

Draft Pending Adoption

Draft: 8/28/23

Property and Casualty Insurance (C) Committee
Seattle, Washington
August 15, 2023

The Property and Casualty Insurance (C) Committee met in Seattle, WA, Aug. 15, 2023. The following Committee members participated: Alan McClain, Chair (AR); Grace Arnold, Co-Vice Chair (MN); Larry D. Deiter, Co-Vice Chair (SD); Mark Fowler (AL); Ricardo Lara (CA); Andrew N. Mais and George Bradner (CT); Gordon I. Ito represented by Kathleen Nakasone (HI); Amy L. Beard represented by Patrick O'Connor (IN); James J. Donelon (LA); Mike Chaney and Andy Case (MS); D.J. Bettencourt (NH); Glen Mulready (OK); Kevin Gaffney (VT); and Allan L. McVey represented by Erin Hunter (WV). Also participating was: Peg Brown (CO).

1. Adopted its Spring National Meeting Minutes

Commissioner Arnold made a motion, seconded by Director Deiter, to adopt the Committee's March 24 minutes (see *NAIC Proceedings – Spring 2023, Property and Casualty Insurance (C) Committee*). The motion passed unanimously.

2. Adopted the Reports of its Task Forces and Working Groups

Commissioner Lara made a motion, seconded by Director Deiter, to adopt the following task force and working group reports: the Casualty Actuarial and Statistical (C) Task Force; the Surplus Lines (C) Task Force; the Title Insurance (C) Task Force; the Workers' Compensation (C) Task Force; the Cannabis Insurance (C) Working Group (Attachment One); the Catastrophe Insurance (C) Working Group (Attachment Two); the Terrorism Insurance Implementation (C) Working Group; and the Transparency and Readability of Consumer Information (C) Working Group. The motion passed unanimously.

3. Adopted the Regulatory Guide to Understanding the Market for Cannabis Insurance: 2023 Update

Commissioner Lara thanked Brown for her hard work in leading updates to the *Regulatory Guide to Understanding the Market for Cannabis Insurance*. Brown said the Cannabis Insurance (C) Working Group published the original white paper in 2019. At that time, the cannabis industry was in its infancy, and many insurance gaps for cannabis-related businesses existed. Since 2019, the cannabis industry has become more sophisticated. It has also continued to rapidly expand, driving new product development, infrastructure changes, and the need for businesses to provide ancillary services. The state of cannabis regulation, particularly at the state and local levels, has also evolved significantly since the last white paper. For these reasons, the original white paper needed to be updated to be of benefit to state insurance regulators.

Brown said the Working Group was officially tasked with providing an updated white paper in 2022. Since then, it has been exploring emerging issues, primarily in the commercial cannabis space, through presentations, panel discussions, and hearings held during open meetings. Information gained through these was leveraged to inform the content of the updated white paper.

Brown explained the Working Group designated a drafting group to develop the white paper after it reviewed and approved an outline during an open meeting. The drafting group held bi-weekly drafting sessions until completion. Drafting group member states included California, Colorado, Illinois, Oregon, Vermont, and Washington. The Insurance Services Office (ISO) and American Association of Insurance Services (AAIS) contributed educational materials and revisions to the sections of the white paper that discuss their products and services. The Working

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Group was presented with periodic updates on the working drafts during open meetings so it could provide feedback.

Brown said the Working Group has not encountered any controversy related to the updated white paper. The white paper avoids advocacy-oriented discussion and focuses on issues affecting affordability and availability of insurance for cannabis-related risks in states that have legalized its use. The white paper finds that although capacity has improved since the first white paper's publishing, most of the commercial insurance for cannabis-related businesses is still found in the nonadmitted market. This affects smaller industry players most as the nonadmitted market does not offer the "off-the-shelf" insurance solutions typically available in the admitted market. Insurance gaps are most prevalent in the emerging areas of the cannabis industry, such as ancillary services, cannabis-infused products, and social consumption lounges. Among the potential structures being explored to facilitate cannabis-related business coverage are: the use of state-based commercial insurance programs, risk retention groups (RRGs), captives, and joint underwriting associations (JUAs).

Brown said the Working Group adopted the 2023 update to the *Regulatory Guide to Understanding the Market for Cannabis Insurance* white paper during an open meeting on July 18. The adoption followed an extensive public comment period.

Commissioner Lara made a motion, seconded by Commissioner Arnold, to adopt the *Regulatory Guide to Understanding the Market for Cannabis Insurance: 2023 Update* (Attachment Three). The motion passed unanimously.

4. Heard a Presentation on Telematics

Micheal DeLong (Consumer Federation of America—CFA) said consumer protections related to telematics programs are needed at the state level to protect consumers and make sure telematics programs improve pricing fairness and incentivize safe driving. He noted that telematics is an insurance program that captures consumers' driving data from cars, via devices, built-in technology, and mobile phones. Telematics programs use that data to assess consumers' driving behavior and driving patterns, as well as to calculate insurance premiums. He said savings and surcharges vary by company, and some companies say they do not surcharge people with bad driving behavior.

