Why Do Some States Regulate Insurance Prices?

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Is There A Market Failure That Would Require Price Regulation?

- Structure
  - Monopoly power
- Conduct
  - Predatory pricing
  - Price Gouging
- Performance
  - Excess profits

Justifications for Price Regulation:

1. The industry exhibits market power and poses anticompetitive risks on consumers

2. Price regulators are better at setting consumer prices

3. Price regulations reduce consumer prices

4. Price regulations reduce market inefficiencies and costs

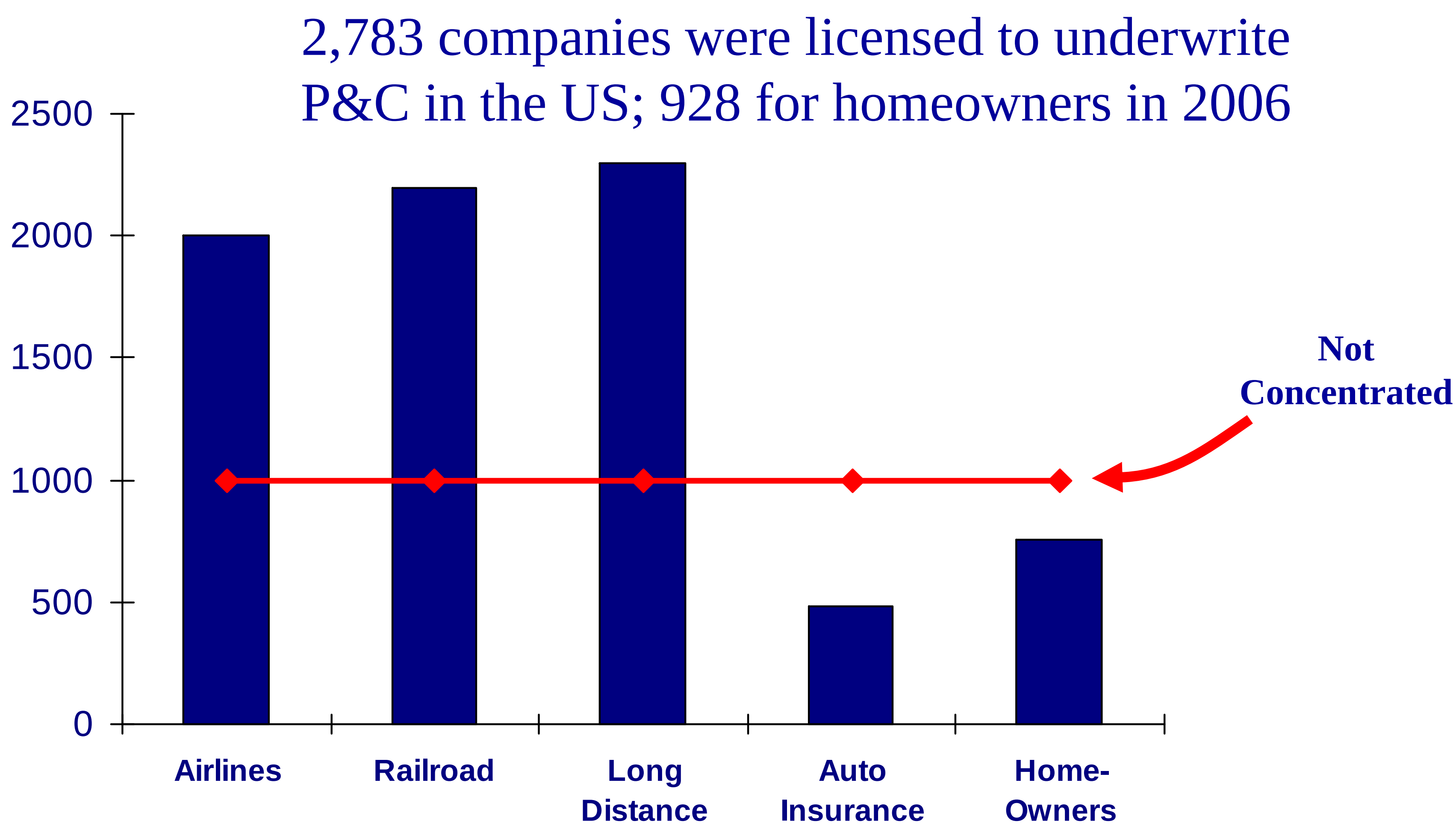
5. Price regulations reduce industry profits

