SENATE……..No. 2251

The Commonwealth of Massachusetts

Report

of the

SENATE COMMITTEE ON
POST AUDIT AND OVERSIGHT

entitled

Behind Closed Doors:

Rate-Setting for Homeowners
Insurance in Massachusetts

(under the provisions of Section 63 of Chapter 3
of the General Laws, as most recently amended by
Chapter 557 of the Acts of 1986)

April 28, 2016

The Commonwealth of Massachusetts

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April 26, 2016

Mr. William F. Welch, Clerk of the Senate
State House, Room 335
Boston MA 02133

Dear Clerk Welch:

Pursuant to M.G.L. Chapter 3, Section 63, as most recently amended by Chapter 557 of the Acts of 1986, the Senate Committee on Post Audit and Oversight respectfully submits to the full Senate the following report: Behind Closed Doors: *Rate Setting for Homeowners Insurance in Massachusetts*.

This report is based on research by the Senate Committee on Post Audit and Oversight, including a public hearing held by the Committee on September 22, 2015 where the Committee hear testimony from the Commissioner of Insurance, several of the largest insurers in the state, a representative of the Attorney General and others. Committee staff also interviewed many insurance and insurance law experts, reviewed industry literature and conducted legal research on insurance and public records.

The report presents the Committee's findings, as well as several recommendations for the Division of Insurance and the Legislature to make the home insurance rate-setting process more transparent, to probe home insurance rate requests more assertively, and to provide consumers with the information they need to compare options for this complex product. If the Division and the Legislature employ these recommendations, they will make great strides toward a more competitive, fairer insurance market.

Respectfully filed by the Senate Committee on Post Audit and Oversight,

Senator Michael J. Barrett, Chair

Senator Benjamin B. Downing, Vice Chair

Senator Jason M. Lewis

Senator Michael O. Moore

Senator Bruce E. Tarr

Senator James T. Welch

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INTRODUCTION

In 2015 the Massachusetts Division of Insurance ("Division" or "DOI") considered, and granted, requests by several of the state's biggest insurers to raise their rates on homeowners coverage by as much as 9%.[1] These were substantial adjustments, affecting a considerable number of residents. Yet neither the public, nor state legislators, nor insurance experts in the state Attorney General's office, were informed of the requests. Later, when staff to the Attorney General were able to analyze industry documents filed in secret with the Division, they deemed two of the largest increases unlawfully excessive.[2] Regardless, the Division had the last word. As of the date of this report, both rates remain in effect.

Concerned about the lack of advance notice, the absence of outside participation, and the size of the increases, the Senate Post Audit and Oversight Committee undertook this inquiry into Massachusetts' process for overseeing homeowners insurance. On September 22, 2015, the Committee held a public hearing in which it heard from, among others, the Commissioner of Insurance and other DOI officials, executives of three of the state's largest insurers, a representative of the Attorney General, and several citizen experts.[3] Before and after the hearing, the Committee chair and staff interviewed witnesses, conducted research, reviewed academic studies, attended public informational sessions run by the agency, and corresponded with a number of interested parties.

Members of the Committee know that provision of homeowners insurance is a business, subject to costs and risks and deserving of a decent rate of return. But we also believe that rate requests are substantial enough on occasion to warrant regulatory hearings informed by the views not only of industry but also of consumers. This hardly seems like too much to ask.

SUMMARY OF COMMITTEE FINDINGS

1. DOI has discretion to provide public notice and allow public input, but doesn't use it

With respect to the lack of timely information that attends even the largest homeowners increases, there is responsibility to go around. The statutory language on DOI rate filings is contradictory and inconclusive. One provision favors delay: "A filing and supporting information shall be open to public inspection after the filing becomes effective."[4] But another permits timely information-sharing: "The commissioner may also call a hearing at any time prior to the proposed effective date of any filing."[5] In the case of these significant rate hikes, had the Commissioner called a hearing prior to the effective dates of the increases, and chosen to make

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[1] *See*, *e.g.*, Deirdre Fernandes, *Winter bill for homeowners insurance comes due*, BOSTON GLOBE, July 13, 2015, *available at* https://www.bostonglobe.com/business/2015/07/12/winter-bill-for-homeowners-insurance-comes-due/125kxlyUsTcTW1FJwsVQGJ/story.html.

[2] Letter from Glenn Kaplan, Ins. & Fin. Servs. Bureau Chief, Mass. Att'y Gen.'s Office to Sen. Michael J. Barrett, Chair, Mass. Sen. Post Audit & Oversight Comm. (Nov. 30, 2015) (on file with the Committee and appended to this report).

[3] See Appendix for full list of witnesses at the Committee's Sept. 22, 2015 hearing.

[4] Mass. Gen. L. ch. 174A § 6(a); ch. 175A § 6(a) (2014).

[5] Ch. 174A § 7(c); ch. 175A § 7(c).

the hearing public, he would have provided the notice and opportunity to be heard that was lacking.

The Division can find further encouragement for timely information-sharing in the state's public records law, reflective of the General Court's overarching preference for making information available in useful fashion to citizens.[6] Chapter 66 of the General Laws states, "Every person having custody of any public record, as defined in clause Twenty-sixth of section seven of chapter four, shall, at reasonable times and without unreasonable delay, permit it, or any segregable portion of a record which is an independent public record, to be inspected and examined by any person."[7] The statute creates a "presumption that the record sought is public."[8] A DOI official, pressed by the Committee to defend the agency's undisturbed stretch of secret regulation, mentioned the law's "deliberative process" exemption. But the plain language of this exemption indicates it does not apply to industry filings, as it refers only to work produced by agency staff themselves.[9]

The Division's own statutory charge is complex, requiring it to safeguard the fiscal health of insurance carriers even as it serves the community's interest in high quality but affordable coverage. This cannot be easy. Nonetheless, in a time of profound public mistrust of both governmental and financial elites, the Committee finds no justification for a regulatory process marked by a no-exceptions rejection of public notice, informational access, and consumer input. The DOI, drawing on the flexibility afforded by its rate-setting statute and the public records law, can, if it chooses, provide online notice of rate requests as they are submitted, create online access to the pertinent filings, invite citizen comment and, when the stakes are high enough, permit citizen participation in formal proceedings.

Notwithstanding this flexibility, at last year's September hearing Division professionals conceded to Senators that the agency has not held a public hearing on an increase in ordinary home insurance rates in living memory, if ever.[10]

We have listened respectfully to insurance industry executives. They voice concerns about the possible disclosure of material useful to competitors. We find there is no meaningful reason to keep rate requests secret across the board. The current statute mandates that everything becomes public anyway, but only when new rates take effect -- essentially, a fait accompli. Industry has cited no information to the Committee that such a peculiar timing arrangement is needed to protect a legitimate competitive advantage of the filer, when the public interest argues for earlier information sharing.

In their evaluation of multiple filings, Committee staff found no information that (1) included important elements of previously undisclosed product features or company strategy, (2) appeared

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[6] Ch. 4 § 7, twenty-sixth); Ch. 66.

[7] Ch. 66 § 10(a).

[8] Ch. 66 § 10(c).

[9] Ch. 4 § 7, twenty-sixth(d) (creating an exemption in public records law for "inter-agency or intra-agency memoranda or letters relating to policy positions being developed by the agency; but this subclause shall not apply to reasonably completed factual studies or reports on which the development of such policy positions has been or may be based").

[10] *Hearing before the Mass. Sen. Post Audit & Oversight Comm.*, 189th Gen. Ct. (Sept. 22, 2015) (statement of Daniel Judson, Comm'r of Ins., Mass. Div. of Ins.; statement of Glenn Kaplan, Ins. & Fin. Servs. Bureau Chief, Mass. Att'y Gen.'s Office).

to be so time-sensitive that earlier release would have transferred inappropriate advantage to competitors, and (3) in light of the two preceding considerations, rose to a level of seriousness substantial enough to justify DOI's overriding the public interest in timely access. In rare cases, DOI may find that it is critical for the health of the market that a filing be temporarily withheld from public view, necessitating delay. But neither the Division nor any insurer has, to date, presented the Committee with so much as a single example of such a filing.

Past Legislatures bear some responsibility for the current state of affairs. The original rate-filing statute was borrowed largely from model legislation promulgated nationwide by insurance regulators in the 1940s. While the agency has the discretion under current law to go in a new direction, one supportive of public participation, for the sake of clarity the General Court should legislate further and mandate DOI's commitment in this regard.

2. Once it bars other parties from the process, DOI does not do enough on its own to evaluate rate requests

DOI, by choice, goes it alone, serving as sole guarantor of Massachusetts' interest in fair homeowners rates. This has not proven to be a good arrangement for citizens. The Committee finds that, in three areas critical to the conduct of thorough rate reviews, DOI does not question industry assertions hard enough.

Weather models. In a filing for a rate increase, much depends on a firm's dollar payouts to insured parties, projected for the next year. Estimates of these rely heavily on meteorological predictions, with special emphasis on the likelihood of hurricanes, extreme winter conditions, and other extraordinary events. In support of its case, the firm offers up reports by outside vendors in possession of computerized weather models.

The Committee finds that DOI, in its consideration of rates for the regular homeowner, does not press insurers hard enough on the assumptions, inputs and calculations that lay behind weather predictions. An independent understanding of weather models is a prerequisite for effective evaluation of rate requests. Yet the agency often accepts, without serious inquiry, weather predictions for large swatches of territory, such as the entire East Coast, that do not include specifics on New England. Even more broadly, the agency appears to accept, at face value, protestations by insurers that they do not know very much -- or cannot discuss very much -- because information about each model must be guarded from competitors. Testimony and comment received from outside experts suggest that DOI's unquestioning acceptance of unexamined weather models comes too easily, too often, and at too high a cost.[11]

Reinsurance. Sellers of homeowners insurance are themselves buyers of reinsurance, a means of spreading out the risk of financial loss. In their filings, insurers often cite the cost of reinsurance

[11] *Hearing before the Mass. Sen. Post Audit & Oversight Comm.*, 189th Gen. Ct. (Sept. 22, 2015) (statements of Glenn Kaplan, Ins. & Fin. Servs. Bureau Chief, Mass. Att'y Gen.'s Office; Stephen D'Amato, former Chief, State Rating Bureau, Mass. Div. of Ins.; Paula Aschettino, President, Citizens for Homeowners Ins. Reform); Telephone Interview with Patricia A. McCoy, Professor, Boston College Law Sch. (Sept. 3, 2015); Telephone Interview with Alex Winslow, Exec. Dir., Texas Watch (Sept. 9, 2015); Telephone Interview with John Aloysius Cogan, Jr., Associate Professor, Univ. of Conn. L. Sch. (Sept. 14, 2015); Telephone Interview with Birny Birnbaum, Exec. Dir., Ctr. for Econ. Justice (Sept. 14, 2015).

as a significant portion of their overall expenses. Needless to say, there is nothing wrong in general with reinsurance. The problem for regulators comes when they try to evaluate the reasonableness of reinsurance charges that insurers enter into their expense calculations. Reinsurers tend to situate their financial operations offshore, beyond the reach of curious federal and state regulators. Further complicating the picture, several major insurers buy reinsurance from corporate sibling companies. In communications with DOI, staff to the Attorney General emphasize what they regard as agency under-scrutiny of reinsurance cost estimates used to support insurer rate requests.[12] The Committee shares the Attorney General's concern.

Policy cancellations and nonrenewals. Insurers manage their risk pools, and by extension their losses, by declining to renew policies on properties they find too risky. Property owners often question the reasonableness and consistency of cancellations and nonrenewals, and state law tasks DOI with monitoring industry activity in this respect. But DOI collects data only for certain urban and coastal zip codes. This saps the agency's ability to spot certain patterns of discrimination, including discrimination by other geographic distinctions or by level of risk.

3. Once rates are set, DOI lags other regulators in arming consumers with information

Massachusetts buyers of homeowners insurance are in some ways set up for success. They have an adequate number of carriers (68, according to the most recent information available from DOI) from which to choose. Aggregate market share of the 10 largest companies does not appear large enough to squelch competition from the remaining firms.

It is all the more telling, then, that consumers find it difficult to compare offerings on cost, quality and convenience.[13] Homeowners confront an advanced case of information asymmetry, the condition of sellers knowing a great deal -- and buyers knowing little -- about a complicated product. Independent brokers may step in to help narrow the imbalance, but they don't do business with 68 homeowners carriers; most deal with a dozen, and often fewer.

In the 21st century world of information and the Internet, Massachusetts consumers deserve tools that let them do sophisticated shopping. Regulatory and consumer protection agencies in states like Texas,[14] California[15] and Delaware[16] provide online comparison engines that do a good job

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[12] Letter from Glenn Kaplan, Ins. & Fin. Servs. Bureau Chief, Mass. Att'y Gen.'s Office, to Joseph Murphy, Acting Comm'r., Mass. Div. of Ins. (Oct. 30, 2009); Letter from Glenn Kaplan to Kevin Beagan, State Rating Bureau Chief, Mass. Div. of Ins. (Nov. 17, 2011); Letter from Glenn Kaplan to Kevin Beagan (Feb. 28, 2012) (all letters on file with the committee).

[13] *E.g.*, *Informational Hearings on the Mass. Voluntary Market for Homeowners' Ins.*, Mass. Div. of Ins. (Oct. 21, 2015; Dec. 2, 2015) (statements of Chris Bartlett, Lowell resident and Martha Muldoon, New Bedford resident).

[14] Tex. Dep't of Ins., Homeowner/Condo/Renter Sample Rates, https://apps.tdi.state.tx.us/helpinspublic/Start.do?type=res (last visited Mar. 2, 2016).

[15] Cal. Dep't of Ins., 2015 Homeowners Premium Survey, https://interactive.web.insurance.ca.gov/survey/index.jsp (last visited Mar. 2, 2016).

[16] Del. Dep't of Ins., Home Ins. Rate Comparison, http://compare.delawareinsurance.gov/Consumer/InsuranceTypeSelection.aspx (last visited Jan. 13, 2016).

on rates and coverage. Massachusetts, in contrast, makes little use of government websites for this purpose,[17] and there are no alternative sources of effective information.

4. Beset by weak DOI regulation and poor consumer information, local homeowners face rising premiums

In 2007-2013, average Massachusetts premiums for regular homeowners insurance rose 21.6%,[18] far outpacing inflation (12.9%).[19] A 21.6% increase is astounding, considering that, during the same dismal stretch, average Massachusetts home values fell 11% [20] and median household income fell 4.7%.[21] In contrast to home insurance, over the same period costs of auto insurance crept up a modest 2.8%.[22] Compared to those who pay ordinary -- the term of art in the industry is "voluntary" -- home insurance rates, owners of the state's smaller pool of high-risk properties made out much better; premiums for homes covered by the FAIR Plan, so called,[23] rose 6.7%.[24]

Meanwhile, the results for sellers of homeowners insurance are as bright as the results for buyers are grim. Insurers here are much more profitable, by every measure, than most of their counterparts across the country. For the 10-year period 2004-2013, the most recent year for

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[17] Mass. Div. of Ins., Home Ins., http://www.mass.gov/ocabr/insurance/home-insurance (last visited Feb. 11, 2016).

[18] MASS. DIV. OF INS., ANNUAL HOME INS. REPORT FOR CALENDAR YEAR 2007 (2008) (on file with the Committee); MASS. DIV. OF INS., ANNUAL HOME INS. REPORT FOR CALENDAR YEAR 2008 (2009) (on file with the Committee); MASS. DIV. OF INS., ANNUAL HOME INS. REPORT FOR CALENDAR YEAR 2009 (2010), *available at* http://www.mass.gov/ocabr/docs/doi/consumer/mass-home-insurance-2009.pdf; MASS. DIV. OF INS., ANNUAL HOME INS. REPORT FOR CALENDAR YEAR 2010 (2011), *available at* http://www.mass.gov/ocabr/docs/doi/consumer/mass-home-insurance-2010.pdf; MASS. DIV. OF INS., ANNUAL HOME INS. REPORT FOR CALENDAR YEAR 2011 (2012), *available at* http://www.mass.gov/ocabr/docs/doi/consumer/mass-home-insurance-2011.pdf; MASS. DIV. OF INS., ANNUAL HOME INS. REPORT FOR CALENDAR YEAR 2012 (2013), *available at* http://www.mass.gov/ocabr/docs/doi/consumer/mass-home-insurance-2012.pdf; MASS. DIV. OF INS., ANNUAL HOME INS. REPORT FOR CALENDAR YEAR 2013 (2014), *available at* http://www.mass.gov/ocabr/docs/doi/consumer/mass-home-insurance-2013.pdf.

[19] Bureau of Labor Statistics, http://www.bls.gov/regions/new-england/data/consumerpriceindex_northeast_table_pdf.pdf (last visited Mar. 3, 2016).

[20] Lincoln Inst. of Land Policy, Land Prices by State, https://www.lincolninst.edu/subcenters/land-values/data/landdata-states-2015q1.xls (last visited Feb. 5, 2016).

[21] Dep't of Numbers, Massachusetts Family Income, http://www.deptofnumbers.com/income/massachusetts/#family (last visited Feb. 5, 2016).

[22] Ins. Info. Inst., Auto Ins., http://www.iii.org/fact-statistic/auto-insurance (last visited Mar. 17, 2016).

[23] The FAIR Plan, which is discussed in more detail later in this report, is an insurer of last resort, created by state law, which offers coverage for homes in designated coastal and urban locations where residents may not be able to obtain private insurance because they are considered high risk.

[24] MASS. DIV. OF INS., ANNUAL HOME INS. REPORT FOR CALENDAR YEAR 2007 (2008) (on file with the Committee); MASS. DIV. OF INS., ANNUAL HOME INS. REPORT FOR CALENDAR YEAR 2008 (2009) (on file with the Committee); MASS. DIV. OF INS., ANNUAL HOME INS. REPORT FOR CALENDAR YEAR 2009 (2010), *available at* http://www.mass.gov/ocabr/docs/doi/consumer/mass-home-insurance-2009.pdf; MASS. DIV. OF INS., ANNUAL HOME INS. REPORT FOR CALENDAR YEAR 2010 (2011), *available at* http://www.mass.gov/ocabr/docs/doi/consumer/mass-home-insurance-2010.pdf; MASS. DIV. OF INS., ANNUAL HOME INS. REPORT FOR CALENDAR YEAR 2011 (2012), *available at* http://www.mass.gov/ocabr/docs/doi/consumer/mass-home-insurance-2011.pdf; MASS. DIV. OF INS., ANNUAL HOME INS. REPORT FOR CALENDAR YEAR 2012 (2013), *available at* http://www.mass.gov/ocabr/docs/doi/consumer/mass-home-insurance-2012.pdf; MASS. DIV. OF INS., ANNUAL HOME INS. REPORT FOR CALENDAR YEAR 2013 (2014), *available at* http://www.mass.gov/ocabr/docs/doi/consumer/mass-home-insurance-2013.pdf.

which data are available, average underwriting profit was 16.9% in Massachusetts versus 1.3% nationally.[25] Average return on net worth was 17.6% versus 6.6% nationally. The average loss ratio for Massachusetts property insurers came in below the national average in nine out of the 10 years.[26]

As a further comment on these trends, we now have a recent communication to the Committee from staff to state Attorney General Maura Healey. The AG's insurance experts inform us that the high 2015 rate increases granted by DOI to MAPFRE and Safety Insurance, two of the four largest property insurers in Massachusetts, "are of serious concern to the Attorney General's Office."[27] These staff specialists, afforded access to materials only after rates took effect, determined that profit estimates in the documents are "arbitrary and not supported by sufficient data."[28] They determined as well that estimated catastrophe losses -- those related to a specific weather event that generates a large number of claims totaling a large dollar amount -- were calculated using a "biased" approach designed to "increase their revenues."[29] The bottom line: the rates approved by DOI are unlawfully "excessive."[30]

RECOMMENDATIONS

1. DOI should use its existing authority to open up the process

Having found that DOI has discretion -- thanks to its own rate filing statute and the Commonwealth's public records law -- to put an end to exclusionary practices and open up the process, the Committee urges the agency to do so. The Division should, as a matter of course, provide online notice of rate requests as soon as they're filed, create timely online access to pertinent filings, and invite public comment. In select cases, to ensure comprehensive review of the financial and economic issues involved, it should go further and order public hearings.