DeLong said safe drivers should, in theory, earn lower premiums, but there are concerns about the use of telematics related to transparency, data uses, consumer privacy, actuarial soundness, and fairness. He said telematics programs use hard braking, the time someone is driving, the distance or miles traveled, how quickly someone accelerates, their speed, cornering, and location. He said one company collects phone data even when a person is not driving. He said most drivers still do not have telematics-based auto insurance despite a lot of promotion and marketing from insurers. Consumers are wary of telematics for several reasons: concerns about privacy, worries about control over their information, and vulnerability to data hacks and breaches.

DeLong said the CFA believes that the NAIC should develop and provide guidance on telematics for departments of insurance (DOIs) and lawmakers. He said there are few state laws, regulations, or bulletins addressing telematics. He said better oversight, whether in the form of a model law or bulletin, or other guidance for state insurance regulators, would help protect consumers from harmful practices and their resulting consequences.

DeLong said there are several key objectives of telematics consumer protections: transparency clarity concerning all variables used in telematics programs along with consumer-facing explanations of the weight given to each variable; actuarial support for each variable included in the telematics algorithm and further demonstration that variables used do not result in unfair discrimination on a protected class basis; strict limits on the data collected and used by auto insurers; strong privacy standards; and testing for unfair and unintentional bias.

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DeLong said he believes insurers should provide their customers with a list of all variables used to calculate their premiums, in a format approved by the DOI. The list should be presented in an easily understandable manner for consumers and include an explanation of what each variable is assessing. The list should also disclose the relative weight given to each variable in the telematics algorithm, in a way that makes it clear how much impact each variable will have on consumer premiums. Insurance companies should disclose all the data they are collecting, but consumers need more detail, more explanations about how they are being evaluated, and why each item is needed to evaluate their insurance risk.

DeLong said companies should demonstrate to state insurance regulators why each of the factors is relevant and should be collected. There should be actuarial support for each variable. Regulators should only allow data that is both demonstrably related to the risk of loss and not unfairly discriminatory. He said insurers should provide actuarial justification and causative explanation for each data point used. He said insurers must also demonstrate that each component meets the standards for fair and unfair discrimination as understood in a civil rights context so a component cannot disproportionately harm consumers of a certain race or ethnicity or related to another protected class status. He said justification should be required whether an insurance company uses its own program or a third-party telematics program.

DeLong said the use of telematics should encourage driver safety and reduce insurance costs, and telematics should not be allowed to become a platform from which consumers are turned into products. He said there should be strict limits on the data collected and used by insurers. Insurers, and any third party managing a telematics system on an insurer's behalf, must only be allowed to collect data necessary to calculate a consumer's premium in accordance with the approved telematics program. He also noted that policyholders should have the right to access, review, contest, and use any data collected as part of a telematics program. He said he believes that, beyond its use for insurance rating, the only other appropriate uses of the data are driving safety communications, crash response, and claims handling. With respect to the use of data for handling claims, a condition for allowing insurers to use that data must be that the data is equally available to consumers for their use in the claims process.

DeLong said there should also be strong privacy standards for consumer data, and these standards should synchronize with the NAIC privacy model. Rules should be clear that data collected shall not be sold, loaned, rented, shared, monetized, or used in any way beyond the approved auto insurance purposes. Consumers should have access to all data collected and information about how and where the data is stored, and how long data will be maintained by the company. Insurers should meet standards for protections against hackers and should report any data breaches and other malicious activities to the appropriate authorities. He also noted that policyholders should have the right to opt out of a telematics program and to be rated without usage-based data in a manner that is not unfairly discriminatory.

DeLong said ensuring equity in the use of telematics requires testing for unfair discrimination and bias. He said charging higher premiums to consumers who drive at night or to those with varying time of day driving patterns could harm lower-income consumers who often work night shifts or jobs with inconsistent hours, with no control over their schedules. He said telematics programs should be subject to algorithmic bias testing. The focus should be on assessing the outcomes of the telematics algorithm, such as how much a customer is charged as a result of the telematics system and whether any data elements of the program are driving protected class discrimination.

Commissioner Mulready asked if there is an analysis of how states treat the usage of telematics. DeLong said most states do not have specific laws or regulations concerning telematics, although New York has some guidelines.

5. Heard Presentation on Underinsurance Issues

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Ken Klein (California Western School of Law) said he has been conducting research into underinsurance. He said most homeowners in the U.S. believe they are fully insured, but they are significantly underinsured. He worked with the California DOI to obtain two years of fire claims. He said the data shows that after a catastrophe, about 95% of homeowners have less coverage than what it would take to rebuild. He said most homeowners are at least 57% underinsured. He said the explanation is not demand surge because many of the claims were not total losses, and they experienced 24% demand surge compared to underinsurance of 57%. He also said homeowners are not choosing to underinsure because many homeowners bought Extended Replacement Cost where they chose 100% of the estimate of reconstruction costs. He said these homeowners still have inadequate insurance, including the extended replacement coverage (ERC), at least 60% of the time. Klein said in the non-catastrophe losses, homeowners were underinsured 77% of the time by an average of 35.5%.

