



Consumer Federation of America

Comments of Consumer Federation of America During Workshop Regarding Catastrophe Modeling and Ratemaking

April 23rd, 2024

Thank you for this opportunity to comment on the Department's draft regulations to allow property and casualty insurers to use catastrophe models for the purposes of ratemaking in homeowners insurance and other lines. I am Michael DeLong with Consumer Federation of America, an association of consumer organizations across the country, founded in 1968 that works to advance the consumer interest through research, advocacy, and education. Please note that these comments also reflect the views of CFA-member organization Consumer Federation of California.

California can be a leader in ensuring that the best science is deployed by insurers to help the property insurance market, state regulators, and the public to understand, price, and mitigate climate change-driven risk. But to accomplish that, the rules for the use of catastrophe models must not compromise transparency and public scrutiny to preserve corporate secrecy.

As a starting point, we want to note that we were surprised and dismayed that the draft regulations neither propose to create nor even contemplate a public wildfire model for California. Virtually every consumer representative who has presented on this topic has urged the Department to move in this direction. But this draft does nothing that leads toward a modeling framework that is explicitly constructed in the public interest.

We believe that the Department of Insurance and State of California, in partnership with the state's world class public research universities, could develop a robust catastrophe model that could meet the critical risk projection needs of insurers. We urge the Department to use this opportunity to re-craft the draft regulations such that they are focused on the build out of a public model that would be the default tool for determining the appropriate wildfire catastrophe adjustment to incorporate into property insurers' rates. We do not mean to suggest that this is a simple project, just that it is a critically important one. This is the moment to get this right.

Even if, through this process, the Department develops an effective mechanism to allow for public scrutiny of private catastrophe models, the Department needs a reliable benchmark for evaluating those models. If a private model used by an insurer produced a rate that was significantly different from the public California wildfire model, the Department would know that further scrutiny of the insurer's modeling was needed to ensure it was not producing an excessive, inadequate, or unfairly discriminatory rate and to correct errors identified through this benchmarking process. But the Department would need to lead this effort, and we do not see that in this draft.

With respect to the “pre-application required information determination” (PRID) procedure, we will briefly highlight a few of our concerns.

The output of the PRID procedure is extremely vague. It does not require that a rate filing that relies on that model include any actual data or scientific support or measures of uncertainty or sources of information. The only required result of the PRID is that a rate filing includes “Information that demonstrates the model uses established concepts, data, equations, and principles,” *etc.* Without much more precise minimum requirements, every PRID procedure could end up with nothing more than a formal statement that merely says that the Model Advisor has determined that the model uses established concepts, data, *etc.* In essence, all this requires is a stamp of approval coming out of the confidential procedure. Any actual scrutiny would have happened behind closed doors with all participants legally bound to refrain from detailing what, for example, they may have found to be deeply flawed about the scientific information or any other aspects of the model.

But even this closed door, confidential scrutiny of the catastrophe model does not appear to demand any conclusions about model reliability, robustness, fairness, or any consumer protection standard whatsoever. While there are standards of practice rules governing the acceptability of the model in the draft regulation and the secret PRID hearings appear to allow for examination of the model, the Model Advisor is not tasked with making rulings on or ordering changes to the model. Instead, this is just a process for determining what needs to be included in the filing. Any problems identified during the PRID die in the PRID once the Model Advisor provides the necessary affirmation, and the Commissioner and public will never be allowed to know about those problems.

Even if the Model Advisor determines that more than an affirmation was required to be transmitted, the draft regulation does not provide any threshold required data, information, scientific reliability, *etc.* that would be essential for rate review in every instance in which modeling is used. This lack of clear standards of minimally required technical information would result in uneven public access to, and regulatory scrutiny of, insurers’ use of these models. Additionally, nothing in the draft regulation requires any testing of the model for biases or other unintended disparate impacts the model may have on people of color or others according to their protected class status.

As we conclude, we want to highlight that there is nothing in this testimony that is meant to oppose the notion that modeling techniques can help improve insurance ratemaking in an environment in which climate change has altered the risk landscape in California and across the globe. To protect Californians and the insurance market, the Department should work to elicit the best approaches to managing the strengths and weaknesses of models for achieving this response to climate risk. But this draft regulation provides no roadmap for California to have a model built to do that in a manner that prioritizes the public interest. Instead, it focuses on how to preserve corporate privacy in matters that are of critical public importance.