Other states do this. North Carolina changed its laws in 2009 to allow a public comment period for every home insurance rate filing, and recently concluded the state's first public hearing on voluntary market rates in 20 years.[31] More than half of states post home insurance rate filings online after they've been approved.[32] Several states, including Rhode Island, Connecticut, Idaho, Oregon and California, post the filings while they are still under review.[33] Massachusetts,

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[25] Ins. Info. Inst., Average Expenditures for Auto Ins. by State, http://www.iii.org/table-archive/21247 (last visited Feb. 5, 2016).

[26] NAT'L ASS'N OF INS. COMM'RS, REPORT ON PROFITABILITY BY LINE BY STATE IN 2013 149, 150, 152, 237, 238, 240 (2014) *available at* http://www.naic.org/prod_serv/PBL-PB-14.pdf.

[27] Letter from Glenn Kaplan, Ins. & Fin. Servs. Bureau Chief, Mass. Att'y Gen.'s Office to Sen. Michael J. Barrett, Chair, Mass. Sen. Post Audit & Oversight Comm. (Nov. 30, 2015) (on file with the Committee).

[28] *Id.*

[29] *Id.*

[30] *Id.*

[31] Filing Dated Jan. 3, 2014 by the N. C. Rate Bureau for Revised Homeowners' Ins. Rates & Homeowners Ins. Territory Definitions, N.C. Dep't of Ins., Docket No. 1719 2 n.2 (Dec. 18, 2014) (order); N.C. GEN. STAT. § 58-36-15(b).

[32] Nat'l Ass'n of Ins. Comm'rs, SERFF Filing Access, http://www.serff.com/index_sfa.htm (last visited Jan. 13, 2016) (map of states providing online access to filings).

[33] Nat'l Ass'n of Ins. Comm'rs, SERFF Filing Access: Rhode Island, https://filingaccess.serff.com/sfa/home/RI (last visited Mar. 17, 2016); SERFF Filing Access: Connecticut, https://filingaccess.serff.com/sfa/home/CT (last visited Mar. 17, 2016); SERFF Filing Access: Idaho, https://filingaccess.serff.com/sfa/home/ID (last visited Mar. 17, 2016); SERFF Filing Access: Oregon, https://filingaccess.serff.com/sfa/home/OR (last visited Mar. 17, 2016); Rate

a progressive state and a leader in innovative technology, ought to be at the forefront of providing online access to information that affects consumers, not one that lags behind dozens of other states.

2. The General Court should require transparency at DOI

The record shows that the agency's regulation of regular home insurance rates is remarkably low-energy. Members of the House and Senate should take legislative action, clarifying to the Division that there is no permissible rationale for adherence to the practice of non-transparency.

In February 2016, the Senate approved language requiring DOI to post homeowners rate requests and supporting information online within three business days of receipt. Included in the Senate version of public records reform and dependent, as of the publication date of this report, on acceptance by a Conference Committee of the House and Senate, this breakthrough would bring transparency to a corner of the Massachusetts economy in desperate need of it. Industry filings are already submitted to DOI via an online system that can easily be broadened to afford public access, so the agency could comply with a legislative directive promptly.

3. The General Court should authorize the AG to order a limited number of homeowners hearings on her own initiative

Within the professional lifetimes of staff to both the Insurance Commissioner and the Attorney General, DOI has not once exercised its power to hold hearings on regular home insurance rates.[34] Over this period, DOI has not only declined to act on its own initiative; it has denied petitions for hearings by the Attorney General and others.[35]

No question, formal proceedings of this kind are time- and labor-intensive. The option to hold them should be employed carefully. Still, in the Committee's view, the Division's embrace of complete abstinence has rendered the hearing option a dead letter, with implications for the agency's ability to deter industry over-reaching.

Because the status quo risks harm to citizens of the Commonwealth, the Committee recommends passage of new legislation giving the state Attorney General the authority to order a small number of public hearings -- perhaps up to four a year -- on requests for increases in regular

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Regulation Branch, Calif. Dep't of Ins., Web Access to Rate & Form Filings, http://www.insurance.ca.gov/0250-insurers/0800-rate-filings/0050-viewing-room/ (last visited Mar. 17, 2016).

[34] *Hearing before the Mass. Sen. Post Audit & Oversight Comm.*, 189th Gen. Ct. (Sept. 22, 2015) (statements of Daniel Judson, Comm'r of Ins., Mass. Div. of Ins.; Glenn Kaplan, Ins. & Fin. Servs. Bureau Chief, Mass. Att'y Gen.'s Office; Stephen D'Amato, former Chief, State Rating Bureau, Mass. Div. of Ins.).

[35] Letter from Kevin Beagan, State Rating Bureau Chief, Mass. Div. of Ins., to Glenn Kaplan, Ins. & Fin. Servs. Bureau Chief, Mass. Att'y Gen.'s Office (June 14, 2012) (acknowledging that insurers' use of catastrophe models had been called into question, but stating that the Division did "not agree that it is appropriate to hold adjudicatory hearings on individual voluntary rate filings at this time."); Letter from Daniel Judson, Comm'r of Ins., Mass. Div. of Ins., to Paula Aschettino, President, Citizens for Homeowners Ins. Reform (Sept. 14, 2015) (denying request from consumer to hold a hearing on MAPFRE filing due to lack of standing as an "aggrieved person").

home insurance rates. While DOI would continue to conduct all proceedings, the Attorney General would participate as a matter of right, as an advocate for consumers.[36]

The AG's office employs several insurance experts in its Insurance and Financial Services Bureau. It retains a number of others for its work on the more heavily-regulated FAIR Plan, as discussed later in this report. As the state's consumer advocate in chief, the AG ought to have the opportunity to get involved in regular home insurance filings in this limited capacity in order to address excessive rate requests.

4. DOI should issue regulations to govern both rate requests and hearing requests

Though authorized by law to adopt regulations governing regular homeowners rate proceedings,[37] DOI has never done so. The agency evaluates rates -- and approves or rejects them -- in an environment bereft of written rules and standards. Likewise, the agency rules on requests for hearings without any regulatory guidance. The agency should issue draft regulations, solicit comment, and finalize written procedures to govern its review of rate requests and hearing requests.

5. DOI should push harder on weather models, reinsurance cost estimates, and policy cancellations and nonrenewals

Weather models. Three times in recent years -- in 2009, 2011 and 2012 -- staff to the Attorney General have written the Division to voice concerns about the prominent reliance in regular home insurance filings on weather model predictions. In the two more recent letters, the staff presented grounds for their belief that the models afford too little insight into conditions specific to Massachusetts.[38] In its eventual response, the Division agreed "to hold a public hearing in 2012 to review catastrophe models in detail and evaluate the features of the models, including

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[36] This recommendation is based upon a similar arrangement that Connecticut uses in the health insurance context. There, the state's appointed Healthcare Advocate negotiated an agreement with the Commissioner of Insurance that permits the Advocate to order up to four hearings per year on health insurance rate hikes. Since the officials reached this agreement in 2011, the Advocate has only called for a hearing once, and in that case the Commissioner stated that it was his decision to hold a hearing, rather than the Advocate's. *See*, *e.g.*, Arielle Levin Becker, *Both sides praise health insurance rate review compromise*, CONN. MIRROR, July 26, 2011, *available at* http://ctmirror.org/2011/07/26/both-sides-praise-health-insurance-rate-review-compromise; Arielle Levin Becker, *Healthcare advocate wants hearing on Anthem rate request*, CONN. MIRROR, June 6, 2014, *available at* http://ctmirror.org/2014/06/06/healthcare-advocate-wants-public-hearing-on-anthem-rate-hike-proposal.

[37] Mass. Gen. L. Ch. 174A § 15(d); Ch. 175A § 15(d) (2014) ("The commissioner may make reasonable rules and regulations necessary to effect the purpose of this chapter.").

[38] Letter from Glenn Kaplan, Ins. & Fin. Servs. Bureau Chief, Mass. Att'y Gen.'s Office, to Joseph Murphy, Acting Comm'r., Mass. Div. of Ins. (Oct. 30, 2009); Letter from Glenn Kaplan to Kevin Beagan, State Rating Bureau Chief, Mass. Div. of Ins. (Nov. 17, 2011); Letter from Glenn Kaplan to Kevin Beagan (Feb. 28, 2012) (all letters on file with the committee).

the calibrations that are specific to Massachusetts experience."[39] No such hearing has been held. The issues are important and have not gone away. DOI should make good on this pledge.

As this report discusses, insurers rely heavily on weather models to predict future losses. Weather models are created by a small number of outside vendors that provide this service for all insurers. DOI does not receive specific information about these models, and to date has not pushed insurers to reveal more details. DOI can and should require insurers to provide much more information in order to gauge that the weather models are sufficiently tailored to Massachusetts and that vendors are using actuarially sound methodologies.

Reinsurance. In the 2009 letter, Attorney General staff questioned what they regard as agency under-scrutiny of reinsurance cost estimates presented by insurers.[40] The Committee shares the Attorney General's concern. DOI should require that insurers provide specific information regarding their reinsurance costs, as well as the underlying weather models used by reinsurers to justify premiums. Like the losses predicted by weather models, reinsurance makes up a substantial portion of the premiums charged to customers. Without probing the underlying components of this cost -- the weather models used by reinsurers, for instance, which were a significant issue in the FAIR Plan proceedings of 2013 -- DOI is simply rubber-stamping this large portion of customers' rates.

Policy cancellations and nonrenewals. As we've indicated, state law requires DOI to collect data on insurance policies cancelled and non-renewed in the "urban and coastal" areas of Massachusetts,[41] but the agency is also free to range beyond this minimum requirement. Periodically, at the very least, DOI should sample for other instances of possible discrimination. Insurers must be free to choose their own pools of risk and to manage them, but consumers should also have access to information about which insurers are declining to renew policies, for what reasons, and in which locations. To permit this to happen, the General Court should amend the statute to require that DOI collect additional data.

6. Either DOI or the General Court should compel insurers to notify people about new rates

DOI should promulgate a regulation requiring insurers to give clear notice to homeowners when they roll out major rate increases. Consumers typically are not informed of rate changes -- they simply receive a bill for a premium based on the new rate and the annually updated assessment of their home.[42] Insurers are not required to inform customers, so they do not. If customers received notice that their premiums were going to increase, they would have time to shop for a different policy prior to renewal of their existing policies. If DOI does not act, the Legislature should enact language mandating notification.

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[39] Letter from Kevin Beagan, State Rating Bureau Dir., Mass. Div. of Ins., to Glenn Kaplan, Ins. & Fin. Servs. Bureau Chief, Mass. Att'y Gen.'s Office (June 14, 2012) (on file with the Committee).

[40] Letter from Glenn Kaplan, Ins. & Fin. Servs. Bureau Chief, Mass. Att'y Gen.'s Office, to Joseph Murphy, Acting Comm'r., Mass. Div. of Ins. (Oct. 30, 2009).

[41] Mass. Gen. L. ch. 175 §§ 4A, 4B (2014).

[42] Interview with Stephen D'Amato, former Chief, State Rating Bureau, Mass. Div. of Ins., in Boston, Mass. (Aug. 11, 2015); Interview with Paula Aschettino, President, Citizens for Homeowners Ins. Reform, in Boston, Mass. (Sept. 2, 2015).

7. DOI should create an online premium comparison tool for homeowners insurance

DOI should follow the examples of Texas,[43] California[44] and Delaware,[45] among others, by creating and maintaining an online comparison engine for homeowners insurance. This tool should, at a minimum, let consumers compare carriers on coverage and charges, without having to contact multiple agents or request quotes from multiple insurers. DOI already offers Massachusetts consumers a rudimentary application for auto policies,[46] and has the authority and ability to create such a tool for homeowners.

REGULATION OF HOME INSURANCE RATES IN MASSACHUSETTS

Overview

The Division of Insurance regulates rates and other terms and conditions for voluntary market homeowners insurance, pursuant to chapters 174A and 175A of the Massachusetts General Laws. Massachusetts has what is known as a "file and use" system; insurers provide DOI with comprehensive information regarding proposed rates and the cost and loss estimates underlying them, but need not await the agency's formal approval before using the new rates.[47] As a practical matter, agency review takes approximately 60 days, and insurers wait out the process before applying new rates.[48, 49]

Chapters 174A and 175A establish the broad standard by which DOI reviews insurers' rate requests. DOI must approve proposed rates if it finds they are not "excessive, inadequate or unfairly discriminatory."[50] The burden lies with the insurer to provide sufficient information to enable DOI to make this determination.[51] The agency may disapprove the rates if it finds the

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[43] Tex. Dep't of Ins., Homeowner/Condo/Renter Sample Rates, https://apps.tdi.state.tx.us/helpinspublic/Start.do?type=res (last visited Mar. 2, 2016).
[44] Cal. Dep't of Ins., 2015 Homeowners Premium Survey, https://interactive.web.insurance.ca.gov/survey/index.jsp (last visited Mar. 2, 2016).
[45] Del. Dep't of Ins., Home Ins. Rate Comparison, http://compare.delawareinsurance.gov/Consumer/InsuranceTypeSelection.aspx (last visited Jan. 13, 2016).
[46] Mass. Div. of Ins., Auto Premium Comparisons, http://www.mass.gov/ocabr/insurance/vehicle/auto-insurance/auto-insurance-premium-comparisons.html (last visited Jan. 13, 2016).
[47] Mass. Gen. L. ch. 174A § 6(a) (2014); ch. 175A § 6(a) (2014) (Insurers may start using requested rates as soon as 15 days after the request is filed, if DOI does not reject the request.).
[48] This was the case for the 14 rate filings approved by DOI that were reviewed by the Committee.
[49] *Hearing before the Mass. Sen. Post Audit & Oversight Comm.*, 189th Gen. Ct. (Sept. 22, 2015) (written testimony of Daniel Judson, Comm'r of Ins., Mass. Div. of Ins., at 3) ("In practice, the Division has been targeting a 60 day review period since 2007.") *See also* MASS. DIV. OF INS., BULLETIN NO. 2008-08, GUIDELINES FOR THE SUBMISSION OF FORM, RATE AND RULE FILING MATERIALS FOR REVIEW BY THE MASS. DIV. OF INS. 1 (May 20, 2008) ("[DOI's] goal is to review all such filings and either to approve, disapprove, place on file, or reject them within 60 days.").
[50] Ch. 174A § 5(a)(2); ch. 175A § 5(a)(4).
[51] Travelers Indemnity Co. v. Comm'r of Ins., 362 Mass. 301, 305 (1972) (holding that there is an implicit requirement in the "excessive, inadequate or unfairly discriminatory" standard of ch. 175A § 5(a)(4) that the insurer provide "adequate evidence . . . to enable the Commissioner to establish a range of reasonableness.").

documentation insufficient. DOI may ask the insurer for clarification, may question the assumptions or inputs in the rate-setting formula used, or may reject the rate request.[52]

"Excessive, inadequate or unfairly discriminatory," the standard used by most insurance regulators nationwide to review rate requests, is not given more elaborate meaning in the Massachusetts General Laws or any DOI regulations. It is, however, a topic covered in various treatises on insurance law, some of which DOI relies upon in its work.[53] The terminology was adopted at the annual conference of the National Association of Insurance Commissioners (NAIC) in 1945, following federal legislation declaring that the insurance industry was to be regulated by the states.[54] Insurers are entitled under the law to charge rates that permit a "reasonable margin for underwriting profit."[55]

Rate requests can be filed at any time. There is no requirement that insurers must submit a filing every year, but neither are they limited to just one filing a year. Revised rates take effect for each customer on a rolling basis, when he or she next renews coverage after the "effective date" set by the insurer.

Insurance rate setting is a forward-looking exercise, where insurers must set prices based upon predictions of their costs, losses and target profit. Insurers are not permitted, under the laws and actuarial principles, to raise rates in order to recoup past losses, even when losses were much higher than those projected for a given year.[56] Conversely, DOI may not force insurers to return funds received from customers when losses are much lower than projected.[57] The Massachusetts Supreme Judicial Court explained in 1987 that "[i]nsurance rate making is essentially prospective in nature. Massachusetts law no longer makes provisions for a 'second look' at the rates and does not provide for a rebate to the insurers or to the policyholders if past rate predictions ultimately turn out to be wrong."[58]

The public interest in regulating rates has to do with the fact that most consumers do not purchase homeowners insurance voluntarily; they're required to do so as a condition of obtaining a mortgage. The regulating agency guards against any insurer temptation to exaggerate projected losses or inflate associated business costs.

How insurers prepare rate change requests

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[52] Ch. 174A § 6(a); ch. 175A §§ 6(a) & 7(a). If DOI wishes to reject a rate request, it must first hold a hearing where the insurer may present further evidence to support its request. Ch. 174A § 6(a); ch. 175A §§ 6(a) & 7(a).
[53] Actuarial Standards Board, Actuarial Standards of Practice, *available at* http://www.actuarialstandardsboard.org/standards-of-practice (last visited Jan. 4, 2016); Cas. Actuarial Soc., CAS Code of Prof'l Conduct (Nov. 12, 2000), *available at* http://www.casact.org/professionalism/policiesProc/index.cfm?fa=code; CAS. ACTUARIAL SOC., STATEMENT OF PRINCIPLES REGARDING PROP. AND CAS. INS. RATEMAKING (May 1988), *available at* http://www.casact.org/professionalism/standards/princip/sppcrate.pdf.
[54] McCarran-Ferguson Act, 59 Stat. 33 (1945) (codified as amended at 15 U.S.C. §§ 1011-1015 (2016)).
[55] Mass. Gen. L. ch. 175A § 5(a)(1) (2014).
[56] Massachusetts Auto. Rating & Acc. Prev. Bureau v. Comm'r of Ins., 401 Mass. 282, 294 (1987).
[57] *Id.*
[58] *Id.*

Before an insurer files for a rate change, it first prepares a set of documents that it will submit to DOI to support the proposed rate. These documents lay out calculations of the company's expected losses due to claims paid out, anticipated expenses and anticipated earned premiums.

