HOUSE RESEARCH ORGANIZATION bill analysis | 4/30/97 | HB 1853 Eiland (CSHB 1853 by Eiland)

SUBJECT: Coverage limits and reinsurance policies for catastrophic property insurance

COMMITTEE: Insurance — committee substitute recommended

VOTE: 8 ayes — Smithee, Van de Putte, Averitt, Bonnen, Eiland, G. Lewis, Olivo, Wise

0 nays

1 present, not voting — Burnam

WITNESSES: For — Jim Shawn, Texas Catastrophe Property Insurance Association

Against — Jay Thompson, Association of Fire and Casualty Companies of Texas

On — Lyndon Anderson, Texas Department of Insurance

BACKGROUND: The Catastrophe Property Insurance Pool Act governs the availability and issuance of insurance coverage for coastal areas subject to frequent and severe windstorm or hail damage. Under the act, the Texas Catastrophe Property Insurance Pool Association ("CatPool"), composed of all property and casualty insurers doing business in Texas, is charged with developing a plan of operation for windstorm and hail insurance in catastrophic areas, issuing policies, proposing rates within statutory guidelines, reinsuring and ceding reinsurance. The CatPool serves as the insurer of last resort for residential and commercial properties unable to get insurance through the regular, or voluntary, market.

The Catastrophe Property Insurance Pool Act sets maximum coverage limits for various properties insured by the CatPool. The insurance commissioner has the authority to increase these maximum limits for inflation.

The insurance companies that make up the CatPool must pay all policyholder claims. The CatPool can offset future losses either by setting up a reinsurance program or by establishing a catastrophe reserve trust fund at the Texas Department of Insurance (TDI). Insurers pay into the trust fund a portion of excess premium income to provide a reserve against significant

CatPool losses. If CatPool losses exceed premium income in any calendar year, the first $100 million in losses is assessed to member insurers, based on the volume of insurance each company sells. Any losses in excess of $100 million is paid from the trust fund. If losses exceed the amount in the trust fund, insurers are assessed an additional $200 million. If losses exceed this amount, insurers can deduct the additional amount paid from their state premium tax.

DIGEST: CSHB 1853 would increase maximum coverage limits in the CatPool and allow the CatPool to enter into certain reinsurance arrangements.

The bill would authorize the following increases in maximum coverage:

- from $250,000 to $350,000 for individually owned townhouses, residences and contents;
- from $750,000 to $1.5 million for apartments and condominiums;
- from $2 million to $2,192,000 for buildings owned and/or occupied by a governmental entity;
- from $100,000 to $125,000 for contents in apartment, residential condominiums, or owner-occupied townhouses; and
- from $1 million to $1.5 million for commercial buildings.

(The current maximum limits, adjusted for inflation, are slightly higher. For example, the adjusted limit for townhouses currently is $288,000.)

CSHB 1853 would authorize the CatPool to propose to the insurance commissioner annual increases in the maximum limits based on annual increases in construction costs. Within 10 days of determining the proposed adjustments, the CatPool would be required to file the proposed adjustments with the commissioner in writing. The filing would have to include information about current and proposed filings as well as a brief summary of how the proposed increase was determined. The commissioner would be required to approve, disapprove, or modify the proposed adjustments to the limits within 60 days of receiving the filing. The filings could not be heard by the State Office of Administrative Hearings.

CSHB 1853 would authorize the CatPool to both purchase reinsurance and collect excess premium income in a trust fund at TDI to offset future losses. The bill also would authorize the CatPool to offer supplemental reinsurance policies for property owners who could not get full coverage through the CatPool. The commissioner would have to adopt rules to implement this arrangement; the CatPool could not offer reinsurance policies until the rules were adopted. Rulemaking procedures under this section would not be conducted by the State Office of Administrative Hearings.

CSHB 1853 would take effect September 1, 1997, and would apply only to policies issued or delivered after January 1, 1998. The CatPool would be required to propose initial adjustments to the maximum coverage limits by September 30, 1997.

SUPPORTERS SAY:

CSHB 1853 would help the CatPool serve its mission of ensuring that homeowners in coastal counties have access to adequate wind and hailstorm coverage. Current coverage limits make it difficult for many homeowners and commercial property owners in Galveston, Corpus Christi and other parts of the Texas coast to adequately insure their properties. Between 1972 and 1996, the CatPool's commercial and dwelling coverage limits have increased 10 and 14 percent respectively, while during the same period the consumer price index rose 379 percent. Commercial properties in particular need the increased protection that would be provided by CSHB 1853.

The CatPool estimates that CSHB 1853 would increase its exposure along the entire Texas coast by only $300 million. This is a small percentage of the CatPool's approximately $10 billion in annual premium volume.

At the same time, CSHB 1853 would help reduce insurers' losses in the event of a major hurricane or other weather-related disaster by allowing the CatPool to purchase reinsurance in addition to operating the Catastrophe Reserve Trust Fund, which currently contains about $200 million. The CatPool estimates that it can purchase $200 million worth of reinsurance for $10 million in excess premium income. This reinsurance policy would create another layer of protection, in addition to the trust fund, against major losses. Under current law, if a major hurricane led to $1 billion worth of losses the CatPool could not cover, insurers would receive premium tax credits from the state for a portion of their losses. The reinsurance funds would reduce the amount insurers could claim in premium tax credits, thereby cutting the state's losses in the case of a major catastrophe.

CSHB 1853 would also allow the CatPool to offer low-cost, one-stop shopping for consumers who needed more insurance coverage than the CatPool could provide. Currently, homeowners and commercial policyholders must buy additional windstorm and hail coverage through unregulated surplus lines. Under CSHB 1853, the CatPool, following rules promulgated by TDI, would make arrangements with reinsurers to offer this additional coverage to individual policyholders. Consumers would probably save money because the CatPool would be able to buy reinsurance coverage in bulk for a number of individual policyholders. These policies would cost less than policies sold individually.

OPPONENTS SAY:

CSHB 1853 would allow the CatPool to increase its exposure at a time when it is not in a position to cover losses if a major hurricane hits the Texas coast. The $200 million in the CatPool's Trust Fund would probably cover only a portion of losses in a major hurricane; insurance companies would have to pay the rest of the cost. By raising maximum limits, the CatPool would be significantly increasing the possibility of major insurance company losses if a severe hurricane devastated the Texas coast.

CSHB 1853 would encourage the construction of expensive homes, condominiums and other structures along the Texas coast by allowing the CatPool to increase maximum liability limits to $350,000 for homes and townhouses, and nearly double maximum coverage for condominiums and apartments. These seacoast properties would be most vulnerable to losses in the event of a major hurricane. The CatPool's mission is to provide adequate protection from wind and hail damage for homeowners and commercial properties in Texas coastal counties; it should not be in the business of insuring expensive seacoast properties. Current maximum limits, which are adjusted annually for inflation, are sufficient to provide adequate coverage for most property owners in coastal areas.

NOTES:

The committee substitute allowed the CatPool to purchase reinsurance and operate the Catastrophe Reserve Trust Fund and offer reinsurance for individual policyholders, and changed from September 1 to September 30 the date the CatPool would have to propose to the insurance commissioner adjustments to maximum coverage limits.

HB 3031 by Eiland, which would allow CatPool insurers to recommend raising deductibles and lowering coverage, and HB 3383 by Eiland, which would authorize a rollback of CatPool rates if stricter building codes were adopted, are also on the calendar for second reading today.