Report on Availability and Affordability of Personal and Commercial Property and Casualty Insurance in Coastal Areas in Maryland

Therese M. Goldsmith
Commissioner

October 2012

List of Figures and Tables

Figures

Tables

List of Hearing Exhibits

1. Notice of Quasi-Legislative Hearing

2. Who is the RAA? Document

3. Testimony of the American Insurance Association

4. American Insurance Association Natural Catastrophe Agenda – To Reduce Loss and Promote Stability

5. Statement of Robert Detlefsen on behalf of the National Association of Mutual Insurance Companies

6. State Beach and Windstorm Plans – An Overview of Operations and Financial Structures

7. Senator James Mathias – Letter and Attachments

8. PCI Special Report – Availability and Affordability of Personal and Commercial Property and Casualty Insurance in Maryland's Coastal Areas, dated 12/13/11

9. Joint Insurance Association Report

9A. Joint Insurance Association Supplement

10. Testimony of Minor Carter

11. Maryland Insurance Administration – List of Approved Surplus Lines Insurers

12. Maryland Insurance Administration – 2011 Report on the Availability and Affordability of Health Care Medical Professional Liability Insurance in Maryland, August 2011 (Exhibit A4, Pg. 3)

13. Insurance Article § 19-212, Plan of Material Reduction

14. Presidential Major Disaster Declarations During Hurricane Season in Maryland

15. Karen Clark & Company - Using Catastrophe Models and Other Tools to Assess Hurricane Risk - NAIC Fall Meeting - November 4, 2011

16. Property Clams Services Information

17. Status of the South Carolina Wind and Hail Underwriting Association – Status Report for 2009 - Submitted by South Carolina Dept. of Insurance (Pgs. 28 – 39)

18. Coastal Market Assistance Program Pamphlet: & CMAP Plan of Operations

19. 2010 Report of the Climate Change - Insurance Advisory Committee

20. State of Connecticut Insurance Department - A Report on the Availability of Homeowners Insurance Along the Connecticut Coastline, December 5, 2006

21. Lloyds' America, Inc. – Comments

22. Independent Insurance Agent – Written Comments

23. Testimony Insurance Agents and Brokers of Maryland and written comments from E. Larry Sanders, Edward 1. Sanders Insurance Agency, Inc., dated 12/13/11

24. Excel Spreadsheet with accompanying data back-up regarding the rate of return on the homeowner's insurance line in the aggregate, submitted by Matt Wulf, Reinsurance Association of America, dated 12/14/11

25. Supporting Documentation from Reinsurance of America, dated 12/14/11

26. Supporting Documentation from the Maryland Association of Mutual Insurance Companies, dated 12/14/11 - 12/16/11

27. Comments of State Farm Insurance Company, dated 12/16/11

28. Joint Insurance Association's Lower Eastern Shore Policy Count Comparison, dated 12/16/11

29. Allstate Insurance Company' s written testimony, dated 12/16/11

30. Written comments from Jim Fowler, Fowler Insurance, Inc., dated 12/16/11

31. People's Insurance Counsel Division – Letter and Attachment, dated 12/29/11

32. Supporting Documentation from Allstate Insurance Company, dated 1/09/12

Table of Contents

I. Executive Summary

On December 13 and 14, 2011, the Maryland Insurance Administration ("MIA") held a quasi-legislative hearing on the Availability and Affordability of Personal and Commercial Property and Casualty Insurance in Coastal Areas of Maryland (the "Hearing"). The Hearing was prompted by a combination of events, including, among other things: (1) the decision of State Farm Fire and Casualty Company ("State Farm") to cease underwriting new or renewal homeowners and renters insurance policies in the State for risks located on a barrier island, within 2,500 feet of the coast, or within 500 feet of large bodies of water; (2) the earlier decision of Allstate Insurance Company and Allstate Indemnity Company (collectively, "Allstate") to cease underwriting new homeowners and renters policies in essentially all of St. Mary's, Somerset, Talbot, Wicomico and Worcester Counties, along with significant parts of Anne Arundel, Calvert, Charles, Dorchester, Prince Georges and Queen Anne's Counties),[1] and (3) a continuing trend in insurers' adoption of underwriting standards that offer or require deductibles equal to a percentage of the "Coverage A Dwelling Limit" of a homeowners insurance policy in the case of a hurricane or other storm ("percentage deductibles").

The purpose of the Hearing was to gather information to assist the Commissioner in determining whether Marylanders living and conducting business in coastal areas of the State have adequate access to affordable property and casualty insurance, and to formulate any appropriate action plans or policy options regarding such access. The MIA received information from 15 individuals or entities in the form of written testimony and/or oral testimony. Participants included policyholders, insurers, insurance producers, trade association representatives, the Joint Insurance Association ("JIA"), and the People's Insurance Counsel Division of the Office of the Maryland Attorney General ("PICD").

Most testimony and other evidence gathered in the course of this proceeding indicated that property and casualty insurance generally is available for homeowners and businesses in coastal areas of the State. The very small residual market in the State, even in coastal areas, supports a conclusion that competitive insurance products are available for Marylanders in those areas. Anecdotal evidence suggested, however, that in certain coastal areas – Ocean City, in particular − non-admitted carriers command a large share of the market. An issue that many witnesses raised was a need for enhanced consumer understanding about the insurance products they are purchasing, beyond an understanding of the premiums they pay. Coverage limits and deductible amounts were identified as aspects of insurance policies about which some consumers are unaware. To address this issue, the MIA is developing a consolidated consumer-friendly disclosures form for the General Assembly's consideration. The MIA also is promulgating regulations that specifically address insurer disclosures regarding the manner in which percentage deductibles are applied.

[1] State Farm and Allstate are the two top underwriters of personal lines property insurance policies in the State, with a combined market share of approximately 36 percent of premiums written. Maryland Insurance Administration, *2011 Report on the Effect of Competitive Rating on the Insurance Markets in Maryland*, Ex. 2 (December 1, 2011).

To the extent that availability concerns become more prevalent in all or part of Maryland's coastal zone in the future, the State could consider adopting initiatives that have been enacted in other states, such as insurer tax credits or grants, to encourage participation in the coastal market. Another potential approach involves the establishment of a Coastal Market Assistance Program to assist current or prospective homeowners in coastal areas of the State in finding homeowners insurance. The MIA intends to investigate further the details of such programs adopted in Connecticut and New York. Alternatively, the State could consider prohibiting insurers from canceling or refusing to underwrite or renew a particular insurance risk or class of risk based solely on the geographic location of the risk, as New Hampshire and Rhode Island have done. Such an approach could discourage carriers from participating in Maryland's markets, however, or could result in premium rate increases and subsidization by policyholders in lower-risk areas of policyholders in higher-risk areas. Any of these options would require legislative action.

With respect to affordability, the most recent available data from the National Association of Insurance Commissioners ("NAIC") indicates that the total average annual premium for dwelling fire and homeowners owner-occupied policies in Maryland compares favorably to the nationwide average ($778 in Maryland versus $875 nationally), and falls slightly below the national median (24th lowest of 51 jurisdictions).[2] Maryland's property and casualty insurance market remains competitive, and there are wide ranges of rates available in many areas of the State, including coastal areas. Premium rates have risen moderately in recent years, however, and such increases may be difficult for some policyholders to afford, especially in coastal areas such as Baltimore City, Somerset County, and Wicomico County, where the percentage of the population with incomes below the federal poverty level is substantially above the Statewide average.

Hearing participants identified as key contributors to premium rate increases: (1) the increased exposure to loss demonstrated retrospectively by higher than average losses in recent years and projected prospectively through new catastrophe models; and (2) rising property repair and replacement costs. In addition, although some witnesses testified that the cost of reinsurance has been relatively stable over the past several years, others pointed to volatility in reinsurance costs over the past two decades and expressed concern that increased exposure projections could result in increased reinsurance rates that, in turn, would result in increased premiums for policyholders. Policy options to address these key contributors could include: (1) requiring insurers to use only catastrophe models approved by the Florida Commission on Hurricane Loss Projection Methodology, or establishing a similar Maryland Commission; (2) enacting mitigation initiatives such as uniform enforcement of a Statewide building code; consumer tax credits, deductions, or exemptions for mitigation measures; or mitigation grants for fortification measures to existing homes; or (3) providing state income tax deductions for consumers based on need or on the establishment of a catastrophe savings account. With one exception, all witnesses expressing a view on the matter agreed that there is no demonstrated need to establish a reinsurance catastrophe fund in Maryland.

[2] 2009 Dwelling Fire, Homeowners Owner-Occupied, and Homeowners Tenant and Condominium/Cooperative Unit Owner's Insurance.

Insurers and insurer trade associations identified percentage deductibles as one way to control premium costs and to encourage carriers to remain in higher risk areas of the Maryland market. They also contended that percentage deductibles provide homeowners with an incentive to take steps to mitigate potential storm-related damage before it happens, thereby reducing exposure and further controlling costs. There was consensus, however, that consumers often may not understand that they have a percentage deductible, or the manner in which it is applied. As noted above, disclosures required under regulations currently being developed by the MIA are designed to help address this issue. Potential legislative policy options regarding the application of percentage deductibles include limiting carriers' ability to impose hurricane deductibles to once per calendar year, as Florida, Louisiana, and Rhode Island have done, or requiring any insurer that requires a percentage deductible for certain types of losses to offer a range of such deductibles. The latter approach arguably balances the interests of consumers and carriers by providing consumers with the opportunity to "buy down" high percentage deductibles while at the same time allowing carriers to appropriately manage their risk through higher premiums for products with lower percentage deductibles.

II. Introduction

On December 13 and 14, 2011, the Maryland Insurance Administration ("MIA") held a quasi-legislative hearing on the Availability and Affordability of Personal and Commercial Property and Casualty Insurance in Coastal Areas of Maryland (the "Hearing"). The Hearing was prompted by a combination of events, including, among other things: (1) the decision of State Farm Fire and Casualty Company ("State Farm") to cease underwriting new or renewal homeowners and renters insurance policies in the State for risks located on a barrier island, within 2,500 feet of the coast, or within 500 feet of large bodies of water; (2) the earlier decision of Allstate Insurance Company and Allstate Indemnity Company (collectively, "Allstate") to cease underwriting new homeowners and renters policies in essentially all of St. Mary's, Somerset, Talbot, Wicomico and Worcester Counties, along with significant parts of Anne Arundel, Calvert, Charles, Dorchester, Prince Georges and Queen Anne's Counties);[3] and (3) a continuing trend in insurer's adoption of underwriting standards that offer or require deductibles equal to a percentage of the "Coverage A Dwelling Limit" of a homeowners insurance policy in the case of a hurricane or other storm ("percentage deductibles").

The purpose of the Hearing was to gather information to assist the Commissioner in determining whether Marylanders living and conducting business in coastal areas of the State have adequate access to affordable property and casualty insurance, and to formulate any appropriate action plans or policy options regarding such access. Specifically, Hearing participants were encouraged to present information and supporting data on the following:

- The current number of admitted carriers, excess and surplus lines carriers, residual market mechanisms, captives and reinsurers offering property and casualty insurance products in coastal areas of the State;

[3] State Farm and Allstate are the two top underwriters of personal lines property insurance policies in the State, with a combined market share of approximately 36 percent of premiums written.

- The types of products offered in coastal areas of the State by admitted carriers, excess and surplus lines carriers, residual market mechanisms, captives and reinsurers;

- The rates and deductibles offered per carrier in coastal areas within the State;

- The impact, if any, of coastal markets on the availability and affordability of personal and commercial property and casualty insurance in non-coastal areas of the State;

- The effectiveness, cost, and long-term viability of alternative market mechanisms, such as limited coverage products, wind pools, the expansion of residual market mechanisms, and catastrophe funds that have been implemented or are being considered in other states or by the federal government; and

- Initiatives adopted in other states to increase availability and affordability of personal and commercial property and casualty insurance in coastal areas.

The MIA received information from 15 individuals or entities in the form of written testimony and/or oral testimony. Participants included policyholders, insurers; insurance producers, trade association representatives, the Joint Insurance Association ("JIA"), and the People's Insurance Counsel Division of the Office of the Maryland Attorney General ("PICD"). A number of exhibits were introduced during the course of the Hearing. A copy of the Hearing transcript and all exhibits may be accessed at http://www.mdinsurance.state.md.us/sa/consumer/topical-hearings.html.

The remainder of this Report first summarizes certain background information, including relevant insurance laws and certain geographic and demographic information about Maryland's coastal zone, in Section III. Section IV provides information regarding Maryland's coastal property insurance marketplace, including types of policies available in the market, types of carriers issuing those policies, the use of catastrophe modeling in the market, and the role of building codes in managing and mitigating risks in coastal communities. In Section V, the Report summarizes information gathered during this proceeding related to the availability of property and casualty insurance in coastal areas of the State, including the testimony of insurer trade associations, producers and producer trade associations, consumers, and consumer advocates. Section VI summarizes information regarding the affordability of that insurance, including information about insurance premiums in Maryland and its coastal areas, key factors contributing to premium rates, insurers' application of percentage deductibles in the case of a hurricane or other storm, and potential issues regarding subsidization of higher risk policyholders by lower risk policyholders. Section VII contains potential policy options regarding availability and affordability of property and casualty insurance in Maryland's coastal areas, at least most of which would require legislative changes, and Section VIII summarizes the MIA's findings and conclusions.

III. Background

A. Relevant Insurance Laws

An overview of the substantive and procedural requirements imposed on property and casualty insurers through the Insurance Article is useful in order to have a full understanding of the current state of the marketplace in the coastal areas. Broadly, the Insurance Article, which is enforced by the Commissioner, imposes certain obligations on insurers before they can refuse to issue or renew policies in various geographic areas of the State. There also are notice requirements that vary depending on the type of insurance in question relating to premium increases, cancellations and nonrenewals. In addition to underwriting requirements, including the use of what are known as percentage deductibles, the Insurance Article governs rate making by insurers.