Myth #1:

The industry exhibits market power and poses anticompetitive risks for consumers

Industry Concentration – 2006

HHI Indexes for Select Industries



Sources: American Association of Railroads, FCC, American Insurance Association, and AM Best

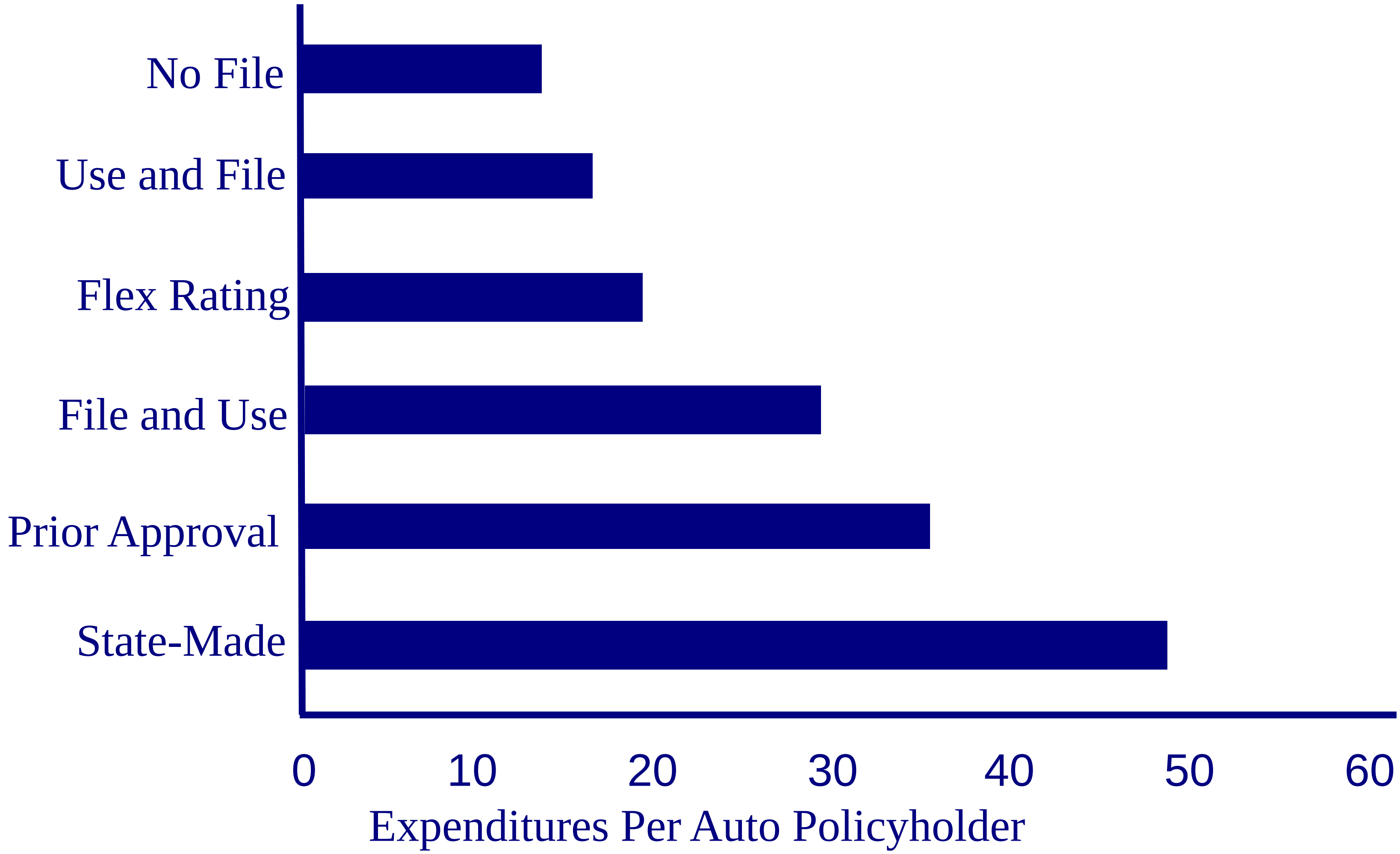
Myth #2:

Price regulators are better at setting consumer prices

What is the Right Price?

