to display their non-wind, wind, and hurricane premiums separately on the policy declarations page.
- Require Companies to provide consumers with a uniform disclosure form, or check list, showing what coverage is and is not included in their policy.
- Implement new statute requiring Homeowners filing data to be made public information on the DOI website.