1. Underwriting Restrictions

Underwriting is the process by which an insurer determines what risks it is willing to accept and whether to insure, or continue to insure, a particular risk, such as a particular home. This process is governed by § 27-501 of the Insurance Article, which prohibits an insurer from canceling or refusing to underwrite or renew a particular insurance risk or class or risk except by the application of standards that are reasonably related to the insurer's economic and business purposes. Underwriting standards need not be filed with the Commissioner in the normal course, but the Commissioner may, and often does, examine such standards to ensure compliance with the Insurance Article. Section 27-501 is part of Title 27, which deals with unfair trade practices and other prohibited practices in all lines of insurance and plays a major role in defining and prohibiting discrimination. Earlier this year, the Court of Appeals affirmed that § 27-501 is relevant to an insurer's determination not to write in the coastal areas of the State.[4]

Similar to § 27-501, § 19-107 prohibits a property and casualty insurer from refusing to issue or renew a contract of property insurance, casualty insurance, or motor vehicle insurance solely because the "subject of the risk" or the insured's address is located in a certain geographic area of the State unless the designation of the geographic area by the insurer has an objective basis and is not arbitrary or unreasonable. Section 19-107 is a "file and use" statute, which means that an insurer is not required to obtain the Commissioner's approval or permission before implementing its geographic designation, so long as that designation is filed with the Commissioner at least 60 days before the risk is refused. Despite the file and use status of the statute, the Commissioner has successfully prevailed upon several insurers to withhold implementing their geographic designations until the Commissioner has had an opportunity to review the filing in detail.

Both § 19-107 and § 27-501 were considered by the Commissioner when Allstate gave notice to the Commissioner of its intent to cease writing new property insurance policies in St. Mary's, Somerset, Talbot, Wicomico, and Worcester Counties, and significant parts of Anne Arundel, Calvert, Charles, Dorchester, Prince George's, and Queen Anne's Counties. After reviewing the catastrophic risk planning modeling utilized by Allstate, the Commissioner

[4] *See People's Insurance Counsel Division v. Allstate Insurance Co.*, No. 60, Sept. Term 2011 (Jan. 25, 2012).

approved the filing. The Court of Appeals affirmed the Commissioner's decision, finding no error in the conclusion that the geographic designations was reasonably related to Allstate's economic and business purposes and was not arbitrary or unreasonable.

The use of catastrophic risk planning models is governed by § 19-211, which requires an insurer to file with the Commissioner any specific model used in setting a rate or refusing to issue or renew homeowner's insurance because of the geographic location of the risk and to make arrangements to explain to the Commissioner, as well as to the PICD, the data used in the model and the manner in which the output is obtained.[5]

One additional statute that relates to underwriting is § 19-212, which imposes certain obligations on insurers before implementing a "material reduction" of the in force homeowner's insurance policies for an insurer on a Statewide basis. To qualify as a "material reduction," the reduction must, during a one-year period, be three percent or more of the in force homeowners policies cancelled or nonrenewed solely based on the geographic location of the risk. The Commissioner must approve such a filing if the insurer demonstrates that the material reduction is accomplished in a manner that minimizes market disruption in the areas where the reduction takes place.

2. Notice Requirements

The Insurance Article also imposes certain procedural notice requirements on insurers for cancellation, nonrenewals, and for some premium increases. These notice requirements are found in Subtitle 6 of Title 27. The notice requirements vary based upon whether the insurance policy constitutes "commercial" or "personal" insurance. Generally speaking, notices of the amount of renewal and expiring policy premiums, cancellations or nonrenewals must be provided at least 45 days before the proposed cancellation or expiration of the policy, except in the case of nonrenewals arising from nonpayment of premium.[6] The notices must state the "actual reason for the cancellation or refusal to renew a policy and must give notice of the right to replace the insurance through the Maryland Property Insurance Availability Act or through another plan for which the insured may be eligible.[7]

3. Rate Making Requirements

The method by which an insurer determines the premium to charge for a risk the company has decided to insure or continue to insure is known as rating or rate making. Title 11 of the Insurance Article governs this process. Rates may not be excessive, inadequate or unfairly discriminatory.[8] A rate may not be based on a geographic area itself, though underlying risk considerations, even if expressed in geographic terms, may be used.[9] As a result, proximity to coastal waters often is utilized by insurers as a risk consideration.

[5] The information filed under § 19-211 is statutorily considered to be proprietary and confidential commercial information.
[6] *See* Ins. Art. §§ 27-602, 27-603, 27-607 and 27-608.
[7] *See* Ins. Art. §§ 27-602, 27-603, 27-604, and 27-605.
[8] Ins. Art. §§ 11-205(d) and 11-306(b).
[9] Ins. Art. §§ 11-205(f)(4) and 11-306(e)(4).

Insurers are required to offer at least one actuarially justified premium discount on a policy of homeowners insurance to those policyholders who submit proof of improvements made to the insured premises as a means of mitigating loss from a hurricane or other storm.[10] The installation of hurricane shutters, reinforced roof coverings and roof to wall connections, tie downs, the repair or replacement of exterior doors (including garage doors), hurricane resistant trusses, studs and other structural components and "any mitigation effort that materially mitigates loss from a hurricane or other storm otherwise covered under the policy" are included as examples of the types of measures for which a premium discount should be provided.[11]

4. *Limitations on Percentage Deductibles*

The Insurance Article imposes procedural and substantive restrictions on the use of percentage deductibles (a deductible that is based on a percentage of the coverage under the policy) for homeowners insurance policies applicable in the case of a hurricane or other storm. Such deductibles may only be applicable beginning at the time the National Hurricane Center of the National Weather Service issues a hurricane warning for any part of the State where the insured's home is located and ending 24 hours following the termination of the last hurricane warning issued for any part of the State in which the insured's home is located.[12]

An insurer that adopts an underwriting standard that requires a percentage deductible in the case of a hurricane or other storm must provide the policyholder with an annual statement explaining the manner in which the deductible is applied and submit a copy of the form of the annual statement to the Commissioner prior to use.[13] Those insurers that adopt an underwriting standard that requires a deductible that exceeds 5 percent of the "Coverage A—Dwelling Limit" of the policy in the case of a hurricane or other storm may not utilize the underwriting standard until it files the underwriting standard with the Commissioner and receives approval of the underwriting standard in writing.[14]

B. Maryland's Coastal Zone

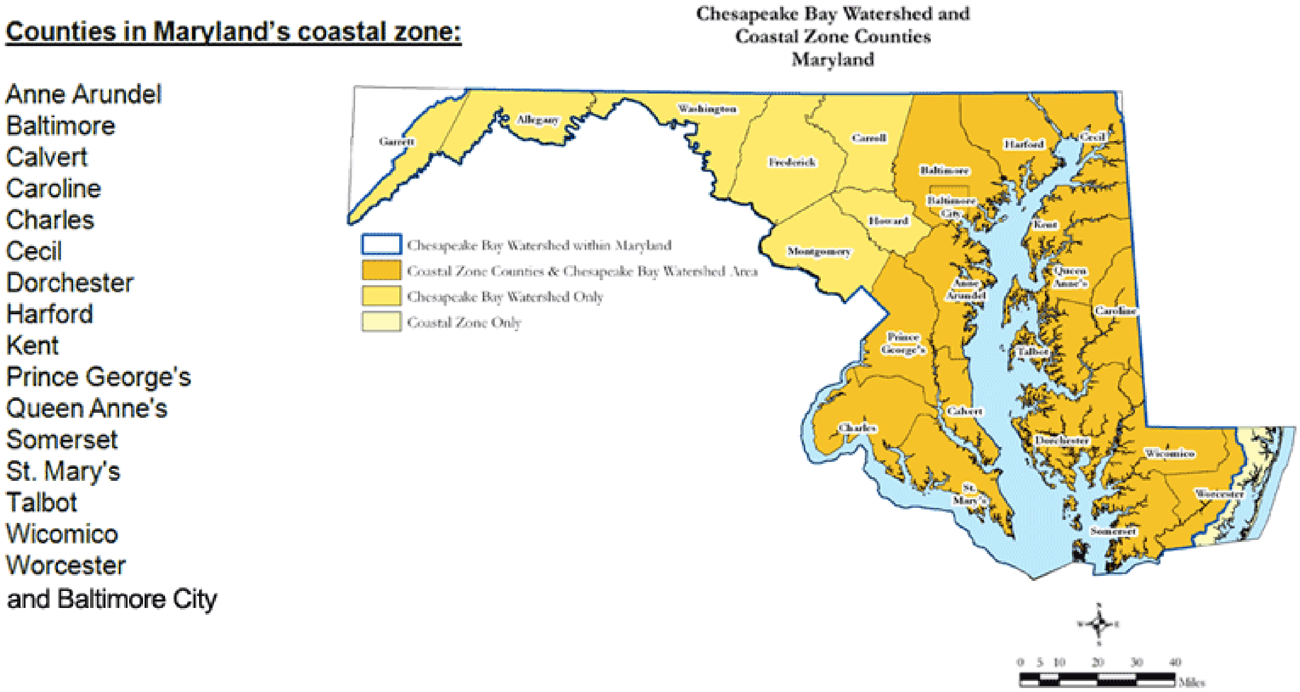
With nearly 3,200 miles of coastline,[15] Maryland is among the states most vulnerable to rising sea levels and severe weather associated with climate change. Jurisdictions within Maryland's coastal zone include Anne Arundel, Baltimore, Calvert, Caroline, Cecil, Charles, Dorchester, Harford, Kent, Prince George's, Queen Anne's, St. Mary's, Somerset, Talbot, Wicomico, and Worcester Counties and Baltimore City.[16] "This area encompasses

---

[10] *See* Ins. Art. § 19-210.
[11] Ins. Art. § 19-210(b).
[12] Ins. Art. § 19-209(b).
[13] Ins. Art. § 19-209(c).
[14] Ins. Art. § 19-209(a).
[15] United States Department of Commerce, National Oceanic and Atmospheric Administration, *Ocean and Coastal Resource Management: Ocean and Coastal Management in Maryland, available at* http://coastalmanagement.noaa.gov/mystate/md.html
[16] Maryland Department of Natural Resources, *Where We Work, Maryland's Coastal Zone*, http://www.dnr.state.md.us/ccp/where_we_work.asp

approximately two-thirds of the State's land area and is home to almost 70 percent of Maryland's residents."[17]

Figure 1[18]



[17] Maryland Department of Natural Resources, *Where We Work, Maryland's Coastal Zone*, http://www.dnr.state.md.us/ccp/where_we_work.asp
[18] Maryland Department of Natural Resources, *Where We Work, Maryland's Coastal Zone*, http://www.dnr.state.md.us/ccp/where_we_work.asp

As illustrated in Table 1 below, in recent years, population growth in many coastal areas of the State has outpaced the Statewide rate. For example, in the 10 years between 2000 and 2010, the populations of Calvert and Charles Counties grew at a rate approximately three times that of overall population growth in the State.

Table 1

Maryland Population Figures and Rates of Change in Populationfrom 1960 to 2010

Jurisdiction	Percent of Population - 2010	Type of Population Change		2010	2000	1990	1980	1970	1960	Percent of Population - 1960
Maryland	100.0%	Change from 1960 to 2010	**86.2%**	5,773,552	5,296,486	4,781,468	4,216,975	3,922,399	3,100,689	100.0%
		Average Decennial Change	**13.2%**							
Anne Arundel County	9.3%	Change from 1960 to 2010	**160.2%**	537,656	489,656	427,239	370,775	297,539	206,634	6.7%
		Average Decennial Change	**21.1%**							
Calvert County	1.5%	Change from 1960 to 2010	**460.7%**	88,737	74,563	51,372	34,638	20,682	15,826	0.5%
		Average Decennial Change	**41.2%**							
Carroll County	2.9%	Change from 1960 to 2010	**216.6%**	167,134	150,897	123,372	96,356	69,006	52,785	1.7%
		Average Decennial Change	**25.9%**							
Cecil County	1.8%	Change from 1960 to 2010	**108.9%**	101,108	85,951	71,347	60,430	53,291	48,408	1.6%
		Average Decennial Change	**15.9%**							
Charles County	2.5%	Change from 1960 to 2010	**349.9%**	146,551	120,546	101,154	72,751	47,678	32,572	1.1%
		Average Decennial Change	**35.1%**							
Frederick County	4.0%	Change from 1960 to 2010	**224.5%**	233,385	195,277	150,208	114,792	84,927	71,930	2.3%
		Average Decennial Change	**26.5%**							
Harford County	4.2%	Change from 1960 to 2010	**219.1%**	244,826	218,590	182,132	145,930	115,378	76,722	2.5%
		Average Decennial Change	**26.1%**							
Howard County	5.0%	Change from 1960 to 2010	**694.1%**	287,085	247,842	187,328	118,572	61,911	36,152	1.2%
		Average Decennial Change	**51.3%**							
Montgomery County	16.8%	Change from 1960 to 2010	**185.0%**	971,777	873,341	757,027	579,053	522,809	340,928	11.0%
		Average Decennial Change	**23.3%**							
Prince George's County	15.0%	Change from 1960 to 2010	**141.6%**	863,420	801,515	729,268	665,071	660,567	357,395	11.5%
		Average Decennial Change	**19.3%**							
Queen Anne's County	0.8%	Change from 1960 to 2010	**188.5%**	47,798	40,563	33,953	25,508	18,422	16,569	0.5%
		Average Decennial Change	**23.6%**							
St. Mary's County	1.8%	Change from 1960 to 2010	**170.2%**	105,151	86,211	75,974	59,895	47,388	38,915	1.3%
		Average Decennial Change	**22.0%**							
Wicomico County	1.7%	Change from 1960 to 2010	**101.3%**	98,733	84,644	74,339	64,540	54,236	49,050	1.6%
		Average Decennial Change	**15.0%**							
Worcester County	0.9%	Change from 1960 to 2010	**116.8%**	51,454	46,543	35,028	30,889	24,442	23,733	0.8%
		Average Decennial Change	**16.7%**							

Average Decennial Change — Represents the average exponential growth per 10 year period.