- Prices set too high – gouging
- Prices set too low – solvency

Average Variation From Price Trend



Myth #3:

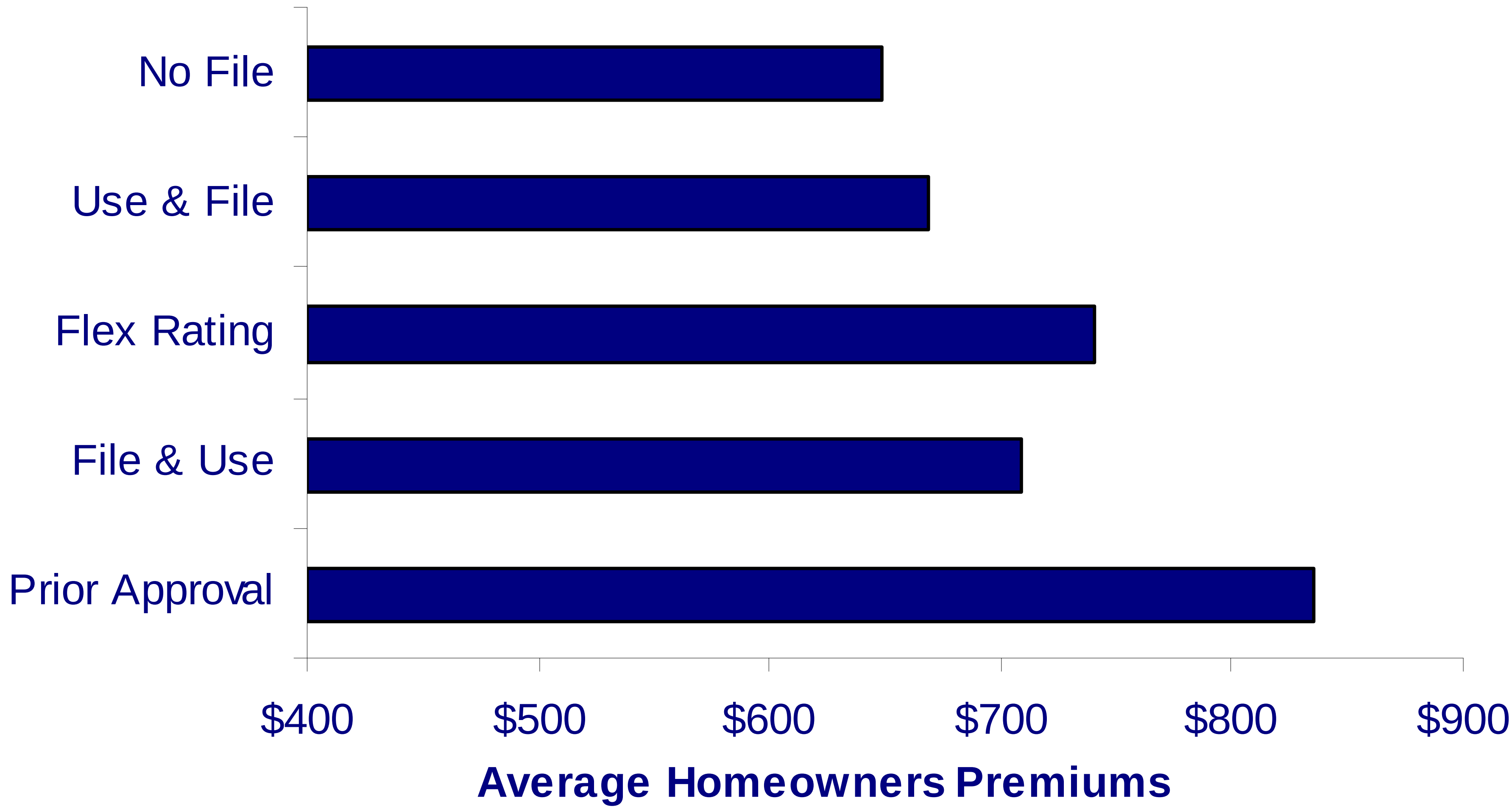
Price regulations reduce consumer prices

Price Deregulation Produced Lower Consumer Prices

Industry	Price Decline in 2 Years	Price Decline in 5 Years	Price Decline in 10 Years
Gas	10-38%	23-45%	25-57%
LD	5-16%	23-41%	40-47%
Airlines	13%	12%	29%
Trucking	Not Avail.	3-17%	28-56%
Railroads	4%	20%	44%

