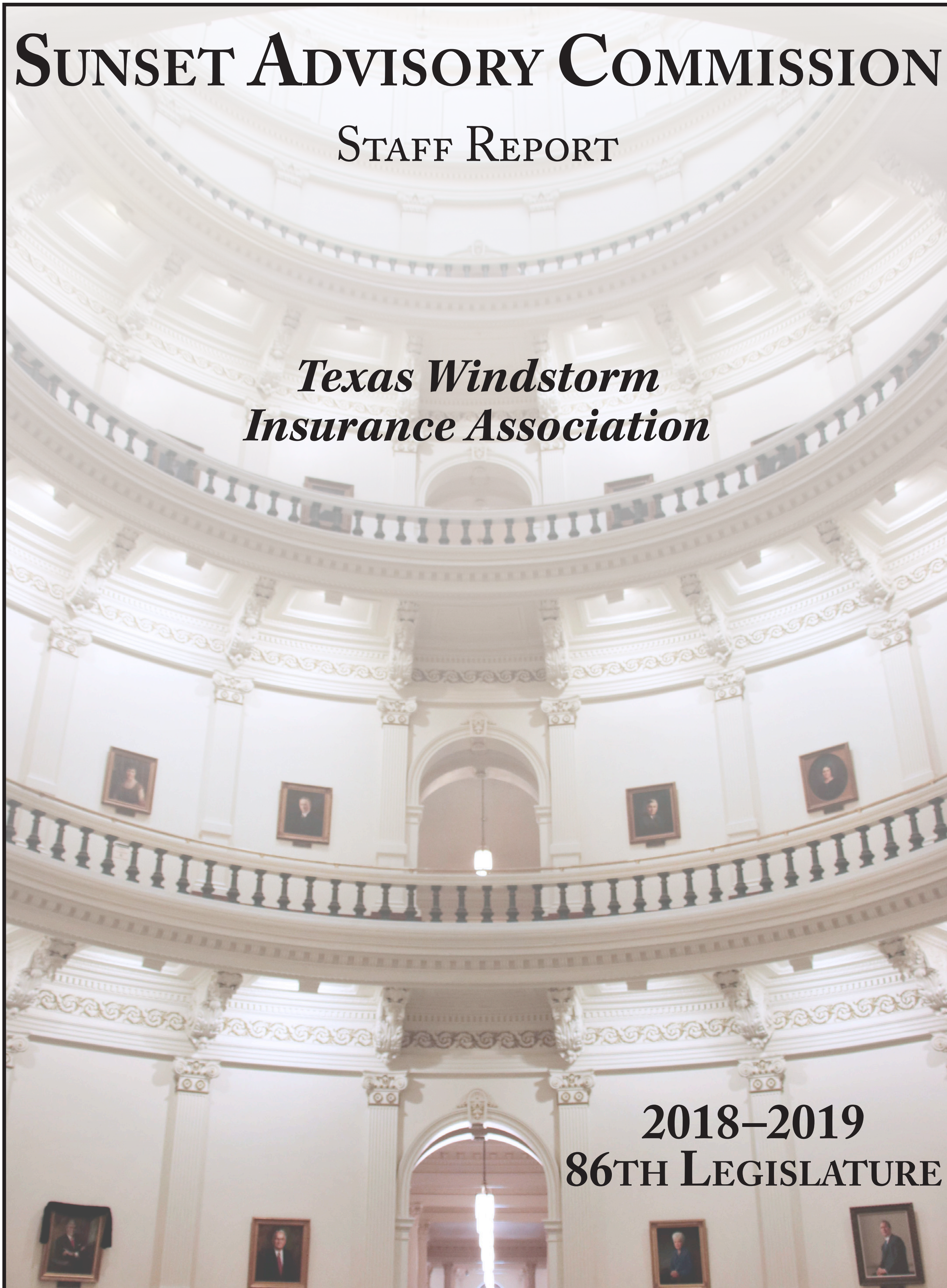
Sunset Advisory Commission

Staff Report



Texas Windstorm Insurance Association

2018–2019
86th Legislature

Sunset Advisory Commission

Cover Photo: The Texas Capitol rotunda houses the Texas Governors and Presidents Portrait Gallery. The gallery includes portraits of every government leader in Texas' history, including several presidents when Texas won its independence from Mexico and became a republic. Photo Credit: Janet Wood

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How to Read Sunset Reports

Each Sunset report is issued *three times*, at each of the three key phases of the Sunset process, to compile all recommendations and actions into one, up-to-date document. Only the most recent version is posted to the website. (**The version in bold is the version you are reading**.)

1. Sunset Staff Evaluation Phase

   Sunset staff performs extensive research and analysis to evaluate the need for, performance of, and improvements to the agency under review.

   First Version: The *Sunset Staff Report* identifies problem areas and makes specific recommendations for positive change, either to the laws governing an agency or in the form of management directives to agency leadership.

2. Sunset Commission Deliberation Phase

   The Sunset Commission conducts a public hearing to take testimony on the staff report and the agency overall. Later, the commission meets again to vote on which changes to recommend to the full Legislature.

   Second Version: The *Sunset Staff Report with Commission Decisions*, issued after the decision meeting, documents the Sunset Commission's decisions on the original staff recommendations and any new issues raised during the hearing, forming the basis of the Sunset bills.

3. Legislative Action Phase

   The full Legislature considers bills containing the Sunset Commission's recommendations on each agency and makes final determinations.

   Third Version: The *Sunset Staff Report with Final Results*, published after the end of the legislative session, documents the ultimate outcome of the Sunset process for each agency, including the actions taken by the Legislature on each Sunset recommendation and any new provisions added to the Sunset bill.

