



## Homeowners' Insurance



### The Issue

Reform of the Texas homeowners' insurance market in 2003 called for a file-and-use regulatory system. However, in 2009, the Sunset Review Commission's Staff Report on the Texas Department of Insurance (TDI) rightly concluded that the "Legislature cannot judge the success of the shift to file-and-use rate regulation because the system has not been fully implemented." Conditions have little improved since the report was issued.

One reason for the incomplete implementation is TDI's use of both pre-market and post-market regulatory tools—the Insurance Code grants TDI authority to reject rates both before and after being used in the marketplace. Failure to implement file-and-use is a problem because pre-market regulation hinders timely entry of rates into the marketplace and disrupts market pricing.

The price disruption is aggravated by Texas' non-renewal law, which prohibits insurers from non-renewing high claims policies, even when the damage was a product of the policyholders' own negligence. This forces insurers to base their coverage and rates on non-actuarial principles and discourages insurers from establishing specialized markets to cover high-risk areas.

A related problem is TDI's focus on "affordability." Ultimately, a regulatory stance focused on affordability reduces investment, hinders competition, and puts insurers at risk of insolvency. An example of the danger of focusing on affordability—rather than solvency—is the failure of Texas Select Lloyds in 2006, at a time when TDI was committing significant resources to pursuing legal actions against two major insurance companies for excessive rates.

Furthermore, statutory calls for rates neither "excessive" nor "inadequate" are at odds with each other, creating regulatory uncertainty. This conflicting statutory guidance stands in the way of true file-and-use rate regulation in the Texas homeowners' insurance market.

### The Facts

- Senate Bill 14 (2003) called for a transition to a file-and-use regulatory system for homeowners' insurance, with the intention of having a file-and-use system in place as of December 1, 2004.
- Texas' system of rate regulation for homeowners insurance includes pre-market and post-market regulatory tools, where rates can be rejected before or after they are first used in the marketplace. This prevents insurers from basing rates on actuarial principles and reduces competition in the marketplace.
- TDI's belated implementation of a 1997 provision allowing insurers to use national forms, along with lawsuit abuse, caused premiums to rise dramatically. This delay ultimately cost consumers more than \$900 million. After TDI allowed insurers to use non-standard forms in 2002, mold claims plummeted and rates stabilized.

### Recommendations

- Adopt a true file-and-use system allowing the Commissioner to disapprove only rates in use.

- Shift the focus from blocking “excessive” rates to guarding against inadequate or discriminatory rates.
- Implement a true file-and-use system for policy forms, and focus policy-form regulation on the wording and clarity of an insurance form rather than the content of a form.
- Allow the Commissioner to place under prior approval only those companies whose financial positions warrant increased supervision in order to maintain solvency.
- Permit insurers to non-renew, or add a premium surcharge to, high claim policies, especially where those claims were a product of negligence or misuse of the claims process.

## Resources

*Non-Renewing Costly Policies in Texas’ Homeowners’ Insurance Market*, by Kathleen Hunker, Texas Public Policy Foundation (2014).

*More Intervention in the Insurance Marketplace: SB 871* by Bill Peacock, Texas Public Policy Foundation (Mar. 2011).

*Freedom of Contract Creates Regulatory Certainty and Lower Insurance Rates* by Ryan Brannan, Texas Public Policy Foundation (Mar. 2011).

*Consumers, Competition, and Homeowners’ Insurance* by Bill Peacock, Texas Public Policy Foundation (May 2010).

*Homeowners’ Insurance: The Problem with Prior Approval* by Bill Peacock, Texas Public Policy Foundation (May 2009).