In certain coastal areas, the rate of change in population density, expressed in terms of persons per square mile, also has exceeded the Statewide rate in recent years. Of particular note, between 2000 and 2011, increases in population density in Southern Maryland and the Upper Eastern Shore regions were more than double and one-and-one-half times the Statewide rate, respectively.[19]

Table 2

JURISDICTION	Land Area (sq. mi.)	POPULATION Census 2000	Estimates 2005	Estimates 2008	Estimates 2009	Census 2010	Estimates 2011	POPULATION PER SQUARE MILE 2000	2005	2008	2009	2010	2011	Population Density Change	Percent Density Change
Maryland	**9773.8**	**5,296,647**	**5,592,379**	**5,684,965**	**5,730,388**	**5,773,552**	**5,828,289**	**541.9**	**572.2**	**581.7**	**586.3**	**590.7**	**596.3**	**54.4**	**10.00%**
Baltimore Region	**2236.8**	**2,512,557**	**2,599,352**	**2,632,756**	**2,648,486**	**2,662,691**	**2,680,756**	**1,123.30**	**1,162.10**	**1,177.00**	**1,184.00**	**1,190.40**	**1,198.50**	**75.2**	**6.70%**
Anne Arundel	415.9	489,677	516,171	525,304	532,395	537,656	544,403	1,177.30	1,241.00	1,262.90	1,280.00	1,292.60	1,308.90	131.6	11.20%
Baltimore	598.6	753,947	789,110	798,651	801,808	805,029	809,941	1,259.60	1,318.30	1,334.20	1,339.50	1,344.90	1,353.10	93.5	7.40%
Carroll	449.1	150,881	165,519	167,433	167,028	167,134	167,288	335.9	368.5	372.8	371.9	372.1	372.5	36.5	10.90%
Harford	440.3	218,914	238,402	242,779	243,685	244,826	246,489	497.1	541.4	551.3	553.4	556	559.8	62.6	12.60%
Howard	252.0	247,876	268,590	278,405	283,061	287,085	293,142	983.5	1,065.70	1,104.60	1,123.10	1,139.10	1,163.10	179.6	18.30%
Baltimore City	80.8	651,262	621,560	620,184	620,509	620,961	619,493	8,059.80	7,692.20	7,675.20	7,679.20	7,684.80	7,666.60	-393.2	-4.90%
Washington Suburban Region	**1643.6**	**1,870,242**	**1,996,003**	**2,022,201**	**2,046,116**	**2,068,582**	**2,097,772**	**1,137.90**	**1,214.40**	**1,230.30**	**1,244.90**	**1,258.60**	**1,276.30**	**138.4**	**12.20%**
Frederick	662.9	195,277	221,201	229,286	230,942	233,385	236,745	294.6	333.7	345.9	348.4	352.1	357.2	62.6	21.20%
Montgomery	494.4	873,874	921,531	942,748	959,013	971,777	989,794	1,767.40	1,863.80	1,906.70	1,939.60	1,965.40	2,001.80	234.4	13.30%
Prince George's	486.3	801,091	853,271	850,167	856,161	863,420	871,233	1,647.40	1,754.70	1,748.30	1,760.60	1,775.60	1,791.60	144.2	8.80%
Southern Maryland Region	**1037.4**	**281,276**	**321,725**	**333,492**	**336,321**	**340,439**	**345,870**	**271.1**	**310.1**	**321.5**	**324.2**	**328.2**	**333.4**	**62.3**	**23.00%**
Calvert	215.2	74,556	86,294	87,788	88,244	88,737	89,256	346.5	401	408	410.1	412.4	414.8	68.3	19.70%
Charles	461.0	120,524	138,560	143,783	144,804	146,551	149,130	261.4	300.6	311.9	314.1	317.9	323.5	62.1	23.70%
St. Mary's	361.2	86,196	96,871	101,921	103,273	105,151	107,484	238.6	268.2	282.1	285.9	291.1	297.5	58.9	24.70%
Western Maryland Region	**1531.5**	**236,672**	**246,146**	**251,534**	**252,199**	**252,614**	**252,946**	**154.5**	**160.7**	**164.2**	**164.7**	**164.9**	**165.2**	**10.6**	**6.90%**
Allegany	425.4	74,909	73,979	74,638	75,101	75,087	74,692	176.1	173.9	175.4	176.5	176.5	175.6	-0.5	-0.30%
Garrett	648.0	29,852	30,083	30,222	30,145	30,097	30,051	46.1	46.4	46.6	46.5	46.4	46.4	0.3	0.70%
Washington	458.1	131,911	142,084	146,674	146,953	147,430	148,203	287.9	310.1	320.2	320.8	321.8	323.5	35.6	12.40%
Upper Eastern Shore Region	**1589.0**	**209,286**	**229,249**	**237,735**	**238,989**	**239,951**	**241,262**	**131.7**	**144.3**	**149.6**	**150.4**	**151**	**151.8**	**20.1**	**15.30%**
Caroline	320.1	29,735	31,416	32,983	33,013	33,066	32,985	92.9	98.1	103	103.1	103.3	103	10.2	10.90%
Cecil	348.1	85,964	96,836	100,232	100,816	101,108	101,694	246.9	278.2	287.9	289.6	290.4	292.1	45.2	18.30%
Kent	279.4	19,201	19,695	20,150	20,132	20,197	20,204	68.7	70.5	72.1	72	72.3	72.3	3.6	5.20%
Queen Anne's	372.2	40,580	44,879	47,063	47,532	47,798	48,354	109	120.6	126.4	127.7	128.4	129.9	20.9	19.20%
Talbot	269.1	33,806	36,423	37,307	37,496	37,782	38,025	125.6	135.3	138.6	139.3	140.4	141.3	15.7	12.50%
Lower Eastern Shore Region	**1735.2**	**186,614**	**199,904**	**207,247**	**208,277**	**209,275**	**209,683**	**107.5**	**115.2**	**119.4**	**120**	**120.6**	**120.8**	**13.3**	**12.40%**
Dorchester	557.5	30,671	31,422	32,466	32,470	32,618	32,640	55	56.4	58.2	58.2	58.5	58.5	3.5	6.40%
Somerset	327.2	24,746	25,793	26,474	26,425	26,470	26,339	75.6	78.8	80.9	80.8	80.9	80.5	4.9	6.40%
Wicomico	377.2	84,638	92,508	97,111	98,069	98,733	99,190	224.4	245.3	257.5	260	261.8	263	38.6	17.20%
Worcester	473.2	46,559	50,181	51,196	51,313	51,454	51,514	98.4	106	108.2	108.4	108.7	108.9	10.5	10.60%

[19] Maryland Department of Planning, *2011 Maryland Statistical Handbook*, at 6, *available at* http://www.mdp.state.md.us/msdc/md_statistical_handbook11.pdf.

In addition, between 2006 and 2010, the rate of home ownership in 12 of the 17 coastal counties exceeded the Statewide rate of 69 percent, and many of the housing units in the coastal zone were constructed after 1999.[20] Taken as a percentage of the overall housing stock in the jurisdiction, Baltimore City had the lowest percentage of new construction at 3.3 percent, whereas St. Mary's County had the highest, at 19.4 percent.[21] The median value of all owner-occupied housing units in Maryland is $329,400. In nine counties -- Anne Arundel, Calvert, Carroll, Charles, Frederick, Howard, Montgomery, Queen Anne's and Talbot -- the median values exceed the Statewide median value. Five of those counties are located in the coastal zone. Of the 17 jurisdictions in the coastal zone, Calvert County had the highest median housing value of $392,000, while Somerset County had the lowest, at $155,900.[22]

Table 3

1	Calvert	$392,900
2	Queen Anne's	$375,700
3	Anne Arundel	$370,100
4	Charles	$355,800
5	Talbot	$352,400
6	St. Mary's	$327,800
7	Prince George's	$327,600
8	Harford	$298,800
9	Worcester	$289,100
10	Kent	$281,100
11	Baltimore	$269,900
12	Cecil	$261,200
13	Caroline	$228,100
14	Dorchester	$205,000
15	Wicomico	$195,100
16	Baltimore City	$160,400
17	Somerset	$155,900
Ranking of 2011 Median Housing Values		

Taken together, these data suggest that in Maryland's coastal zone, there are more people living more closely together in higher valued, relatively new homes than there were just a decade ago. According to the Property Casualty Insurance Association of America ("PCI"), the number of insured households also has increased in these areas. "From 2005 to 2009, the number of insured housing units in Baltimore County and Anne Arundel County grew more than 10 percent. Similarly, the number of insured housing units in Calvert, Charles and St. Mary's counties increased 7.5 percent while Eastern Shore insureds grew the most, 13.4 percent, over this period."[23] In written comments filed after the conclusion of the Hearing, State Farm Fire

[20] U. S. Census Bureau, 2006-2010 American Community Survey.
[21] U. S. Census Bureau, 2006-2010 American Community Survey.
[22] U.S. Census Bureau, http://quickfacts.census.gov.
[23] Exhibit 8, *PCI Special Report: Availability and Affordability of Personal and Commercial Property and Casualty Insurance in Maryland's Coastal Areas* at 2, 7.

and Casualty Company, the largest homeowners insurer in Maryland, stated that "[m]anaging [its] coastal exposure has become more important as more people move to the coast," and that "[a] hurricane on the coast today can cause dramatically higher losses than when the coast was less populated."[24]

IV. Maryland's Coastal Property Insurance Marketplace

A. Types of Property Insurance[25] Policies Available to Maryland Homeowners, Renters, and Businesses

1. Homeowners Policies

A homeowners insurance policy provides coverage for a residential dwelling, appurtenant structures, contents, additional living expenses, liability and medical payments to others. Coverage for renters and condominium unit owners also is written on forms that are designated as homeowners policies. In its most expansive form, a homeowners policy provides replacement cost coverage against all risks, unless otherwise excluded. Other types of homeowners policies provide coverage only for named perils (causes of loss), or on an actual cash value (depreciated) basis.

2. Dwelling Fire Policies and Allied Lines Policies

As an alternative to homeowners policies, "dwelling policies" or "dwelling fire policies" provide protection against specifically named perils (fire and extended coverage for the perils of windstorm, hail, explosion, riot, smoke, vandalism, malicious mischief, civil commotion and the fire-related water damage) only for the dwelling and contents. Allied lines policies often are purchased in conjunction with dwelling fire policies to provide additional property coverage for named perils such as sprinkler leakage, rain, non-fire related water damage and earthquake.

3. Commercial Policies

A commercial property can be used for any number of purposes or business pursuits; therefore, underwriting a commercial property risk is much more complex than underwriting a personal property risk. Not only is information required regarding the structure(s) being insured, but also regarding improvements or alterations made to serve the business' interests. As a result, the types of coverage provided under a commercial property policy can and do differ depending on the risk being insured.

[24] Exhibit 27 at 1.

[25] "'Property insurance' means insurance on real or personal property on land, in water, or in the air or an interest in real or personal property against loss or damage from any hazard or cause and against loss that is consequential to the loss or damage.''' It "includes fire insurance, flood insurance, extended coverage insurance, homeowners insurance, farm owners insurance, allied lines insurance, earthquake insurance, growing crops insurance, aircraft physical damage insurance, automobile physical damage insurance, glass insurance, livestock insurance, and animal insurance." "'Property insurance' does not include insurance against legal liability for loss or damage to real or personal property." Ins. Art. § 1-101(gg)(1)-(3).

B. Issuers of Policies to Maryland Homeowners, Renters and Businesses

1. Admitted and Nonadmitted ("Surplus Lines") Insurers

In Maryland, property insurance is provided to consumers by authorized insurers or surplus lines insurers. An authorized insurer, sometimes referred to as an "admitted" insurer, holds a certificate of authority issued by the Commissioner, and its business practices are subject to the MIA's full regulatory authority with respect to the sale, advertising, underwriting, rate making and claims handling of insurance policies issued and delivered in the State.

Surplus lines insurance is available to Marylanders who cannot obtain insurance from an authorized insurer. Generally speaking, a property risk cannot be underwritten by a surplus lines insurer unless a diligent search has occurred and the risk has been declined by three authorized insurers conducting business in Maryland. Surplus lines insurers do not hold a certificate of authority issued by the Commissioner. Accordingly, all policies written in the surplus lines market must be endorsed or stamped as follows: "This insurance is issued by a non-admitted insurer not under the jurisdiction of the Maryland Insurance Commissioner."[26] Surplus lines insurers are not required to file their rates or forms with the MIA. Some non-admitted companies may utilize policy forms developed by rating organizations such as the Insurance Services Office (ISO), just as admitted insurers do;[27] however, the MIA would be unaware of any changes or modifications that non-admitted carriers may have made to those forms.

Table 4 below summarizes the annual homeowners insurance premiums written by authorized insurers and surplus lines insurers in Maryland from 2009 through 2011:[28]

Table 4

Year	Type	Homeowners	% Change
2009 Total	Admitted	1,247,409,767	
2010 Total	Admitted	1,276,321,441	2.3%
2011 Total	Admitted	1,310,970,372	2.7%
2009 Total	Surplus	803,392	
2010 Total	Surplus	939,493	16.9%
2011 Total	Surplus	1,363,446	45.1%

As indicated by Table 4, homeowners insurance written in the surplus lines market has increased by 16.9 percent from 2009 to 2010, and by an additional 45 percent from 2010 to 2011. As a percentage of the total homeowners insurance market (both admitted and non-admitted),

[26] Ins. Art. § 3-308.
[27] Tr. 17.
[28] NAIC, *Market Analysis Share Report for 2009, 2010 and 2011*, available by contacting the NAIC at 816-783-8300.

however, the increase in market share for surplus lines carriers is negligible, rising from 0.06 percent in 2009 to 0.10 percent in 2011.

Table 5 below summarizes annual dwelling fire and allied lines premiums written by authorized insurers and surplus lines insurers in Maryland from 2009 through 2011. [29] As Table 5 illustrates, there were more than $151 million in dwelling fire insurance premiums and $102 million in allied lines insurance premiums written in Maryland in 2011 by admitted and non-admitted insurance companies. Of that total, 23 percent of the dwelling fire insurance premiums and 19 percent of the allied lines premiums were written in the non-admitted market. From 2009 through 2011, there has been a decline in the percentage of dwelling fire and allied lines premiums written in the surplus lines market.