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Summary of Sunset Staff Recommendations

Summary

The Legislature created what is now known as the Texas Windstorm Insurance Association (TWIA) in 1971, after Hurricane Celia caused significant damage to the coast. For the next 30 years TWIA operated largely under the radar until 2008, when Hurricane Ike exposed how unprepared TWIA was to handle a major storm. TWIA received more than 90,000 claims, swamping its small and inexperienced staff. TWIA took more than 250 days on average to pay out the claims, policyholders ended up disputing 10,000 of the claims, and lawsuits from these claims continue to this day. In 2009, in response to TWIA's poor handling of Hurricane Ike claims, the Legislature began reshaping TWIA, making significant changes to its statute and funding structure, and charging the Texas Department of Insurance with more oversight of TWIA's operations. This Sunset review is the latest in a long line of reviews and audits of TWIA, but it is particularly timely, as Hurricane Harvey presented the first true test of TWIA since its overhaul. Although TWIA's operations demonstrate significant improvement, Hurricane Harvey revealed fundamental flaws in the design of TWIA's funding structure and highlighted TWIA's contradictory directives.

TWIA's long-term stability and financial health ultimately depend on legislative action.

In the aftermath of Hurricane Harvey, TWIA is broke, in debt, and facing a shrinking revenue pool. The Legislature designed TWIA to balance competing interests: first, to provide insurance to those who cannot purchase it elsewhere and second, to rely primarily on premiums and debt repaid by policyholders for its funding, with TWIA receiving no general revenue or tax dollars. These mandates create an inherent tension. Despite complaints from coastal communities about the cost of windstorm insurance, TWIA provides the majority of residential windstorm insurance on the coast, providing a large pool of premiums. However, TWIA's premiums are not high enough to cover the cost of future claims and expenses. Keeping premiums as they are means financing these future claims with debt, which is expensive for the policyholders who have to repay it. At the same time, raising premiums to make TWIA's funding design sustainable may make windstorm insurance too expensive for some coastal residents. In effect, this system of opposing forces leaves TWIA policyholders alone to weather the storms.

TWIA is only subject to review, not abolishment, under the Sunset Act, so the Sunset Commission and Legislature do not have to take any action to continue TWIA.[1] However, the Sunset review found Texas has a continuing need for adequate windstorm insurance, but TWIA's current structure, particularly its funding arrangement, is too uncertain to endorse. While Sunset staff would normally provide recommendations to help improve TWIA's structure, staff cannot recommend a clear path to a sustainable structure that does not run afoul of one or the other legislative mandates presently controlling TWIA. Ultimately, TWIA's long-term stability and financial health depend on the Legislature taking action.

Stabilizing TWIA's structure would require the Legislature to focus on either ensuring TWIA insurance is available and affordable to those who need it most, or supporting and shoring up TWIA's current funding structure by allowing TWIA to function like an independent insurance company with adequate (higher) rates and fewer restrictions. In Issue 1, Sunset staff outlines steps the Sunset Commission or Legislature could take to help stabilize TWIA by supporting one mandate over the other, and provides information on entirely different structures that could also be considered. Sunset staff does not take a position on any of these options, but felt the review of TWIA would be incomplete without providing information needed to help the commission or the Legislature improve TWIA's structure and stability, should either choose to do so.

The subsequent issues in the report include more typical Sunset staff recommendations to improve the effectiveness and efficiency of TWIA's operations and focus TWIA on its core functions, regardless of its structure. Sunset staff recommends changes to improve TWIA's customer service, decrease costs to policyholders, and ensure TWIA can respond more quickly to legislative changes. For example, Sunset staff recommends allowing policyholders to pay premiums in installments and streamlining policy renewal, allowing policyholders to avoid the cost of premium financing and reducing administrative burdens. Additional recommendations would ensure TWIA communicates better with its stakeholders, handles claims in a timely and fair manner, and minimizes surprises when policyholders go through the claims process. While these recommendations would work within any structure, they would do little to improve the state of windstorm insurance along the Texas coast without additional solutions to address TWIA's underlying design. The following material summarizes Sunset staff recommendations on the Texas Windstorm Insurance Association.

Issues and Recommendations

Issue 1

TWIA's Competing Statutory Mandates Leave Its Sustainability in Question.

To ensure Texans can continue to live and work in our coastal communities, the state has a continuing need for adequate windstorm insurance. However, the Legislature has given TWIA opposing mandates that are driving TWIA to the brink of financial extinction. TWIA's current funding structure centers on premiums and debt repaid by premiums. TWIA's revenue from premiums is not enough to pay future claims, meaning TWIA will likely have to go into more debt if there is another hurricane — further increasing costs to policyholders. At the same time, the Legislature designed TWIA to provide insurance for those who cannot purchase it elsewhere. If TWIA were to regain financial stability through raising premiums, TWIA may become too expensive for coastal residents. Restructuring TWIA to embrace one mandate or the other would ensure TWIA can sustainably fulfill its mission. Either method would improve the financial health and long-term outlook of TWIA.

Key Recommendation

- Continue TWIA as an insurer of last resort, or continue TWIA as an insurance company reliant primarily on premium funding.

Issue 2

Inefficient Renewal Requirements and Payment Policies Increase Costs for Policyholders.

TWIA's insurance policy renewal process is unnecessarily burdensome, increasing costs for policyholders and workloads for insurance agents. Further, TWIA's statutory inability to accept installment payments causes some policyholders to incur additional financing costs on top of their premium payments. TWIA also increases workload by not billing policyholders directly or accepting credit card payments. Streamlining renewal and payment processes would allow TWIA to provide better customer service and reduce workload for insurance agents.

Key Recommendations

- Require TWIA to automatically offer policy renewal unless new information is necessary.
- Authorize TWIA to accept installment premium payments and credit card payments.
- Establish separate insurance agent commission rates for new applications and automatic renewals.
- Direct TWIA to directly bill customers for premiums for automatic renewals.

Issue 3

Despite Improvements in Claims Handling, TWIA's Hurricane Harvey Response Highlights Difficulties for Policyholders.