Insurers' projected losses are calculated based on loss ratios[59] and loss adjustment expenses.[60] Estimation of these loss factors turns on past loss experience and forward-looking projections about weather and other variables that impact customer claims. Insurers hire modeling companies to assist them in the murky business of estimating future losses. An insurer's loss ratio is an important indicator of its financial standing. Likewise, the industry-wide loss ratio is critical to gauging the sector's overall health. A low loss ratio means greater profit.

Expenses consist of commissions paid to brokers, taxes, reinsurance charges, general administration, and return on equity. Return on equity is the insurer's selected income target.[61]

Using the loss and expense estimates as inputs, the insurer applies a formula to calculate the change in its rate from the previous year that will be necessary to cover the losses and expenses while meeting a target profit. This rate change is known as the "indicated rate."

The rate that is actually requested by the insurer, called the "proposed rate," is a separate number, generally lower than the indicated rate. Insurers apparently select the proposed rate based on what they believe the market will bear.[62] For instance, in 2015, MAPFRE filed a rate request for an 8.9% increase, while its indicated rate increase was 14.2%.[63] Plymouth Rock filed for a 7.7% increase, while its indicated rate increase was more than three times greater: 23.0%.[64] The Division requires a justification for the difference in indicated and proposed rates. But the justifications in rate request documents reviewed by the Committee have been cursory -- for instance, Plymouth Rock Group stated "market competition" as its explanation.[65]

While the rate request documents directly support the indicated rate, DOI also accepts the data and projections as supportive of the "proposed rate." DOI representatives have stated that direct support for the "proposed rate" is not necessary because analysts review its appropriateness without regard to the indicated rate.[66] It is not clear why the indicated rate is relevant to the rate request or to DOI's analysis of the rate request.

Process of filing a rate change request

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[59] A loss ratio is the percent of earned premiums that an insurer pays out for customer claims.
[60] Loss adjustment expenses are the costs to the insurer of processing and settling claims.
[61] Return on equity is also referred to as cost of capital.
[62] *Hearing before the Mass. Sen. Post Audit & Oversight Comm.*, 189th Gen. Ct. (Sept. 22, 2015) (statement of Cara Blank, Prop. Cas. Actuary, State Rating Bureau, Mass. Div. of Ins.).
[63] MAPFRE U.S.A., Rate Filing CMRC-129987068, Apr. 20, 2015 (rate) (on file with the Committee).
[64] Bunker Hill Ins. Co., Rate Filing PRAC-130020577, Apr. 18, 2015 (actuarial memo.) (on file with the Committee).
[65] Bunker Hill Ins. Co., Rate Filing PRAC-130020577, Apr. 18, 2015 (rate filing abstract) (on file with the Committee).
[66] *Hearing before the Mass. Sen. Post Audit & Oversight Comm.*, 189th Gen. Ct. (Sept. 22, 2015) (statement of Cara Blank, Prop. Cas. Actuary, State Rating Bureau, Mass. Div. of Ins.).

A rate filing formally begins when an insurer initiates the process on the System for Electronic Rate and Form Filing (SERFF). SERFF is a web site established by NAIC for regulators and insurers.[67] The insurer uploads its rate request documents and DOI later downloads them.

DOI analysts correspond with the insurer's rate filing attorney through a forum on the SERFF system, and may request additional information or justification for particular inputs into the calculations. This online forum is the primary means by which the Division asks questions of the insurer or requests revisions or clarifications.[68] Exchanges between the DOI and the insurer conducted through SERFF are documented in the rate filing. The parties may also communicate by phone, which is not thoroughly documented in the SERFF record.[69]

When DOI analysts are satisfied that they have received sufficient information to justify the insurer's requested rate change, the rate request is "placed on file." DOI generally does not issue affirmative approvals, since approval is not required by statute or regulation. Placing a request on file is an indication to the insurer that DOI does not plan to reject it. At this point the rate review process is usually complete. However, placing a rate on file is not an irrevocable action; DOI can still raise concerns and the insurer may still make small modifications, such as changing the effective date of the proposed rates. It is only at the effective date that the documents become publicly available. And it is only at this point that an "aggrieved" party may learn of the rates and request a hearing.

Lack of public hearings on homeowners insurance

To examine rate request documents, a person – even the Attorney General -- must contact DOI and ask if any new requests have been placed on file, then either visit DOI's Boston office in person or request that a CD-R copy be mailed. DOI has declined to participate in an optional SERFF program that allows easier access to documents.[70]

DOI may, at the Commissioner's discretion, call a hearing on any rate request it receives.[71] Oddly, the agency is not required to have a hearing on a request except when it intends to reject it.[72] In such a case, an insurer can instead withdraw the request and file a new one, a less burdensome option than defending the original filing at a hearing. Withdrawing and filing anew also has the effect of concealing the insurer's original request, indefinitely, from the public and from any government official outside the Division.

In addition to allowing the Commissioner to hold hearings, Chapters 174A and 175A of the Massachusetts General Laws establish that any "person or organization aggrieved with respect to

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[67] *See* Sys. for Elec. Rate & Form Filing, http://www.serff.com (last visited Jan. 4, 2016).
[68] *Hearing before the Mass. Sen. Post Audit & Oversight Comm.*, 189th Gen. Ct. (Sept. 22, 2015) (statement of Cara Blank, Prop. Cas. Actuary, State Rating Bureau, Mass. Div. of Ins.).
[69] References to phone conferences do appear in the filings reviewed by the Committee, and this practice was confirmed by the testimony of Property Casualty Actuary Cara Blank at the Sept. 22, 2015 hearing.
[70] Nat'l Ass'n of Ins. Comm'rs, SERFF Filing Access, http://www.serff.com/index_sfa.htm (last visited Jan. 13, 2016).
[71] Mass. Gen. L. ch. 174A § 7(c); ch. 175A § 7(c) (2014).
[72] Ch. 174A § 7(a); ch. 175A § 7(a); Ins. Rating Board v. Comm'r of Ins., 358 Mass. 171, 176-77 (1970) (holding that the Commissioner may not reject rates filed pursuant to chapter 175A of the Massachusetts General Laws without first holding an adjudicatory hearing).

any filing which is in effect" may request a hearing before DOI.[73] The agency has complete discretion to grant or deny such a hearing.[74] The Attorney General's office has requested hearings on regular homeowners rates at least twice in the past six years.[75] Consumer advocates have made at least one request during this time.[76] All requests were denied. None of the current or recent officials at DOI with whom the Committee spoke or from whom it received testimony could recall a time when a hearing was held on request. Based upon the testimony of these officials and a representative from the Attorney General's office, the Committee understands there has not been a hearing on a rate request in at least 15 years, and possibly much longer.[77]

Contrast: the FAIR Plan

For Massachusetts residents who live in urban or coastal areas deemed high-risk, there is an alternative insurance option, the residual market or "FAIR Plan." About 9.9% of Massachusetts properties are covered by the FAIR Plan, accounting for 11.6% of premiums paid.[78] The market was created by Massachusetts (and other states) during the 1960s civil rights era, in response to red-lining, discrimination by insurers in the provision of coverage to urban and minority homeowners.

The FAIR Plan is run by an umbrella group called the Massachusetts Property Insurance Underwriters Association (MPIUA). Sellers of homeowners insurance in Massachusetts are required to belong to MPIUA and must share in its costs relative to their shares of the market.[79]

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[73] Ch. 174A § 7(b); ch. 175A § 7(b).

[74] Ch. 174A § 7(b); ch. 175A § 7(b) ("If the commissioner shall find that the application is made in good faith, that the applicant would be so aggrieved if his grounds are established, and that such grounds otherwise justify holding such a hearing, he shall, within thirty days after receipt of such application, hold a hearing . . . .").

[75] Letter from Glenn Kaplan, Ins. & Fin. Servs. Bureau Chief, Mass. Att'y Gen.'s Office, to Joseph Murphy, Acting Comm'r., Mass. Div. of Ins. (Oct. 30, 2009) (requesting rate review hearing to assess insurers' use of particular discredited hurricane models); Letter from Glenn Kaplan to Kevin Beagan, State Rating Bureau Chief, Mass. Div. of Ins. (Nov. 17, 2011) (requesting that the State Rating Bureau "seek the initiation of administrative rate proceedings" for insurers relying on weather models that had been rejected in Fair Plan proceedings); Letter from Glenn Kaplan to Kevin Beagan (Feb. 28, 2012) (requesting that DOI hold hearings on individual rate filings relying on "untested, and often discredited, hurricane models" even if a separate, general hearing were held to assess the hurricane models themselves); Letter from Kevin Beagan to Glenn Kaplan (June 14, 2012) (stating that the Division did "not agree that it is appropriate to hold adjudicatory hearings on individual voluntary rate filings at this time.") (all letters on file with the Committee).

[76] Letter from Daniel Judson, Comm'r of Ins., Mass. Div. of Ins., to Paula Aschettino, President, Citizens for Homeowners Ins. Reform (Sept. 14, 2015) (denying request from MAPFRE customer for a hearing on MAPFRE rate request due to lack of standing as an "aggrieved person") (on file with the Committee).

[77] *Hearing before the Mass. Sen. Post Audit & Oversight Comm.*, 189th Gen. Ct. (Sept. 22, 2015) (statements of Daniel Judson, Comm'r of Ins., Mass. Div. of Ins.; Glenn Kaplan, Ins. & Fin. Servs. Bureau Chief, Mass. Att'y Gen.'s Office; Stephen D'Amato, former Chief, State Rating Bureau, Mass. Div. of Ins.).

[78] MASS. DIV. OF INS., ANNUAL HOME INS. REPORT FOR CALENDAR YEAR 2014 1 (2015), *available at* http://www.mass.gov/ocabr/docs/doi/consumer/mass-home-insurance-2014.pdf.

[79] Mass. Gen. L. Ch. 175C § 4(a) (2014) ("All insurers licensed to write and engaged in writing in this commonwealth, on a direct basis, basic property insurance or any component thereof in multi-peril policies, shall cooperate in organizing a joint underwriting association which shall provide basic property insurance to eligible applicants who are otherwise unable to obtain such coverage in the voluntary market. Every such insurer shall be a member of the association and remain a member as a condition of its authority to transact such insurance within the commonwealth."); § 4(e) ("All members of the association shall participate in its writing, expenses, profits and

The Division closely regulates the FAIR Plan, its rates and its terms.[80] In sharp contrast to the larger "voluntary" market, MPIUA requests for changes to rates or terms trigger a rigorous process of public hearing and review that includes document discovery, testimony, cross-examination and public comment.[81] The Attorney General's office is entitled to participate as a matter of right, as an advocate for consumers.[82] Other participants are the MPIUA itself, in support of its rate and terms request, but also the State Rating Bureau (SRB), a once-prominent but now obscure department within DOI that acts as an occasional advocate for consumers.[83] Officers of the Division preside over FAIR Plan rate hearings. The process takes months and results in a written decision by the Commissioner.

The Commissioner of Insurance denied the three most recent FAIR Plan requests for rate increases, in 2007, 2011 and 2013. Most recently, the Commissioner rejected the 2013 request because (1) the model used for hurricane damage projections was insufficiently tailored to Massachusetts and (2) plan administrators failed to demonstrate that reinsurance costs incorporated into the rates were reasonable.[84]

At the Committee's September 22 oversight hearing, insurers were unable to explain whether or in what way their hurricane models and reinsurance policies differ from those of the FAIR Plan.

2015 Rate increases

At the Senate Post Audit hearing, three insurers that had received recent rate approvals testified: MAPFRE U.S.A, Safety Insurance Group and Plymouth Rock.

- MAPFRE U.S.A., the largest property insurer in the state with 13% of the voluntary market,[85] won an initial increase of 0.3%, effective January 1, 2015, and a second increase of 8.9%, effective eight months later, on August 1, 2015, for a total increase of 9.2% during 2015.

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losses in the proportion that the premiums written by each such member for basic property insurance . . . bear to the aggregate premiums for such insurance written in the commonwealth by all members of the association.").

[80] *See Procedures Concerning Rate Filings Made Pursuant to MGL c.175C and the Conduct of Hearings on Such Filings*, 211 Mass. Code Regs. §§ 101.00, *et seq*. (2007).

[81] §§ 101.00 *et seq*.

[82] §§ 101.02, 101.06, 101.07.

[83] §§ 101.05, 101.06, 101.07. The SRB has an odd dichotomy of roles with regard to rates for different types of insurance. It is a consumer representative with regard to auto, workers' compensation and some types of health insurance. It is the neutral decision maker for life, property, liability and some other types of health insurance. Mass. Gen. L. ch. 26 § 8E (2014); Mass. Div. of Ins., State Rating Bureau, http://www.mass.gov/ocabr/government/oca-agencies/doi-lp/doi-departments/state-rating-bureau.html (last visited Jan. 13, 2016).

[84] Decision & Order at 34-35, Mass. Prop. Ins. Underwriting Ass'n 2013 Rate Filings, R2013-01 (Mass. Div. of Ins.) (June 5, 2014).

[85] MASS. DIV. OF INS., ANNUAL HOME INS. REPORT FOR CALENDAR YEAR 2014 5 (2015), *available at* http://www.mass.gov/ocabr/docs/doi/consumer/mass-home-insurance-2014.pdf.

- Safety Insurance Group, 4th largest company in the market with a 7.2% market share,[86] received a rate increase of 3.3%, effective December 1, 2014, and a second increase of 9.1%, effective 11 months later, on November 1, 2015, for a total increase of 12.7% in less than a year.

- Plymouth Rock Group, the state's 16th largest insurer with a 2% market share, received rate increases of 7.99% in 2013, 9.1% in 2014, and 7.7% in 2015, for a three-year increase of 27.0%.[87]

DISCUSSION OF FINDINGS

1. DOI has discretion to provide public notice and allow public input, but doesn't use it

The impetus for the Committee's investigation into rate increases for homeowners insurance was the news that very large increases had been approved without any notice to the public, the Legislature or the Attorney General. What the Committee learned was even more surprising -- not only was no notice given, but no one outside the Division has access to any of the information or documents prior to the new rates' effective date. In fact, no one can learn that a rate request has been filed until the effective date. Even when the rates take effect, no notice is given to the public, to customers of the insurers, to consumer advocates such as the Attorney General or to anyone outside of the Division.

Generally, all documents that DOI receives or creates are considered public records, subject to Massachusetts' public records statute, Chapter 66 of the General Laws. However, DOI considers rate filing documents to be subject to a public records exemption, and therefore not public prior to their effective date. It claims two bases for this exemption: the "deliberative process" exemption and the statutory exemption.

However the deliberative process exemption, in the clear language of the public records definition statute, is limited to "inter-agency or intra-agency memoranda or letters relating to policy positions being developed by the agency."[88] It is also limited in time; when deliberations have ended, these memoranda become a part of the public records unless they fall into another of the enumerated exemptions to the public records law.[89]

The statutory exemption, which DOI treats as supplemental to the deliberative process exemption, covers documents that are "specifically or by necessary implication exempted from

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[86] *Id.*
[87] Mass. Div. of Ins., All rate changes in the homeowners insurance market, 2004-2015. (Sept. 29, 2015) (spreadsheet on file with the Committee).
[88] Mass. Gen. L. ch. 4 § 7, twenty-sixth(d) (2014).
[89] Babets v Sec. of Exec. Off. of Health & Human Servs., 403 Mass. 230, 237 (1988) ("By its terms, this exemption protects such documents from disclosure only while policy is "being developed," that is, while the deliberative process is ongoing and incomplete."); Globe News. Co. v Driscoll, 2000 WL 1716253, at *2 (Mass. Super. Nov. 16, 2000) (ordering Commissioner of Education to provide requested MCAS results to the Boston Globe because they were not "inter-agency or intra-agency memoranda" and were "reasonably completed.").

disclosure by statute."[90] The exemption language in the relevant law applies narrowly only to documents specifically named or described.[91] The relevant DOI statute states: "A filing and supporting information shall be open to public inspection after the filing becomes effective."[92] DOI, at its discretion, could opt to make this information available to the public sooner, but to date they have chosen to use this language as the basis for withholding the records while they are under review. For rates that are rejected or withdrawn, DOI chooses not to ever make the documents public.

2. Once it bars other parties from the process, DOI does not do enough on its own to evaluate rate requests

Several aspects of calculating insurers' losses and expenses are not fully shared with DOI. They represent significant actuarial judgments on the part of the insurers that are relevant to the excessiveness or adequacy of the proposed rates. DOI could ask for more details but it chooses not to.

Weather models. Estimating the frequency and severity of hurricane storms, including the likely damage they would cause to Massachusetts housing stock is one such aspect. These models have been routinely analyzed in FAIR Plan rate setting proceedings and were taken up by a special legislative commission addressing the home insurance market. The Attorney General's Office has disputed the use of available hurricane models for not having been proven to "produce accurate and reasonable estimates that are appropriate for use in Massachusetts."[93] We heard from insurance and weather modeling experts that hurricane models used by insurers in Massachusetts are not particular to our state, to regions within the state or to the state's climatological history.[94] This means that homeowners living inland face rates based on hurricane predictions estimated for coastal areas, including Florida, Louisiana and the Caribbean. In contrast, Massachusetts has experienced very few hurricanes in recorded history.

Despite concern that weather models are a factor in the rise of home insurance premiums, DOI has made no effort to analyze the underlying data and assumptions of the models. DOI is too ready to accept the weather model vendors' claims that the models contain proprietary intellectual property requiring protection from competitors.[95]

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[90] Ch. 4 § 7, twenty-sixth(a) (records that are protected from disclosure by statute are not public records).
[91] *See Lafferty v Martha's Vineyard Comm'n*, 2004 WL 792712 (Mass. Super. Apr. 9, 2004), at *6 ("As to records not specifically addressed in [the statute] they must be disclosed . . . .") (holding that correspondence between the Martha's Vineyard Comm'n and state ethics commission that was not specifically related to particular ethics inquiries and advisory opinions was not exempted under statute deeming such inquiries and opinions confidential).
[92] Ch. 174A § 6(a) (2014); ch. 175A § 6(a).
[93] Letter from Glenn Kaplan, Ins. & Fin. Servs. Bureau Chief, Mass. Att'y Gen.'s Office, to Joseph Murphy, Acting Comm'r, Mass. Div. of Ins. (Oct. 30, 2009).
[94] Telephone Interview with Kerry Emanuel, Professor, Mass. Inst. of Tech. (Sept. 11, 2015); Telephone Interview with Burt Feinberg, Mathematician, and Peter Leight, Asst. Att'y Gen., Mass. Att'y Gen.'s Office (Aug. 31, 2015).
[95] SPECIAL COMM'N TO REVIEW THE CURRENT STATE OF THE HOMEOWNERS INS. MKT. IN THE COMMONWEALTH, FINAL REPORT TO THE MEMBERS OF THE MASS. STATE LEGISLATURE 3 (2007).

The AG's Office has written three times to the Division of Insurance, in 2009, 2011 and 2012, to address the impact of insurers' use of these models. In 2009, Glenn Kaplan, Chief of the Insurance and Financial Services Division of the Attorney General's Office, wrote:

> *I write to express our Office's concern with respect to current homeowner insurance premiums in Massachusetts and, in particular, the use of unproven and in some cases discredited hurricane models to justify rates that are vastly higher than necessary to cover Massachusetts losses… One of the principal reasons for the very low loss ratios and corresponding high profitability of homeowners insurance in Massachusetts is the use of modeled hurricane loss provisions in Massachusetts homeowner insurance rates.*[96]

Tellingly, in 2007 and 2013, proposed rate increases for the FAIR Plan were rejected based upon the use of hurricane models DOI itself found insufficiently tailored to Massachusetts. The models used to justify regular homeowners rates have not been shown to be materially different.

