

Seeking to create a new basis for allegations under Texas Ins. Code Article 21.21, Texas Insurance Commissioner Jose Montemayor has proposed a new rule making it an unfair or deceptive trade practice for Texas insurers to refuse to sell a homeowners policy based on a prior mold or water claim without first inspecting the property. The Commissioner's proposal will now undergo a review and comment process. This proposal is problematic for many reasons including its unprecedented restrictions on underwriting and the unjustified expansion of new statutory claims against insurers.

Here is the proposed rule can be reviewed at

SUBCHAPTER J. PROHIBITED TRADE PRACTICES 28 TAC §21.1007

The Texas Department of Insurance proposes new §21.1007, concerning unfair trade practices. The new section is proposed to eliminate unfair competition and unfair discrimination and to promote the availability and affordability of residential property insurance. The proposal prohibits an insurer from using water damage claim history as an underwriting guideline or to rate a new policy if an inspection has not been conducted by the insurer to determine the condition of the property. The proposed section is necessary as it has come to the attention of the Department that certain insurance companies are rating and declining to write residential property insurance policies based on the existence of a prior water damage claim. The apparent motivation for the use of water damage claim history to rate policies or as an underwriting guideline is to offset losses resulting from and to avoid future claims for mold damage. The Department believes that the decision to increase the premium on a policy or decline to write a policy based on water damage claim history rather than ascertaining the condition of the property through an inspection is unfair and should be prohibited. The denial or rating of insurance based on a prior water damage claim is based on the unsubstantiated assumption that a previous water damage claim resulted in improper repair of the damaged property. Whether or not prior water damage has been repaired can only be determined by an inspection of the property. The Department has previously prohibited underwriting guidelines based on the age and value of homes because of the unfair nature of guidelines that broadly deny coverage to a class of homes instead of underwriting each home based on the actual condition of the property. At the present time, although several insurers are using water damage claim history as an underwriting guideline, none have provided the data or actuarial analysis that shows the use of this guideline is actuarially sound. Further, underwriting guidelines based on water claim history without inspection abrogate an applicant's right to use the voluntary inspection program to qualify for a residential property insurance policy as established by the legislature in Texas Insurance Code Article 5.33B. Section 4 of Article 5.33B states, "the existence of an inspection certificate issued under this article creates the presumption that the property condition is adequate for residential property insurance to be issued." Section 4 (c) of Article 5.33B further specifies that "an insurer who receives an inspection certificate may not use property condition as grounds for refusing to issue or renew residential property insurance unless the insurer reinspects the property and specifies the areas of deficiency in its declination letter." Clearly, the legislature intended for consumers to be able to purchase insurance for their property or to be informed of the existing property conditions that need to be corrected to qualify for insurance and not be burdened with guidelines such as a prior water claim which they cannot erase from their record. However, an insurer may rate or decline to write residential property insurance based on a previous claim for water damage when the insurer has inspected the property using specific and objective criteria to evaluate the repair and has ascertained that the water damage has not been repaired.

The Department will consider the adoption of new §21.1007 in a public hearing under Docket Number 2532, scheduled for 9:30 a.m. on October 22, 2002, in Room 100 of the William P. Hobby, Jr. State Office Building, 333 Guadalupe Street, Austin, Texas.

Marilyn Hamilton, Associate Commissioner, Property and Casualty Division, has determined that for each year of the first five years the proposed section is in effect, there will be no fiscal implications for state government or local government as a result of enforcing or administering the proposed section. Ms. Hamilton has also determined that for each year of the first five years the proposed section will be in effect, there will be no adverse effect on local employment or the local economy.

Ms. Hamilton has further determined that for each year of the first five years the proposed section is in effect, the public benefit anticipated as a result of adopting the section will be the increased availability and affordability of residential property insurance through out the state. Additionally, insurers that conduct inspections of the property sought to be insured will glean much more objective information on which to base their underwriting decisions. Ms. Hamilton estimates that for the first year that the section is in effect, the primary cost to persons required to comply with the proposed section will be those costs that are required for the insurers to notify their personnel of the change in underwriting guidelines and rating and the updating of an agent's residential property policy writing manual with no additional costs to comply thereafter. The notification to the insurers' personnel would initially involve sending an electronic or paper copy memo to the affected persons informing them of the change in underwriting guidelines and rating. The labor cost estimate for sending this notification is estimated to be \$.50 per person notified and is based on a time estimate of 2 minutes for each notification at \$.25 per minute. The 2001 Occupational Employment Statistics survey published by the Texas Work Force Commission shows that the mean hourly wage for insurance processing clerks in Texas is \$14.68 and based on this statistic the labor cost for such clerks is approximately \$.25 per minute. The additional cost of sending this notice also includes \$.40 for postage and \$.05 for system, printing, and paper. The total estimated cost per notice is \$.95. The actual total cost to each insurer will vary depending on the number of agents that are employed by each insurer who would need to receive the notice. Additionally, it is likely that most of these notices will be sent electronically and since the computer systems needed to send these notices are already in place, the cost to provide the notices will probably be very minimal.