Although TWIA has greatly improved its claims handling since Hurricane Ike in 2008, confusion over TWIA's claims process has led to frustration for policyholders, and the Sunset review found areas where TWIA could benefit from further improvements. Specifically, having clear authority in statute to issue supplemental payments, a standard tool private insurers use to settle claims more quickly, would help TWIA address policyholder concerns about delayed claims processing and low claims payments. Additionally, removing the statutory requirement to assess the replacement cost of a property at the time of loss would help limit confusion and uncertainty for TWIA policyholders. Finally, TWIA could improve its response to policyholder frustration over claim resolution by implementing a post-hurricane communication plan with more continuous input and feedback from policyholders.

Key Recommendations

- Authorize TWIA to issue supplemental payments.
- Require TWIA to only assess the replacement cost of a property at the time TWIA issues or renews the policy.
- Direct TWIA to develop a post-hurricane communication plan with more input from stakeholders.

Issue 4

TWIA's Assumption Reinsurance Depopulation Program Is Unnecessarily Complicated and Inefficient.

Statute requires TWIA to administer two depopulation programs to reduce the number of TWIA policies. While both programs have moved thousands of policies to the private market, the Assumption Reinsurance Depopulation Program is extremely complex to administer and creates unnecessary confusion. The program's complexity requires logistical and financial gymnastics for both TWIA and the participating insurance companies, and understandable policyholder confusion causes delays in claims handling. Further, insurance company interest in the Assumption Reinsurance Depopulation Program is limited and many insurance agents either cannot or choose not to participate, making the program inefficient. Discontinuing the Assumption Reinsurance Depopulation Program would allow TWIA to operate more efficiently and decrease policyholder confusion. TWIA would continue to see the benefits of depopulation through the administration of its other, less complicated depopulation program.

Key Recommendation

- Eliminate the Assumption Reinsurance Depopulation Program.

Issue 5

TWIA's Process for Issuing Windstorm Certificates of Compliance Is Duplicative and Poses Risks to Public Safety.

The Texas Department of Insurance (TDI) sets the windstorm building code to ensure buildings along the coast can weather serious storms. Both TDI and TWIA issue a certificate of compliance to certify buildings meet the windstorm code. However, TWIA is ill suited to ensure windstorm code compliance, as TWIA is not a regulatory state agency. Additionally, the existing process at TWIA for property owners to get a certificate is insufficient to account for any construction errors and potentially exposes TWIA to additional liability when insuring properties. TDI has an existing regulatory framework to ensure compliance, respond to complaints, and provide necessary expertise. Consolidating all windstorm certificate issuance at TDI would increase customer service, decrease duplication of efforts, and ensure certified buildings meet windstorm code.

Key Recommendations

- Transfer the issuance of WPI-8-C windstorm certificates from TWIA to TDI.
- Remove the ability to obtain a WPI-8-C windstorm certificate based on design alone.

Issue 6

TWIA Lacks Certain Good Government Standards That Would Enhance Responsiveness, Transparency, and Accountability.

The Sunset review found TDI's current rulemaking process for TWIA impedes TWIA's ability to quickly implement statutory changes and respond nimbly to stakeholder needs. Since TWIA is not a state agency it cannot have rulemaking authority, but it could operate in a manner similar to an advisory board under a regulatory agency. Expressly authorizing TWIA to propose rules and requiring TDI to take action would give TWIA's stakeholders another forum to provide feedback, and also would allow TWIA to react to circumstances more efficiently. Additionally, TWIA could benefit from applying several standard elements considered in all Sunset reviews to ensure open, responsive, and effective government. TWIA's governing statutes do not include a standard provision relating to board member training, which would ensure members understand the board's role in rulemaking, nor does statute include a provision about public member conflicts of interest, which would provide some measure of accountability to ensure board members do not take advantage of their official positions.

Key Recommendations

- Authorize TWIA to formally propose rules to TDI.
- Apply standard across-the-board requirements related to public membership.
- Require TWIA board members to publicly disclose specific conflicts of interest.

Fiscal Implication Summary

Overall, the recommendations in this report would have no fiscal impact to the state, as TWIA is not a state agency and receives no funding from tax dollars or the General Revenue Fund. However, as summarized below, some recommendations could have a fiscal impact to TWIA or the state that cannot be determined at this time.

Issue 1 — The recommendations would have a significant impact on ensuring TWIA is financially solvent and able to provide windstorm and hail insurance on the Texas coast.

Issue 5 — TDI already has processes in place for issuing and managing certificates of compliance that could be used for issuing TWIA's certificates of compliance. While TDI currently provides certificates of compliance at no cost, statute authorizes TDI to charge a fee for certificates of compliance, and TDI can ensure the fee covers the cost of issuing the additional certificates if necessary.

1 All citations to Texas statute are as they appear on http://www.statutes.legis.texas.gov/. Section 2210.002(b), Texas Insurance Code.

Association at a Glance

Association at a Glance

The Texas Windstorm Insurance Association (TWIA) is a nonprofit insurance provider created by the Legislature in 1971 with the purpose of being an insurer of last resort on the Texas coast.[1] As identified in the map, *TWIA Coverage Area,* TWIA provides windstorm and hail insurance for residential and commercial property owners in designated coastal counties who are unable to purchase coverage in the private insurance marketplace.[2] Insurance policies from TWIA supplement traditional property insurance and do not cover flood, fire, theft, or other threats. In 2017, TWIA had about 240,000 policies covering more than $60 billion in property value. Like private insurance companies, TWIA operates with regulation and oversight from the Texas Department of Insurance.