Reinsurance. Like hurricane loss modeling, this has been a concern of consumer advocates and the Attorney General's Office in discussions of rate fairness. Reinsurance is purchased to reduce underwriting risk. The insurer files a claim on its reinsurance policy when it has extraordinarily high claims after very severe weather or other covered damage to insured properties.

Insurers purchase reinsurance from dozens of companies, most of which are headquartered outside the United States and are therefore not subject to U.S. or Massachusetts regulation or oversight. Some insurers may even purchase reinsurance from a division of their own company, as is the case with MAPFRE U.S.A.[97] Generally, the cost of reinsurance makes up a significant portion of the insurance premiums charged to consumers. Reducing risk is a crucial part of insurance companies' business model, and reinsurance is a key part of risk management. However, in states where it is under-regulated, reinsurance has become a budget item where companies can beef up their expenses, and then set customers' rates based on the expectation that they will earn a certain percentage of those expenses back as profits.[98]

Lack of access to key information makes it difficult for regulators to analyze the appropriateness of the cost of reinsurance. A compounding factor is that the price of reinsurance for insurers is also based on hurricane loss models. Consumer advocates and concerned parties fear that insurers are overcharging consumers on the basis of costs for inflated reinsurance coverage.

Mr. Kaplan, in his 2011 letter, estimated that the use of "untested and discredited hurricane models" and "inflated reinsurance provisions" resulted in consumers being overcharged for homeowners insurance by at least a half billion dollars for the period 2004 to 2010. He requested that the State Rating Bureau initiate administrative rate proceedings to review voluntary market rate requests that were on file at that time, with a specific focus on hurricane

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[96] Letter from Glenn Kaplan, Ins. & Fin. Servs. Bureau Chief, Mass. Att'y Gen.'s Office, to Joseph Murphy, Acting Comm'r, Mass. Div. of Ins. (Oct. 30, 2009).

[97] Letter from Daniel P. Olohan, Exec. Vice Pres., Gen. Counsel & Sec'y, MAPFRE U.S.A, to Rosalie Fazio-Eynullayeva, Counsel, Mass. Sen. Post Audit & Oversight Comm. (Sept. 8, 2015) (responding to Committee's request for information) (on file with the Committee).

[98] Decision & Order at 29-34, Mass. Prop. Ins. Underwriting Ass'n 2013 Rate Filings, R2013-01 (Mass. Div. of Ins.) (June 5, 2014) (ruling that inconsistency in the choice of weather models used by reinsurers led to a conclusion that reinsurer profits could not be justified).

models and reinsurance provisions.[99] In response, the Division agreed to hold proceedings related to hurricane and other catastrophe modeling in 2012. [100] The AG's office responded, offering to lend its expertise to assist DOI in putting together a comprehensive review of hurricane models, and reiterating its concerns.[101] However, to date DOI has not held any such proceedings.

Policy cancellations and nonrenewals. Risk held by a homeowners insurance company can also be mitigated by cancelling policies or failing to renew policies of individuals who have filed several claims within a period of time or whose homes are located in areas with higher incidences of damage. Cancellation of a homeowners policy, when either the insurer or the homeowner breaks the policy before the end of its term, is permissible in certain circumstances. [102] Insurers are always free to non-renew a policy. DOI collects cancellation and nonrenewal data from the companies that make up the top 25 in market share in designated urban and coastal zip codes. This data is reported in the agency's annual report on home insurance. However, no data is collected for other regions, and DOI does not appear to consider cancellations or nonrenewals in reviewing loss estimates that underlie rate requests.

3. Once rates are set, DOI lags other regulators in arming consumers with information

Consumers in Massachusetts are in some ways set up for success by the insurance market here. Buyers can choose from 68 carriers, as of the most recent information available from DOI. The aggregate market share of the ten largest companies is not big enough to stifle competition from smaller businesses.

Yet consumers find it difficult to compare offerings on cost, quality and convenience.[103] They are up against an advanced case of information asymmetry. Sellers know a lot about a complex product, while buyers know very little. Consumers can work with independent brokers who may make things less complicated. But brokers don't do business with all 68 homeowners carriers; most only deal with a dozen or fewer.

Homeowners need more -- much more -- information about the different premiums charged by each of the insurers from which they can choose. DOI does not provide consumers with any resources to compare premiums and coverage available from insurers. Insurers are not required to make basic pricing information available in a way that would help differentiate among their options. Even for shoppers who seek competitive quotes -- a time-consuming task that requires providing a great deal of personal information to brokers -- it can be very hard to compare these

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[99] Letter from Glenn Kaplan, Ins. & Fin. Servs. Bureau Chief, Mass. Att'y Gen.'s Office, to Kevin Beagan, State Rating Bureau Dir., Mass. Div. of Ins. (Nov. 17, 2011) (on file with the Committee).
[100] Letter from Kevin Beagan, State Rating Bureau Dir., Mass. Div. of Ins., to Glenn Kaplan, Ins. & Fin. Servs. Bureau Chief, Mass. Att'y Gen.'s Office (June 14, 2012) (on file with the Committee).
[101] Letter from Glenn Kaplan, Ins. & Fin. Servs. Bureau Chief, Mass. Att'y Gen.'s Office, to Kevin Beagan, State Rating Bureau Dir., Mass. Div. of Ins. (Feb. 29, 2012) (on file with the Committee).
[102] Mass. Gen. L. ch. 175 § 99 (2014).
[103] *E.g.*, *Informational Hearings on the Mass. Voluntary Market for Homeowners' Ins.*, Mass. Div. of Ins. (Oct. 21, 2015; Dec. 2, 2015) (statements of Chris Bartlett, Lowell resident and Martha Muldoon, New Bedford resident).

complex offerings. Effective competition requires that we solve this information asymmetry by arming consumers with tools to understand their choices.

Massachusetts consumers ought to have an online tool to research homeowners insurance offerings. As mentioned, regulatory and consumer protection agencies in states like Colorado,[104] Florida[105] and Delaware[106] have set up comparison engines that show rates and coverage. Massachusetts, in contrast, makes little use of government websites to explain options.[107] There are no other places to get a comprehensive picture.

4. Beset by weak DOI regulation and poor consumer information, local homeowners face rising premiums

As of the Committee's hearing, there were 68 home insurance providers in Massachusetts.[108] The top 10 insurers sell 66% of all home insurance in the state, based on total premiums collected.[109] According to NAIC's 2014 Homeowners Competition Report, nine firms left the market and 13 entered the market in the previous five years.[110]

Despite these characteristics, which are sometimes indicative of a market competitive on coverage and prices, Massachusetts premiums are rising rapidly. Between 2007 to 2013,[111] the average premium increased 21.6%.[112] This rate of growth outpaced regional inflation by almost

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[104] Colo. Div. of Ins., A Shopping Tool for Homeowners Ins., https://drive.google.com/file/d/0BwguXutc4vbpTEppYW9LZzJDZGM/view?pli=1 (last visited Jan. 13, 2016).
[105] Fla. Office of Ins. Regulation, CHOICES: Homeowners Rate Comparison Tool, https://choices.fldfs.com/pandc/homeowners?_ga=1.28251772.1534060163.1442437314 (last visited Jan. 13, 2016).
[106] Del. Dep't of Ins., Home Ins. Rate Comparison, http://compare.delawareinsurance.gov/Consumer/InsuranceTypeSelection.aspx (last visited Jan. 13, 2016).
[107] Mass. Div. of Ins., Home Ins., http://www.mass.gov/ocabr/insurance/home-insurance (last visited Feb. 11, 2016).
[108] *Hearing before the Mass. Sen. Post Audit & Oversight Comm.*, 189th Gen. Ct. (Sept. 22, 2015) (written statement of Daniel Judson, Comm'r of Ins., Mass. Div. of Ins., at 14).
[109] MASS. DIV. OF INS., ANNUAL HOME INS. REPORT FOR CALENDAR YEAR 2014 5 (2015), *available at* http://www.mass.gov/ocabr/docs/doi/consumer/mass-home-insurance-2014.pdf.
[110] NAT'L ASS'N OF INS. COMM'RS, 2014 COMPETITION DATABASE REPORT 32 (2015), *available at* http://www.naic.org/documents/prod_serv_statistical_clr_ops.pdf.
[111] The time period of 2007 to 2013 is the most recent available for all data in this paragraph and in the following chart titled "Rates of Change in the Home Ins., Housing and Construction Industries."
[112] MASS. DIV. OF INS., ANNUAL HOME INS. REPORT FOR CALENDAR YEAR 2007 (2008) (on file with the Committee); MASS. DIV. OF INS., ANNUAL HOME INS. REPORT FOR CALENDAR YEAR 2008 (2009) (on file with the Committee); MASS. DIV. OF INS., ANNUAL HOME INS. REPORT FOR CALENDAR YEAR 2009 (2010), *available at* http://www.mass.gov/ocabr/docs/doi/consumer/mass-home-insurance-2009.pdf; MASS. DIV. OF INS., ANNUAL HOME INS. REPORT FOR CALENDAR YEAR 2010 (2011), *available at* http://www.mass.gov/ocabr/docs/doi/consumer/mass-home-insurance-2010.pdf; MASS. DIV. OF INS., ANNUAL HOME INS. REPORT FOR CALENDAR YEAR 2011 (2012), *available at* http://www.mass.gov/ocabr/docs/doi/consumer/mass-home-insurance-2011.pdf; MASS. DIV. OF INS., ANNUAL HOME INS. REPORT FOR CALENDAR YEAR 2012 (2013), *available at* http://www.mass.gov/ocabr/docs/doi/consumer/mass-home-insurance-2012.pdf; MASS. DIV. OF INS., ANNUAL HOME INS. REPORT FOR CALENDAR YEAR 2013 (2014), *available at* http://www.mass.gov/ocabr/docs/doi/consumer/mass-home-insurance-2013.pdf.

9 percentage points.[113] Over the same time, the median income of the state's households fell by close to 5%[114] and average home values in the state, a factor used by insurers to set rates, dropped 11%.[115] In comparison, the growth in average premiums paid by homeowners under the FAIR Plan was 6.7%[116] and the average cost of auto insurance rose by 2.8%.[117] Consumers are not doing well, while insurers are doing very well.

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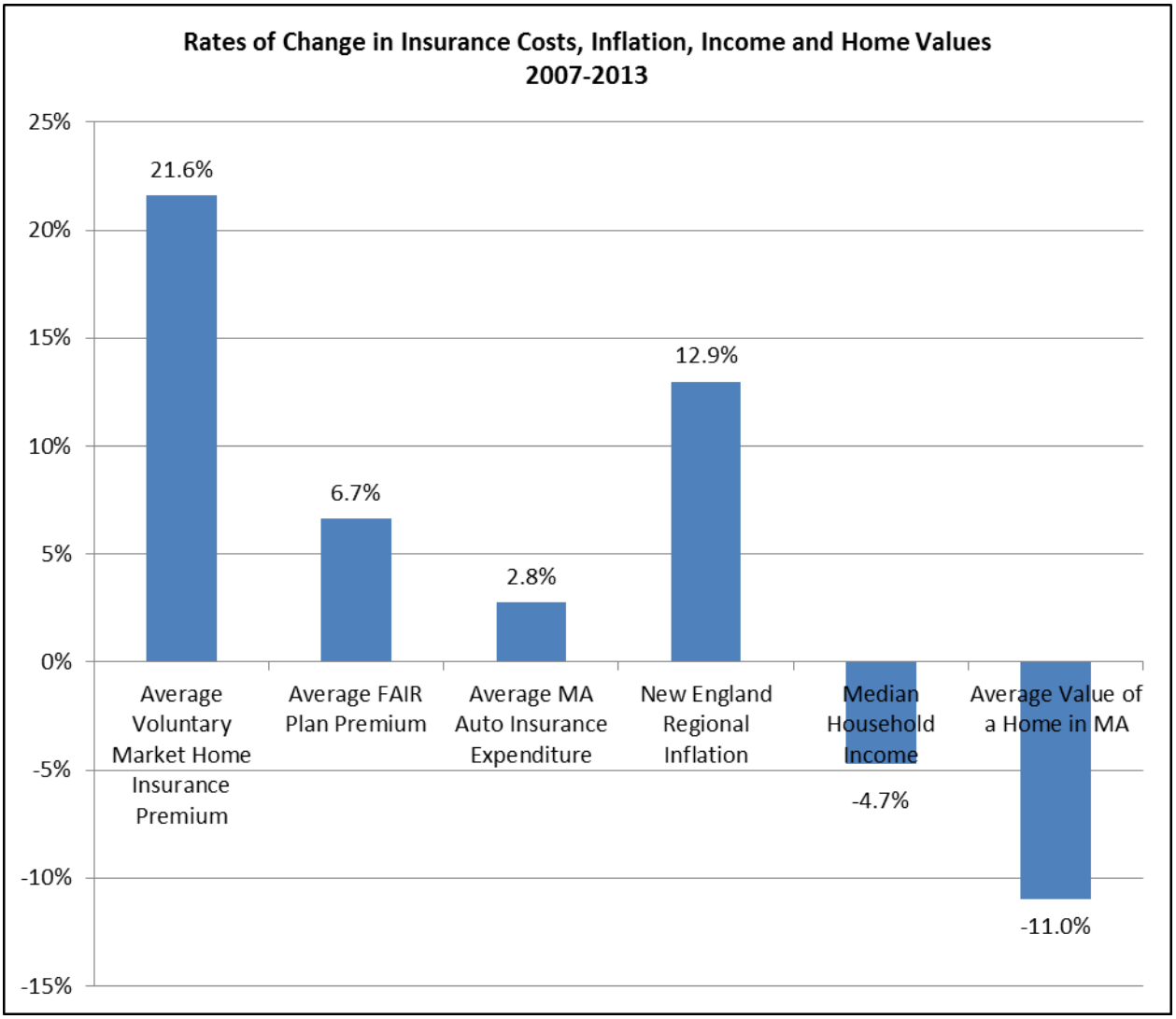
[113] Bureau of Labor Statistics, http://www.bls.gov/regions/new-england/data/consumerpriceindex_northeast_table_pdf.pdf (last visited Mar. 3, 2016).

[114] Dep't of Numbers, Massachusetts Family Income, http://www.deptofnumbers.com/income/massachusetts/#family (last visited Feb. 5, 2016).

[115] LINCOLN INST. OF LAND POLICY, LAND PRICES BY STATE, https://www.lincolninst.edu/subcenters/land-values/data/landdata-states-2015q1.xls (last visited Feb. 5, 2016).

[116] MASS. DIV. OF INS., ANNUAL HOME INS. REPORT FOR CALENDAR YEAR 2007 (2008) (on file with the Committee); MASS. DIV. OF INS., ANNUAL HOME INS. REPORT FOR CALENDAR YEAR 2008 (2009) (on file with the Committee); MASS. DIV. OF INS., ANNUAL HOME INS. REPORT FOR CALENDAR YEAR 2009 (2010), *available at* http://www.mass.gov/ocabr/docs/doi/consumer/mass-home-insurance-2009.pdf; MASS. DIV. OF INS., ANNUAL HOME INS. REPORT FOR CALENDAR YEAR 2010 (2011), *available at* http://www.mass.gov/ocabr/docs/doi/consumer/mass-home-insurance-2010.pdf; MASS. DIV. OF INS., ANNUAL HOME INS. REPORT FOR CALENDAR YEAR 2011 (2012), *available at* http://www.mass.gov/ocabr/docs/doi/consumer/mass-home-insurance-2011.pdf; MASS. DIV. OF INS., ANNUAL HOME INS. REPORT FOR CALENDAR YEAR 2012 (2013), *available at* http://www.mass.gov/ocabr/docs/doi/consumer/mass-home-insurance-2012.pdf; MASS. DIV. OF INS., ANNUAL HOME INS. REPORT FOR CALENDAR YEAR 2013 (2014), *available at* http://www.mass.gov/ocabr/docs/doi/consumer/mass-home-insurance-2013.pdf.

[117] Ins. Info. Inst., Average Expenditures for Auto Ins. by State, http://www.iii.org/table-archive/21247 (last visited Feb. 5, 2016).



Profitability is an indication of an industry's health. Regarding insurance, a healthy market means that companies are able to remain solvent and importantly, continue to offer this essential product to consumers. However, according to home insurance experts, high profitability suggests that rates are not actuarially fair to consumers.[118] Key indicators of profitability, as identified by the NAIC, are underwriting profit, return on net worth and loss ratio. By each of these metrics, home insurers in Massachusetts are thriving.

For the 10-year period of 2004-13, the average underwriting profit[119] for Massachusetts home insurers was 13 times greater than the national average -- 16.9% in Massachusetts versus 1.3% nationally.[120]

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[118] Telephone Interview with Patricia A. McCoy, Professor, Boston College Law Sch. (Jan. 27, 2016); Telephone Interview with Stephen D'Amato, former Chief, State Rating Bureau, Mass. Div. of Ins. (Jan. 28, 2016); E-mail from John Aloysius Cogan, Jr., Assoc. Professor, Univ. of Conn. Law Sch., to Rosalie Fazio-Eynullayeva, Counsel, Mass. Sen. Post Audit & Oversight Comm. (Feb. 1, 2016, 16:01 EST) (on file with the Committee).

[119] Underwriting profit is an insurer's premiums earned minus its losses and expenses.

[120] NAT'L ASS'N OF INS. COMM'RS, REPORT ON PROFITABILITY BY LINE BY STATE IN 2013 150, 238 (2014), *available at* http://www.naic.org/prod_serv/PBL-PB-14.pdf.

Over that same period, Massachusetts home insurers earned an average of 17.6% annual return on net worth -- the 11th highest out of the 50 U.S. states and the District of Columbia.[121] Home insurers nationwide had an average annual return on net worth of 6.6%,[122] while the long-term average return on net worth for the property/casualty insurance sector, which includes homeowners insurance, is 9%.[123] Of note, Safety Insurance Group and Plymouth Rock Group each based their rates on a 15% return on net worth, while MAPFRE U.S.A. used a weighted return on net worth of 12.2%.[124]

Another indicator of insurer profitability is loss ratio, the percent of premiums received paid out for claims. A lower loss ratio indicates a higher profit, since the insurer retains a larger amount of premiums. In nine out of the 10 most recent years for which data is available, Massachusetts home insurers had a loss ratio lower than the national average.[125] Massachusetts had the 4th lowest loss ratio -- meaning the 4th highest profit, by this measure -- over these 10 years, of the 50 U.S. states and the District of Columbia.