Table 5

Year	Type	Fire	% Change	Allied lines	% Change
2009 Total	Admitted	116,168,593		80,142,306	
2010 Total	Admitted	111,351,013	-4.1%	75,504,133	-5.8%
2011 Total	Admitted	116,057,942	4.2%	83,020,942	10.0%
2009 Total	Surplus	38,894,323		21,923,161	
2010 Total	Surplus	33,974,818	-12.6%	18,201,109	-17.0%
2011 Total	Surplus	35,242,178	3.7%	19,678,194	8.1%

Table 6 below combines premium information for all three types of residential property insurance policies described above: homeowners, dwelling fire, and allied lines. Taken together, admitted carriers' premiums increased slightly from 2009 to 2010, and again from 2010 to 2011. Surplus lines carriers' premiums were more variable, with a substantial decline from 2009 to 2010, and partial recovery from 2010 to 2011.[30]

Table 6

Year	Type	Homeowners	Fire	Allied Lines	Total	% Change
2009	Admitted	1,247,409,767	116,168,593	80,142,306	1,443,720,666	
2010	Admitted	1,276,321,441	111,351,013	75,504,133	1,462,176,587	1.3%
2011	Admitted	1,310,970,372	116,057,942	83,020,942	1,510,049,256	3.3%
2009	Surplus	803,392	38,894,323	21,923,161	61,620,876	
2010	Surplus	939,493	33,974,818	18,201,109	53,115,420	-13.8%
2011	Surplus	1,363,446	35,242,178	19,678,194	56,283,818	6.0%

In 2011, surplus lines carriers wrote approximately 3.6 percent of Maryland's overall residential property insurance premium, compared with 3.5 percent in 2010 and 4.1 percent in 2009. At the

[29] *Id.*
[30] *Id.*

Statewide level, at least, there does not appear to be a clear or substantial trend toward surplus lines carriers commanding a greater share of the residential property insurance market.

Finally, Table 7 below summarizes annual property insurance premiums written by authorized insurers and surplus lines insurers in Maryland from 2009 through 2011 for commercial multi-peril (property) insurance: [31]

Table 7

Year	Type	Commercial Multi-Peril (Property)	% Change
2009 Total	Admitted	340,205,788	
2010 Total	Admitted	338,616,195	-0.5%
2011 Total	Admitted	346,806,320	2.4%
2009 Total	Surplus	14,911,284	
2010 Total	Surplus	7,785,715	-47.8%
2011 Total	Surplus	11,933,424	53.3%

In 2011, 93 insurers in the admitted market wrote 96.7 percent of the total commercial multi-peril property premiums. The remaining 3.3 percent was written by 34 insurers in the non-admitted market.[32] The amount of commercial multi-peril property insurance premium written in the surplus lines market increased on a percentage basis between 2010 and 2011, from 2.2 percent to 3.3 percent; however, it still was less on both an actual dollar basis and percentage basis than the amount written in 2009.

2. The Joint Insurance Association ("JIA")

The JIA is the property insurer of last resort for Marylanders. As such, it serves those individuals and businesses unable to obtain insurance through the competitive property and casualty insurance marketplace. Originally formed in response to the requirements of "Fair Access to Insurance Requirements (FAIR)" federal legislation, it is composed of all admitted property insurance carriers in Maryland. Although the federal legislation is no longer in effect, §§ 25-401 through 410 of Maryland's Insurance Article provide the basis for the continuing operations of the JIA. The JIA can provide insurance coverage only on properties located within the State of Maryland.[33] The Commissioner has the same regulatory authority over the JIA that she has over domestic insurers authorized to conduct business in Maryland.[34]

The JIA offers homeowners policies (HO2 – Broad Form, HO4 – Tenants Form, HO6 – Condominium Owners Form, and HO8 – Modified Coverage From), dwelling fire policies (DP1

[31] *Id.*
[32] NAIC Market Share Analysis and Aggregate Lines reports for 2011, available by contacting the NAIC at 816-783-8300.
[33] Additional information about the JIA is available at http://www.mdjia.org.
[34] Ins. Art. § 25-408.

– Basic Form), and commercial fire policies (Standard Property Policy Form).[35] The JIA's maximum coverage limit is $1,500,000, on property at any one location, with "habitational sub-limits" for Coverage A (Dwelling) of $455,000 and Coverage B (Other Structures) of $228,000.[36] Seasonal property (defined as property unoccupied for three consecutive months) and mobile homes do not qualify for coverage through the JIA's homeowners program.[37]

In 2010, the JIA's market share was 0.09 percent, representing an approximately 60 percent reduction from its 2005 market share of 0.2 percent.[38] At the Hearing, a representative of the JIA testified that the JIA had written only 134 policies on the Lower Eastern Shore as of September 30, 2011. This represented a slight decline from the number of policies in the same area as of September 20, 2010. In Ocean City proper on the Barrier Islands, only six JIA policies were in force as of September 30, 2011.[39]

C. Use of Catastrophe Modeling

Catastrophe modeling has been used by insurers since the late 1980's. Early models were derived using the very limited historical storm or event data that existed. Over time, catastrophe modelers began using computer simulations to estimate the insurance losses that could be sustained due to a catastrophic weather event. These "stochastic" models have a random probability distribution, which can be analyzed statistically. However, models are not designed to precisely predict future catastrophic event. Future weather events are stochastically generated and probable maximum loss calculations are made using a model along with an insurer's exposure data. The models also consider the exceedance probability, or the probability, on average, that an event of a specified magnitude will be equalled or exceeded in any defined period of time.

By estimating the probable maximum loss and the exceedance probability, catastrophe modeling provides insurers with additional information to consider when making risk management decisions. Supporters of catastrophe models assert that they complement traditional actuarial techniques that may fail to accurately capture low frequency/high severity catastrophe risks for which limited historical data exists. In addition, supporters believe:[40]

- Models give insurers the best estimates of exposures for catastrophic loss, which helps ensure that companies have sufficient funds to cover potential future losses.

[35] Exhibit 9, Memorandum from the Joint Insurance Association to the Maryland Insurance Administration (Dec. 14, 2011).
[36] *Id.*
[37] *Id.*; Tr. 163-64.
[38] Maryland Insurance Administration, *2011 Report on the Effect of Competitive Rating on the Insurance Markets in Maryland* (Dec. 1, 2011).
[39] *See* Tr. 161-63; Exhibit 9A.
[40] PCI, *Twenty Years of Progress: Advances in the Property Insurance Industry Since Hurricane Andrew* (August 22, 2012) available at http://www.pciaa.net; Claire Wilkinson, Insurance Information Institute, *Catastrophe Modeling: A Vital Tool in the Risk Management Toolbox* (February 1, 2008) available at http://www.iii.org/media/research/catmodeling.

- Cat models account for changes in the value of exposed property and changes in building codes and building quality.

- Cat models make it easier to target areas predicted to be at greater risk and eliminate the need for less exposed areas to subsidize areas at greater risk.
- Use of models contributes to rate stabilization because models' assumptions, though adjusted to reflect new research, are more stable than short-term catastrophe loss results.

Criticisms of the use of catastrophe modeling include[41]:

- Private modelers are hired by insurance companies and their interests are aligned with their clients, not with the interest of consumers and insurance regulators.

- There is limited transparency about the modeling process because the computer technology is proprietary intellectual property of the modeling company.

- There is significant variability among and between various models' results and models may be easily manipulated to produce a desired result.

- Current weather data seems to suggest an increase in hurricane activity, but improved weather detection methods may explain this increase.

- Modelers lack reliable wind speed data for most storms.

- There is no model for testing loss estimated for credibility.

After the active storm years of 2004 and 2005, which included hurricanes Katrina and Rita, modelers developed near term models designed to precisely predict the actual number of hurricanes in the next five years. This departure resulted in the prediction of significant increases of hurricane activity in the period of 2005 through 2010. The methodology and assumptions supporting the near term-models were controversial, as were their results. For example, the Risk Management Solutions near-term model predicted annualized losses increasing approximately 50 percent in the Gulf of Mexico/Florida region and 40 percent for the rest of the United States. Current data indicates that the near-term models over-predicted the number of hurricanes. No near-term models have ever been approved for use by the Florida Commission on Hurricane Loss Projection Methodology, which is the only independent, state-funded entity created to ensure the validity of catastrophe models in the United States. The Attorney General of Massachusetts also has criticized the use of near-term models, alleging that homeowners' insurance rates in that state have been inflated because of their use.[42]

During the Hearing, Mr. Wulf, on behalf of RAA, noted that changes to one of the larger catastrophe models resulted in a decreased risk of catastrophic loss in coastal areas and an

[41] Karen Clark & Company, *Public Hearing on Catastrophe Models*, Presentation to the NAIC Spring Meeting (March 29, 2011); Karen Clark & Company, *Near Term Hurricane Models How Have They Performed* (December 2008) available by contacting Karen Clark & Company at http://www.karenclarkandco.com.
[42] http://www.mass.gov/ago/news-and-updates/press-releases/2011/2011-11-17-state-rating-board.html

increased risk inland.[43] According to Mr. Carter, on behalf of MAMIC, "[d]epending upon a carrier's footprint in the Mid-Atlantic area," such changes can have a dramatic impact on a company's required reinsurance purchases and it forces carriers to "look hard at their territorial and aggregate exposures in an effort to spread risk."[44] It may not be enough for carriers to simply reduce their risks in traditional coastal areas, when these new models implicate the central and western areas of Maryland. This has a particularly significant impact for smaller companies.[45]

Furthermore, through one of its exhibits, the PICD pointed out that models often are given the imprimatur of pure science when in fact models contain scientific data as well as a number of subjective factors such as judgment calls, expert opinions, estimates, and assumptions.[46] While many urge caution, some in industry argue that States should allow the use of models without prohibition and that transparency should be further limited by passing legislation to "protect business sensitive data, along with admonitory language to prevent political suppression of mode-derived rates."[47]

In a March 2008 report, the Task Force on the Availability and Affordability of Property Insurance in Coastal Areas made a number of recommendations, including the following:

> Require any insurer that seeks to use catastrophe modeling as a basis for its rating and/or underwriting to have its catastrophe model reviewed and approved for use by the Insurance Commissioner. This recommendation would require legislation that would be supplemented by regulation.

As a result, legislation was passed which has been codified as § 19-211 of the Insurance Article. Insurers that utilize catastrophe models in Maryland to set homeowners insurance rates or to prohibit underwriting because of the geographic location of the risk must file the description of the model with the Commissioner and make arrangements for the vendor of the model to explain the data used in the model and the manner in which the output is obtained. Since this legislation's enactment in 2008, the MIA has received over 60 filings from insurers to increase rates, prohibit underwriting in certain geographic areas of the State, or both, based in part on catastrophe models.

D. Building Codes

Development, adoption, implementation and adherence to strong building codes are proven means of managing and mitigation of risks in coastal communities.[48] The written

---

[43] Tr. 47;
[44] Exhibit 10 at 7.
[45] *Id.*
[46] Exhibit 31, Karen Clark & Company, *Using Catastrophe Models and other Tools to Assess Hurricane Risk*, Presentation to the NAIC Fall Meeting (November 4, 2011).
[47] Exhibit 4, *American Insurance Association Natural Catastrophe Agenda – To Reduce Loss and Promote Stability* at 4.
[48] *See A Report to the Governor and the Maryland General Assembly: A Review of Current Statewide Building Codes and Recommendations for Enhancement in Coastal Regions of Maryland* at 3-4 (October 1, 2010), *available*

testimony of James J. Whittle, on behalf of the American Insurance Association, emphasized the impact of strong building codes and their clear link to the reduction of storm-related damage:

> Florida is the "poster child" for the adoption and enforcement of enhanced building codes, and these efforts have more than proven their worth. The evidence was crystal clear in the aftermath of the four hurricanes in 2004. Hurricane Charley – a very intense, Category 4 storm – provided a true test of the newest IRC building codes. One only had to compare homes in the same vicinity built to pre-building code standards and those constructed after the Florida Building Code went into effect. There outcome was dramatic as properly and inspected newer structures fared much better than structures built under the older codes. In fact, a study conducted by Applied Insurance Research-Worldwide (AIR) after Hurricane Andrew found that insured losses would have been reduced by approximately 40% following a storm similar to Hurricane Andrew if all structures were constructed in accordance with the current Florida Building Code. This difference in total probable losses would also be due to a lower impact on personal property losses – furniture, clothing, photo albums, and so forth – as well as structural losses. So, the dreadful, emotional impact of not being able to "replace memories" is itself lessened through smaller losses of personal possessions.[49]

This view was echoed by the Property Casualty Insurance Association of America's Special Report that was introduced during the Hearing:

> By increasing construction standards to make buildings more resistant to damage, the frequency and severity of property claims will decrease over time and provide a positive stabilizing effect on costs. Lower amounts of property damage speeds up the recovery process, causes less disruption for property owners and puts less pressure on the insurance marketplace. Studies have shown that for each dollar increase in construction costs, there is a long-term savings of $3 to $16.
>
> Studies have also found a large reduction in the number of insurance claims filed for homes built under Florida's statewide building code. According to the Insurance Institute for Business and Home Safety, homes built after the post-Hurricane Andrew codes in Florida had 30 percent fewer losses than homes built in the 1980s and 1970s. And only 10 to 20 percent of homes built under the statewide Florida code had filed claims, compared with about 50 percent of homes built before the post-Andrew codes.

---

at http://www.dhcd.maryland.gov/website/About/PublicInfo/Publications/documents/HB-1353_FinalReport_toOCM_09-28-2010%20Caroline.pdf.

[49] Exhibit 3 at 10.