TWIA Coverage Area

Key Facts

- **TWIA board**. The TWIA board of directors, as shown in the table below, consists of nine members appointed by the commissioner of the Texas Department of Insurance, who each serve staggered three-year terms.[3] Three members are industry representatives from companies actively writing and renewing windstorm and hail insurance plans along the coast, three are public members living in different coastal counties served by TWIA, and three are public members who live more than 100 miles from the coast.[4] Additionally, one of the three coastal public members must be an insurance agent. The board does not have rulemaking authority but instead makes recommendations to the commissioner of insurance. The board elects its own chair, vice chair, and secretary/treasurer.[5]

TWIA Board of Directors

Board Member	Qualification
Joshua Fields, Chairman	First Tier Coastal Representative, Harlingen – Insurance Agent
Bryan Shofner, Vice Chairman	Non-Coastal Representative
Debbie King, Secretary/Treasurer	Industry Representative
Michael Gerik	Industry Representative
Karen Guard	Industry Representative
R. Scott Kesner	Non-Coastal Representative
Georgia R. Neblett	First Tier Coastal Representative, Port Aransas
Tony Schrader	Non-Coastal Representative
Chandra Womack	First Tier Coastal Representative, Texas City

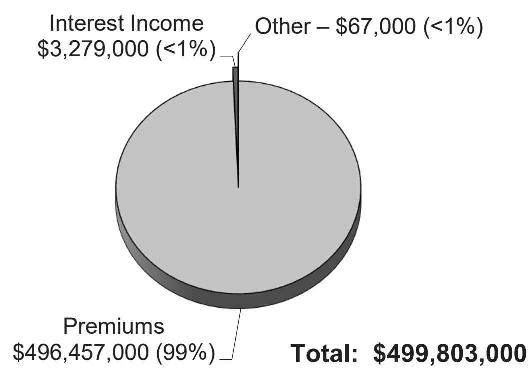
- **Association membership**. Companies providing property insurance in Texas are required to be members of the association unless they qualify for a specific exception, like operating as a farm mutual insurance provider.[6] Member assessments help pay claims and operating expenses of TWIA in the event premiums and other sources of revenue do not fully cover its costs.[7] Member assessments cannot exceed $1 billion collectively in response to a single year's funding needs.[8] When required, each company pays assessments in proportion to their share of business across the state, offset by their coastal windstorm market share. To pay Hurricane Harvey claims, TWIA required additional funding from member assessments for the first time since Hurricane Ike in 2008. In 2018, TWIA collected $281 million in member assessments from 143 member companies. The largest eight companies contributed more than $10 million each; the majority contributed less than $500,000 each.

- **Funding**. TWIA does not receive any appropriations from the General Revenue Fund or any tax dollars. TWIA operates primarily on premiums collected from policyholders, and its expenditures vary widely from year to year, depending on the number and severity of claims. In years without a major coastal storm, TWIA uses annual premium revenues to pay claims and often generates a surplus that is deposited in the Catastrophe Reserve Trust Fund (CRTF), an account outside of the treasury managed by the state comptroller that held almost $750 million before Hurricane Harvey.

  In years with a major storm, TWIA is likely to withdraw funding from the CRTF and may need additional funding to pay for claims and operations. Each year, TWIA must secure funding sources to cover the cost of a storm with a 1 percent chance of occurring through a complex mix of bonds repaid by future premiums, assessments from member insurance companies, and reinsurance.[9] Unlike bonds issued by state agencies, bonds issued by TWIA are not backed by the full faith and credit of the state.[10] Appendix A and Issue 1 provide more detail on how TWIA secures funding after major storms.

  In 2016, the most recent calendar year without a major storm, TWIA collected about $500 million in revenue and expended about $353 million.[11] TWIA deposited the remaining $147 million in revenue into the CRTF. The pie chart, *Texas Windstorm Insurance Association Sources of Revenue*, shows TWIA's funding in 2016, which was primarily comprised of policyholder premiums.

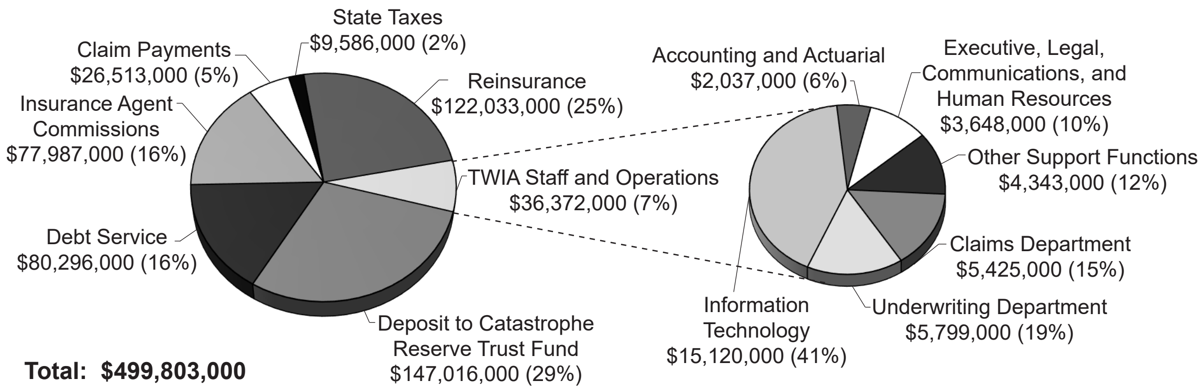
  Texas Windstorm Insurance Assocation Sources of Revenue – 2016

  The pie chart on the following page, *Texas Windstorm Insurance Association Expenditures*, shows expenditures during 2016, including the surplus funds deposited to the CRTF. Statute requires TWIA to deposit any excess revenue into the CRTF to pay claims when there is a large storm or hurricane.[12] Major expenses in 2016 included reinsurance, which is insurance for insurance companies; debt service on bonds; commissions for insurance agents; and claims payments. TWIA reports that as an insurance provider it is not subject to state historically underutilized business purchasing requirements and, as a result, does not have a formal policy to encourage or track the use of historically underutilized businesses.