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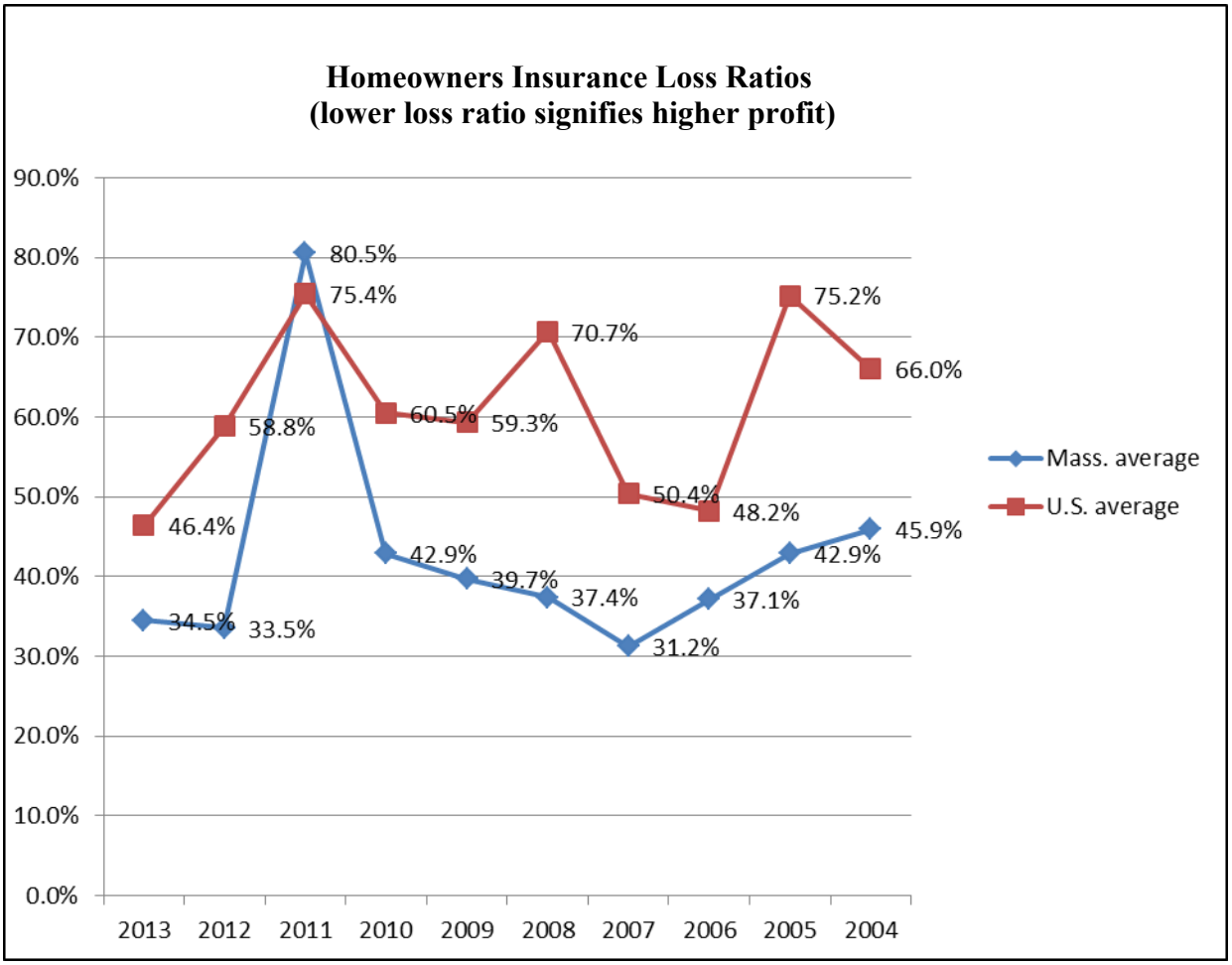
[121] NAT'L ASS'N OF INS. COMM'RS, REPORT ON PROFITABILITY BY LINE BY STATE IN 2013 240 (2014), *available at* http://www.naic.org/prod_serv/PBL-PB-14.pdf Return on net worth is a profitability indicator that measures the portion of a company's profits that is reinvested or returned to shareholders, expressed as a percent of annual premiums received.

[122] NAT'L ASS'N OF INS. COMM'RS, REPORT ON PROFITABILITY BY LINE BY STATE IN 2013 152 (2014) *available at* http://www.naic.org/prod_serv/PBL-PB-14.pdf.

[123] FEDERAL INS. OFFICE, U.S. DEP'T OF TREASURY, ANNUAL REPORT ON THE INS. INDUSTRY (September 2014), *available at* https://www.treasury.gov/initiatives/fio/reports-and-notices/Documents/2014_Annual_Report.pdf.

[124] Safety Ins. Co., Rate Filing SFTY-12989109, Mass. Div. of Ins., Mar. 23, 2015,. Exhibit 8, Sheet 1 (Defining Target Net Income for Profit Model); MAPFRE U.S.A., Rate Filing CMRC-129987068, Apr. 20, 2015, Appendix A (IRR Profit Model - Homeowners); Bunker Hill Ins. Co., Rate Filing PRAC-130020577, Apr. 18, 2015, Exhibit VI (Calculation of Underwriting Profit) (all filings on file with the Committee).

[125] NAT'L ASS'N OF INS. COMM'RS, REPORT ON PROFITABILITY BY LINE BY STATE IN 2013 149, 237 (2014), *available at* http://www.naic.org/prod_serv/PBL-PB-14.pdf.



126, 127

Within Massachusetts, homeowners insurance also had lower loss ratios relative to other lines of insurance. Home insurers had a statewide average loss ratio of 34.5% in 2013, while Massachusetts auto insurers had a loss ratio of 62.4%.[128] Health insurers are now required by Massachusetts law to have loss ratios of 88% or more.[129]

On November 30, 2015, the Attorney General wrote the Senate Post Audit and Oversight Committee that the rate increases granted by DOI to MAPFRE and Safety Insurance, two of the four largest property insurers in Massachusetts, "are of serious concern to the Attorney General's Office."[130] Insurance specialists for Attorney General Maura Healey, afforded access to documents after rates took effect, found that industry profit estimates were "arbitrary and not

[126] *Id.*

[127] A 2011 tornado in western Massachusetts accounts for the sharp spike in losses in 2011.

[128] NAT'L ASS'N OF INS. COMM'RS, REPORT ON PROFITABILITY BY LINE BY STATE IN 2013 62 (2014), *available at*http://www.naic.org/prod_serv/PBL-PB-14.pdf.

[129] Mass. Gen. L. ch. 176J § 6(e) (2014) (requiring loss ratio for health insurers to be 90% in 2013, 89% in 2014, and 88% thereafter).

[130] Letter from Glenn Kaplan, Ins. & Fin. Servs. Bureau Chief, Mass. Att'y Gen.'s Office to Sen. Michael J. Barrett, Chair, Mass. Sen. Comm. on Post Audit & Oversight (Nov. 30, 2015) (on file with the Committee and appended to this report).

supported by sufficient data."[131] They determined as well that estimated catastrophe losses -- those related to a specific weather event that generates a large number of claims totaling a large dollar amount -- were calculated using a "biased" approach designed to "increase their revenues."[132] The bottom line: they concluded that the rates are unlawfully "excessive."[133]

High profits accompanied by significant increases in premiums call into question the capacity of market competition to keep prices reasonably low. Insurance is a regulated industry for precisely this reason. The rate filing review process is designed to provide a layer of protection for consumers.

RECOMMENDATIONS

1. DOI should use its existing authority to open up the process
2. The General Court should require transparency at DOI
3. The General Court should authorize the AG to order a limited number of homeowners hearings on her own initiative
4. DOI should issue regulations to govern both rates requests and hearing requests
5. DOI should push harder on weather models, reinsurance cost estimates, and policy cancellations and nonrenewals
6. Either DOI or the General Court should compel insurers to notify people about new rates
7. DOI should create an online premium comparison tool for homeowners insurance

[131] *Id.*
[132] *Id.*
[133] *Id.*

Appendices

I. Bibliography of Additional Sources Consulted
II. Experts and Advocates Interviewed by Committee Staff
III. Testifiers at Sept. 22, 2015 Committee Hearing
IV. Written Testimony Received at Sept. 22, 2015 Hearing
V. Nov. 30, 2015 Letter from the Attorney General's Office to the Committee

Appendix I: Bibliography of Additional Sources Consulted

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Liberty Mutual Insurance Co., Rate Filing LBPM-130378529, Mass. Division of Insurance, Dec. 23, 2015.

Appendix II: Experts and Advocates Interviewed by Committee Staff

Paula Aschettino, President and Founder, Citizens for Homeowners Insurance Reform
Birny Birnbaum, Executive Director, Center for Economic Justice
Monica Brookman, Assistant Attorney General, Mass. Attorney General's Office
Nonnie Burns, Former Commissioner of Insurance, Mass. Division of Insurance
John Aloysius Cogan, Jr., Associate Professor of Insurance Law, University of Connecticut Law School
Jack Connolly, President and Owner, Wedgwood-Crane & Connolly Insurance Agency
Stephen D'Amato, Former Chief of State Rating Bureau, Mass. Division of Insurance, Former Executive Director of Center for Insurance Research
William A. Delaney, Delaney Legislative Services
Kerry Emanuel, Professor of Atmospheric Science, Mass. Institute of Technology
Burt Feinberg, Mathematician, Mass. Attorney General's Office
Daniel J. Foley, Jr., Vice President of Government Affairs and General Counsel, Mass. Association of Insurance Agents
Glenn Kaplan, Chief, Insurance and Financial Services Division, Mass. Attorney General's Office
Peter Leight, Assistant Attorney General, Mass. Attorney General's Office
Francis A. Mancini, President and CEO, Mass. Association of Insurance Agents
Patricia A. McCoy, Professor of Insurance Law, Boston College Law School
John P. Murphy, Executive Director, Massachusetts Insurance Federation
Peter Robertson, General Counsel, Massachusetts Insurance Federation
Herb Wilkins, Chief Justice Emeritus, Mass. Supreme Judicial Court
Alex Winslow, Executive Director, Texas Watch

Appendix III: Testifiers at Sept. 22, 2015 Committee Hearing

Invited Testifiers:
Massachusetts Division of Insurance
- Daniel Judson, Commissioner
- Gary Anderson, First Deputy Commissioner
- Kevin Beagan, Deputy Commissioner
- Cara Blank, Property Casualty Actuary, State Rating Bureau

Massachusetts Attorney General's Office
- Glenn Kaplan, Insurance and Financial Services Division Chief
- Peter Leight, Assistant Attorney General

Mapfre U.S.A.
- Matthew Wilcox, Senior Vice President and Chief Technical Officer

Safety Insurance Co.
- James Berry, Vice President of Underwriting
- Elizabeth Brodeur, Director of Legal and Regulatory Compliance

Bunker Hill Insurance
- Curt Troutman, Vice President

Stephen D'Amato, Former Director, State Rating Bureau, Massachusetts Division of Insurance and Former Executive Director, Center for Insurance Research
Paula Aschettino, President and Founder of Citizens for Homeowners Insurance Reform
Massachusetts Insurance Federation
- John Murphy, Executive Director

Senator Daniel J. Wolf, Cape and Islands District
Representative James M. Cantwell, 4th Plymouth District

Other Testifiers:
Sherman "Whip" Saltmarsh, President, Saltmarsh Insurance, Former State Representative
Jane Logan, CPCU, Insurance Broker and Consumer Advocate

Appendix IV: Written Testimony Received at Sept. 22, 2015 Committee Hearing

1. Massachusetts Division of Insurance
2. Paula Aschettino
3. Joint Statement by Massachusetts Insurance Federation, American Insurance Association, National Association of Mutual Insurance Companies, and Property Casualty Insurers Association of America
4. Sherman “Whip” Saltmarsh

Massachusetts Division of Insurance

Senate Post Audit Committee

Hearing on Homeowner Insurance

Senator Michael J. Barrett, Chair

Massachusetts State House, Room 428

September 22, 2015

Testimony presented by the Massachusetts Division of Insurance

Daniel R. Judson, Commissioner

Gary Anderson, First Deputy Commissioner

Kevin Beagan, Deputy Commissioner, Health Care Access Bureau

Cara Blank, Property Casualty Actuary, State Rating Bureau

INTRODUCTION:

I appreciate the opportunity to appear before you today. As Commissioner of Insurance, I have the responsibility to regulate the Massachusetts insurance markets in a way that balances the need to maintain and enforce consumer protections with the need for stable markets with readily available coverage. The Insurance Commissioner's challenge is to maintain a market that encourages insurers to develop and offer innovative products that are responsive to consumer needs and preferences while ensuring that the coverage is appropriate and the premiums are reasonable in relation to the insurance risk that is assumed.

One of the functions of the Division of Insurance ("Division") is the review of insurer rate filings to ensure that insurance premiums are not based on unlawful factors, comply with statutory rate standards, and that the underlying rates are reasonable based on an insurer's projected costs.

The Division is pleased to provide the following background, information and data to the Senate Post Audit Committee of the General Court of Massachusetts regarding the homeowners insurance market. This statement addresses the following issues:

- Statutory rate standards and review procedures applicable to property insurance rate filings.
- Availability of homeowners insurance in Massachusetts.
- Affordability of homeowners insurance in Massachusetts.

STATUTORY RATE STANDARDS & REVIEW PROCEDURES FOR PROPERTY INSURANCE RATES

Rate Standards

The statutory rate standards that apply to all property insurance policies require the Division to consider the following cost items in its determination as to whether or not the rates to be charged are excessive, inadequate, or unfairly discriminatory[1]:

[1] M.G.L. c. 174A and M.G.L. c. 175, § 99

- Past and prospective loss experience, within and outside this Commonwealth, over a period of not less than the most recent five-year period for which such experience is available;
- Conflagration and catastrophe hazards, including catastrophe reinsurance and factors relating thereto;
- A reasonable margin for profit and contingencies;
- Dividends, savings or unabsorbed premium deposits allowed or returned by insurers to their policyholders, members, or subscribers;
- Past or prospective expenses, both countrywide and those specific to this state.

Rate filings must also include support, such as the experience or judgment of the insurer, the experience of other insurers or rating organizations, and any other credible information or factors within and outside the Commonwealth[2].

Because of its unique organizational structure, homeowner insurance rate filings submitted by the Massachusetts Property Insurance Underwriting Association ("MPIUA") are subject to additional statutory rate standards that provide additional consumer protection. The MPIUA is not a stand-alone insurance company that is separate and distinct from insurance companies that provide homeowners insurance in the voluntary market. The MPIUA is an insurer of last resort for individuals who are unable to obtain insurance from individual insurance companies through customary sales channels. Massachusetts law[3] requires all licensed Massachusetts property insurers to be members of the MPIUA. The voluntary market insurers are collectively responsible for all expenses and liabilities of the MPIUA, so that homeowners who ultimately obtain coverage from the MPIUA are being underwritten by the industry as a whole rather than by a single insurer.

The MPIUA originated as the Urban Area Insurance Placement Facility authorized under M.G.L. c. 175C which was enacted under Chapter 731 of the Acts of 1968. Through various amendments that have been made to this statute since 1968, the

[2] M.G.L. 174A, § 6.
[3] M.G.L. c. 175C, § 4.

additional statutory rate standards for the MPIUA constrain MPIUA's rates to a level that reasonably approximates rates otherwise in effect in the voluntary market. The statutory method for making such approximations is based on the MPIUA's share of the total homeowner insurance market at a local level. Specifically,

- M.G.L. c. 175C, § 5 requires the Commissioner to consider the experience of the association, the loss experience of insurers in the voluntary market, and the intent of this chapter to make basic property insurance available at a reasonable cost to eligible applicants in large share territories.

- M.G.L. c. 175C, §1 defines a territory as one of the statistical territories approved by the Commissioner[4]. There are currently 27 statistical territories in Massachusetts.

- M.G.L. c. 175C, §1 further defines a large share territory as one in which the three year written premiums of the MPIUA constitute 7% or more of the total premiums written in that territory during that period, subject to various constraints stated in the law. The number of large share territories is limited to a maximum of 13[5].

Rate Review Process

The Division's review of property insurance rate filings submitted by individual insurers is governed by time frames established in M.G.L. c. 174A, §6. Insurers are required to submit rate filings to the Division at least 15 days prior to the effective date of those rates. The Division may extend the review period for an additional 30 days to allow for additional review of the filing. In practice, the Division has been targeting a 60 day review period since 2007.

All rate filings are submitted electronically to the Division through a network administered and maintained by the National Association of Insurance Commissioners. This system provides a proprietary "email system" that allows the Division to communicate with each filing company. In accordance with the

[4] Statistical territories are the territories designated in the statistical plan by the commissioner under the provisions of M.G.L. c. 174A, §12. All insurers must submit data annually according to the provisions of the statistical plan promulgated by the commissioner.
[5] Based on the MPIUA's April 12, 2013 rate filing, the MPIUA has 11 large share territories. The large share territories are portions of Suffolk County, Lawrence, New Bedford, Barnstable, Dukes, Nantucket, Lynn, Fall River, Brockton, Lowell, and portions of Plymouth County.

requirements of M.G.L. c. 174A, §6, the filing, all supporting information, and any correspondence is available for public inspection once the Division's review has been completed.

For reasons of transparency and consistency, it has been the long-standing philosophy of the Division to treat all filings the same way. Over the past eighteen months, the regulatory review process for homeowner insurance rate filings has become more formalized to ensure this kind of consistency. The recently developed procedures were brought about in part because of the addition of staff with a broad range of experience levels, and partly because an insurer's volume of business may limit the level of statistical detail that can be expected to accompany a rate filing.

At present, 47 of the 68 insurer groups that actively write homeowner insurance in Massachusetts have a market share of 1% or less. 1% market share is the equivalent of approximately $20 million in annual premium. Due to the low volume of business, application of traditional actuarial procedures to smaller companies often generates results that are of limited statistical credibility. Many of these filings are supported on the basis of competitor actions or broader segments of industry experience.

For example, an insurer that recently entered the Massachusetts homeowners market, and is now the sixth largest homeowner insurer on the Cape & Islands, still writes less than 1% of the market in total. In addition to relying on competitor rates for its initial entry, this insurer clearly had to rely on the results of hurricane models since it had no previous history in Massachusetts when it entered. Even today, its history in the Commonwealth is still too brief to assign any credibility to its past "catastrophe losses", if any, when determining future rates.

In general, the larger the volume of business written by an insurer, the more statistical detail the Division expects a rate filing to contain in support of a rate change. Detailed data on historic "catastrophe" losses, trends in average claims occurrence rates and claim costs, and prior non-catastrophic loss experience at the territorial level can be reasonably expected in rate filings submitted by larger homeowners insurance groups.

While Massachusetts laws provide guidance on the types of costs that can be incorporated into property insurance rates, neither the law nor the Division prescribe specific ratemaking methods for estimating a future rate. When an

insurer requests a significant rate adjustment, the Division requires the insurer to provide an estimate of its average rate "need" and an estimate of the overall rate change that it is actually proposing. In competitive insurance markets, the proposed rate change is often lower than the insurer's estimate of its rate need.

An insurer's estimate of its future rate "need" is based on a series of subordinate estimates such as the expected change in the cost of services that insurance pays for, the cost of delivering the insurance service itself, and the returns expected for that effort. The Division of Insurance currently employs three credentialed actuaries[6] who evaluate each property/casualty rate filing on its merits, and ensure that the actuarial techniques that are used to make the underlying projections are based on assumptions that fit the circumstances of the filing insurer.

