



Texas / South Central News

## Actuarially Sound Property Rates Remain Elusive Along Texas Coast

By Stephanie K. Jones  
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Insurance company interests have long complained that the state-backed Texas Windstorm Insurance Association charges rates that are not actuarially sound for the risks it insures, making it impossible for private insurers to compete for business in the areas TWIA serves.

Those critics now have an ally in the U.S. Government Accountability Office, which says TWIA — the insurer of last resort for wind coverage for homes and businesses along the Texas coast — charges "premium rates [that] do not fully reflect the risk of loss and would likely need to increase by 20 to 35 percent in order to do so."

In a report to Congress on state-backed natural catastrophe insurance that was released in May, the GAO said that because TWIA's "rates do not fully reflect the risk of loss, and are therefore lower than rates the private market would charge, the program could discourage private market participation."

That is the reality, agrees state Rep. Kelly Hancock of Fort Worth. The additional "reality is TWIA is never going to be actuarially sound. That's the reason why private companies won't write" along the coast, Hancock said during a recent forum on windstorm insurance issues. "It doesn't make financial sense."

TWIA was commissioned by the state legislature in 1971, after losses from a major storm caused private insurers to abandon the coastal region. By the time Hurricanes [Dolly](#) and [Ike](#) hit Texas in 2008, TWIA's catastrophe trust fund had grown to \$480 million, according to TWIA actuary Jim Murphy, speaking at the forum hosted by the Texas Public Policy Foundation.

TWIA paid out \$285 million in claims from Dolly, which made landfall in near Brownsville in July, and the insurer racked up another \$1.8 billion in claims from Ike, which hit near Galveston in September 2008.

Through reinsurance and the trust fund, TWIA was able to handle the claims, but the trust fund was wiped out. The insurer had to start building up the reserves from scratch in 2009, Murphy said.

During the [2009 legislative session](#), lawmakers changed TWIA's funding structure, not only to help the company's ability to pay claims going forward but to encourage private insurance companies to re-enter the market.

Insurance companies previously were on the hook for unlimited assessments for TWIA losses with limited ability to recoup the assessments from policyholders, the GAO noted in its report. The unlimited assessments were a big unknown and all property insurers are subject to them, so the carriers pushed for an assessment cap.

The 2009 legislation created a three-tiered structure for issuing post-event bonds, up to a cap of \$2.5 billion. The first layer — \$1 billion — would be paid with assessments to TWIA policyholders. The second \$1 billion would be paid with a 70/30 split of assessments on all Texas property policies — 70 percent of the assessments would go to coastal policyholders and the remaining would apply to inland policyholders. Assessments to property insurers operating in Texas would cover the remaining amount of \$500 million.

"How TWIA losses would be funded if a storm caused more than \$2.5 billion in losses for TWIA is not clear," according to the GAO report.

It's also unclear in the current financial environment if the first \$1 billion in post-event bonds could be sold, said Murphy. There would not likely be a problem selling the second two levels of bonds if they are needed, he said.

After Ike, state lawmakers gave TWIA the choice between building up its reserves again or buying reinsurance, Murphy said. Legislators indicated they preferred that TWIA forego reinsurance and build up the trust fund, so that's what the insurer did.

TWIA has positioned itself put between \$150 to 200 million a year in the trust fund. "So it's not as bad as it looks ... at least in the long term," Murphy said. "If we can have few good years we can build up the trust fund."

The problem, he added, is the short term. "There's no way of funding a major event this year or next year," he said.

### Other Changes

Legislative changes in 2009 also adjusted the methodology used to set TWIA's premium rates, the GAO noted in its report, authorizing the insurer to use catastrophe models in determining rates.

According to the GAO and others, TWIA needs to significantly raise its rates, but the insurer is constrained legislatively, and by [regulators](#), in what it can do at any given time.

State Rep. Solomon Ortiz Jr. of Corpus Christi noted, however, that while premiums may not be actuarially sound, the insurer's rates have been on the rise. "TWIA's rates have increased in the last four years," he said. "Just recently 12 percent and there's probably another 5 percent increase coming here soon."

Many policyholders must show that they have [flood insurance](#) and Murphy said TWIA now requires a [six-month policy](#) at minimum in order to "prevent people from jumping in and out of the market."

### Discount or Rate Hike?

TWIA offers a 15 percent premium discount to policyholders who mitigate their property against wind losses. To qualify for the discount, policyholders must obtain a windstorm certificate from an authorized inspector. According to the GAO, however, the mitigation discount program could serve to encourage property owners to forego or reduce mitigation efforts, because TWIA's rates remain lower than private market rates.

Many of Ortiz's constituents who live in older homes actually see the discount as a 15 percent increase in their rates because it's almost impossible to obtain a certificate for older structures, he said.

"What happens if you don't have that certificate and you've never had it for 20 or 30 years? Try and find an inspector to inspect your house and give you that certificate," Ortiz said. "It's not going to happen. ... Engineers and others simply will not touch this. ... They essentially would have to destroy part of the home to make sure it qualifies."

He said his office receives calls all the time from constituents seeking help with obtaining windstorm certificates.

"We pretty much say: good luck. If you don't have it and you're not building a new home or doing some major remodeling or rebuilding of your home, the reality is you're not going to get it," Ortiz said.

### Are Reforms Working?

It's too early to tell how well TWIA reforms from 2009 are working, according to Rep. Ortiz. "I don't think time has gone long enough to see where they've made an impact."

TWIA's policy count increased from 68,756 policyholders in 2001 to 232,000 policyholders in 2008, Rep. Hancock said. "That's 55 percent of the Gulf Coast region which is now insured by the state of Texas."

Ortiz said the policy count seems to be stabilizing, however. "Private insurers have pretty much shed the policies they wanted to get rid of," he said.

"Many have said that the private market has been unstable because of the unlimited assessments," Ortiz said. "Hopefully with the reforms that have been made and the caps [on assessments] ... insurers will re-enter the market. Have we seen that? Not necessarily. ... This is a big concern and we hope over time some of these companies re-enter the market."

Rep. Hancock, who describes himself as a free market advocate and a small business owner, said in his "ideal world, a pure free market world, the responsibility for compensating employees so they could afford an actuarially sound insurance policy along the coast would rest with the employers, the businesses."

He acknowledged that's not going to happen. "I have yet to find a large company who's willing to subsidize their employee payment" to the extent that employees could afford actuarially sound insurance rates for their coastal property.

While Hancock maintained that he is not "a fan of subsidizing coastal insurance," the "reality is the coast is the economic engine of the state," he said. "It is vitally important to the state of Texas."

He said it's important to "face the reality of where we are as a state. And evaluate: are we running this business that we've entered into in a proper way? So that those we are writing policies for, those that we are insuring, we can actually fulfill the obligations and the promises that we made."

Ortiz said more time is needed to see whether recent changes will make a difference. He also suggested that new ideas need to be developed. But he was skeptical that there will ever be an ultimate solution.

"Will the windstorm issue ever be settled? I seriously doubt it," Ortiz said.

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