  In 2017, TWIA's expenditures significantly increased due to Hurricane Harvey, totaling $1.7 billion. In addition to revenue from premiums, TWIA used $743 million from the CRTF, $448 million in bond proceeds from a previous bond issuance, and $281 million in member assessments. Expenditures for personnel increased by about 200 percent to $59.2 million, and claims payments increased by more than 4,800 percent to $1.3 billion, due to the large number of claims and corresponding need for additional staff.

Texas Windstorm Insurance Association Expenditures – 2016



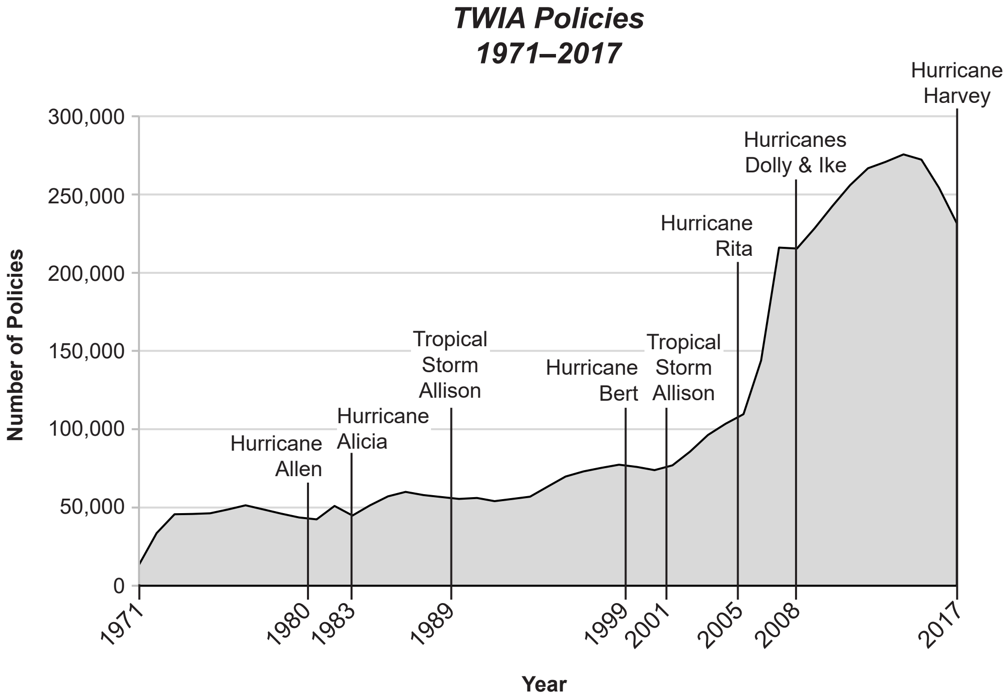
- **Staffing**. In 2016, TWIA employed 218 staff at the agency's headquarters in Austin, with an additional 25 contract employees and a third-party call center. The 218 employees work for both TWIA and Texas FAIR Plan — another insurance plan administered by TWIA — and are allocated based on need. TWIA alone required about 158 full-time employees in 2016. At the end of 2017, TWIA had 228 employees and an additional 402 contracted staff. TWIA employees are not state employees and do not receive state benefits. Appendix B compares TWIA's workforce composition with the percentage of minorities in the statewide civilian workforce for the past three years.

  Unlike some major private insurance companies, TWIA does not contract with or employ insurance agents, but instead pays a commission to agents from other carriers or independent agencies who represent property owners purchasing insurance from TWIA. TWIA also does not employ its own adjusters; independent adjusters assess claims and TWIA pays these adjusters as contractors. At its peak, TWIA had nearly 2,500 independent adjusters handling Hurricane Harvey claims.

- **Insurance underwriting**. TWIA's primary function is to provide insurance to coastal property owners unable to buy insurance for wind and hail damage through the private market. Like other insurance providers, TWIA has an underwriting department, which issues policies after assessing properties for eligibility and insurability. To be eligible to purchase insurance from TWIA, property owners must have a declination of coverage from a private insurance company, insurable property that may need to be certified as meeting building codes for withstanding storms, and, if appropriate, flood insurance.[13] TWIA cannot decline customers for other factors, such as credit scores or income levels, like private insurance companies can.

  The chart on the following page, *TWIA Policies*, shows the number of policies TWIA has written each year since its creation in 1971, after Hurricane Celia, as well as some of the other major storms that impacted the Texas coast. The number of TWIA policies increased significantly after costly storms in the early 2000s, including Hurricane Katrina, resulted in private insurers leaving coastal windstorm markets nationwide. In 2017, TWIA had 231,633 residential policies and 11,008 commercial policies, which represent approximately 51 percent of the property insurance policies in the 14 eligible counties. Galveston, Brazoria, and Nueces counties have the highest number of TWIA policyholders.

- **Claims**. The claims department assesses storm damage, pays policyholder claims, and handles disputes about coverage and claims payments. Coverage for a claim typically includes replacement cost and, if necessary, living expenses while the policyholder's home is being repaired. TWIA processed 18,889 claims in 2015 and 8,393 in 2016.



As of July 2018, TWIA had received 76,056 claims for Hurricane Harvey damage, 95 percent of which have been closed. Typically, TWIA closes claims within 16 days, but Hurricane Harvey claims took an average of 40 days due to the high volume. Around 3,250 Hurricane Harvey claims (4.3 percent) are in some phase of dispute, which includes about 700 in the initial stages of litigation.

- **Depopulation**. In 2015, to encourage growth in the private coastal insurance market, the Legislature authorized two programs designed to shift policies out of TWIA and into private insurance companies through a process called depopulation.[14] Under the depopulation programs, TWIA shares policy information with participating private insurers who can make offers to take over TWIA policies subject to approval by the policyholder and their insurance agent. The Voluntary Market Depopulation Program allows insurers to make offers on a policy-by-policy basis when each policy comes up for renewal, while the Assumption Reinsurance Depopulation Program follows a structured timeline to transfer a large number of policies on June 1 each year. Between the start of the depopulation programs in 2015 and June 1, 2018, TWIA has transferred 15,761 policies to six companies in the private market.