From a regulatory and consumer protection perspective, the most important determination as to whether an insurer's rate filing is adequately supported is based on whether the Division's estimate of the rate need reasonably approximates an insurer's rate request using consistent and documented actuarial procedures that take into account the unique circumstances of each insurer, and the regulatory[7] profit and contingency loads that are applied uniformly to all homeowners filings submitted by insurers.

M.G.L. c. 174A, §§7(a) & 7(c), permit the Commissioner to call for a hearing at any time before or after an individual insurer's rate filing takes effect. From 1991 to present, no such hearing has been called in connection with a homeowner insurance rate filing. There are two primary reasons for this:

- The homeowner insurance market is competitive. Since the Insurance Services Office stopped publishing rates based on industry loss and expense experience in 1991[8], most homeowner insurers base their rates, at least in part, on their own loss experience, and entirely on the basis of their own expenses. The level of competition in the homeowner insurance market has been further bolstered by the 2008 introduction of

[6] For the purpose of reviewing property and casualty insurance rate filings, the Division employs two Associates and one Fellow of the Casualty Actuarial Society (www.casact.org). These actuaries are subject to a Professional Code of Conduct dictated by the American Academy of Actuaries (www.actuary.org), and ongoing continuing education requirements.

[7] The Division applies a fixed regulatory profit and contingency loading in its evaluation of all rate filings submitted under M.G.L. c. 174A. The benefits of a single regulatory standard in competitive markets are that it helps ensure a level playing field across the industry, and at the same time ensure that rates are reasonable for consumers.

[8] See Division of Insurance Bulletin 90-05.

competitive rate regulation in the private passenger auto insurance market[9].

- Communications between the Division and the insurance industry are far more convenient and direct than they were in 1947 when M.G.L. c. 174A was first enacted. Rate filings that concern the Division are first discussed directly with the insurer, and, to date, resolution of the Division's concerns has been achieved without the need to call a hearing.

The review process for MPIUA homeowner insurance rate filings is different. This is because individual insurer underwriting guidelines are a primary influence on the number of policies ultimately issued through the MPIUA, and the fact that the voluntary homeowner insurance market proportionately shares all financial losses or profits associated with the insurance provided by the MPIUA as if they were their own. To deter any sort of monopolistic behavior on the part of the industry, M.G.L. c. 175C requires the Commissioner to hold a hearing on MPIUA rate filings, and prevents any changes in those rates until they are formally approved by the Commissioner.

M.G.L. c. 175C further requires the Commissioner to disapprove any rate change in a large share territory that exceeds the average of the statewide average rate changes taken by the ten largest homeowner insurers[10] in the year prior to the date the MPIUA proposes revising its rates. For example, when the MPIUA filed[11] to increase rates for single family homes effective July 1, 2013, the statute would have limited any change in large share territory rates to 6.0% which was the average of the overall average rate changes of the 10 largest homeowner insurers during calendar year 2012.

In territories where the MPIUA is not large, M.G.L. c. 175C permits the Commissioner to disapprove any proposed rate that is higher than the 90th percentile of the rates charged by the 10 largest homeowner insurers in those territories during the prior calendar year.

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[9] 5 of the 15 insurers that have entered the private passenger automobile insurance market since 2008 were established homeowner insurers prior to that time.

[10] Appendix 1 documents the average rate changes for each insurer group that was one of the top ten homeowner insurers in Massachusetts in any year between 2005 and 2014.

[11] The MPIUA's most recent homeowner insurance rate filing was submitted on April 12, 2013. This filing was disapproved in its entirety by the commissioner of insurance on June 5, 2014.

Chapter 436 of the Acts of 2004 amended M.G.L. c. 175C, §5 to permit the MPIUA to recognize the expected costs of hurricane losses and reinsurance costs in its rates without limitation by the statutory caps imposed on each territory. The MPIUA submitted a filing on September 9, 2005 seeking a 12.5% increase to its rates. After a lengthy hearing[12], the Commissioner of insurance approved a rate increase of 12.4% to take effect on October 1, 2006[13]. The Commissioner of insurance has not approved a rate increase for the MPIUA since that time.

AVAILABILITY OF HOMEOWNERS INSURANCE IN MASSACHUSETTS

Factors Affecting Insurer Participation in Property Insurance Markets

Massachusetts law[14] permits recognition of the potential losses associated with significant weather events in homeowner insurance premiums, such as the snow storms we experienced this past February or hurricane Irene in 2011.

It is a well accepted principle in insurance that, absent any major weather events in a given year, the premiums collected on policies issued during that year should be sufficient to cover all insurance claims that can be expected to arise, the expenses incurred by the insurer, and yield a reasonable profit. In years when major damages result from weather, insurers expect to cover a portion of those claims from accumulated capital or surplus. In this regard, the amount of capital and surplus that an insurer has on hand often dictates the type and amount of risk the insurer can write without a high risk of financial impairment or insolvency.

An important estimate that is used to guide such decisions with respect to property insurance is the value of the probable maximum loss that may result from any single weather event. Probable maximum loss is not the largest possible loss that can occur, but it is one that can be reasonably expected from time to time. A homeowner insurer's estimate of its probable maximum loss, together with the estimated likelihood that such a loss will occur, is used to determine how much capital or surplus the insurer needs to have on hand if it is to continue to write property insurance in the following year. Depending on the results of this risk

[12] Regulation 211 CMR 101 was promulgated by the Division of Insurance following the first rate hearing of the MPIUA that commenced on September 5, 2005 in order to provide for a more expedited process.
[13] The rates effective October 1, 2006 reflected an average hurricane loss load that was based on the average produced by the AIR and RMS hurricane models, along with the net cost of reinsurance purchased by the MPIUA.
[14] M.G.L. c. 174A and M.G.L. c. 175C.

management exercise, an insurer may make one or more of the following decisions:

1. Increase or decrease the number of property insurance policies that the insurer will issue in the coming year.

2. Adjust its prices to manage the risk to surplus to a financially responsible level.

Since an insurer's capital and surplus is available to pay for claims from any type of insurance policy in any area of the country, its estimate of probable maximum loss to property from any single weather event is not confined to damages that result to Massachusetts properties. The snowstorms of February provide a good illustration of this. The chart below displays estimates of the total homeowners losses associated with two of the winter storms that occurred in February that affected Massachusetts and the insured losses in all states and all lines of insurance.

Insured Losses Associated with Winter Storms in 2015

Event Dates	All States/All Lines	Massachusetts/Homeowner Only
February 14 -15	$466,200,000	$150,500,000
February 16 - 22	$2,060,000,000	$386,300,000

Source: Property Claims Services

Since no insurer is able to predict exactly when a major weather event is going to occur, property insurance premiums reflect an average "catastrophe" load for such events that is collected each year. In the years when no "catastrophe" adversely affects an insurer's earnings, the "load" is realized as profit and the capital or surplus account increases. This assures that sufficient capital is available to continue writing property insurance in subsequent years, and to cover any "catastrophe" that will occur eventually.

Recent Changes in Insurer Participation in the Homeowner Insurance Market

One of the tools that insurers commonly use to manage their financial risk to extreme weather losses, as well as prices for their property insurance policies, is

scientifically calibrated weather models. These models came into existence shortly after Hurricane Andrew hit Florida in 1992.

Beginning in 1993, many homeowner insurance companies withdrew from insuring Massachusetts homes and other properties largely because the cost of the additional capital required to remain in that market was too high[15]. The insurers that remained on the coast, however, did not have sufficient capital or surplus to insure these abandoned homeowners voluntarily, which ultimately forced these people to seek insurance coverage through the MPIUA.

M.G.L. c 174A, §5, requires the Division of Insurance to give due consideration to conflagration and catastrophe hazards, including catastrophe reinsurance when determining whether a rate filing meets the statutory standards of being neither excessive, nor inadequate, nor unfairly discriminatory. In order to maintain a viable voluntary property insurance market in coastal communities, the Division of Insurance began to accept homeowner insurance rate filings that incorporated catastrophe loads generated from hurricane models in 2002[16]. Because Massachusetts law did not permit the estimated cost of hurricane losses in MPIUA's homeowner insurance rates until October 1, 2006[17], it is not surprising that the percentage of homes insured by the MPIUA in coastal Massachusetts communities[18] went from 5% in 1997 to 26% in 2006.

As of year-end 2013, the most recent year for which industry data is publicly available, the MPIUA continues to insure 10% of homes in Massachusetts [19]. The primary impact of the statutory amendments to M.G.L. c. 175C that allowed the MPIUA to add the expected costs of hurricanes and reinsurance in their rates was to prevent any further increase in the MPIUA's market share.

Competitive Dynamics in the Homeowner Insurance Market

[15] 1998 Homeowner Report, page 14.
[16] M.G.L. c. 174A was amended in 1996 to permit recognition of catastrophe reinsurance and other factors in rates (Chapter 93, section 2).
[17] Recognition of predicted hurricane losses was included in M.G.L. c. 175C, §5 in 2004 in Chapter 436.
[18] Coastal communities include Barnstable, Dukes, & Nantucket counties, New Bedford, Fall River, and portions of Plymouth County. The percentage of homes insured is based on the number of written exposures in these territories for properties insured under owners forms as reported in the annual Homeowner Insurance Market report filed by the commissioner of insurance in 1998 and 2007.
[19] See Appendix 2 for a history of the percentage of homes insured by MPIUA from 2000 through 2013.

Despite the dominant market position of the MPIUA in certain coastal communities, the Massachusetts homeowner insurance market continues to demonstrate a robust level of competition.

Ease of market entry and exit is an important feature of competitive markets. 68 insurer groups wrote at least $10,000 in annual premium during 2014, which remains unchanged from the number of insurer groups actively writing in 2005. Over the course of this ten year period, twelve insurer groups entered the market, and twelve insurer groups exited the market[20].

Two of the new entrants represented insurer groups that also entered the market to write private passenger auto insurance. Another new entrant has emerged as the sixth largest voluntary insurer on the Cape and the Islands as of December 31, 2013. 2014 was the most active year for new entrants with three insurer groups beginning operations in the homeowner insurance market.

Of the twelve insurers that left the market, three departed as a result of insolvency, and one departed because the insurer simply closed.

The profitability of the Massachusetts homeowner insurance market is reasonable with respect to the exposure it presents and the results that have been obtained in other New England states. The industry-wide return on net worth (capital and surplus) as estimated by the National Association of Insurance Commissioners is shown below for each New England state for select years and the ten year period ending December 31, 2013.

	Homeowners Return on Net Worth*			All Lines Return
Coastal State	2008	2011	2004-2013	2004-2013
Maine	-1.8%	14.8%	14.8%	14.3%
New Hampshire	-12.7%	12.9%	13.0%	12.0%
Massachusetts	20.1%	-10.3%	17.6%	11.1%
Rhode Island	22.4%	4.4%	20.9%	10.5%
Connecticut	21.7%	-32.7%	14.6%	10.3%

Source: *NAIC Report on Profitability By Line By State: 2013*

* Net worth is capital and surplus

[20] See Appendix 3 for details regarding insurer entries, exits, and mergers in the Massachusetts homeowners insurance market from 2006 through 2014.

AFFORDABILITY OF HOMEOWNER INSURANCE POLICIES

In 2013, the average premium to insure a single home with the MPIUA was $1,619 compared with an average premium of $1,273 for a policy issued in the voluntary market.

While extremely damaging weather events are easy to identify once they occur, even "normal" weather varies in intensity from one year to the next. The statutory requirement[21] that an insurer consider the past five years of loss experience when estimating its future rate need helps to smooth out the peaks and valleys of recent weather patterns. The table below displays data that was contained in a homeowner insurance rate filing that was recently placed on file[22] by the Division. This table shows the history of claims associated with significant weather events that affected Massachusetts (excluding losses associated with hurricane Irene, superstorm Sandy, and portions of the tornados that affected Springfield[23]), along with the premium that would be available to pay for those claims if they occurred in 2014.

Accident Year Ending	Net Losses Associated with Large Weather Events (000s)	Adjusted Earned Premium (000s)
9/30/2003	$5,971	$80,965
9/30/2004	$3,256	$79,542
9/30/2005	$4,150	$75,127
9/30/2006	$2,976	$72,338
9/30/2007	$1,105	$74,245
9/30/2008	$0	$81,421
9/30/2009	$6,998	$92,819
9/30/2010	$8,147	$112,412
9/30/2011	$45,049	$130,696
9/30/2012	$7,586	$138,730
9/30/2013	$4,219	$140,026
9/30/2014	$5,516	$141,935

[21] M.G.L. c. 174A, §5
[22] State tracking number 15MAR23-109.
[23] These claims are not reflected directly in the estimate of future rate need. The results of a hurricane model are used to estimate future rate needs for this specific type of risk.

Two things are notable about this history of results. First, there are some years when losses associated with significant weather events are minor or non-existent. Second, in the case of this insurer, the most significant weather event in the historical period occurred within the most recent five year period.

A number of actuarial techniques exist that either remove or adjust losses such as these from the five year experience period that is considered when estimating future rates for "normal weather." The effects of extreme weather events are averaged over a longer period of time, and are applied as a separate loading in the estimate of future rates. The table below shows the effect on the loss ratio of simply removing the losses shown above.

Accident Year Ending	Direct Earned Premium (000s)	Incurred Losses at 9/30/14 (000s)	Incurred Losses X Cat at 9/30/14 (000s)	Loss Ratio	Loss X Cat Ratio
9/30/2010	$76,984	$33,350	$26,467	43.3%	34.4%
9/30/2011	$92,933	$72,330	$33,813	77.8%	36.4%
9/30/2012	$106,218	$40,263	$33,594	37.9%	31.6%
9/30/2013	$117,484	$46,682	$42,864	39.7%	36.5%
9/30/2014	$128,632	$50,438	$45,332	39.2%	35.2%
Total	$522,251	$243,062	$182,070	46.5%	34.9%

Ratemaking methods for any line of property and casualty insurance are intended to strike a balance between rate stability and rate responsiveness. Future rate estimates based on actuarial smoothing methods help to minimize the premium effects of unusually severe weather events on a year over year basis.

Absent any change in the underlying risk, consumers expect that changes in the price of their insurance are comparable to changes in the cost of services that the insurance pays for. Unusually large price changes at renewal, which the consumer perceives to be "for no apparent reason," can be expected to motivate a consumer to shop for insurance elsewhere. A $100 increase in annual premium is a common industry benchmark that is believed to trigger shopping.

Premiums for homeowner insurance are based primarily on the insured value of the property, construction type, home maintenance, and fire protection. These factors underlie the differences in average premiums for homeowner insurance across the

state. The table below displays the 2013 average written premium[24] for each of the three major homeowner products, along with the percentage change in premium that is generated by a $100 increase.

Product	Average Written Premium	% Increase Due to $100 Change
Owners Coverage	$1,308	+7.6%
Tenant Coverage	$211	+47.4%
Condo Coverage	$452	+22.1%

Because consumers are free to shop their homeowner insurance policy at any time, most insurers attempt to manage their rate changes to a level that minimizes the risk of policyholder defection, while at the same time being adequate to cover the expected costs of the policy. The table below provides a count of the number of homeowner rate filings based on the overall rate level effect of each filing for each of the past five years, and 2015 to date.

Overall Average Rate Change Associated with Homeowner Insurance Rate Filings

Overall Rate Level Effect	New Business Effective Date in Year						
	2015	2014	2013	2012	2011	2010	2009
<= -10.0%							
>-10%, <=-7.5%							1
>-7.5%, <=-5.0%							1
>-5.0%, <=-2.5%					1	2	1
>-2.5%, <=.0.0%	9	14	9	5	8	8	12
>0%, <=2.5%	2	5	4	4	5	6	6
>2.5%, <=5.0%	6	12	10	16	10	10	2
>5.0, <=7.5%	8	6	4	5	8	1	2
>7.5%,<=10.0%	6	12	19	8	5	3	3
>10.0%				2	3	3	2
Total	31	49	46	40	40	33	30

* The following filing types were omitted:
- Filings that introduced new discounts or products applicable to new business only
- Filings that introduced new programs, tiers, or insurer entry into the MA market
- Filings that amended personal umbrella or mobile home rates only
- Filings that were compelled by statutory changes (i.e. Chapter 453 of Acts of 2008)
- Filings that contain rate effects exclusively for tenants or condo policies
- Loss cost filings submited by licensed rating organizations

[24] Premiums are developed from Exhibit 5C of the 2014 Homeowner Insurance Report filed by the commissioner of insurance.

CONCLUSION

In conclusion, I thank the Committee for the opportunity to appear today and to provide what I hope has been useful information regarding the process utilized by the Division of Insurance to ensure that homeowner's insurance rates are both available and affordable for Massachusetts consumers. Our healthy homeowner's insurance market provides an excellent opportunity for consumers to shop around for the coverages and price which best suits their needs, and I encourage them to do so whether through direct writing companies or with the professional assistance of the many licensed insurance agents and brokers in Massachusetts. I also want to thank the Division of Insurance staff seated here with me today, as well as the many others back at our office, for their professionalism, dedication and daily commitment to this Commonwealth and its insurance consumers.

Appendix 1

Average Overall Homeower Insurance Rate Changes for Top Ten Ranking Homeowner Insurers Within the Period 2005 - 2014

Group Name	Company Name	2010	2011	2012	2013	2014	2015
MAPFRE	Commerce/Citation	1.3%	3.8%	8.5%	0.5%	2.3%	0.3% & 8.9%
Liberty	Liberty Insurance Corporation | Liberty Mutual Fire Insurance Company | LM Insurance Corporation | The First Liberty Insurance Corporation	8.9%	8.8%	4.5%		3.0%	
	Liberty Mutual Insurance Company | LM General Insurance Company | Liberty Mutual Personal Insurance Company		6.3%	4.0%	4.5%	3.0%	
	Safeco Insurance Company of Indiana | General Insurance Company of America | Safeco Insurance Company of America | American States Insurance Company					4.1%	5.7%
Arbella		4.8%	5.7%	6.1%	9.0%	7.1%	2.6%
Safety	Safety Insurance Company | Safety Indemnity Insurance Company | Safety Property and Casualty Insurance Company	3.9%	6.6%	7.4%	3.3%	2.6%	9.1%
	Safety Insurance Company | Safety Indemnity Insurance Company Safety Property and Casualty Insurance Company						
Andover	Cambridge Mutual Fire Insurance Company | Merrimack Mutual Fire Insurance Company		1.6%	7.8%			
	Merrimack Mutual Fire Insurance Company				8.1%		
Chubb	Chubb Indemnity Insurance Company						0.0%
	Federal Insurance Company | Great Northern Insurance Company | Pacific Indemnity Company | Vigilant Insurance Company	-0.6%	4.2%	3.9%	3.6%		
Travelers	The Phoenix Insurance Company | The Standard Fire Insurance Company | The Travelers Indemnity Company | Travelers Commercial Insurance Company	2.6%	5.9% & 0.5%	9.5%		6.4%	
Amica	Amica Mutual Insurance Company	6.0%	5.8%		8.0% & -0.1%	0.0%	
Vermont Mutual	Northern Security Insurance Company, Inc. | Vermont Mutual Insurance Company	1.1%		4.3%	2.9%	0.5%	
USAA	Garrison Property and Casualty Insurance Company | USAA General Indemnity Company	4.5%	0.0%	7.7%	0.0%		6.3%
Quincy			4.0%	-1.0%	8.3%	3.7%	0.0%
Hanover		3.1%	4.7%	7.3%	8.7%		5.5%
Metropolitan		1.3%		3.6%	3.6%		

Appendix 2
Page 1

MPIUA Owners Policy Market Penetration Results

Year	% Homes Insured by MPIUA
2000	3.7%
2001	4.2%
2002	4.7%
2003	5.6%
2004	7.3%
2005	9.1%
2006	10.3%
2007	10.9%
2008	10.3%
2009	9.8%
2010	9.9%
2011	9.6%
2012	9.7%
2013	10.2%

Source: Written house years for owners policies as published in the Homeowner Insurance Reports filed by the commissioner of insurance in 2001 through 2014.