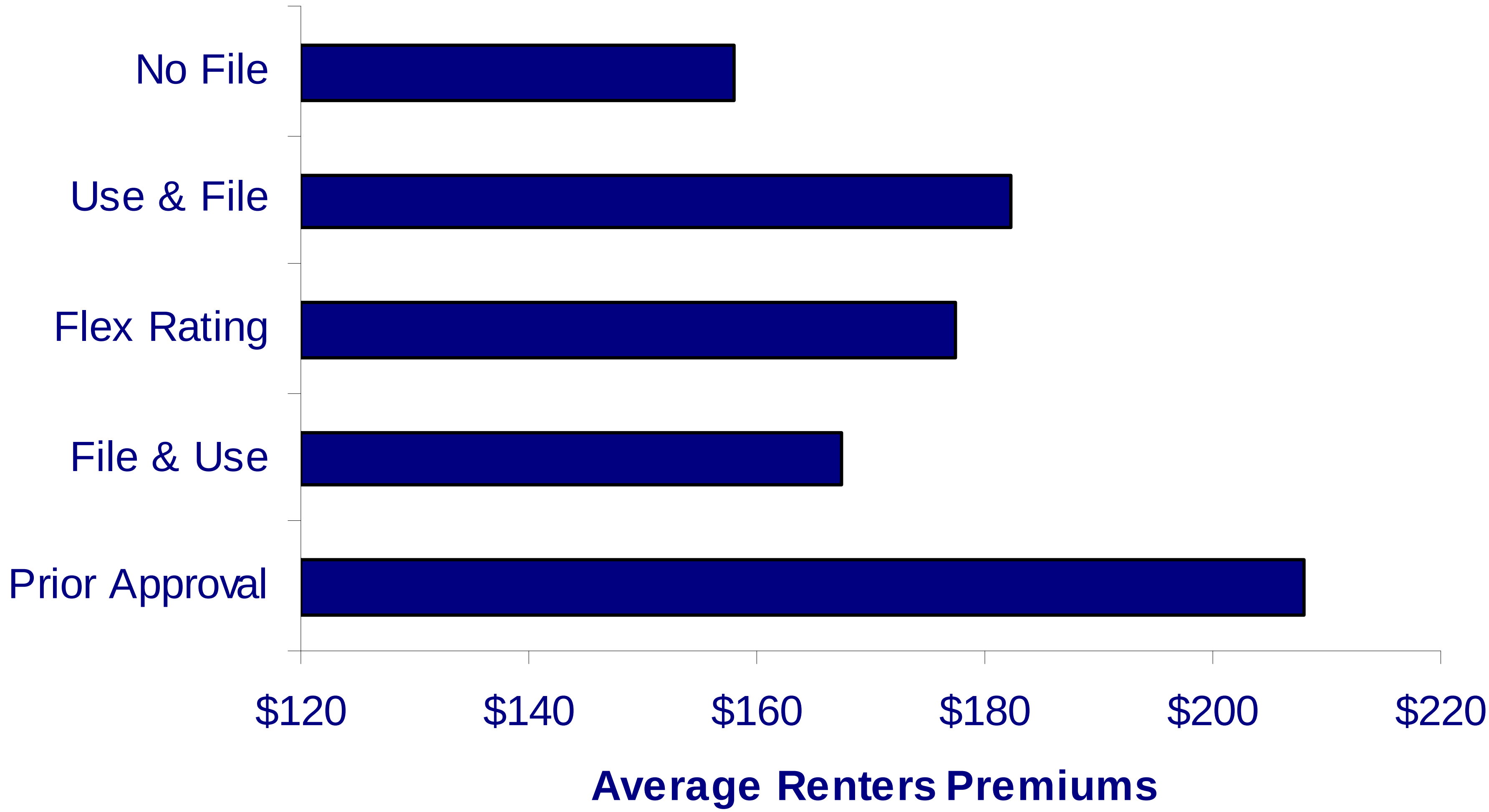
Sources: Crandall, Ellig, Morrison, Winston, et. al.