- **Windstorm certification**. To obtain insurance from TWIA, most property owners must have a windstorm certificate of compliance that verifies the property meets applicable building code requirements for withstanding major storms. The Texas Department of Insurance oversees the traditional certification process, which involves inspections throughout the construction period, while TWIA oversees the process for certificates of compliance on completed projects, where inspections are not required during construction.[15] TWIA issued 4,422 certificates of compliance on completed projects in 2017 and an additional 8,984 in the first half of 2018.

- **Texas FAIR Plan**. The Legislature authorized the creation of the Texas Fair Access to Insurance Requirements (FAIR) Plan Association in 1995. In 2002, the commissioner of insurance activated the Texas FAIR Plan to address insurance availability problems resulting from the mold crisis.[16] The mold crisis arose after high numbers of mold and water damage claims were filed in Texas and private insurance companies significantly reduced selling new and renewed insurance policies to

Texans. The Texas FAIR Plan provides residential property insurance throughout the state when no private company will provide coverage, currently having almost 105,000 policies in force.[17] The Texas FAIR Plan is a separate company and has its own governing board, but is administered by TWIA through a service agreement.

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1 All citations to Texas statutes are as they appear on http://www.statutes.legis.texas.gov/. Section 2210.001, Texas Insurance Code.

2 State Board of Ins., *TX Catastrophe Property Insurance Pool Act — Designation of Catastrophe Areas,* No. 168789 (June 2, 1971).

3 Sections 2210.102–.103, Texas Insurance Code.

4 Section 2210.102, Texas Insurance Code.

5 Section 2210.104, Texas Insurance Code.

6 Sections 911.001(b) and 2210.006(b), Texas Insurance Code.

7 Sections 2210.051(b) and 2201.052(a), Texas Insurance Code.

8 Sections 2210.0725, 2210.074, and 2210.0742, Texas Insurance Code.

9 Subchapter B-1, Chapter 2210, Texas Insurance Code.

10 Op. Tex. Att'y Gen. No. GA-1012 (2013).

11 TWIA uses calendar years, not state fiscal years, for their accounting.

12 Section 2210.452(c), Texas Insurance Code.

13 Section 2210.202, Texas Insurance Code.

14 Subchapter O, Chapter 2210, Texas Insurance Code.

15 Section 2210.2515, Texas Insurance Code.

16 "About Us," Texas FAIR Plan Association, https://www.texasfairplan.org/about-us/.

17 Chapter 2211, Texas Insurance Code; "TFPA by the Numbers," Texas FAIR Plan Association, https://www.texasfairplan.org.

Issues

Issue 1

TWIA's Competing Statutory Mandates Leave Its Sustainability in Question.

Background

The Legislature created what is now the Texas Windstorm Insurance Association (TWIA) in 1971, after Hurricane Celia caused $3.2 billion in damage along the Texas coast in 1970.[1] The Legislature established TWIA's primary purpose as providing an "adequate market for windstorm and hail insurance" on the coast.[2] The Legislature has detailed three statutory findings describing TWIA's purpose:

1. Windstorm and hail insurance on the coast is necessary to the economic welfare of the state.
2. TWIA shall not be a direct competitor with the private insurance market and should serve as an insurer of last resort.
3. TWIA shall provide windstorm and hail insurance coverage to those who are unable to obtain coverage in the private market.[3]

TWIA currently operates as an insurance company, but with much more specific regulation and statutory limitations — namely TWIA must strive to not take on new policyholders unless they cannot otherwise find coverage. With 228 employees, TWIA underwrites policies, collects premiums, and pays claims. TWIA covers windstorm, hail, and in certain instances, wind-driven rain damage in 14 counties along the Texas coast.[4]

In 2017, TWIA had 231,633 residential policies and 11,008 commercial policies, and received 76,056 claims as a result of Hurricane Harvey. In a year without a hurricane, TWIA typically receives between 3,000 and 12,000 claims. Since 1971, TWIA has collected $4.15 billion in premiums and paid out $4.18 billion in claims.[5] TWIA does not receive any general revenue funds or tax dollars.

TWIA, like other insurance companies, sets its insurance rates based on the amount of claims TWIA expects to pay its policyholders in the future. TWIA must set rates to cover the years without hurricanes, when it receives 3,000 to 12,000 claims, as well as years with hurricanes, when it may receive more than 70,000 claims. Insurance companies calculate a policyholder's premium by multiplying the cost to replace the insured property by the insurance rate. The average TWIA homeowner in 2017 had $265,328 in windstorm insurance coverage, with an annual premium cost of $1,625.

TWIA pays claims and other expenses with revenue from premiums and contributes any amounts above that year's losses and expenses into the Catastrophe Reserve Trust Fund. To pay for claims that exceed that year's premiums, statute requires TWIA to access other funding sources, detailed in the textbox on the following page, *Sources of Funding for TWIA Hurricane Claims*, and illustrated in Appendix A.[6]

Sources of Funding for TWIA Hurricane Claims

Catastrophe Reserve Trust Fund: TWIA deposits excess premium revenue in an account outside the treasury managed by the state comptroller and administered by the Texas Department of Insurance to pay for claims when there is a major storm.

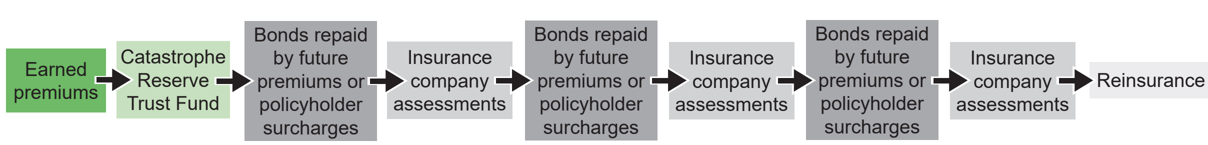
Bonds: statute requires TWIA to issue bonds to pay for claims, which must be repaid by premiums or surcharges on policyholders.