> In order to be effective, enforcement of a uniform statewide building code is critical. Enforcement ensures compliance with the building code and is a key factor in saving lives and minimizing the impact of a natural disaster on overall losses and premiums.[50]

In Maryland, the Department of Housing and Community Development (DHCD) is responsible for adopting the Statewide building code, referred to as Maryland Building Performance Standards (MBPS). The MBPS is based on the International Building Code and the International Residential Code and also may contain recommendations from the State Fire Marshall and the Maryland Department of Labor, Licensing and Regulation. Although Maryland law requires local jurisdictions to adopt the MBPS, the jurisdictions are permitted to amend the standards "to suit local conditions."[51] The Honorable James N. Mathias, Jr. provided verbal and written testimony regarding steps that Ocean City has taken to enhance the ability of buildings in that community to withstand damage.[52] However, local jurisdictions also may amend the MBPS in ways that could weaken protections against wind and other storm damage. According to Mr. Whittle, on behalf of AIA, the impact of allowing the counties to reduce MBPS standards means that "some of your most exposed properties and residences and communities may not have the best code."[53]

Following the Hearing, Allstate submitted a December 31, 2011 report by the Insurance Institute for Business & Home Safety (IBHS) entitled, *Rating the States: An Assessment of Residential Building Code and Enforcement Systems for Life Safety and property Protections in Hurricane-Prone Regions*.[54] The report provides an "analysis, evaluation and comparison of regulations and processes governing residential building construction in the 18 states most vulnerable to catastrophic hurricanes along the Atlantic Coast and Gulf of Mexico." On a scale of 100, IBHS assigned a score of 73 to Maryland, ranking it tenth among the 18 states surveyed. The report cited weaknesses reflected in Maryland's score included the ability of local jurisdictions to amend the MBPS, thereby defeating the goal of uniformity and potentially weakening protections; deficiencies in inspector certification and training, such as a lack of an inspector designation program, no requirement for inspectors to take a code class prior to becoming certified and no mechanism for consumers to file a complaint against inspectors; no testing of general contractors prior to licensing; and a lack of continuing education requirements for those trades requiring an examination (plumbing, mechanical and electrical).[55]

---

[50] Exhibit 8 at 13 (internal citations omitted). *See also* testimony of W. Minor Carter on behalf of Maryland Association of Mutual Insurance Companies, Exhibit 10 at 14-15; Tr 76-77, 113-115, 124, 136-137.
[51] *A Report to the Governor and the Maryland General Assembly: A Review of Current Statewide Building Codes and Recommendations for Enhancement in Coastal Regions of Maryland* at 4 (October 1, 2010), available at http://www.dhcd.maryland.gov/website/About/PublicInfo/Publications/documents/HB-1353_FinalReport_toOCM_09-28-2010%20Caroline.pdf.
[52] Exhibit 7 at A1.
[53] Tr. 77.
[54] Exhibit 32; *also available at* http://64.16.194.32/content/data/file/ibhs-rating-the-states.pdf.
[55] *Id*. at 10.

The conclusions reached by DHCD in its report to the Governor and General Assembly suggest that adoption of the MBPS, without amendment, in the coastal communities may lead to construction that is adequate, but not optimal.[56] To optimize protection, the report recommends the adoption of enhanced designs in areas prone to high winds and flooding.

V. Availability of Property and Casualty Insurance in Coastal Areas of the State

Maryland's homeowners insurance marketplace is moderately concentrated, but competitive.[57] There currently are over 130 admitted carriers underwriting homeowners insurance in Maryland, generating a total of more than $1.31 billion in premium for 2011. The premium volume for homeowners insurance underwritten by nine (9) non-admitted insurers was $1.36 million in 2011. When expressed as a percentage of the written premium, the top eight insurer groups underwrite more than 75 percent of the total homeowners coverage offered throughout the state of Maryland. The market share of the top two insurer groups (State Farm and Allstate, respectively) expressed as a percentage of the homeowners insurance written premium is 36 percent.[58]

As summarized more fully below, testimony from a broad range of interested parties supports the conclusion that Maryland's property and casualty insurance market remains competitive throughout the State, and that personal and commercial property and casualty insurance is available in the State's coastal region.

A. Insurer Trade Associations' Perspectives

The MIA received oral testimony or written comments or testimony from representatives of six insurer trade associations addressing the question of the availability of property and casualty insurance in coastal areas of the State: (1) James J. Whittle, on behalf of the American Insurance Association ("AIA"); (2) Robert Enten, Don Griffin, and Jeff Junkas on behalf of Property and Casualty Insurers Association of America ("PCI"); (3) Robert Detlefesen, Ph.D., on behalf of the National Association of Mutual Insurance Companies ("NAMIC"); (4) W. Minor Carter, on behalf of the Maryland Association of Mutual Insurance Companies ("MAMIC"); (5) Bryson Popham on behalf of the Maryland Excess and Specialty Lines Association ("MESLA"); and (6) Matthew Wulf, on behalf of the Reinsurance Association of America ("RAA").

From AIA's perspective, Maryland's property insurance market is "strong and stable."[59] According to AIA (citing A.M. Best data), property insurers gained as well as lost market share

[56] *A Report to the Governor and Maryland General Assembly: A Review of Current Statewide Building Codes and Recommendations for Enhancements in Coastal Regions of Maryland* at 11-14 (Oct. 1, 2010), *available at* http://www.dhcd.maryland.gov/website/About/PublicInfo/Publications/documents/HB-1353_FinalReport_toOCM_09-28-2010%20Caroline.pdf.
[57] Maryland Insurance Administration, *2011 Report on the Effect of Competitive Rating on the Insurance Markets in Maryland* (Dec. 1, 2011) (Herfindahl-Hirschman Index (HHI) of 1,116 suggested a modest reduction in market concentration for homeowners insurance in 2010 from the prior year).
[58] *NAIC-Market Analysis Share Report for 2011*, available by contacting the NAIC at 816-783-8300.
[59] Tr. 65.

in Maryland during the period from 2008 through 2010.[60] During the same three-year period, market share for the top ten writers in the State was reduced by .5 percent, demonstrating less concentration and greater competition.[61] AIA views this as "a perfect example of the homeowners' insurance market working exactly as it should when given the opportunity."[62]

On behalf of PCI, Mr. Griffin testified that, "compared to other states with coastal exposure, Maryland probably has one of the most competitive markets."[63] PCI reported that, "The data shows that homeowners insurance is generally available and affordable for Maryland residents in all areas of the state. Market competition is extremely strong throughout the state."[64] According to PCI, since 2005, an additional 84 property and casualty insurers have entered Maryland's insurance market, increasing the total to nearly 800.[65] This figure includes 23 additional surplus lines carriers, for a total of 114 surplus lines writers, all of whom are believed to offer products in coastal areas of the State.[66] PCI concluded that, "[b]y all standard indicators, the evidence strongly points to residents in this state having good access to homeowners coverage in coastal areas at relatively low prices."[67] "Maryland has a positive insurance environment which is conducive to promoting long-term availability and affordability of property casualty insurance for the benefit."

Dr. Detlefsen, on behalf of NAMIC, cautioned against State-imposed rate suppression and underwriting restrictions in catastrophe-prone coastal regions, which, he said, are "largely responsible for insurance availability problems in coastal areas."[68] According to Dr. Detlefsen, "if government rate regulation prevents insurers from covering their claim costs, replenishing surplus reserves to pay future claims, and making a profit, then many have no choice but to exit the market. The surest way to increase the supply of insurance in catastrophe-prone coastal regions is to remove government restrictions on pricing and underwriting."[69]

On behalf of MAMIC, Mr. Carter testified: "the members of MAMIC firmly believe that the market is working and no changes are warranted at this time. However, given the increasing number of catastrophes and the introduction of new hurricane models, there may be constriction of the marketplace due to the lack of capacity in the future."[70] He noted that when determining the amount of coastal business they will write, insurers consider how their business plans will be viewed by the MIA, reinsurers, and insurance rating agency A.M. Best.[71]

---

[60] *See* Exhibit 3 at 5.
[61] *Id.*
[62] *Id.; see also Maryland Insurance Administration, 2011 Report on the Effect of Competitive Rating on the Insurance Markets in Maryland* at 4 (Dec. 1, 2011) (suggesting a modest reduction in market concentration for homeowners insurance in Maryland between 2009 and 2010).
[63] Tr. 123.
[64] Exhibit 8 at 1, *PCI Special Report: Availability and Affordability of Personal and Commercial Property and Casualty Insurance in Maryland's Coastal Areas* at 1 (Dec. 13, 2011).
[65] *Id.* at 5 (citing National Association of Insurance Commissioners database, via Highline Data LLC).
[66] *Id.* at 6.
[67] *Id.* at 16.
[68] Exhibit 5, Statement of Robert Detlefsen on behalf of the National Association of Mutual Insurance Companies.
[69] *Id.*
[70] Tr. 175-76.
[71] Tr. 213-15.

Speaking for MESLA, Mr. Popham noted that unlike the JIA residual market mechanism, surplus lines insurers are not obligated to accept any risk or to do business in Maryland.[72] Mr. Popham testified that "we have a vibrant and vigorous surplus lines market in Maryland," and that his clients report "that they have no problem with market availability."[73] He highlighted one member of MESLA, All Risks, Ltd. ("All Risks"), which he stated is one of the largest surplus lines brokers in the country, is located in Maryland, and does business in Maryland. Surplus lines carriers for which All Risks writes include Lloyds of London, Lexington, Markel, United National and Scottsdale, all of whom "are writing freely in Maryland today."[74] According to Mr. Popham, the coverage terms of residential property insurance policies offered by these nonadmitted carriers "typically are similar, if not identical, to the terms offered by admitted carriers."[75] In Worcester County, the average risk written by All Risks is under $300,000.[76]

Testifying on behalf of the RAA, Mr. Wulf emphasized the role of reinsurance in the availability of property and casualty insurance in Maryland markets. He stated that reinsurance "allows small carriers to build capacity and compete in the market with some of the larger carriers."[77] According to RAA, "Reinsurers, utilizing their global resources, play an essential role in the U.S. economy and help protect America by spreading the risk and impact of natural disasters among different market segments. For the unparalleled 2005 hurricane losses, U.S. insurers retained 38.9% of the loss, Bermuda reinsurers 24%, U[.]S[.] reinsurers 11.5%, European reinsurers 12.6%, Lloyds 12.3% and all others .7%."[78] RAA maintains: "There is no reinsurance availability problem. After the massive influx of capital to the reinsurance sector since 2005, the temporary period of reinsurance demand exceeding supply has ended."[79]

Mr. Carter, on behalf of MAMIC, noted that although "[t]he Maryland insurance market is working at this time, . . . demands for increased reinsurance coverage could restrict the market. Smaller companies with a relatively concentrated geographic area may have difficulty if capacity is reduced. Nonetheless, at this point, action by regulators is not warranted."[80]

B. Producers' and Producer Trade Associations' Perspectives

Two producer trade associations and five producers doing business in coastal areas of the State provided oral and written testimony in connection with the Hearing. Specifically, the MIA heard from: (1) The Independent Insurance Agents of Maryland ("IIAM"), a state trade association representing over 200 independent insurance agencies in the State; (2) Insurance Agents and Brokers of Maryland ("IABM"), a state trade association comprised of approximately 250 member agencies throughout Maryland; (3) Reese Cropper, III, CIRMS, of Insurance Management Group, Inc., in Ocean City, Maryland; (4) George Bradford Reeves, a fifth generation owner of the independent, family-owned Combs, Drury, Reeves Insurance

[72] Tr. 16.
[73] *Id.*
[74] Tr. 17.
[75] *Id.*
[76] Tr. 17-18.
[77] Tr. 43.
[78] Exhibit 2 (citing Dowling and Partners).
[79] *Id.*
[80] Exhibit 10 at 2.

Agency in St. Mary's County; (5) Mike Wheaton, Vice President of the Associated Insurance Centers, Inc., with offices in Ocean City and on the Lower Eastern Shore; (6) E. Larry Sanders, III, CIC, President, Edward L. Sanders Insurance Agency, Inc., with offices in La Plata (Charles County) and Prince Frederick (Calvert County); and (7) James R. Fowler, CPCU, of Fowler Insurance, Inc., a small, independent agency located in Ocean Pines, Worcester County.

In anticipation of the Hearing, IIAM conducted an informal survey of its members regarding the availability and affordability of personal and commercial insurance in coastal areas of the State. The survey results suggested that availability had declined "to a small degree" as compared with two years ago. IIAM attributed this small perceived decline to "the cyclical nature of the markets," however, and concluded that "there are a solid number of carriers from the standard market as well as the excess and surplus lines markets" writing personal and commercial property and casualty insurance in Maryland's coastal region.[81]

Similarly, representatives of IABM testified that, "In communicating regularly with our member agencies on this issue, it is clear that our agents believe that there are still markets available for coastal properties. While some of our agents have experienced a 'clamping down' on coastal properties by not writing new business and not renewing policies, our agents believe that this does not necessitate any regulatory or legislative action at this time."[82]

Mr. Reeves testified that his agency has no problem placing business for families, farmers, and small businesses on the Western Shore. He contracts with ten admitted carriers for personal lines of insurance, and with approximately 15 markets in total, including specialty lines such as Federal crop insurance and as well as surplus lines.[83] Mr. Reeves' agency uses primarily admitted insurers, only occasionally turning to non-admitted carriers for seasonal homes, where occupancy or the condition of the property can be an issue.[84] In Mr. Reeves' view, changes in the markets over the last five years "have not been due to coastal issues or availability," but rather, he suspects, have been "due to the down turn in the economy."[85]

Likewise, Mr. Sanders stated that "[m]any admitted insurance carriers actively write homeowners insurance in Southern Maryland," although "policy terms and conditions may and do vary from carrier to carrier." His agency writes for State Auto, Cincinnati, Selective, Brethren Mutual, and Frederick Mutual, among others. According to Mr. Sanders, "[t]he Southern Maryland Homeowners Insurance marketplace remains competitive with a variety of consumer options."[86]

Both producers with offices in Ocean City also stated that they were not having difficulty placing business. *See, e.g.,* Testimony of Mr. Cropper, Tr. 12 ("Although not all insurance carriers are willing to insure in coastal areas, there's no availability crisis. Firemen's Fund, CHUBB, Chartis, Windsor-Mount Joy, Brethren, are just a few that have been willing to insure some risk in the coastal areas subject to strict and prudent underwriting."); Testimony of Mr.

[81] Tr. 250; Exhibit 22.
[82] Tr. 10; Exhibit 23 at 2.
[83] Tr. 254.
[84] Tr. 258.
[85] Tr. 255.
[86] Exhibit 23 at 5.