Rates and State Filing Requirements - Homeowners



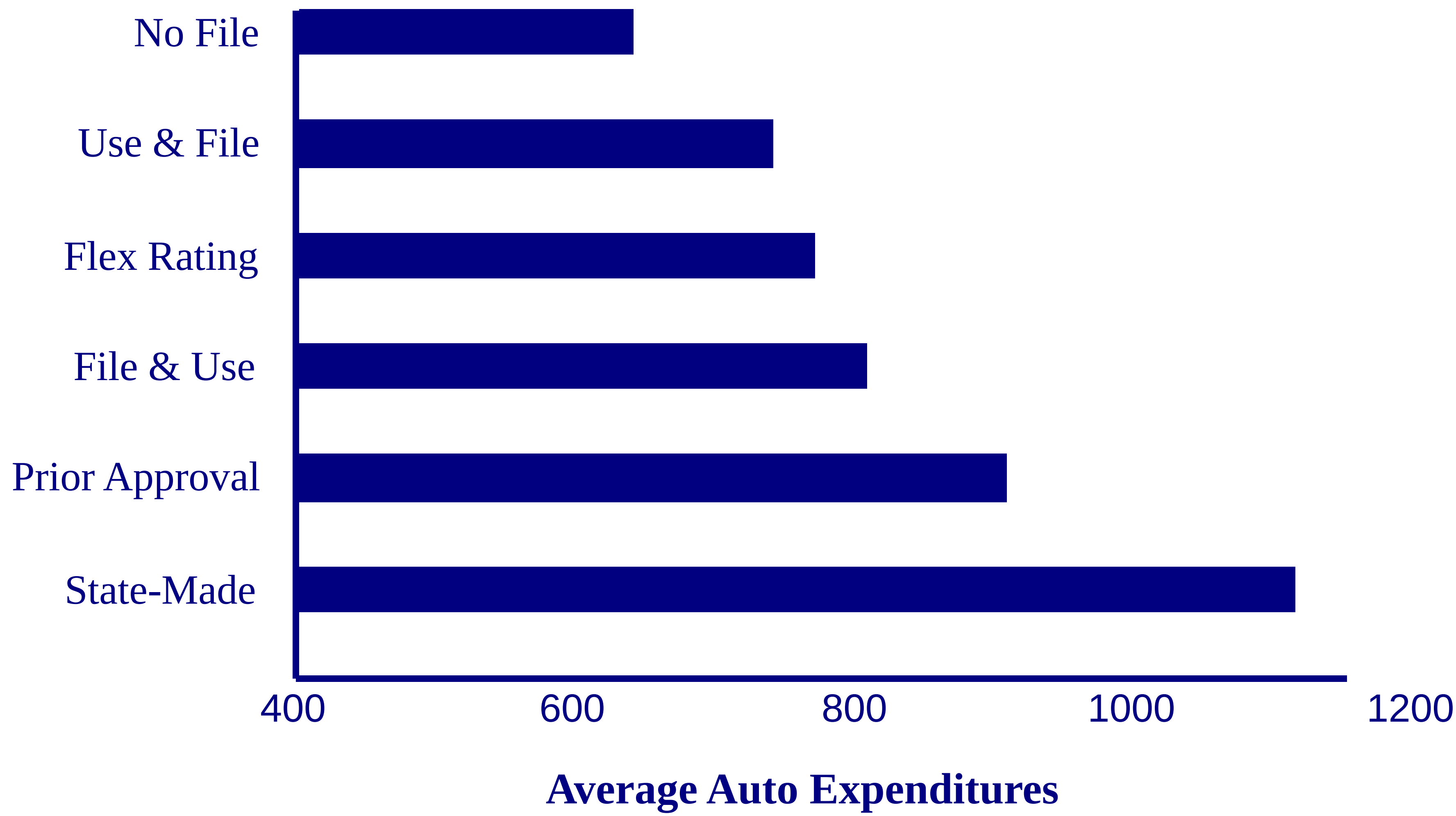
Data Excludes Texas

Rates and State Filing Requirements - Renters



Data Excludes Texas

Rates and State Filing Requirements – Auto



Data Excludes Texas

Myth #4:

Price regulations reduce market costs

Cost of Excessive Insurance Homeowners and Automobile Insurance Regulation

State	Annual Household Cost of Regulation
Massachusetts	$415
North Carolina	$318
Florida	$300
Maryland	$247
California	$238
New York	$216
Hawaii	$207
Louisiana	$207
Pennsylvania	$207
Texas	$185
Michigan	$168