Klein said insurers use algorithms at point-of-sale (POS) to estimate reconstruction cost. He said the estimates are presented to customers as the insurer's estimated cost of reconstruction based on the information the insurer has about the house. He said the customer is given the right to select either more or less Coverage A than the estimate, but the customer typically is not given any information about error rates in the algorithm-generated estimates or any other reasons to doubt the accuracy of the estimates. Klein said the error rate of the algorithm-generated estimates apparently is significant and typically is significantly low. He noted the insurer's internal data makes error rates in algorithm-generated reconstruction estimates easily calculatable and knowable to insurers, but insurers cannot unilaterally adjust their pricing to correct for the error rates without causing competitive issues through high prices.

Klein said that although he reviewed 8,000 large loss claims, the data is not conclusive because data does not exist to compare claims that insurers internally identified as total losses to the amount of the POS estimated reconstruction cost for each claim.

Klein suggested that state insurance regulators should require insurers to report the following for each total loss claim: the insurer's POS estimated reconstruction cost and the estimation software used to determine that estimate; any updated estimated reconstruction cost and the software used for following years; the dwelling reconstruction coverages and the coverage limit of Coverage A; the incurred loss; and whether the loss occurred in a catastrophe.

Klein also said state insurance regulators should adopt the approach of California and Colorado in terms of disclosure rules by requiring insurers to: 1) make annual calculations of the error rates of their POS reconstruction cost algorithm; and 2) disclose to insureds their error rate within the algorithm so the insured can decide which coverage amount to choose. He said this would reduce the frequency of unintended underinsurance. Klein said this research would be published in January 2024.

6. Discussed Insurance Issues Related to Public Schools

Commissioner Mulready said he is hoping to learn from other states about how they are dealing with rising insurance rates for public schools. He said Oklahoma had two self-insurance pools for public schools, but one recently went out of business. He said 61 reinsurers participate in the pool with \$25 billion in property. The pool has seen a 262% loss ratio over the past six years. He said the program has a pilot program to conduct water and temperature monitoring in an attempt to keep claims down. Some schools are changing deductibles to improve rates. He noted that an Oklahoma company runs one of the three pools in the state of Texas. He said the Oklahoma legislature is looking into these insurance issues.

Commissioner McClain said Arkansas is seeing similar issues with rates. He said a recent tornado caused \$100 million in losses to schools. He said Arkansas has 24 reinsurers participating in its pool. Director Wing-Heier said two pools are merging in Alaska. She said members of the pool are responsible for losses. Commissioner

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Mulready said that is the case in Oklahoma as well and that when the prior pool went under, there were assessments to those school districts to pay for losses. Commissioner McClain said the Committee will look to have future discussions on this issue.

Peter Kochenburger (University of Connecticut School of Law) said this issue is national in scope. He said access to cyber insurance is difficult due to school vulnerabilities. He also said he has conducted work on the cost of insuring armed security.

7. Announced the Property Insurance Data Call Project

Commissioner McClain said state insurance regulators understand that increasing frequency and severity of weather events, rising reinsurance costs, and inflationary pressures are making property insurance availability and affordability more challenging for a growing number of regions across the country. These dynamics can vary significantly within a relatively small geographic area, so while a state's property insurance market may be generally healthy overall, there can be localized protection gaps that challenge certain communities.

Commissioner McClain said state DOIs have robust financial data to understand the impact of these forces on insurers' solvency and investments and can assess the strength and resilience of the industry, but many states lack granular data on how this translates to availability and affordability of coverage for consumers in some areas. He noted NAIC Members adopted a 2023 charge for the Property and Casualty Insurance (C) Committee to: "Assist state insurance regulators in better assessing their markets and insurer underwriting practices by developing property market data intelligence so regulators can better understand how markets are performing in their states, and identify potential new coverage gaps, including changes in deductibles and coverage types, and affordability and availability issues."

Commissioner McClain said interested regulators have begun preliminary scoping work to identify regulatory issues and considerations related to affordability and availability for which data is lacking, and then intend to refine a data template to respond to those specific needs of state insurance regulators. He said that although there is federal interest in this issue and proposals to gather data directly from insurers, NAIC Members believe the states have both the expertise and necessary regulatory authority to gather, analyze, and use data about their unique market conditions and meet the needs of policyholders, so they are best positioned to lead this work.

Commissioner McClain said that as the data template is developed over the coming weeks, state insurance regulators will work with interested parties in ensuring regulators receive accurate and meaningful data to meet regulatory needs.

Birny Birnbaum (Center for Economic Justice—CEJ) said in 1991, the Texas DOI tried to obtain data for a redlining study. He said they could not get the data from statistical agents, so the DOI developed a new data collection program for effective market monitoring through a single statistical agent. The new statistical plan was based on transactional-level reporting. He said this structure would work for state insurance regulators in conducting analyses to determine which insurers are writing in what areas and at what price. He said workers' compensation has a similar type of detailed transaction-level reporting. He said state insurance regulators should not try to become data collectors, but they should reform the statistical agent reporting system.

Having no further business, the Property and Casualty Insurance (C) Committee adjourned.

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