The updating of the insurers' residential property policy writing manual would involve amending the affected pages of the manual, printing the updated pages, and mailing them out to the agents. The labor cost estimate for amending the manual pages would be \$20 for each insurer that is currently using the prohibited guideline. This labor cost estimate is based on a time estimate of one hour for an insurance underwriter to make the necessary changes to the manual pages. The 2001 Occupational Employment Statistics survey published by the Texas Work Force Commission shows that the mean hourly wage for insurance underwriters in Texas is \$20.42. The labor cost estimate for handling the transmittal of the manual pages to the agents is estimated to be \$.75 per agent and is based on a time estimate of 3 minutes per transmittal at \$.25 per minute. The 2001 Occupational Employment Statistics survey published by the Texas Work Force Commission shows, as noted above, the labor cost for insurance processing clerks in Texas is approximately \$.25 per minute. The additional costs per transmittal of the manual pages also include \$.40 for postage and \$.05 for system, printing, and paper. The total estimated cost per transmittal of the manual updates is \$1.20. The actual total cost to each insurer will vary depending on the number of agents that are employed by each insurer who would need to receive the manual updates.

The assumptions on which these costs are based may change as the Department receives data during the comment period. The cost per hour of labor will not vary between the large and small businesses. There is no anticipated adverse economic effect on small or micro-businesses who are required to comply with the proposed section other than those outlined above and these businesses should recognize benefits through the revitalization of the economy resulting from the increased availability and affordability of residential property insurance. Regardless of the economic effect, it is neither legal or feasible to waive the requirements of the proposed rule for small or micro-businesses because of the disparate treatment that would result to consumers if small and micro-businesses were able to apply a different claims underwriting and rating standard.

To be considered, written comments on the proposed section must be submitted no later than 5:00 p.m. on October 21, 2002 to Gene Jarmon, Acting General Counsel and Chief Clerk, MC 113-2A, Texas Department of Insurance, P. O. Box 149104, Austin, Texas, 78714-9104. An additional copy of the comment should be simultaneously submitted to Marilyn Hamilton, Associate Commissioner, Property and Casualty Division, MC 104-PC, Texas Department of Insurance, P. O. Box 149104, Austin, Texas, 78714-9104.

The new section is proposed pursuant to the Insurance Code Articles 21.21, 5.33B, 5.98 and §36.001. The Insurance Code Article 21.21 §13(a) provides that the Commissioner of Insurance may promulgate and enforce reasonable rules and may order such provision as necessary to accomplish the purposes of Article 21.21. Article 21.21 §1(a) provides that the purpose of Article 21.21 is to regulate trade practices in the business of insurance by defining, or providing for the determination of, all such practices in this state which constitute unfair methods of competition or unfair or deceptive acts or practices and by prohibiting the trade practices so defined or determined. Article 21.21 §1(b) provides that Article 21.21 shall be liberally construed and applied to promote its underlying purposes as set forth in §1 of Article 21.21. Article 21.21 §3 provides that no person shall engage in this state in any trade practice which is defined in Article 21.21 as, or determined pursuant to Article 21.21 to be, an unfair method of competition or an unfair or deceptive act or practice in the business of insurance. Article 5.33B establishes a voluntary inspection program to further the availability of residential property insurance for those that meet minimum standards for property condition insurability. Article 5.98 provides that the Commissioner of Insurance may adopt reasonable rules that are appropriate to accomplish the purposes of Chapter 5, Texas Insurance Code, Rating and Policy Forms, and which contain statutes governing residential property insurance. Insurance Code §36.001 authorizes the Commissioner of Insurance to adopt rules for the conduct and execution of the duties and functions of the Texas Department of Insurance only as authorized by statute.

The following statutes are affected by this proposal: Insurance Code Articles 21.21, 21.49-2B, 21.49-2E, and 5.33B

§21.1007. Prohibition of the Use of Underwriting Guidelines Or Rating Based On A Water Damage Claim.

(a) Purpose. The purpose of this section is to address unfair competition and unfair discrimination in the residential property insurance market and promote the affordability and availability of residential property insurance by prohibiting insurers from rating or declining to write residential property insurance based on a previous claim for water damage on the property sought to be insured when the insurer has not inspected the property to ascertain the condition of the premises and whether or not the water damage has been repaired.

(b) Definitions. The following words and terms, when used in this section, shall have the following meanings, unless the context clearly indicates otherwise.

(1) Residential property insurance--Insurance against loss to real or tangible personal property at a fixed location provided in a homeowners policy or residential fire and allied lines policy.

(2) Underwriting guideline--A rule, standard, marketing decision, guideline, or practice; whether written, oral, or electronic; used by an insurer or its agent to bind, accept, reject, cancel, or limit coverages made available to classes of consumers.

(3) Consumer--The person making the application to insure a property and includes both existing insureds and applicants for insurance.

(c) Prohibition.

(1) An insurer shall not use an underwriting guideline or rate based on a previous claim for water damage in making a decision regarding the writing of residential property insurance.

(2) The failure to comply with this subsection constitutes an unfair trade practice in the business of insurance in violation of the Texas Insurance Code Article 21.21, and shall be subject to the provisions thereof.

(d) Exception. An insurer may rate or decline to write residential property insurance based on a previous claim for water damage on the property sought to be insured when the insurer has inspected the property, using specific and objective criteria to evaluate the repair, and has ascertained that the water damage has not been repaired.