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MPIUA Rate Change History & Trend in Average Premium

Year	% Rate Change	Change in Avg. Premium
2000	-0.5%	2.9%
2001	-0.2%	6.6%
2002	1.9%	11.2%
2003	2.8%	12.3%
2004	3.2%	10.0%
2005		13.2%
2006	12.4%	15.4%
2007		1.5%
2008		-0.7%
2009		-5.2%
2010	-1.0%	-1.0%
2011		-1.6%
2012		-1.2%
2013		

Source: Written house years for owners policies as published in the Homeowner Insurance Reports filed by the commissioner of insurance in 2001 through 2014.

Appendix 3

Year	Entry	Exit	Merger/Acquisition
2006		Sompo Japan Ins Co Shelby/Vesta (insolvent)	General Casualty acquired by QBE.
2007	General Casualty	Philadelphia Indemnity	Patrons Mutual acquired by State Auto Insurance Group.
2008	Selective Insurance	Balboa Insurance	American Modern Home purchased by Munich Re. American States (Safeco) merged with Liberty. Commerce was acquired by MapFre.
2009	IDS Property & Casualty Axis Reins. Co.	Eastguard Ins. Co. Nationwide	
2010	Privilege Underwriters	Atlantic Mutual (insolvent) Providence Washington (closed in 2004)	Hingham Mutual/Danbury merged with New London County Mutual
2011	United P&C Ins. Co. American Strategic		Penn Millers acquired by ACE. Countryway merged with the VAFB
2012	Universal Property & Casualty	Lumberman's Mutual Casualty in run-off since 2003. Harleysville merged with Nationwide Arrowwood Indemnity (553)	Stillwater acquired Fidelity National P&C
2013	Farmers Insurance Gp	Great American	American Family Life Insurance acquired Homesite. Pennsylvania Lumberman's Mutual merged with Indiana Lumberman's Mutual
2014	Starr Indemnity & Liability Centauri Companion		OneBeacon sold to Tower Insurance Group Tower was sold to AmTrust

Paula Aschettino

Paula Aschettino

(1)

Thank you for the opportunity to speak today on this important subject.

I am Paula Aschettino, Chair and Founder of Citizens for Homeowners Insurance Reform, a large grassroots organization of over 8000 members, started in 2006.

We have been fighting for justified rates and reasonable premiums in Homeowners Insurance. I come today as a representative of all homeowners in MA.

I have visited Hurricane Modeling Companies, testified at the Fair Plan rate hearings, attended and spoke at the Florida Hurricane Commission, testified before the Financial Services Committee and met with the DOI and past Commissioner. Our organization is a member of the Consumer Federation of America , I am an active member of their Insurance Committee.

After the passage of the Acts of 2004, which were pushed by the insurance industry and reinsurance industry, requiring the Commissioner of Insurance to consider predicted hurricane losses and the cost of reinsurance in rate filings, the Cape and Islands experienced a 25% rate increase and a continued increase most every year thereafter.

We have held the Fair Plan back from rate hikes but have been unable to hold off the Voluntary Market.

The premium increase of the Voluntary Market for the Cape and Islands, from the mid 1990's- 2012 is 437% - Inland territories of like kind have experienced a 100% increase during that same timeframe.

Our average homeowner premiums at the Cape are $2600.00.for a modest $300k replacement value home, plus citizens must pay high wind deductibles of 3-5% of the replacement value of their home.

Risk has been shifted to the citizens and this problem is growing into other parts of the State. Replacement values are increasing in unjustified amounts as well.

This increases consumer payments for deductibles, increases premiums and reduces risk to the insurer.

(2)

Who verifies the accuracy of these data sources? Companies providing computer programs such as Marshal Swift who has a monopoly on replacement cost are not required to have proof on accuracy . Actuarial data need to be validated as to where they get their information and how do they calculate for the MA rate filings.

My replacement value on a 2800sq ft. Cape home ,age 1850 ,not on the water, updated, went from $ 350,000 replacement value and premium of $1300 with Hingham mutual in 1998 with a $ 1,000 all perils deductible and no wind deductible to a replacement value of $ 735,000 same house, with a $ 5,000 all perils deductible and wind deductible of 5% ,$36,500, before insurance kicks in and the premium is $ 3,135 after adding an alarm system to bring down the cost my insurer is Citation Insurance. FROM to 4200

Why does our MA DOI not deny these excessive rate filings? Are they justified?

Let's look at the Voluntary Market past history in MA.

The Voluntary Market in MA has experienced very low loss ratios over the past 20 yrs. Since 2006 loss ratios have been in the range of 38-45%- that's 38 cents of premium is paid toward losses- unheard of!

In 2011 the tornado in Western Ma resulted in loss ratios in the high 80% range. One bad year does not make a trend.

The records from the DOI report snow in MA from 1972 to 2013 has varied in amounts. In 1995 we had 107 inches of snow- and recent years of 2012- 9.3 inches, 2007 17.1 inches yet 2005 86 inches. I feel from the historic past the snow of last year was not so out of the ordinary and losses according to many insurers were not catastrophic.

According to industry newsletters the P/C Insurers have made record profits in the first quarter of 2015 in spite of the harsh winter. Net income after taxes grew to $ 18.2 billion in the first quarter from $ 13.9 billion first quarter 2014.

The Munich Reinsurance report showing $1.8 billion paid for insured loss first quarter, told me that number is a combination of insurers and reinsurers costs.

NOT All COST To PRIMARY INSURERS — misleading info AS USUAL

(3)

Since consumers pay the cost of the annual reinsurance treaty purchased by the insurance company in their premium, the policyholders have already paid for the loss if it happened. Most years we pay the high cost of risk and it never happens thank God.

But insurers make out anyway. Insurers get kickbacks, split commissions on these multi- million dollar reinsurance contracts.

Not only do the citizens pay to the cost of the insurer's reinsurance but according to testimony in the 2007 Fair Plan Hearing by a consultant from Milliman , Inc. ,an actuary company working for the Fair Plan, the reinsurance purchase by the MPIUA purchasing $80 million gives $8 million to the reinsurance broker, a 10%commission which is added to the cost within rates.

But the Broker and MPIUA made an arrangement that the broker would take

$ 2.75 million (the first 1 million + 25% of $7 million and the MPIUA would receive $ 5.25million (75% of the 7 million). The MPIUA said they would purchase "approximately" $ 85.7 million in reinsurance with the kickback of $5.25 million- Did they? Who checks? Did the policyholders pay the same? Did they use all the money? Remember, the MPIUA is the Voluntary Market Insurers. who checks?

The voluntary Market uses a File and Use method, meaning they file the rate filing and if the Commissioner does not deny the filing within 15 days or 30 day if needed, the rate goes into effect. There is no public hearing like the Fair Plan.

File and Use does not diminish nor negate careful scrutiny of all parts of the filing, requiring proof and justification of all data in order to apply state statutes that rates are not excessive inadequate of unfairly discriminatory.

"Standards" were set in the MPIUA Rate Denial of 2014- the DOI wrote a 35 page document giving careful explanation as to why the filing was denied and it was for the lack of proof (And) that hurricane models used were not (PROVEN) calibrated for MA and proof on the vulnerability of our MA homes to hurricanes. The reinsurance purchased was not proven to have been carefully calculated. Many other details were written by

(4)

our MA DOI and these Standards should apply to all homeowners insurance filings in MA.

Since 50% Of coastal premiums and 25 % of inland premiums are based on hurricane risk- the DOI must demand proof and justification the rate filings are based on accurate possibility of losses in MA.

Robert Hunter, Director of Insurance for the Consumer Federation of America, former Commissioner of Texas, whose testimony is relied upon in Congress, states MA is "raping it's consumers with its high rates."

"MA has some of the highest profits in P/C insurance in the USA according to the National Association of Insurance Commissioners.

Why are consumers overpaying? Where is our Commissioner of insurance and why is the MA DOI not doing its duty to regulate this industry which is required by the existing statues.

Homeowner insurance is regulated to the extent that rates are not excessive, inadequate or unfairly discriminatory.

I recently submitted a request to the Commissioner of Insurance under Chp 175A sect 7 (b) for a hearing on the Commerce/Citation Insurance Rate Filing.

Last week a letter from the Commissioner denying my request, no show of injury or harm.

This rate hike will cost 214,000 MA consumers $ 21,591,556- Some consumers around the state will see 10.1% increase. The Cape and Islands will see an increase of close to 10% and they have been overcharged for years with losses.

The consumer has no advocate, protector, if the Commissioner does not feel the rate is excessive and does not invite the Attorney General to hold a hearing.

This needs to change. Consumers are paying multi millions, billions to the insurance industry.

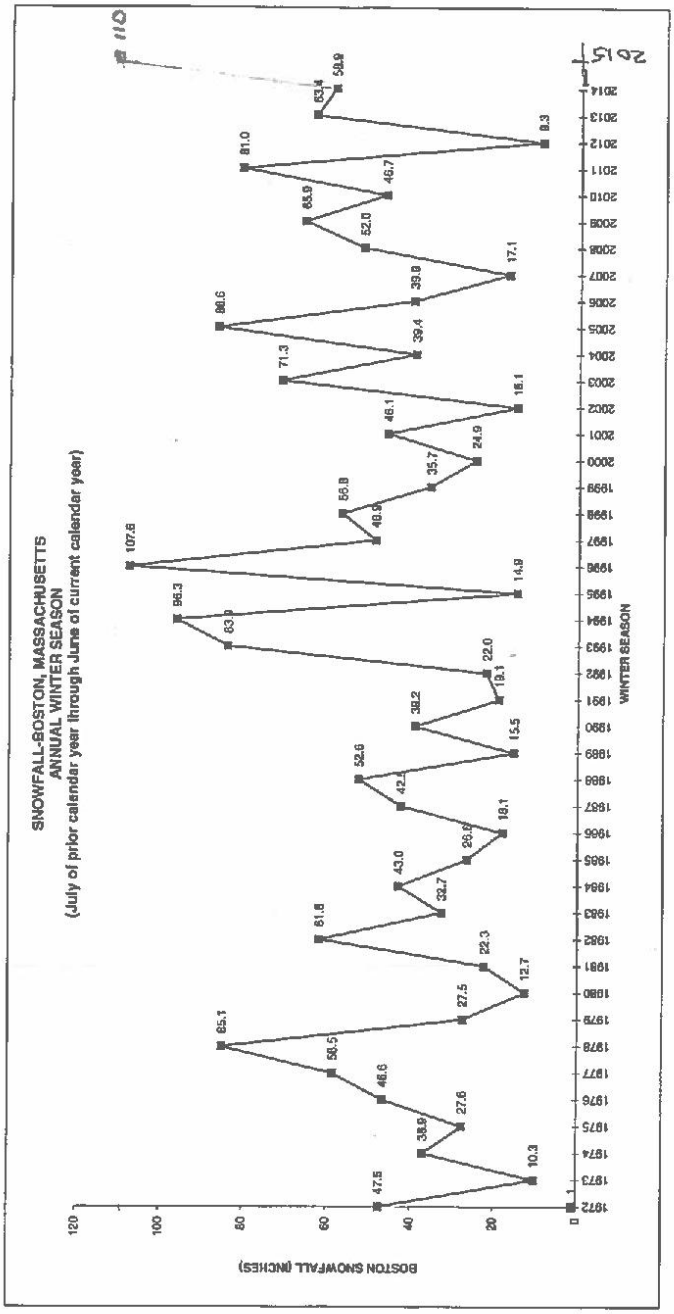
(5)

I ask that the State Legislature pass Sarah Peakes Bill # 926 which would state the requirements in rate filings.

I feel the Commissioner has the power and duty under the law to implement all the Standards described in the MPIUA RATE DENIAL 2014 but it would be a great backup to have House Bill 926 Pass now so consumers are protected.

Paula Archetto
Chair of Citizens 9/22/15
for Homeowners Insurance Reform.

Exhibit 7B


SNOWFALL-BOSTON, MASSACHUSETTS
ANNUAL WINTER SEASON
(July of prior calendar year through June of current calendar year)
BOSTON SNOWFALL (INCHES)
WINTER SEASON
2015

Joint Statement of Trade Associations

JOINT INSURANCE COMPANY TRADE ASSOCIATIONS' STATEMENT TO THE SENATE POST AUDIT & OVERSIGHT COMMITTEE REGARDING HOMEOWNERS' INSURANCE RATES

September 22, 2015

This statement is submitted jointly by the Massachusetts Insurance Federation (the "Federation"), the American Insurance Association ("AIA"), the National Association of Mutual Insurance Companies ("NAMIC"), and the Property Casualty Insurers Association of America ("PCI") to the Senate Post Audit & Oversight Committee in connection with its examination of homeowners' insurance rates. Together, these trade associations account for most of the homeowners' insurance business written in the Commonwealth. We submit this statement to provide the Committee with some important facts and a broader context about the Massachusetts homeowners' insurance market and its regulatory structure.

WHO WE ARE

The Massachusetts Insurance Federation ("The Federation") is the leading voice of property casualty insurance companies in the Commonwealth. Its members account for 60% of the voluntary homeowners' insurance premiums in the state. In addition to its 24 member insurance companies, three national property casualty insurance company trade associations (The American Insurance Association, The National Association of Mutual Insurance Companies, The Property Casualty Insurers Association of America) are associate members of the Federation.

In addition, the Insurance Information Institute ("III") has provided information that is included in this statement. The III is a non-profit organization that performs research and analysis of critical insurance issues.

OVERVIEW

By all indications, the Massachusetts homeowners' insurance market is healthy and competitive, providing consumers with a large variety of companies, coverage and premium options. Furthermore, the statutory rate regulatory structure – which is based on a competitive market model – is working as intended. The Division of Insurance provides focused and careful oversight of insurers and the marketplace through its expert staff, ensuring that rates meet the statutory standard that they not be excessive (to prevent exorbitant profits), inadequate (to make sure insurance companies are financially solvent so they can pay claims) or unfairly discriminatory (price differences reflect exposure and expense differences).

THE MASSACHUSETTS HOMEOWNERS INSURANCE MARKET

The Massachusetts homeowners' insurance market consists of two major components – the voluntary market and the residual market in the form of the

Massachusetts Property Insurance Underwriting Association (commonly known as the FAIR Plan).

The Voluntary Market. There is a vibrant and competitive voluntary insurance market for homeowners' insurance in the Commonwealth. In 2013, more than $2 billion in premiums was written in the voluntary market by 76 different companies , according to the Division of Insurance's Annual Home Insurance Report for Calendar Year 2013 (the most recent report available). See http://www.mass.gov/ocabr/docs/doi/consumer/mass-home-insurance-2013.pdf .

That business is widely dispersed, with no company or group having a dominant market share. The largest writer in 2013 was MAPFRE (former known as Commerce) with a 11.2% share of the market. The 10 top-writing companies accounted for only 58.1% of the total voluntary market, indicating that the market in not very concentrated. Consumers enjoy a wide variety of choice and no single player dominates the market.

Competitiveness. The competitiveness of the Massachusetts homeowners insurance market is further confirmed by the Herfindahl-Hirshman Index ("HHI") and other data. The HHI is, according to the U. S. Department of Justice ("DOJ"), a commonly accepted measure of market concentration.[1]

The III has calculated the HHI for the Massachusetts homeowners' insurance market. That calculation shows that the Massachusetts market has an HHI value of 576, which is less than all the other New England states except Connecticut (which is only slightly less at 568). The III explains that markets with scores of less than 1,500 are not concentrated. Based on its HHI score, the III concludes as follows: "The Massachusetts homeowners insurance market is competitive and not concentrated." See Appendix A, p.2.

The III has also computed the number of homeowners' insurers in the Northeast States. That analysis indicates the Massachusetts has more homeowners' insurance company options than in any other New England state. See Appendix A, p.3.

Massachusetts' homeowners insurance market is competitive and unconcentrated. That means an insurer must be cognizant of strong rate competition. If a company seeks too-large of an increase in rates, it can easily find itself losing business. Thus,

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[1] The DOJ explains the HHI as follows: " . . . The HHI takes into account the relative size distribution of the firms in a market. It approaches zero when the market is occupied by a large number of relatively equal size and reaches its maximum of 10,000 points when a market is controlled by a single firm. The HHI increases both as the number of firms in the market decreases and as the disparity in size between those firms increases.

The [government] agencies generally consider markets in which the HHI is between 1,500 and 2,500 points to be moderately concentrated, and consider markets in which the HHI is in excess of 2,500 points to be highly concentrated. . . ."

Massachusett's competitive market incents insurers to maximize rating accuracy and minimize rate increases to preserve market share.

Voluntary Market Average Premiums. According to data compiled by PCI from the National Association of Insurance Commissioners ("NAIC"), the average premium in 2012 for the standard homeowners' insurance policy in Massachusetts was $1,150, compared to the national average $1,034. Although Massachusetts has the 11th highest average premium among the states and the District of Columbia, when homeowners' premiums are viewed as a percentage of income, Massachusetts is lower than the countrywide average and ranks 25th among the states. See Appendix B.

The NAIC also reported that the average premium for the country rose 5.6% in 2012, 7.7% in 2011, 3.3% in 2010, 6% in 2009 and 1% in 2009. In the most recent 5-year period (2008 through 2012), the NAIC data indicate that countrywide average homeowners' premium has risen from $791 in 2008 to $1,034 in 2012, an increase of 30.7% or slightly more than 6% per year. By comparison, in Massachusetts the average rose from $1,026 in 2008 to $1,150 in 2012-- an increase of only 12.1%. In general, homeowners' premiums have been consistently rising around the country but the rate of increase has happened more slowly in Massachusetts.

The FAIR Plan. The FAIR Plan is the statutorily created residual market mechanism for homeowners' insurance. It makes property insurance available to any applicant who cannot obtain coverage in the voluntary market. Under the FAIR Plan statute, all companies writing property insurance in the Commonwealth are required to participate in the FAIR Plan and to share in the writings, expenses, profits and losses in proportion to each company's writings of property insurance. See G.L. c. 174C, § 4. The FAIR Plan has been designed to operate in a manner similar to a traditional insurance company in that it inspects property, collects premium, issues its own policies, and adjusts its own claims.

One indicator of the competitiveness and health of the voluntary homeowners' insurance market is the declining market share of the FAIR plan in recent years. In 2007, the FAIR plan's size peaked with 16.1% of the total homeowners' premium written in the state. This pinnacle followed 5 years of significant growth—starting from 5.9% of the market in 2002. Since 2007, the FAIR Plan's market share has been steadily declining and by the end of 2013 it was down to 12.1% of the total homeowners' written premium in the state. See the DOI 2013 Homeowner Report. While still a larger than desirable residual market, the trajectory has been headed in the right direction because of the vibrancy of the voluntary market.