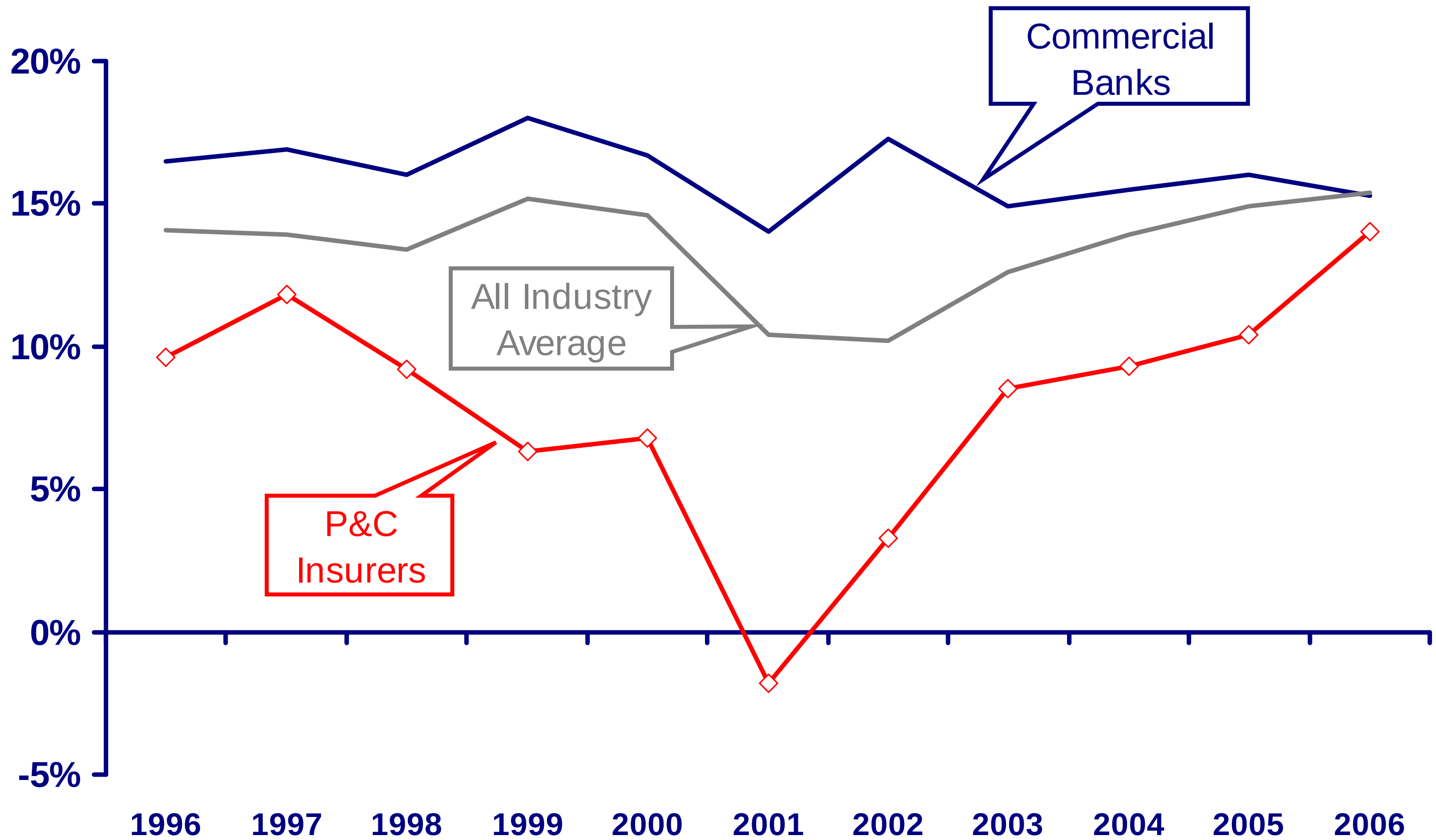
Source: American Consumer Institute, ConsumerGram, March 27, 2008.