Wheaton, Tr. 260 ("We have not had any problem placing business, either standard or excess surplus lines. One way or the other, we're going to find a way to place business."). Mr. Cropper observed that "admitted carriers have been doing far more business in the last ten years than they ever have, I think in my 30 years at the beach."[87] Both witnesses estimated that in Ocean City, they placed approximately two-thirds of their business with surplus lines carriers (Mr. Cropper: 65-70%; Mr. Wheaton: 60-70%).[88] According to Mr. Wheaton, those figures have remained stable over the past 10 years.[89] Mr. Wheaton noted that just a mile outside of Ocean City, "that number goes down dramatically," and that "[i]n Berlin, which is six miles west, pretty much everything there is in the standard market."[90]

Mr. Cropper stated that the products he has seen offered by non-admitted carriers recently have included more coverages than in the past, although he believes they generally lack what he referred to as "the extras," such as coverage for damages to fences or shrubs. In his view, consumers in the non-admitted market are "looking for the trade off of, more economical, looking for the catastrophe coverage, and not all the bells and whistles and low deductibles."[91]

In contrast, through written comments submitted after the Hearing, Mr. Fowler, in Ocean Pines, observed that "availability and affordability for coastal property insurance is a frustrating situation that has gotten worse."[92] His agency represents seven admitted personal lines carriers: Safeco, Fidelity National, Fireman's Fund, Peninsula, Encompass, Foremost and Universal (Arrowhead). He noted that, "[i]n the past couple of years these insurers have implemented more restrictive 'coastal' underwriting guidelines to limit 'new' business and/or increased the annual premiums for the existing book of business. The effect is that our agency no longer has a viable 'admitted' market for new Homeowners business."[93] According to Mr. Fowler, for new homeowners business, his agency "can only offer quotes from 'non-admitted' insurers for most Worcester County locations."[94] He specifically identified one such non-admitted insurer that, in his view, "understands the coastal market and offers good coverage options for a reasonable premium."[95] For commercial accounts, his agency is limited to two admitted carriers, both of whom, he said, have underwriting restrictions based on distance to the coast or tidal water.[96]

[87] Tr. 25-26.
[88] Tr. 32, 258.
[89] Tr. 257.
[90] Tr. 258.
[91] Tr. 30-31.
[92] *See* Exhibit 30.
[93] *Id*.
[94] *Id*.
[95] *Id*.
[96] *Id*.

C. Consumer and Consumer Advocate's Perspectives

Senator James N. Mathias, Jr., Maryland State Senator from Legislative District 38 (which includes significant coastal areas on the Eastern Shore), testified that he believes there is universal agreement that "the availability is there."[97] But while availability is not a concern, "affordability is another matter," as are deductibles, exclusions, and other limitations on coverage.[98]

Susan Cohen, of the PICD, testified that "the market in the coastal region is working," and that the People's Insurance Counsel Division does not receive complaints or inquiries from consumers in coastal areas of the State who cannot find insurance.[99] She stated that surplus lines companies are "filling the gap" created by certain admitted companies who have decided over the last several years not to write policies in certain coastal areas.[100] Ms. Cohen expressed concern over the lack of statutory authority requiring that surplus lines companies file their rates and forms with the MIA, and about a relative paucity of information about their activities in the marketplace.[101] She acknowledged, however, that availability could be impacted if non-admitted carriers decided not to write in Maryland's coastal regions, and that "it's hard for me to say that consumers are really not well served by the non admitted market writing coverage over there."[102]

D. Evidence from the Residual Market

One indicator of the availability of private insurance options for homeowners and businesses is the percentage of business held by the JIA, the State's residual property insurer. In 2010, the JIA's Statewide market share was 0.09 percent, representing an approximately 60 percent reduction from its 2005 market share of 0.2 percent. These figures suggest that homeowners insurers are competing for greater market share by accepting more risk.[103]

PCI concurred, noting: "While the private market is expanding, in contrast, the residual market mechanism (*i.e.*, the Maryland Joint Insurance Association) intended to be the 'market of last resort' and supplement the private market – not compete with or displace it – experienced a 40 percent reduction in both the number of applications and policies issued, according to the latest data available."[104]

With respect to coastal areas of the State specifically, the AIA provided testimony showing that the number of JIA policies in force in coastal areas in the State in 2011 ranged from a low of 8 in Calvert County (down from 12 in 2010) to a high of 1331 in Baltimore City (down from 1700 in 2010).[105] Overall, there was an approximately 16.69 percent decline in JIA

[97] Tr. 116-18.
[98] Tr. 118.
[99] Tr. 218.
[100] Tr. 219-20.
[101] Tr. 222-24.
[102] Tr. 225.
[103] Maryland Insurance Administration, *2011 Report on the Effect of Competitive Rating on the Insurance Markets in Maryland* at 4 (Dec. 1, 2011).
[104] Exhibit 8 at 1-2.
[105] Exhibit 3 at 3.

policies in coastal counties and Baltimore City between September 30, 2010 (2,655 policies) and September 30, 2011 (2,212 policies).[106] According to the AIA: "These numbers suggest that there is a healthy homeowners insurance market in coastal Maryland."[107]

The AIA further testified:

> According to U.S. Census Bureau data estimates, there were 1,606,243 households in the coastal areas of Maryland in 2009. MJIA policies currently in force (2212) represent only .1377% of all those households. In other words, [JIA] coastal exposures are exceptionally small and actually declining, whereas the private market continues to meet the needs of all but a few coastal policyholders.
> ***
> When compared to Florida, the absence of a coastal problem in Maryland is profound. As of December 6, 2011 Florida Citizens Property Insurance Corporation, the state owned property residual market, had 1,482,707 policies in force with a total exposure of over $515 billion dollars in insured valued. Moreover, Florida Citizens' policy in force count grew 42 percent in the 21 months ending Sept. 30th 2011. Indeed, since January 1st policies grew from just under 1.3 million to 1,482,707, or over 14% in less than a year. In fact, Florida Citizens is now the largest homeowner insurer in the state with 16% of the market and a larger still share of the coastal market in Florida. Florida Citizens has more than $515 Billion in total exposure whereas the total exposure for [JIA] (both coastal and non-coastal) is a little over $456 Million. Thus, Maryland's residual market exposure is an astounding one thousandth that of Florida.[108]

E. Summary and Conclusions

With the exception of Mr. Fowler, Hearing participants concurred that property and casualty insurance is available for homeowners and businesses in coastal areas of the State. Anecdotal evidence suggests that in certain coastal areas – Ocean City, in particular − non-admitted carriers meet a large share of that need. As discussed in Section IV.B. above, however, non-admitted carriers' increase in market share Statewide was negligible as a percentage of the total homeowners insurance market from 2009 to 2011, and there was a decline in the percentage of fire and allied lines premiums written in the surplus lines market during that same period. The JIA's very small residual market share, even in coastal areas, supports a conclusion that competitive insurance products are available for homeowners in those areas.

An issue that many witnesses raised, however, was a need for enhanced consumer understanding about the insurance products they are purchasing, beyond an understanding of the premiums they pay.[109] According to producer Larry Sanders in La Plata, "[c]onsumers emphasize policy pricing too greatly with little attention given to coverages and policy

[106] *Id.* at 4.
[107] *Id.*
[108] *Id*. at 4.
[109] *See, e.g.,* Tr. 34-37, 129-133, 252-253.

language."[110] Coverage limits and deductible amounts were identified as aspects of insurance policies about which some consumers are unaware. One witness suggested a signed disclosure at the time of purchase as one possible option to address this issue.[111]

VI. Affordability of Property and Casualty Insurance in Coastal Areas of the State

A. Premiums in Maryland and in Coastal Areas of the State

AIA and PCI both noted the large number of admitted and non-admitted insurers competing for business in Maryland, which fosters competitive pricing and helps maintain affordability.[112] According to the National Association of Insurance Commissioners' most recent data, for 2009, the total average annual premium for dwelling fire and homeowners owner-occupied policies in Maryland compared favorably to the nationwide average ($778 in Maryland versus $875 nationally), and fell slightly below the national median (24th lowest of 51 jurisdictions).[113]

Producers' observations regarding premium rates in recent years were mixed. On the one hand, in connection with its informal member survey, IIAM reported: "When asked about the issue of affordability compared with two years ago, on average, our members felt that it had . . . worsened to a small degree. Again, this change reflects the normal ebb and flow of the markets and the nature of the risk."[114] In his written comments, Mr. Fowler observed that although some carriers offer renewals in certain areas at "reasonable prices," other carriers' 2011 renewal premiums increased by 20 percent to 60 percent in the areas of Ocean Pines, Berlin, Willards, Bishopville, and Ocean City.[115] In Mr. Cropper's view, "Premiums and deductibles along coastal regions may be higher than a consumer feels is fair. However, owning properties in high risk areas such as the coastline . . . means the cost of living in those areas is going to be higher."[116] According to Mr. Popham, testifying on behalf of MESLA, average premiums for residential property insurance in Worcester County "are around $1,500."[117]

The Maryland Insurance Administration issues a report entitled, *Homeowners Insurance: A Comparison Guide to Rates* (the "Guide"), in February and August of each year. The Guide provides rates from several dozen participating companies for six different homeowners, condominium and renters policy scenarios (reflecting the home value, type of construction, deductible amounts, and contents and liability coverage), for a particular zip code in each county and Baltimore City. As PCI noted, the Guide reflects a wide range of rates available in at least certain coastal areas of the State. For example, in the 2011 Guide, "annual insurance company rates for Special Form HO-3 in Queen Anne's County for a house with frame construction,

---

110 Exhibit 23 at 5.
111 Tr. 130.
112 Exhibit 3 at 5; Exhibit 8 at 6.
113 NAIC, *2009 Dwelling Fire, Homeowners Owner-Occupied, and Homeowners Tenant and Condominium/Cooperative Unit Owner's Insurance: Market Distribution and Average Cost by Policy and Amount of Insurance* (Dec. 2011).
114 Exhibit 22 at 1.
115 Exhibit 30.
116 Tr. 12-13.
117 Tr. 17-18.

$100,000 liability coverage, $500 deductible, and water and sewer endorsement can vary anywhere between $487 and $1,654[,]" indicating, in PCI's view, that "homeowners are able to select from a wide range of competitive rates offered by many different carriers."[118]

Notwithstanding the range of rates available in some areas, however, an analysis of the rates provided by insurers from February 2007 through February 2012 suggests that, on average, homeowners insurance rates have risen moderately each year, with changes varying by geographic region. Although coastal county rates are somewhat higher than non-coastal rates, on average, non-coastal county rates have increased slightly more than coastal county rates during this time period. But any rate increase - however moderate - may be especially difficult for policyholders in certain coastal areas of the State to afford. According to U.S. Census Bureau data, in six coastal counties and in Baltimore City the percentage of the population with incomes below the federal poverty level from 2006 to 2010 exceeded the Statewide average of 8.6 percent -- in some cases, such as Baltimore City, Somerset County, and Wicomico County, by substantial margins.

Table 8

Coastal Zone	% Population Below Federal Poverty Level
Anne Arundel	5.3
Baltimore City	21.3
Baltimore County	8.1
Calvert	4.4
Caroline	11.5
Cecil	9.0
Charles	5.2
Dorchester	13.4
Harford	5.6
Kent	12.2
Prince George's	7.9
Queen Anne's	5.5
St. Mary's	7.1
Somerset	18.6
Talbot	6.1
Wicomico	14.3
Worcester	10.1
Statewide Average	8.6

Source: U.S. Census Bureau, http://quickfacts.census.gov.

[118] Exhibit 8 at 9.

B. Key Factors Contributing to Premium Rates

At least three key contributors to premium rates were identified in the course of these proceedings. First, Hearing participants pointed to increased exposure as evidenced by higher than average losses in recent years and the projections from new catastrophe models.[119] Second, on behalf of the AIA, Mr. Whittle stressed the contribution of rising property repair and replacement costs:

> [I]t's very important that escalation in property repair costs and replacement costs rising is a continuing and ongoing issue. Those industries continue to do their business, and the costs of that are obviously worked into insurer's premium that the consumer pays. So as the costs to repair and replace properties continue to escalate, that is a necessary cost that's built into a premium structure.[120]

Third, some witnesses emphasized the cost of reinsurance as a key contributor to premium rates, although this point was the subject of some debate. According to RAA:

- Brokers report that:
    - Early 2011 saw a continuing (since 2007) downward trend in reinsurance catastrophe pricing.
        - Brokers reported price decreases of 5% to 10%, on a risk-adjusted basis, for U.S. property catastrophe treaties renewing at January 1 that include hurricane exposure. These price drops follow decreases of 5% to 25% (10% to 25% for Florida June 1 business) in 2010.
        - Mid-year broker reports showed renewal pricing ranging from flat to up 15%.
    - Brokers report that the effect on pricing from higher than average losses, and catastrophe model changes, has been mitigated by reinsurers' strong balance sheets and a supply that continues to exceed demand for reinsurance.[121]

At the Hearing, Mr. Wulf clarified: "[W]e've seen over the past three, four years, that the cost [of reinsurance] has actually fluctuated very little to actually gone down – the rate, excuse me. But the cost could go up if you purchase more reinsurance."[122]

[119] *See, e.g.*, Exhibit 2 at 2, 4 (RAA); Tr. 176-81 (MAMIC).
[120] Tr. 71.
[121] Exhibit 2 at 4 (emphases omitted).
[122] Tr. 47.