Member assessments: statute requires property insurance companies in Texas to pay up to a combined $1 billion for TWIA claims, allocated according to the companies' market share in the state.

Reinsurance: insurance for insurance companies. TWIA paid reinsurance companies $166 million in premiums with the agreement that reinsurance companies will provide up to $2.2 billion in funds if claim expenses exceed approximately $3 billion.

- First, TWIA must exhaust funds collected from premiums paid that year.[7]
- Second, TWIA must use funds from the Catastrophe Reserve Trust Fund.[8] The money in the Catastrophe Reserve Trust Fund is primarily from previous years' excess premiums.[9]
- Third, if TWIA's policyholders have claims that cost more than both the premium revenue and the Catastrophe Reserve Trust Fund, statute requires TWIA to issue up to $500 million in bonds.[10] Statute requires these bonds to be repaid using future premiums revenue or a premium surcharge on all TWIA policyholders.[11]
- Fourth, if claims exceed these three previous funding sources, TWIA will collect up to an additional $500 million through assessments on most companies who sell property insurance in Texas.[12]
- Fifth, if claims exceed these four previous categories, TWIA will issue another $250 million in bonds.[13] These bonds can be repaid using future premiums revenue or through a surcharge on policyholders. Policyholders can include both TWIA policyholders and anyone who has property or automobile insurance in the 14 coastal counties and applicable parts of Harris County.[14]
- Any further expenses will be paid for through alternating additional insurance company assessments and bonds, for a total of $1 billion in bonds and $1 billion in insurance company assessments.
- Once TWIA has spent all revenue from authorized bonds and assessments to pay claims, TWIA can access funds from reinsurance — insurance for insurers.[15] TWIA must purchase reinsurance to ensure its combined funding can cover policyholders' claims if the Texas coast experienced a one in 100-year storm — meaning a storm of a magnitude that has a 1 percent probability of hitting the coast every year.[16]

How TWIA Pays for Claims



To eventually pay for more than $1.6 billion in Hurricane Harvey claims, in addition to operating expenditures, TWIA will end up spending $451 million in earned premiums, $734 million from the Catastrophe Reserve Trust Fund, $500 million in bond proceeds, and $281 million in assessments on property insurance companies.[17]

Findings

The state has a continuing need for windstorm insurance along the coast.

TWIA's primary purpose — the provision of an adequate market for windstorm and hail insurance on the coast — continues to be necessary.[18] Without an adequate insurance market, and TWIA offering windstorm insurance for individuals who are unable to obtain insurance in the private market, many coastal residents may be forced to go without insurance or move out of those counties, which could negatively impact the industries that significantly contribute to Texas' economy. The coastal counties, not including Harris County, are home to five ports of entry and two U.S. military installations. The major industries in the Gulf Coast region include chemical manufacturing, oil and gas extraction and processing, and tourism.

TWIA provides half of all the residential windstorm insurance on the Texas coast.

As expensive hurricanes continue to hit coasts along the Gulf of Mexico, TWIA has historically taken on more policies and a greater portion of the windstorm insurance market. The state currently incentivizes private market insurance companies to sell residential and commercial insurance along the coast in a number of ways, and the private market has been expanding slowly over the past few years. However, the number of policies at TWIA remains high — TWIA provides about half of all residential windstorm insurance in the coverage area. Without TWIA, there is no guarantee private insurance companies would sell more insurance on the coast or that they would sell insurance at a reasonable price for most Texans living in coastal counties.

The Legislature has given TWIA opposing mandates, increasing the risk of TWIA's financial extinction.

The Legislature requires TWIA to operate both as an independent insurance company and an insurer of last resort, but these two requirements are in constant tension. To function as an independent insurance company, TWIA needs higher rates and a larger, more diverse pool of policyholders; to function as an insurer of last resort, TWIA needs reasonable rates that consumers can afford and a smaller risk pool to limit its liability. Currently, TWIA struggles to function as both, as it is forced to offer insurance at reasonable rates to a large pool of high-risk policyholders, creating an unsustainable situation.

Statute requires TWIA to offer insurance at reasonable rates to a large pool of high-risk policyholders.

- **TWIA's current funding structure is geared toward higher costs and debt-based financing**. In the aftermath of Hurricane Harvey, TWIA has depleted its savings account, is using premiums to pay debt service, and faces upcoming storm seasons with a shrinking revenue pool. Statute forces TWIA to first rely on premium funding and debt — repaid by future policyholders — to pay for hurricane claims, and does not contemplate consecutive years with major storms. When another storm hits, TWIA cannot retain any saved premiums for future hurricane claims and must tap the same resources again. Relying on premiums alone could be a sustainable model, but TWIA's rates are too low to fit this model.

TWIA has a large risk pool and corresponding liability. The Legislature designed TWIA to operate as an insurer of last resort, but TWIA currently provides windstorm insurance to 51 percent of the residential market in the coastal counties, providing as much as 73 percent of all residential windstorm insurance in Calhoun County, 70 percent in Aransas County, and 64 percent in both Galveston County and Matagorda County in 2017. Providing windstorm insurance to such a large percentage of residents of the coast increases TWIA's risk pool, meaning TWIA would need significantly more funding if another hurricane hits the Texas coast.

TWIA's rates would need to increase by 32 percent to cover anticipated residential claims and expenses.