… Across the U.S., $14 Billion Annually in Overpayments

Myth #5:

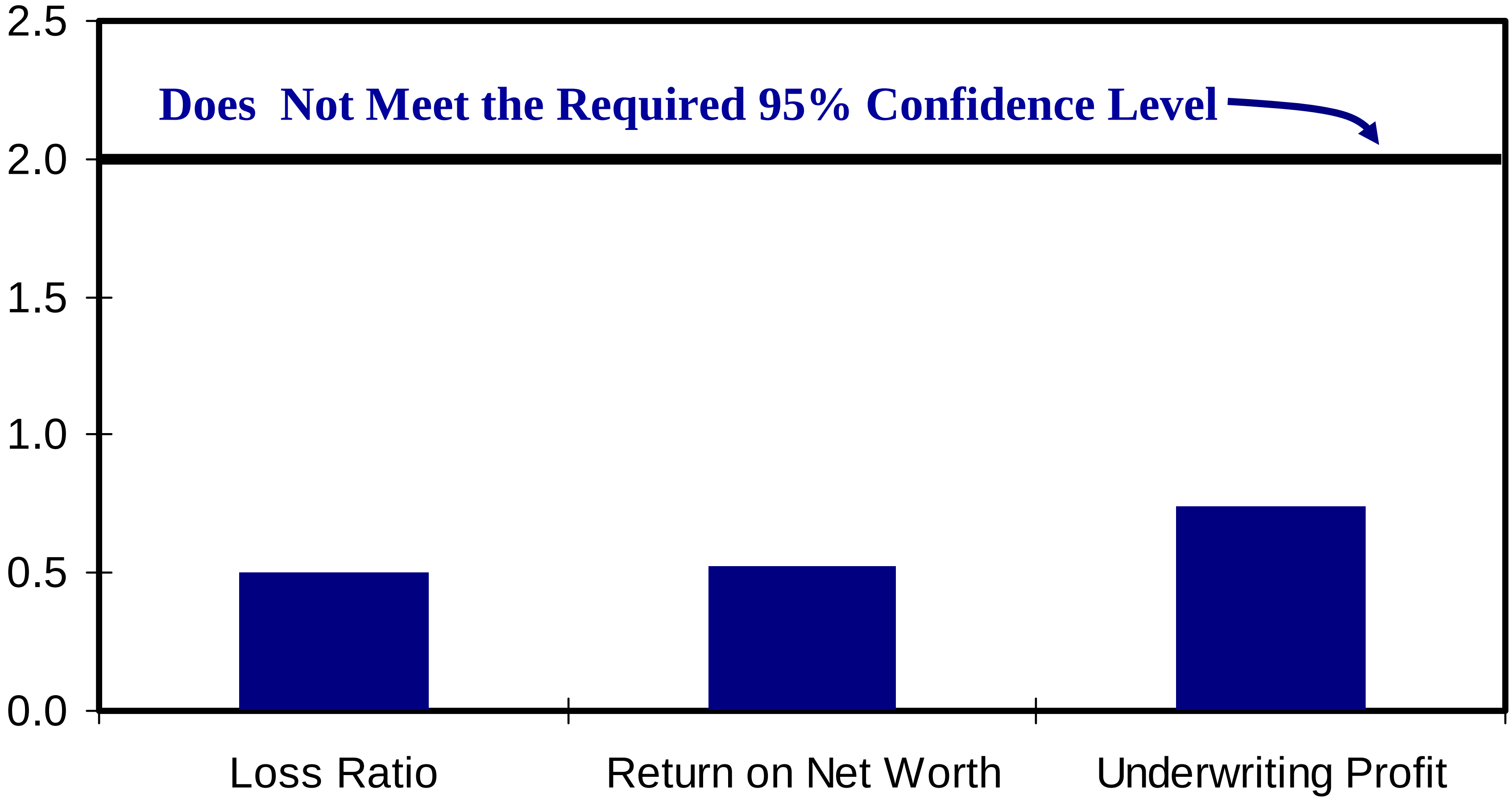
Price regulations reduce industry profits

Comparing ROE Across Industries



Source: Powell, "Assault on the McCarran-Ferguson Act and the Politics of Insurance in the Post-Katrina Era," Journal of Insurance, v26n3: 3-21 (Spring 2008).

Price Regulation Does Not Significantly Lower Profits



Industry Profits:
How Does Texas Compare to the US?