In written comments submitted after the Hearing, however, Allstate stated:

> [T]he reinsurance market has shown extreme price volatility over the past 20 years. Increased hurricane activity in the Atlantic has led to increased demand, limited supply, and skyrocketing reinsurance prices. Reinsurers are quick to emphasize a modest decline in reinsurance rates in recent years, but they carefully avoid discussing the fact that reinsurance rates remain significantly higher than their pre-Katrina levels, and show no signs of ever retreating. In the wake of catastrophic events this year, the reinsurance market in the United States has again tightened, demonstrating the vulnerability of the market to events around the globe. Allstate is very concerned about the potential adverse impact on 2012 reinsurance prices and availability in light of the hurricanes, earthquakes and tsunamis experienced worldwide during 2011. Predictions made at this hearing of increased capacity and a 'softer' market are no consolation. [123]

Allstate noted that "reinsurance costs are passed on to individual homeowners insurance policyholders in the form of higher premiums" and that "the cost of reinsurance may affect the willingness or ability of a homeowners insurer to assume more risk, thus potentially affecting the availability and affordability of insurance."[124]

On behalf of MAMIC, Mr. Carter testified that reinsurers' rates are "under pressure" due to an increase in disasters in the United States and worldwide.[125] According to Mr. Carter, with the introduction of more sophisticated catastrophe models, insurance industry rating agency A.M. Best now "wants insurers to purchase reinsurance for a 100-year storm, at a minimum, and prefers the companies provide reinsurance for the 250-year storm."[126] MAMIC anticipates that: "As mid-Atlantic exposures estimates increase, the mid-Atlantic insurers will need to buy more capacity from reinsurers. In turn, the reinsurer must either raise more capital to support the needs of the insurers, or the reinsurer must restrict its writing. In any event, reinsurance rates will increase."[127] Such increases can be attenuated, Mr. Carter testified, through insured's deductibles.[128]

C. Percentage Deductibles in the Case of a Hurricane or Other Storm

Until fairly recently, most property and casualty insurers issued homeowners policies with an "all peril" deductible. This meant that regardless of the cause of loss, policyholders would pay a set dollar amount when they filed a covered claim. Over the last few years, some insurers doing business in Maryland have issued policies with a percentage deductible in the event of losses caused either by a hurricane or other storm (in some cases, among other causes of loss). In these circumstances, the insured is responsible for paying a deductible which is a

---

[123] Exhibit 29 at 5. *But see id.* at 1 (Allstate does not currently see in Maryland "a major catastrophic event lead[ing] to a spike in reinsurance costs or a contraction in reinsurance supply, or both").
[124] Exhibit 29 at 5.
[125] Tr. 182-83.
[126] Tr. 186.
[127] *Id.*
[128] *Id.*; Exhibit 10 at 12.

percentage of the Coverage A - Dwelling Limit. For example, if the Coverage A - Dwelling Limit on the policy is $200,000, and the policy is subject to a percentage deductible of 5 percent when damage is caused by a hurricane or other storm, the insured would be responsible for the first $10,000 in damage caused by a covered peril under the policy.

The percentage and use of these deductibles varies by insurer, with the percentage ranging from 1-10 percent of the Coverage A - Dwelling Limit. Some insurers limit percentage deductibles to certain parts of the State, some have mandatory percentage deductibles, others make the percentage deductible an option that consumers may choose, while others continue to use the standard "all peril" deductible.

Insurer trade associations and their members argue that the use of these deductibles allows insurers to continue to offer consumers homeowners coverage in certain parts of Maryland.[129] Others assert that the use of percentage deductibles allows insurers to continue to offer affordable coverage to their policyholders.[130] Still others maintain that percentage deductibles incentivize homeowners to take preventive steps to mitigate the potential for storm-related damage.[131]

Hearing testimony highlighted, however, that consumers may not understand the coverage being provided, especially with respect to the application of percentage deductibles.[132] The MIA's experience after Hurricane Irene also indicated that consumers lacked sufficient understanding of when these deductibles may be imposed and the actual amount of the particular deductible. Also, the required annual statement provided to the policyholders by the insurers appears to be an inadequate means of communicating how and when the percentage deductibles are applied. The MIA has invited and received public comment on draft proposed regulations that would, among other things, require insurers with percentage deductibles to include in the annual statement examples illustrating how a percentage deductible works and what an insured's out-of-pocket obligation would be in those examples.

D. Potential Subsidization Issues

Dr. Robert Detlefsen, on behalf of NAMIC, cautioned against "government rate suppression" that would allow "high-risk property owners to pay artificially low premiums."[133] According to Dr. Detlefsen, such rate suppression "masks the real problem – the growing concentration of people and wealth in high-risk regions – by forcing insurance buyers in low-risk regions to pay inflated priced in order to subsidize the insurance costs of those in high-risk regions."[134] In NAMIC's view, "if government rate regulation prevents insurers from covering their claim costs, replenishing surplus reserves to pay future claims, and making a profit, then

[129] *See, e.g.,* Tr. 74 (AIA) (Percentage and windstorm deductibles "are a necessary part of any insurer's tools in order to manage their exposure.").
[130] *See, e.g.,* Exhibit 26 (MAMIC).
[131] *See* Exhibit 8 at 3 (PCI) (Percentage deductibles "provide incentives for residents to retrofit and strengthen their homes[.]"); Exhibit 27 at 2 (State Farm) ("Insurers must be permitted to utilize deductibles that are sufficient to encourage preparation for disasters by homeowners.").
[132] Tr. 34-37, 129-130, 176-177, 228-229; Exhibit 3 at 7-8.
[133] Exhibit 5 at 3.
[134] *Id.*

many have no choice but to exit the market."[135] NAMIC recommended that "[a]ny special treatment given to lower-income residents in hazard-prone areas who cannot afford the cost of living in those locations should come from general public funding and not through insurance premium subsidies."[136]

Other insurer trade associations, carriers, and producer associations and their members expressed similar concerns. According to Mr. Whittle, on behalf of AIA, "restrictions on percent deductibles for coastal exposures, such as hurricanes and windstorms, can result in transfers of risk inland as insurers will necessarily look to establish and maintain reasonable probable maximum loss exposures. Thus, limitation in one part of a state can impact other parts of a state and this has been seen time and again in Florida for example."[137]

Similarly, in its post-Hearing written testimony, Allstate stated: "Generally, issues of availability and affordability along the coast spill over to non-coastal areas when: (1) insurers must address catastrophe exposure issues subject to a state law, or regulatory mandate, that requires exposure reductions to be taken on a statewide basis; (2) insurers are encouraged by regulators to shift a portion of a proposed rate increase to non-coastal areas to minimize the impact of rate increases on the coast; or (3) a major catastrophic event leads to a spike in reinsurance costs or a contraction in reinsurance supply, or both."[138] Allstate currently does not "see any of these conditions in Maryland."[139] Along the same lines, State Farm opined, "Those residing in disaster prone areas should pay premiums based on the risk presented and share in the risk with appropriate deductibles."[140]

IIAM, on behalf of its independent agent members, attributed higher premiums in coastal areas not only to greater potential losses from hurricanes and other storms, but also to greater exposures arising from second residences that may be unoccupied during major weather events and the winter months, which can lead to frozen pipes, and to burglaries or other criminal activities in unoccupied properties during off season.[141] In its comments, IABM raised similar concerns.[142]

E. Summary and Conclusions

According to the most recent available NAIC data, the total average annual premium for dwelling fire and homeowners owner-occupied policies in Maryland compares favorably to the nationwide average ($778 in Maryland versus $875 nationally), and falls slightly below the national median (24th lowest of 51 jurisdictions).[143] Maryland's property and casualty insurance

[135] *Id.*
[136] *Id* At 5.
[137] Exhibit 3 at 8.
[138] Exhibit 29 at 1.
[139] Exhibit 29 at 1.
[140] Exhibit 27 at 2.
[141] Exhibit 22 at 1.
[142] Exhibit 23 at 3.
[143] NAIC, *2009 Dwelling Fire, Homeowners Owner-Occupied, and Homeowners Tenant and Condominium/Cooperative Unit Owner's Insurance: Market Distribution and Average Cost by Policy and Amount of Insurance* (Dec. 2011).

market remains competitive, and there are wide ranges of rates available in many areas of the State, including coastal areas. Premium rates have risen moderately in recent years, however, and such increases may be difficult for some policyholders to afford, especially in coastal areas such as Baltimore City, Somerset County, and Wicomico County, where the percentage of the population with incomes below the federal poverty level is substantially above the Statewide average.

A key contributor to premium rate increases is the increased exposure to loss demonstrated retrospectively by higher than average losses in recent years and projected prospectively through new catastrophe models. Rising property repair and replacement costs are another contributing factor. And although some Hearing participants testified that the cost of reinsurance has been relatively stable over the past several years, others pointed to volatility in reinsurance costs over the past two decades and expressed concern that increased exposure projections could result in increased reinsurance rates that, in turn, would result in increased premiums for policyholders.

Insurers and insurer trade associations identified percentage deductibles as one way to control premium costs and to encourage carriers to remain in higher risk areas of the Maryland market. They also contend that percentage deductibles provide homeowners with an incentive to take steps to mitigate potential storm-related damage before it happens, thereby reducing exposure and further controlling costs. There was consensus, however, that consumers often may not understand that they have a percentage deductible, or the manner in which it is applied. Disclosures required under regulations currently being developed by the MIA are designed to help address this issue.

Industry representatives, including insurer and producer trade associations and their members, cautioned against the adoption of any State-imposed law, regulation, or policy that would result in the subsidization by policyholders in lower-risk parts of the State of premium or deductible costs for policyholders in higher-risk coastal areas. According to Dr. Detlefsen, on behalf of MAMIC, any such subsidization for lower-income residents in high-risk areas should come from general public funding, not from artificially inflated insurance premiums paid by lower-risk policyholders.

VII. Policy Options

A. Availability

The information gathered in the course of this quasi-legislative proceeding supports a conclusion that property and casualty insurance generally is available for homeowners and businesses in coastal areas of the State. Nearly all witnesses that offered a view on the matter indicated that policies available through the JIA are sufficient to meet the needs of any residual market in coastal areas of the State, and that there is no demonstrated need for alternative market mechanisms such as "wind pools" or "beach plans" available in several other coastal states.[144]

[144] *See, e.g.*, Exhibit 3 at 8 (AIA); Exhibit 5 (NAMIC); Exhibit 8 at 3 (PCI).

From the perspective of at least one small, independent producer in Ocean Pines, however, availability of coastal property insurance has become more restricted in recent years, particularly among admitted carriers.[145] To the extent that property and casualty insurance availability concerns become more prevalent in all or part of Maryland's coastal zone in the future, the State could consider adopting initiatives that have been employed in other states to encourage insurers to enter or remain in the coastal marketplace. For example, South Carolina and Mississippi provide a tax credit for insurers writing coastal policies. In South Carolina, the Coastal Premium Tax Credit reduces premium taxes for new insurance policies that provide property and casualty coverage (including coverage against the perils of wind and hail) on risks located in the area served by the South Carolina Wind and Hail Underwriting Association (Wind Pool). This credit is limited to 25 percent of the premium tax due.[146] Similarly, under the Insure Louisiana Incentive Program, qualifying insurers received matching grants to encourage participation in the voluntary property insurance market.[147] Legislative action would be required in order to establish any such incentives in Maryland.

Another potential approach, adopted in Connecticut and New York, involves the establishment of Coastal Market Assistance Programs (C-MAP) to help current or prospective homeowners in coastal areas find homeowners insurance. Insurance companies in these two states voluntarily offer limited coverage to homeowners that are unable to find a standard homeowners policy due to the proximity of the home to the coastline. The Connecticut C-Map is administered by the Connecticut FAIR Plan.[148] In New York, a similar program is administered by the New York Property Insurance Underwriting Association ("NYPIUA").[149] According to Mr. Wulf, on behalf of RAA, there has been a decline in homeowners resorting to New York's residual market over the last four years, which he attributed to the success of its C-MAP program.[150] The establishment of any such program in Maryland also would require legislative action. The MIA intends to investigate further the details of these programs with the Connecticut Insurance Department and the State of New York Insurance Department.

Alternatively, the General Assembly could consider revising the discrimination in underwriting provisions of the Insurance Article. As discussed in Subsection III.A.1. above, earlier this year the Court of Appeals affirmed that § 27-501 is relevant to an insurer's determination not to write in the coastal areas of the State.[151] Section 27-501(a) provides, in relevant part, that an insurer may not cancel or refuse to underwrite or renew a particular insurance risk or class of risk for any unfairly discriminatory reason and except by the application of standards that are reasonably related to the insurer's economic and business purpose. Section 9-107 prohibits a property and casualty insurer from refusing to issue a contract of property insurance, casualty insurance, or motor vehicle insurance solely because the "subject of the risk" or the insured's address is located in a certain geographic area of the State unless the designation of the geographic area by the insurer has an objective basis and is not arbitrary or unreasonable. The legislature could choose, instead, to prohibit cancellation or

---

[145] *See* Exhibit 30 (Fowler).
[146] *See* South Carolina Bulletin Number 2008-17.
[147] LA. Rev. Stat Ann 22: 2361 et seq
[148] http://www.ctfairplan.com/c-map.html.
[149] http://www.nypiua.com/cmap7.pdf.
[150] Tr. 52-54.
[151] *See People's Insurance Counsel Division v. Allstate Insurance Co.*, No. 60, Sept. Term 2011 (Jan. 25, 2012).

refusal to underwrite or renew a particular insurance risk or class of risk based solely on the geographic location of the risk. Other states that have taken this approach include New Hampshire[152] and Rhode Island.[153]

B. Affordability

Overall, Maryland's homeowners insurance market is competitive, and, according to the most recently available figures from the NAIC, the total average annual premium for dwelling fire and homeowners owner-occupied policies in Maryland compares favorably to the nationwide average and falls slightly below the national median. However, premium rates have risen moderately in recent years, and at least one producer witness has observed substantial premium increases in certain coastal areas of the State. Such increases may be difficult for some policyholders to afford, especially in coastal areas such as Baltimore City, Somerset County, and Wicomico County, where the percentage of the population with incomes below the federal poverty level is substantially above the Statewide average. Hearing participants identified three key contributors to premium rate increases in coastal areas: (1) increased exposure to loss demonstrated by higher than average losses in recent years and projected for future years through new catastrophe models; (2) rising property repair and replacement costs; and (3) reinsurance price volatility and the potential for increased reinsurance costs. Potential policy options to address these and other factors, many of which have been adopted in certain other states, are discussed below.