Increasing Incidence and Costs of Catastrophic Storms. The III compiled information about insured catastrophe losses in Massachusetts between 2005 and 2015, which is enclosed as Appendix C [2] The III summary demonstrates that over that 10-year

[2] It should be noted that the data compiled by the III does not include flooding losses incurred for properties insured under the federal National Flood Insurance Program.

period insured losses from major catastrophes have been on the rise. Those events have resulted in $ 2.316 billion in insured catastrophe losses during that period, and 89% of those losses have been incurred since 2010. The III information also shows that insured catastrophe losses in Massachusetts during 2010, 2011, 2012 and 2015 are among the highest on record. Furthermore, the number of catastrophic events has been trending upward during the same period.[3] With respect to winter storms in particular, the III information shows that Massachusetts insured catastrophe losses from winter storms totaled almost $1 billion in 2015, which was almost 32% of *all* winter storm losses in the U.S. this year. In 2011, Massachusetts winter storm losses total $251 million or 12% of the national total.[4] See Appendix D.

Auto Insurance Managed Competition Impact on the Homeowners Insurance Market and New Homeowners Writers. The Division's Annual Home Insurance Report for Calendar Year 2013 contains a discussion at page 9 regarding the impact of the system of managed competition for auto insurance that was introduced in 2008 on the homeowners' insurance market, as follows:

> As of the printing of this report, 15 insurance companies have entered the Massachusetts' private passenger motor vehicle insurance market since reform. Some of these offer home insurance or are affiliated with home insurance companies. It is expected that these and other companies will look to expand their writing of home insurance in order to increase the marketability of their private passenger coverage.
>
> In addition to the arrival of new companies, since market reform many insurance companies which were already writing personal lines have begun offering expanded multi-policy premium discounts to insureds who buy both their home insurance and automobile insurance coverage from the same company.

http://www.mass.gov/ocabr/docs/doi/consumer/mass-home-insurance-2013.pdf

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[3] These longer term increases in incidence and severity are consistent with climate change trends such as those identified by the federal government. As the 2014 National Climate Assessment observed: "The intensity, frequency, and duration of North Atlantic hurricanes, as well as the frequency of the strongest hurricanes, have all increased since the early 1980s. Hurricane intensity and rainfall are projected to increase as the climate continues to warm." 2014 National Climate Assessment. U.S. Global Change Research Program (13 Participating Federal Agencies) at http://nca2014.globalchange.gov/.

[4] "Winter storms have increased in frequency and intensity since the 1950s, and their tracks have shifted northward. Other trends in severe storms, including tornadoes, hail, and thunderstorms, are still uncertain." 2014 National Climate Assessment at http://nca2014.globalchange.gov/

Furthermore, several companies focusing exclusively on writing homeowners insurance have entered the Massachusetts market in recent years. The combined effect of the introduction of auto insurance managed competition and the entry of several new homeowners' insurance companies has made the homeowners' market even more competitive. See Appendix E.

RATE REGULATION

Statutory Framework and Requirements. Homeowners' insurance rates are governed by two statutes – G.L. c. 174A and G.L. c. 175A. Chapter 174A applies to the property components of the typical homeowners' insurance policy, while chapter 175A applies to the liability portions of the policy.

Each statute was enacted in substantially its current form in 1947 following the decision of the U.S. Supreme Court in *United States v. South-Eastern Underwriters Association*, 322 U.S. 533 (1944), which held that the business of fire insurance is "commerce among the several States," and thus subject to federal regulation under the Commerce Clause and to the federal anti-trust laws. This decision was a significant departure from the view prevailing for almost 75 years after *Paul v. Virginia*, 8 Wall. 168 (1869), holding that the issuance of a policy of insurance was not the transaction of commerce for the purposes of the Commerce Clause. Congress responded to the *South-Eastern Underwriters* decision by enacting the McCarran-Ferguson Act, 15 U. S. C. Sections 1011-1015, which was designed to preserve state regulation of insurance and the exemption of the business of insurance from the federal anti-trust laws to the extent of state regulation. To that end, the Act suspended the application of the federal anti-trust laws to the business of insurance until June 30, 1948 to allow the states to enact rate regulation laws. During this period of delay, the National Association of Insurance Commissioners ("NAIC") developed model property and casualty rate regulatory laws which most states, including Massachusetts, enacted. Most states still have laws similar to those original NAIC model property and casualty rate regulatory statutes.

Rate Standards. The basic regulatory standard in each statute is that rates shall not be "excessive, inadequate or unfairly discriminatory." G.L. c. 174A, § 5(a)(2); G.L. c. 175A, § 5(a)(4). For the property insurance components of homeowners' insurance rates, the principal rating factors required to be considered are: "past and prospective loss experience within and outside this commonwealth, to the conflagration and catastrophe hazards, . . . a reasonable margin for underwriting profit and contingencies, . . . dividends . . . allowed or returned by insurers to their policyholders, . . . past and prospective expenses both countrywide and those specially applicable to this commonwealth, and . . . all other relevant factors within and outside this commonwealth; and in the case of fire insurance rates consideration shall be given to the experience of the fire insurance business during a period of not less than the most recent five-year period for which such experience is available. In considering catastrophe hazards with respect to homeowners insurance rates, the commissioner shall consider catastrophe reinsurance and factors relating thereto." G.L. c. 174A, § 5(a)(3).

The principal factors to be taken into consideration for the liability components of homeowners' rates are slightly different; those factors are: "past and prospective loss experience, within and outside this commonwealth, to catastrophe hazards, if any, . . . a reasonable margin for underwriting profit and contingencies, . . . investment income on unearned premium reserves and loss reserves, to dividends . . . allowed or returned by insurers to their policyholders, . . . past and prospective expenses both countrywide and those specially applicable to this commonwealth, and to all other relevant factors within and outside this commonwealth." G.L. c. 175A, § 5(a)(1).

Required Information. To support a rate filing, an insurer must file with the Commissioner of Insurance (Commissioner) "every manual, minimum, class rate, rating schedule or rating plan, every other rating rule, every special rate . . . and every modification of any of the foregoing which it proposes to use." In addition, the insurer is required to "indicate the character and extent of the coverage contemplated and the extent and nature of any change in rates, rating plans or premium charges." G.L. c. 174A, § 6(a); see G.L. c. 175A, § 6(a).

In addition to the information required by the statutes to be filed, the Division of Insurance (the "Division") has administratively imposed additional requirements on insurers making rate filings. Those additional requirements include checklists for form and rate filings. A copy of the Base Checklist for Property and Casualty Insurance can be found at http://www.mass.gov/ocabr/docs/doi/companies/checklists/propandcas.pdf.

Furthermore, as part of the electronic filing system under which rate and policy form filings are made known as System for Electronic Rate and Form Filing (SERFF), an insurer must complete a Rate Filing Abstract form, which requires that detailed historical and summary information relating to the proposed rate change be provided. A copy of the Rate Filing Abstract form is enclosed as Appendix F. Additional information and/or justification may well be required by the Division of Insurance staff when reviewing an insurer's rate filing. In fact, the statutes specifically authorized the Commissioner to "require an insurer to furnish the information upon which it supports a filing." G.L. c. 174A, § 6(a); G.L. c. 175A, § 6(a).

Division of Insurance Expertise and Review of Filings. It is important to understand that the Division staff reviewing such filings includes experts from a number of different disciplines. G.L. c. 26, § 8E establishes within the Division a rating bureau (known as the State Rating Bureau or SRB) to provide the Commissioner with assistance and expertise in the determination of the appropriate premium charges for the lines of property casualty insurance over which the Commissioner has rate authority (principally auto, homeowners, medical malpractice and workers' compensation). The SRB staff is required to include actuaries, rate attorneys and mathematicians. The SRB costs for these experts and the expenses of the operations of the Bureau are charged to property casualty insurers by way of annual assessments.

The rate statutes provide that an insurer must make a filing "at least fifteen days prior to the proposed effective date." G.L. c. 174A, § 6(a); G.L. c. 175A, § 6(a). In

addition, these provisions allow the commissioner to delay the effective date for an additional thirty days in any case if it is determined that the additional time is needed "to properly examine the filing and any supporting information filed as requested or to permit a hearing thereon." These statutes are technically "file-and-use" rating laws. That means that at the end of the statutorily prescribed review period, the insurer can, technically under the law, proceed to implement the filing if the Division has not taken some formal action to stop the insurer from proceeding. In practice, however, few insurers run the risk of using this authority to "deem" a filing to be in effect upon the expiration of the statutory review period for fear that the Commissioner will later issue an order formally denying approval.

Other States. Most other states have insurance laws with a similar regulatory framework for homeowners' insurance rate filings as Massachusetts. According to an NAIC compendium of those laws, 23 states have so-called "file-and-use" rating laws like the ones for property and casualty rate filings in Massachusetts while 11 other states use more liberal standards of flex rating or use and file. Eighteen states have so-called "prior approval" laws which technically may require the insurance regulator to approve a rate filing before an insurance company may implement it, but many of these laws also have "deemer" time periods allowing an insurer to proceed with the filing after a prescribed period of time. The NAIC compendium is enclosed as Appendix G.

Rate Making from an Insurer Perspective. The development of an insurance company's homeowners' insurance rate filing is an intensive, data-driven process. For example, an insurance company does not know the losses and associated expenses arising from claims as those will occur in the future, sometimes long after the policy has been sold and after the policy term has ended (liability suits may be filed years after the policy term in some instances). To remain competitive, insurers must work very hard to accurately estimate and predict these future expenses. The major components of an insurer's rate filing are estimated future losses, expenses and an amount for profit (which is needed so that the company has sufficient capital to meet its obligations to policyholders). For a more detailed discussion of an insurer's ratemaking process, see Appendix H.

OTHER SIGNIFICANT ISSUES AFFECTING HOMEOWNERS' INSURERS AND THEIR RATES

There are a number of other factors that are important to consider in evaluating insurance companies in the homeowners insurance market, their operations and condition:

• *Rating (A.M. Best).* Ratings by A.M. Best (the leading insurance company rating agency) of at least "A-" or "A" are vital to homeowners' insurance companies. A rating below the "A" level may result in mortgage lenders not accepting the insurance company's coverage for their mortgaged houses. A low rating can also lead to a loss of business for the insurer because agents may be reluctant to place business with a company that does not have an "A" rating. A.M. Best performs a thorough review and analysis of each insurer's financial condition, business plans and operations and carefully

evaluates each company's capitalization to determine if it is adequate for the type and amount of insurance it is underwriting and the riskiness of that business.

• *Capitalization and Leverage Ratios.* In reviewing the financial condition of insurance companies, regulators and rating agencies pay particularly close attention to the capitalization of a company relative to the type and volume of business, as well as its geographic concentration. Thus, companies specializing in writing property or homeowners' insurance in coastal regions that are susceptible to severe storms will be deemed to need more capital than other companies without such exposures or concentration. Similarly, companies specializing in so-called long-tailed lines (the claims for which take a long time to finalize) such as medical malpractice or workers' compensation will need more capital than companies specializing in shorter-tailed lines such as auto insurance.

Companies are also evaluated based, in part, on the amount of business they write relative to their policyholder surplus (net worth). This premium-to-surplus ratio has reduced over time, meaning that regulators require more capital for a given amount of business than they did in the past. Ten or fifteen years ago, the regulatory rule of thumb for property casualty companies was that they should not write more than $3 of premium for every $1 of surplus (a company with $100 million in surplus could write $300 million in business; amount above the premium-to-surplus ratio guideline would invite additional regulatory scrutiny. In recent years, permissible leverage ratios have been reduced so that now the preferred level is close to $1 of premium for every $1 dollar of surplus. For companies with long-tailed lines and catastrophe exposures, the leverage ratios are expected to be even less than 1:1.

• *Reinsurance.* Regulators and rating agencies also require that insurance companies have adequate reinsurance[5] to protect the insurance companies from a large volume of losses and/or catastrophic losses (such as hurricanes). If reinsurance is not provided by reinsurers on approved lists of companies (reinsurers that are well-capitalized), the reinsurance coverage obtained will not be recognized by regulators. Since reinsurance is not subject to rate regulation, insurance companies have to negotiate with reinsurers for the price and terms of the coverage they need. These reinsurance costs must be included in the insurers' rates for their policies.

Thank you for the opportunity to share this information with the Senate Post Audit & Oversight Committee.

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[5] Reinsurance is a transaction in which one insurance company indemnifies, for a premium, another insurance company against all or part of the loss that it may sustain under its policy or policies of insurance. Unlike insurance sold to consumers, neither the rates nor the policy forms for reinsurance are subject to regulation.

John P. Murphy
Executive Director
Massachusetts Insurance Federation

Alison Cooper
Vice President
American Insurance Association

Francis. C. O'Brien
Vice President
Property Casualty Insurers Association of America

Cate Paolino
Director, State Affairs (Northeast)
National Association of Mutual Insurance Companies

Sherman "Whip" Saltmarsh

former State Representative "Whip" Saltmarsh

With a rate hike this high, it would have been prudent for the insurance commission to hold a public hearing before approving an increase of this magnitude.

- The rate increases are excessive. Period.
- The rates should be fair and equitable to both the insureds and the insurers.
- As an agent, I spend the time and the costly manpower to review each and every policy as it comes in and that is how we discovered these surcharges, in addition to the rate increases.
- The approved rate increase for one company, 8.9%, does not include the approved surcharge assessed for losses over $1,000 (which can range from 5% to 47.5% depending upon the number of losses the customer has had).
- The largest approved homeowner rate increase is 9.4% and the smallest is 2.9%.
- Insurance is a consumer-regulated product, as homeowner's insurance is NOT optional to most Massachusetts residents.
- During difficult economic times, customers who have already sustained a financial hardship due to the damage to their home this winter, are now faced with this large rate increase. (And marketing policies to find better coverage or better rates for a customer who sustained a loss is challenging because other companies do not want to take on customers with loss histories, nevermind provide more affordable rates.)

****Approved Requested Rate Hikes**:**

- 9.4% Safety, 8.9% Commerce Mapfre, 7.8% Bunker Hill, 2.9% Arbella
- Average rate increase from the past few years is 2.3%

Specific examples from our agency:

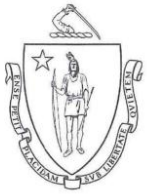
Customer X:

1 loss in 2015 (ice dam), has been with the insurer for 2 years, renewal August 2015 (affected by rate hikes). Received rate increase of 8.9% and a surcharge . His overall renewal premium went up $321, a percentage increase of 15% (went from $1865 to $2186).

Customer Y:

Been with the insurer for 8 years. 2 losses. Surcharge amount $277. Last year's premium $1491, this year increased to $1797. $306 increase, 17% up from last year.

Appendix V: Nov. 30, 2015 Letter from the Attorney General's Office to the Committee



THE COMMONWEALTH OF MASSACHUSETTS
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November 30, 2015

The Honorable Michael Barrett, Chair
Senate Committee on Post Audit and Oversight
State House, Room 416
Boston, MA 02133

Re: Recent Homeowners Insurance Rate Filings and Related Policy Recommendations

Dear Chairman Barrett:

Thank you for the opportunity to testify at the hearing several weeks ago on recent homeowners insurance rate increases. We believe that these increases, coupled with a large number of non-renewals following a historic winter, have created a unique opportunity for policymakers to reevaluate the Commonwealth's role in ensuring consumer access to a transparent, accountable, and consumer-focused homeowners insurance market. This letter is intended to provide you with additional context on recent rate filings, and advance several recommendations that we believe will help the market function more effectively.

As an initial matter, the recent rate increases by several homeowners insurers in Massachusetts are of serious concern to the Attorney General's Office. We believe rates should be fair for all consumers. The rate increases for two filings, MAPFRE and Safety, both of which approach 10%, are driven primarily by two elements in filings: non-hurricane catastrophe losses and profit.

Non-hurricane catastrophe losses are losses from events, such as large winter storms, that generate at least a certain level of claim damage (hurricane losses are calculated separately). However, instead of relying on long-term data as they did in previous projections, these companies are now placing heavier weight on recent experience. For example, MAPFRE now uses non-hurricane catastrophe averages from the last 7-10 years' experience, and Safety gives double weight to the last five years of experience. This approach is often biased; companies shorten the time period for losses when the procedure increases their revenues, but do not give

extra weight to recent experience when catastrophes are low. In fact, ISO, the industry rating organization which files loss cost on behalf of insurers in many states, including Massachusetts, uses a period of fifty years for non-hurricane catastrophes.

A second factor contributing to recent substantial premium increases is an increase in the profit provisions in the filings. Changes in profit are often arbitrary and not supported by sufficient data in the filing. We do not believe it is fair for insurers to take advantage of the recent winter storms to simply increase their bottom lines. Accordingly, we believe the rates for MAPFRE and Safety are excessive. Had they not changed these two provisions in the filing, the rates or MAPFRE would have actually decreased under its new rates, and the rates for Safety would only have increased 2-3% on average under the company's new rate plan.[1]

As such, our office believes that the voluntary homeowners insurance market could benefit from increased transparency, accountability, and a greater focus on consumers. Such enhancements would improve the competitiveness of this voluntary market, helping both ratepayers and companies alike. With those three policy priorities in mind, we offer the following specific recommendations.

First, the current rate-filing process for homeowners insurance involves no disclosure or notice beyond the Commissioner of Insurance. As result, unless the Commissioner exercises his discretion to hold a hearing, consumers and other stakeholders – including our office – do not know when new proposed rates have been filed, what the proposed rates are and what the justifications for the new rates are. The Commissioner is not required to explain his decision to hold or not to hold a hearing, and rate increases often go into effect without a hearing or meaningful public process.

Accordingly, we propose that the existing rate-filing process be supplemented to enhance transparency and accountability. Proposals for new rates, as well as any supplementary materials or information, should be filed publicly with the Commissioner of Insurance. This would empower all potentially impacted stakeholders to understand the proposal at the same time it is filed with the Commissioner, and equip stakeholders to raise any questions or concerns with the Commissioner through a public process.

We also support requiring the Commissioner to publish standards, with input from stakeholders, which would guide his decision as to whether a hearing needs to be held. This hearing could also be used to address stakeholder questions raised after the company's rate filing. Moreover, whenever the Commissioner makes a decision to hold or forego a hearing, he should provide a written explanation of his decision, subject to judicial review. Such procedures would ensure a more transparent rate-setting process that would provide greater accountability to consumers.

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[1] This assumes that other aspects of the company filings remain the same. Other adjustments might make the rates fall. As you know, the issue of whether appropriate hurricane loads and reinsurance expenses are being properly applied in rate filings remains contentious. Our office questioned whether the hurricane and reinsurance portions of the MPIUA's FAIR Plan filing unfairly inflated those proposed rates, and the Commissioner rejected the MPIUA filing.

We appreciate the opportunity to offer our proposals to improve this important market. If you have any questions, please do not hesitate to contact Benjamin Meshoulam, Senior Policy Advisor, at (617) 963-2601.

Sincerely,

Glenn Kaplan, Chief
Insurance and Financial Services Division