The Consumer Federation of America will continue to engage with the Department as you continue to refine your thinking on this issue, and we appreciate the opportunity to present.

Julia Borman from Verisk: thank you to the Department for holding this workshop. Cat modeling is standard practice in the insurance industry and this draft regulation will help modernize California's insurance market. Initial draft is a good first step, but the overall language needs work. Our written comments have more details. Evaluation criteria are not well defined. Review process has the potential to be quite unwieldy—a lot of participants, too much time, and not enough protection for intellectual property.

Draft regulation should be amended to make it clear that the modelers will initiate the review process. California can benefit from lessons in other states, especially in the case of a timeline. Modeler should arrive prepared with baseline materials, regulator reviews them, parties to PRID have the opportunity to ask additional questions.

Allison Adey on behalf of Personal Insurance Federation and NAMIC: We support the goals of the draft regulations, which include rate stability and promoting fairness, as models account for risk mitigation trends. We are concerned that PRID is completely open-ended with no specified time frame for completing the model review. It's like a drawn out legal process—allows anyone to initiate a procedure and provides compensation, which will hinder and delay model approvals just like the current rate approval process. Models are also defined too broadly.

Quick action is needed to stabilize the market and help consumers. We don't think these regulations, as currently drafted, will result in models being approved anytime soon. We recommend these regulations require model review to be completed within three months.

Jamie Knippen from CoreLogic: we are a provider of risk models and seek to quantify risk, including wildfire risk. Cat models are the most fair and accurate way to quantify risk for a business, and California's proposal to allow their use is in the public interest. There is need for further clarifications from CDI about PRID procedure—we will submit a detailed written review. Public information should also exclude confidential information. Shorten the approval process.

Based on wildfire science, cat models deliver a solid platform to base loss reduction strategies on. We are excited to participate in the next steps.

Staci Heaton: I represent 40 rural counties statewide and we have experienced a lot of wildfires, have high insurance rates and rates of nonrenewals. We are very invested in this process. We don't have a position on cat modeling but do have a position on transparency. Whatever models are used need to be as transparent as possible, so consumers know exactly how the rates are being set. We have people who can't get their fire risk any lower but they are still being nonrenewed.

Stephen Young: we strongly support use of cat models in ratemaking. We have submitted a detailed statement. Discussion draft places the burden of proof on establishing actuarial

credibility of models on the insurers. But the draft repeatedly requires insurers to prove they are using the most sound and best scientific information. We regard that as problematic—it implies there is a single demonstrable best approach, which may not be true. Affordability crisis is getting worse. We commend to the Commissioner that regulations and procedures should be quickly implemented—allow quick use of models.

Carmen Balber from Consumer Watchdog: we are very concerned with the state of the regulation as proposed. Algorithms and intelligence will just be tools for price gouging unless the insurance mandates real transparency and has strong regulations. We have repeatedly urged the creation of a public model with deep scientific expertise. This regulation is designed to avoid Prop 103 by creating a pseudo review of models that won't be helpful with little real input from consumers. This regulation does not require review or approval or a model's accuracy. A proposal that protected consumers would identify uniform standards and include uniform requirements for disclosure of information.

Florida, by contrast, has very strong hurricane standards in its models. Models are often inaccurate and contain biases that can perpetuate racism and redlining. Regulation doesn't even mention basic testing. And there is no independent panel. Regulation would allow insurers to evade review, it is a recipe for unjust rate hikes. We urge CDI to have a public cat model and have submitted detailed written comments.

Karl Susman: cat modeling is the rigorous analysis of the potential financial consequences of a loss. With the help of massive data models and sophisticated computers and research, there is a better way to predict future events—cat modeling. It isn't that new. Every state except California allows its use. We support cat modeling.

Sarah Heard: TNC supports the proposed regulation allowing CAT models. We urge you to include more specificity on forests. This is a big step forward. We published a white paper about the insurance benefits of forest restoration.

Carly Fabian from Public Citizen: we urge regulators to recognize the limits of cat models and make sure the benefits go to consumers. Draft regulation—we are concerned that there won't be meaningful transparency and urge you to develop a public model. California is uniquely positioned to lead on this issue. Consider how forward looking data models should take forward looking data and assessments into account. Insurers are not likely to make progress in this area on their own.

Glen Daraskevich: Department should make models confidential.

Bernard Molloy: you should look at the mitigation steps that cities and counties have taken, and how they can be incorporate in the cat models.