1. CAT Model Projections of Loss Exposure

In Maryland, an insurer using a catastrophic risk planning model or other model in setting homeowners insurance rates or refusing to issue or renew homeowners insurance because of the geographic location of the risk must file a description of the model with the Commissioner and make arrangements for the model's vendor to explain to the Commissioner and the PICD the data used in the model and the manner in which the output is obtained.[154] Florida submits catastrophe models used in that state to even greater scrutiny. Florida is the only state with an independent, state-funded entity created to ensure the validity of catastrophe models used in the state. The Florida Commission on Hurricane Loss Projection Methodology is comprised of an independent panel of experts that evaluates computer models and other actuarial methods for projecting hurricane losses. A model cannot be used by an insurer selling insurance in Florida unless it has been approved by the Florida Commission.

Maryland could adopt a policy pursuant to which insurers doing business in the State who use CAT models may only use models approved by the Florida Commission. A benefit of such an approach is that it would allow only the use of models that have been vetted by an independent panel with relevant and highly specialized expertise. A potential downside is that models appropriate for projecting hurricane losses in Florida may not always be completely

---

[152] N.H. Rev. Stat. Ann. §417:4 VIII(e)(defining unfair methods of competition and unfair and deceptive acts and practices in the business of insurance to include refusing to insure risks solely because of place or area of residence).
[153] R.I. Gen. Laws §27-29-4.1 ("No insurance company authorized to do business in this state shall cancel or refuse to issue any type of insurance coverage for an owner occupied dwelling or personal property of every nature and description solely because of the area in which the property is situated.").
[154] Ins. Art. § 19-211(a).

applicable to Maryland risks. In the alternative, Maryland could create its own commission to review CAT models. The cost to establish and maintain such a State-specific commission, however, likely would be substantial.

2. Loss Exposure Mitigation

Numerous witnesses emphasized the important role of mitigating potential exposure to loss in controlling premium costs. The PICD proferred, and the Commissioner admitted, a report entitled, *Status of the South Carolina Wind and Hail Underwriting Association: Status Report for 2009*,[155] which described mitigation as "a critical component" of South Carolina's Omnibus Coastal Property Insurance Reform Act of 2007, and noted that "most of the reforms were aimed at assisting the property owner with the fortification of his residence or business, thereby making it more resistant to hurricane damage." Mitigation initiatives adopted in other states that various witnesses testified could have application in Maryland include: (a) uniform enforcement of a Statewide building code; (b) consumer tax credits, deductions, or exemptions for mitigation measures; (c) mitigation grants for fortification measures to existing homes; and (d) mandatory premium discounts or premium credits for various mitigation measures such as use of storm shutters; use of roof tie-downs; or elevation of property. Each is discussed briefly below.

(a) Uniform Enforcement of Statewide Building Code

As discussed in subsection IV.D. above, although Maryland law requires local jurisdictions to adopt Maryland Building Performance Standards, local jurisdictions may amend those standards "to suit local conditions," which could weaken protections against wind and other storm damage. This local variation was cited as a weakness in a 2011 report by the Insurance Institute for Business & Home Safety (IBHS). Witness testimony in this proceeding reinforced the notion that a strong, uniformly enforced Statewide building code would meaningfully reduce risk exposure in coastal areas of the State, which, in turn, should stabilize premium rates and encourage carriers to write business in those areas.[156] Florida and Louisiana were cited as states with strong statewide and uniformly enforced building codes.

(b) Consumer Tax Credits, Deductions or Exemptions for Mitigation Measures

Under South Carolina's Omnibus Coastal Property Insurance Reform Act of 2007, homeowners are able to obtain tax credits for the costs of taking certain steps to make their homes more resistant to hurricane damage. There are two types of credits available. One is an income tax credit for the actual cost to make the primary residence more resistant to damage from a hurricane, rising floodwater or a catastrophic event. The tax credit for any taxable year is limited to 25 percent of the total costs incurred or $1,000, whichever is less. The other is an income tax credit for state sales taxes paid on tangible personal property used to make a primary

[155] Exhibit 17.
[156] *See, e.g.*, Exhibit 8, PCI Special Report at 13; Exhibit 2 (RAA); Exhibit 10 (Mr. Carter, on behalf of MAMIC) at 2 ("A strong statewide building code should be enacted."); Exhibit 27 (State Farm) at 2 (advocating for "[t]houghtful and responsible land use regulation and strong, well-enforced building codes.").

residence more resistant to damage from a hurricane, rising floodwater or other catastrophic event. This income tax credit is up to $1,500 for state sales or use taxes paid on purchases of tangible personal property used to fortify the residence.[157] In a similar vein, AIA suggested, "States also should create state sales tax holidays for hurricane mitigation and preparedness purchases, or exempt certain items from state sales tax."[158]

(c) Mitigation Grant Programs

South Carolina has established a "safe home" mitigation grant program that provides homeowners grant funds to make owner-occupied property more resistant to hurricane and wind damage. Mitigation work must be performed by contractors that have been approved by the program.[159] Florida had adopted a similar program – "My Safe Florida Home" that was discontinued in 2009 due to budgetary constraints. According to PCI, such initiatives have "demonstrated high benefit-to-cost ratios." PCI reported that, "A study using FEMA data found that on average, a dollar spent on hazard mitigation saves the nation about $4 in future costs."[160]

(d) Premium Discounts or Credits

A number of states require insurers to provide discounts or premium credits for various mitigation measures such as use of storm shutters, use of roof tie-downs, or elevation of property.[161] In Maryland, § 19-210 of the Insurance Article currently requires that "[a]n insurer shall offer at least one actuarially justified premium discount on a policy of homeowner's insurance to a policyholder who submits proof of improvements made to the insured premises as a means of mitigating loss from a hurricane or other storm." It is unclear whether this has been a useful tool to reduce premiums. The MIA will review the extent to which consumers have accessed this opportunity and the resultant premium savings.

3. Reinsurance Costs

Florida has established a catastrophe fund which provides a mechanism for insurers that are writing coastal policies to obtain reinsurance from a State pool. There is debate regarding the effectiveness of the Florida CAT Fund and whether it has led to the stability or instability in the Florida market. In its written comments, for example, the Reinsurance Association of America asserted:

- The Florida Cat Fund is the only reinsurance catastrophe fund in operation. The history of the Florida Cat Fund is not a success.
  - Despite over a decade to build up a capital cushion, the 2004 and 2005 Florida hurricanes left the Cat Fund broke and in debt.
  - The Florida Cat Fund had to issue bonds to meet its obligations to insurers.

[157] *See* http://doi.sc.gov/consumer/Pages/Coastal.aspx#taxcreditinfo; http://doi.sc.gov/faqs/Pages/TaxCredits.aspx.
[158] Exhibit 4, AIA Natural Catastrophe Agenda at 6.
[159] *See* http://www.scsafehome.com/.
[160] Exhibit 8, PCI Special Report at 4.
[161] *See, e.g.*, S.C. Code Ann. § 38-73-1095; LA. Rev. Stat. Ann. §22:1483.

- o Insurers do not pay the bond debt. Consumers and businesses do. They are being taxed on their policies to pay the debt. Consumers can face up to 30 years of taxes.
- o Lower risk policyholders and commercial policy holders are taxed to subsidize those most at risk.
- o In essence, policyholders insure their insurance companies.

- Policyholders purchase insurance to transfer unwanted risk to their insurers. A Cat Fund defeats policyholder expectations by transferring the risk back to consumers.

- Cat Funds violate one of the fundamental tenets of insurance – Spreading the risk. They concentrate the risk in the state, rather than spreading the risk throughout the world wide insurance and reinsurance markets. Risk spreading helps keep insurance affordable. Concentrating risk defeats the benefits of risk spreading and diversification.

- A Cat Fund does not result in more available and affordable insurance. Despite the existence of the Florida Cat Fund and its 2007 $12 billion expansion, insurers continue to non-renew policies and prices continue to be high. [162]

AIA, NAMIC, and PCI expressed similar views. In his testimony on behalf of AIA, Mr. Whittle noted that, unlike the situation in Florida following Hurricane Andrew, "there is no similar reinsurance crisis facing Maryland homeowners' insurers" that would warrant the establishment of a catastrophe fund.[163] According to Mr. Whipple, "[a] case has not been made, either in Maryland or on the federal level, for a state run reinsurance facility to manage natural catastrophe risk. Despite the record-breaking losses in the 2005 hurricane season, the private insurance industry remains in a position to manage this risk without new state or federal cat funds."[164] In Mr. Detlefsen's view, on behalf of NAMIC, "the Florida Catastrophe Fund has been chronically underfunded. Most analysts believe the fund will be incapable of meeting its obligations when the state is struck by a major hurricane or series of storms within a single hurricane season."[165] And according to PCI, it is believed that state cat funds are ineffective in the long run, transferring costs from higher-risk policyholders to lower-risk policyholders and creating rate inequities. In addition, these funds do not reduce the exposure to natural disasters. Instead, they encourage further real estate development in disaster-prone areas, which increases overall risk.[166]

Like AIA, State Farm concluded, "It is not at all clear . . . that the availability and affordability of coastal insurance in Maryland has reached a point that a . . . catastrophe fund is an appropriate avenue to pursue."[167] Allstate, alone, had a different view: "Allstate believes that

[162] Exhibit 2 (internal footnote omitted).
[163] Exhibit 3 at 6.
[164] Exhibit 3 at 6.
[165] Exhibit 5.
[166] Exhibit 8, PCI Special Report at 12.
[167] Exhibit 27 at 3.

a Maryland catastrophe reinsurance fund will help more Maryland homeowners afford adequate insurance protection, without bailouts and subsidies, while providing additional funding from investment income to support important public safety objectives."[168]

4. *Other Options to Address Affordability*

Hearing participants identified a number of other potential policy options to help policyholders afford the cost of insurance. For example, as a part of the Omnibus Coastal Property Insurance Reform Act of 2007, South Carolina passed legislation to permit a state income tax deduction for consumers who establish a catastrophe savings account. The amount that can be contributed to such accounts is based on the amount of the consumer's homeowners policy deductible, if the consumer is insured, or the value of the consumer's legal residence, if the consumer self-insures. Distributions from the account are treated as taxable income unless they are used to cover qualified catastrophe expenses.[169] South Carolina also provides an income tax credit for property and casualty insurance premiums on the taxpayer's personal residence that are in excess of five percent of the taxpayer's adjusted gross income. The maximum credit is $1,250 per year.[170] On behalf of NAMIC, Dr. Detlefsen suggested that the availability of such assistance could be limited to those currently residing in disaster-prone areas, thereby avoiding the creation of incentives "for people not currently living in those areas to move into harm's way."[171]

In another type of affordability measure, Florida, Louisiana, and Rhode Island have enacted legislation limiting carriers' ability to impose hurricane deductibles to once per calendar year.[172] Florida also requires any insurer that requires a percentage deductible for certain types of losses to offer a range of such deductibles.[173] This approach arguably balances the interests of consumers and carriers by providing consumers with the opportunity to "buy down" high percentage deductibles while at the same time allowing carriers to appropriately manage their risk through higher premiums for products with lower percentage deductibles.

VIII. Conclusions

Information gathered in the course of this quasi-legislative proceeding supports a conclusion that property and casualty insurance generally is available for homeowners and businesses in coastal areas of the State, and that the State's residual market mechanism are sufficient to meet the needs of Marylanders having difficulty accessing insurance through the commercial markets. From the perspective of at least one independent producer in Ocean Pines, however, availability of coastal property insurance has become more restricted in recent years, particularly among admitted carriers. To the extent that availability concerns become more prevalent in all or part of Maryland's coastal zone, the State could consider adopting initiatives that have been enacted in other states, such as insurer tax credits or grants, to encourage participation in the coastal market. Another potential approach involves the establishment of a

[168] Exhibit 29 at 5.
[169] *See* Exhibit 17 at 30-31.
[170] *See* S.C. Code Ann. Section 12-6-3670.
[171] Exhibit 5.
[172] R.I. Gen. Laws § 27-5-3.7; FLA. Stat. § 627.701(5); LA. Rev. Stat. Ann. § 22:1337.
[173] FLA. Stat. § 627.701(3).

Coastal Market Assistance Program to help current or prospective homeowners in coastal areas find homeowners insurance. The MIA intends to investigate further the details of these programs in other states. Alternatively, the State could consider prohibiting insurers from canceling or refusing to underwrite or renew a particular insurance risk or class of risk based solely on the geographic location of the risk, as New Hampshire and Rhode Island have done. This approach could discourage carriers from participating in Maryland's markets, however, or could result in premium rate increases across the State and subsidization by policyholders in lower-risk areas of policyholders in higher-risk areas. Any of these options would require legislative action.

With respect to affordability, the most recent available NAIC data indicates that the total average annual premium for dwelling fire and homeowners owner-occupied policies in Maryland compared favorably to the nationwide average ($778 in Maryland versus $875 nationally), and fell slightly below the national median (24th lowest of 51 jurisdictions). Maryland's property and casualty insurance market remains competitive, and there are wide ranges of rates available in many areas of the State, including coastal areas. Premium rates have risen moderately in recent years, however, and such increases may be difficult for some policyholders to afford, especially in coastal areas such as Baltimore City, Somerset County, and Wicomico County, where the percentage of the population with incomes below the federal poverty level is substantially below the Statewide average.

Hearing participants identified key contributors to premium rate increases including: (1) the increased exposure to loss demonstrated retrospectively by higher than average losses in recent years and projected prospectively through new catastrophe models; and (2) rising property repair and replacement costs. Although some witnesses testified that the cost of reinsurance has been relatively stable over the past several years, others pointed to volatility in reinsurance costs over the past two decades and expressed concern that increased exposure projections could result in increased reinsurance rates that, in turn, would result in increased premiums for policyholders. Policy options to address these factors include: (1) requiring insurers to use only catastrophe models approved by the Florida Commission on Hurricane Loss Projection Methodology, or to establish a similar Maryland Commission; or (2) enacting mitigation initiatives such as uniform enforcement of a Statewide building code; consumer tax credits, deductions, or exemptions for mitigation measures; mitigation grants for fortification measures to existing homes; mandatory premium discounts or credits for certain mitigation measures; or state income tax deductions for consumers based on need or the establishment of a catastrophe savings account. With one exception, all witnesses expressing a view on the matter agreed that there is no demonstrated need to establish a reinsurance catastrophe fund in Maryland.