



December 13, 2010

Dear Chairman Corona, Taylor, and Committee Members,

Thank you for your diligence and the opportunity to offer public comments on the Texas Windstorm Insurance Association.

The Heartland Institute, a think tank that aims to discover, develop, and promote free-market solutions to social and economic problems, has long taken a strong interest in the nature and performance of residual property and casualty insurance markets. In this context, Heartland's Austin-based Texas office would like to offer some brief comments concerning TWIA's rates, the adequacy of rates, the availability of TWIA coverage, and the manner in which TWIA operates. We wish to make three major points:

- *TWIA's Rates are Insufficient*
- *TWIA Writes Far Too Many Policies*
- *Despite Generally Competent, Professional Management, Loopholes in State Tort Law Draw Into Question TWIA's Ability to Continue as a Going Concern*

### **TWIA's Rates are Insufficient**

TWIA sells too much coverage for too little money. Thus, its rates are inadequate. As a result of charging rates well below those of the private sector for many types of coverage, TWIA simply does not have sufficient capital—in reserves or reinsurance—to pay claims that are likely to occur.<sup>1</sup> If another storm similar to Ike hit Texas, TWIA would not be able to pay the claims. No private company would—or should—be allowed to price its products in manner like TWIA.

TWIA's inability to set the rates required to remain financially stable stems directly from political decisions made by Commissioner Mike Geeslin. While Geeslin has said that he supports higher TWIA rates, he has denied requests to raise them on multiple occasions.<sup>2</sup> TWIA's current rate structure and its inability to procure sufficient reinsurance crowds private capacity out of the market and leads to a retreat of the private market. The commissioner must approve higher TWIA rates without undue delay in order to address the risk of living along the coastline.

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<sup>1</sup> TWIA Income Statement for period ending July 31, 2010.

<sup>2</sup> Bob Graham. "Texas FAIR Rate Request Denial Disturbing, Analyst Says," Insurance and Financial Advisory, December 1, 2009. <http://ifawebnews.com/2009/12/01/texas-fair-plan-rate-request-denial-disturbing-analyst-says/>

## **TWIA Writes Far Too Many Policies**

In 2007, TWIA wrote just over 100,000 policies; today it writes nearly 250,000 (242,272 to be exact).<sup>3</sup> We believe that this growth—and taxpayers' assumption of liability for 130,000 properties that were previously secured by private homeowners insurance—demonstrates that TWIA coverage is *too available* and that the state entity is serving as a market for first resort rather than the market of last resort suggested in statute. According to the Property Insurance Plan's Services Office, indeed, TWIA is now the nation's largely beach plan by both total premium written and market penetration.<sup>4</sup> ***Between 2008 and 2009, TWIA was the only residual market property insurance mechanism in the country that expanded.*** Since many other factors—hurricane weather forecasts, availability of reinsurance on international markets, and availability of capital for other purposes—are by definition the same throughout the country, this strongly implies that TWIA's problems result from factors unique to Texas and its regulatory climate.

If TWIA is to shrink, it must engage in an aggressive campaign to depopulate its book of business. Additionally, since TWIA is a taxpayer supported entity, it should focus on helping those in true need. To this end, it should be prohibited from insuring vacation homes, homes worth more than \$1 million, and homes that have been rebuilt at least twice before.

## **Operation of TWIA**

TWIA's management, by all accounts, appears highly skilled at operating TWIA and managing its capital in a very challenging environment. That said, various aspects of the regulatory environment put TWIA's future at an enormous risk. In particular, the state's current tort climate poses a great risk to TWIA's ability to continue. A two year statute of would reduce bad faith claims and bring stability to the system.

In addition, with the recent reopening of claims from Hurricane Ike, TWIA is expected to exhaust all \$500M in reinsurance coverage and deplete the Catastrophe Reserve Trust Fund rather than assess the member insurance companies to cover the loss. The legislature will then have little choice but to authorize even more taxpayer-backed debt.

The legislature should bring permanent reform by requiring TWIA to purchase private reinsurance that has served it so well in the past. World reinsurance markets permit Texas to pool its own hurricane risks with that of international floods, accident, and cyclones, thus relieving taxpayers from the crippling effects of poor risk management.

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<sup>3</sup> TWIA Income Statement for period ending July 31, 2010.

<sup>4</sup> Property Insurance Plans Services Office. 2009 Fair and Beach Plan Underwriting Results and Market Penetration Report. "Summary of Five Year Data: 2005-2009," X. Boston: PIPSO, 2010.

## **Concluding Thoughts**

TWIA's writes too many policies and charges too little for them. While competently managed, aspects of the state's tort climate and the rising number of bad faith claims against it pose significant risk to its ability to continue on stable financial footing. The state must review TWIA's activities, restructure it, and modify the legal framework in which it operates.

Sincerely,

Julie Drenner

The Heartland Institute

Texas Director on the Center for Finance, Insurance, & Real Estate