Homeowners Multi-Peril, 10-Year Average

	U.S.	Texas
Incurred Loss Ratio	64.1	62.5
Return on Net Worth	5.0	5.2
Underwriting Profit	-4.1	-3.3

Source: NAIC

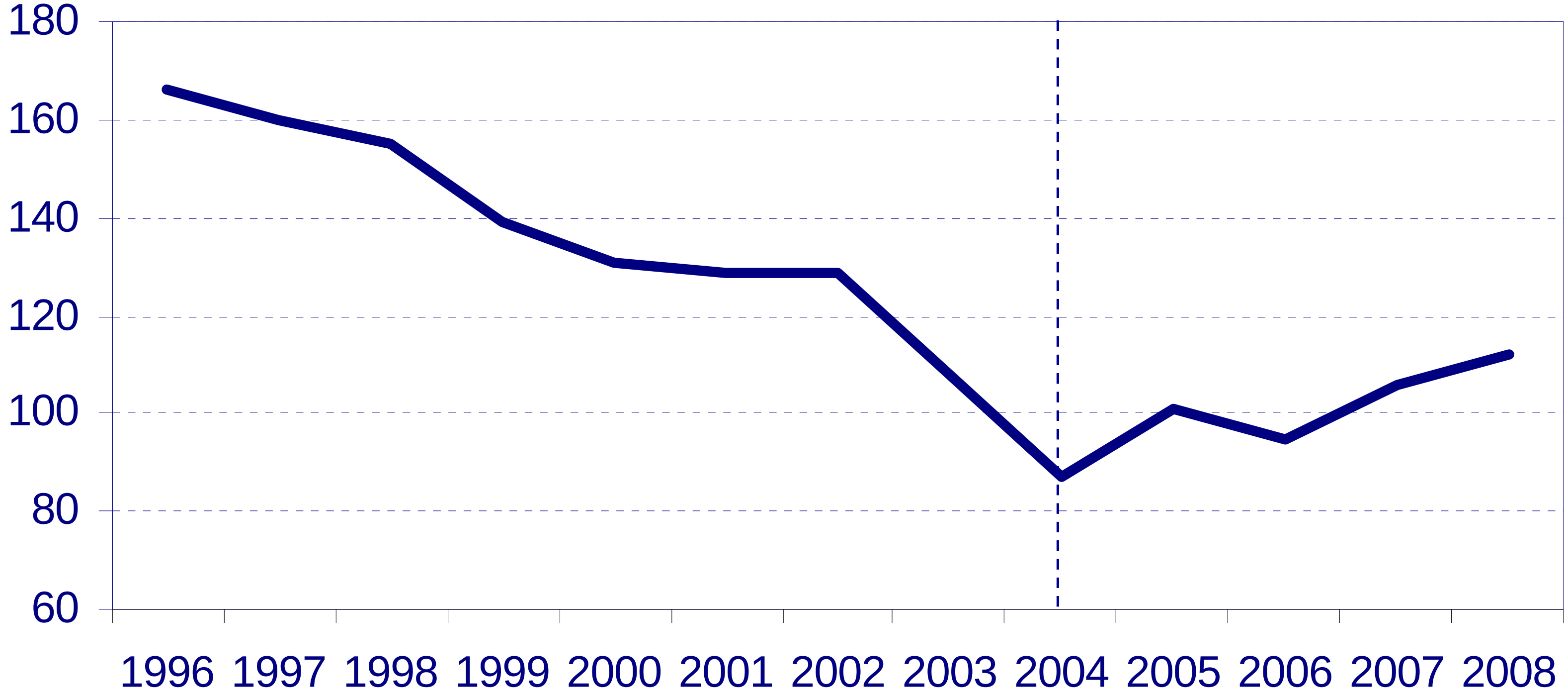
Correcting The "Five Myths" of Regulation With Empirically-Supported Facts:

1. There are ample rivals for price competition
2. The market sets price better than regulators do
3. Price regulation increases consumer prices
4. Price regulation increases market costs
5. Price regulation has no affect on industry profits

There is no empirical evidence of a market failure that would justify price regulation

The Decline in Insurers Has Reversed

Number of Homeowner Insurance Companies
in Texas



Source: TDI

What Needs To Be Done in Texas?

- Transition slowly to risk adjusted premiums
  - Limit rate regulation
    - Permit rate flexibility to transition to rates that reflect risk
    - Move away from prior approval regulation
  - Create the right incentives
    - encourage competitive entry and the inflow of capital into the state
    - Watch coastal development and maintain natural barriers
    - Promote mitigation policies