TWIA's current revenue from premiums is not enough to pay for future claims. TWIA actuaries estimate rates need to increase by 32 percent for residential properties and 37 percent for commercial properties to cover anticipated claims and expenses. In August 2018, the TWIA board of directors voted to increase rates for both groups by 10 percent. If the commissioner of insurance approves the rate increase, TWIA would still not have enough revenue to cover future storm claims and expenses. However, in October 2018, the governor suspended the deadline for the commissioner of insurance to approve the rate increase until June 16, 2019, to give the Legislature time to address any actuarial deficiency at TWIA.[19]

- **Efforts to reduce TWIA's risk pool, a central tenet of an insurer of last resort, negatively impact TWIA's financial health**. Legislative directives, like depopulation, could lead to greater financial instability under the current structure. Discussed further in Issue 4, statute requires TWIA to operate two depopulation programs that allow private insurance companies to take policies from TWIA, limiting TWIA's exposure during a storm. However, these depopulation programs may impede TWIA's ability to generate the revenue necessary to repay previously issued bonds. TWIA's agreement on the bonds assumes that only about 2,000 policies will transfer from TWIA to the private market through the depopulation programs this year. In 2016, insurance companies took on 11,164 depopulated policies — about 11 percent of all depopulation offers that year. This year, insurance companies have made 75,000 depopulation offers, meaning that if 11 percent of policyholders choose to accept their depopulation offers this year TWIA would have to limit the number of policies transferred through depopulation to maintain a stable financial position.

Policyholders bear the brunt of paying back bonds.

- **TWIA's funding structure and inadequate rates compound future costs to policyholders**. With the existing premium rates and funding structure, having inadequate rates means that TWIA is more likely to have to issue bonds against future premiums to pay for storm claims. Issuing and paying back bonds is expensive, and TWIA policyholders bear the brunt of those costs. By not paying adequate rates now, policyholders will have to pay more in debt service and pay more to cover the cost of issuing the bonds.

Unfortunately, another hurricane hitting Texas as it recovers from Hurricane Harvey is a distinct possibility. Between 1900 and 2018 there have been 43 hurricanes in Texas, equaling about a 36 percent chance of a hurricane each year.[20] If a hurricane hits Texas next year, or even a strong hailstorm, TWIA could have to issue another round of bonds against future premiums. Since TWIA would still be paying back previously issued bonds from Hurricane Harvey, it would likely have to issue bonds at a much higher interest rate or pay for the bonds through a direct surcharge on all TWIA policyholders, in addition to the premium policyholders would have to pay.

- **To regain financial sustainability within its current statutory structure, TWIA would likely become prohibitively expensive**. Statute requires TWIA to maintain its financial stability through policyholder premiums — much like a private insurer. However, as premiums increase to pay Hurricane Harvey claims and future claims, policyholders who rely on TWIA to provide insurance when no one else will may be unable to afford the increased premiums. This would leave fewer and fewer policyholders to pay higher and higher premiums. Without an adequate pool of policyholders and adequate rates, TWIA would not be sustainable as an independent insurance company.

Raising rates could mean fewer and fewer policyholders are left to pay higher and higher premiums.

- **Higher rates may force some to go without insurance or abandon jobs on the coast, negatively impacting Texas' economy**. Increasing rates 32 percent to cover future claims would likely be too expensive for the average coastal homeowner, particularly as the coast continues to recover from Hurricane Harvey. If premiums increase substantially, policyholders without a mortgage, such as retirees, may choose not to purchase windstorm insurance and risk substantial losses if there is a hailstorm or hurricane. Policyholders who can no longer afford TWIA's premiums could choose to move out of the coastal counties, negatively impacting the local ports, oil and gas refineries, chemical manufacturing, and tourism industries, which contribute significantly to Texas' economy as a whole.

Adequate rates would likely be too expensive for the average coastal homeowner.

TWIA needs a more sustainable structure to ensure it can fulfill its mission of providing an adequate windstorm insurance market along the coast.

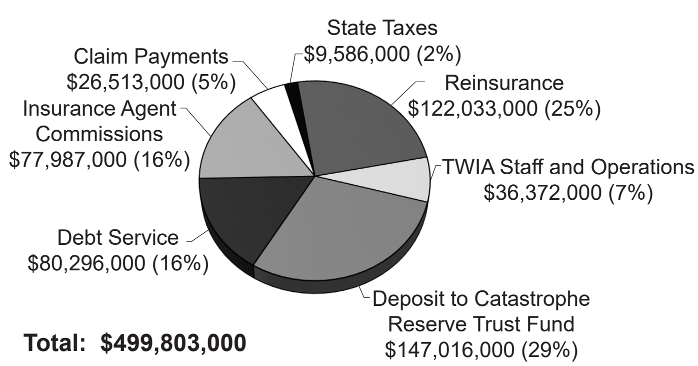
- **The following strategies would structure TWIA to operate more effectively as an independent insurance company, reliant on revenue from premiums**.

  Increase TWIA's revenue by requiring rates to be actuarially sound. As mentioned previously, TWIA's current rates are not actuarially sound and likely will not cover costs for future claims. By not raising rates over time, TWIA will cost policyholders more in the long run if TWIA has to issue bonds against future premium revenue to pay for claims.

  Generate more revenue by investing the Catastrophe Reserve Trust Fund. To generate more revenue to cover future claims, insurance companies typically invest the premiums they collect over time. The comptroller of public accounts holds the Catastrophe Reserve Trust Fund outside the state treasury on behalf of the Texas Department of Insurance, who administers the fund.[21] The Catastrophe Reserve Trust Fund generated only $3.3 million (0.6 percent) in revenue in 2016, when it held nearly $588 million. By not investing the fund and generating revenue when there are funds to invest, given due consideration to concerns of risk and liquidity, TWIA could be missing out on potential revenue to pay future claims.[22]

Decrease costs by reducing insurance agent commissions. Decreasing TWIA's costs could ostensibly increase rate adequacy without raising premiums, but TWIA staff and operations represent only 7 percent of TWIA's expenditures annually, as illustrated in the pie chart, *Texas Windstorm Insurance Association Expenditures*. To make a sizable impact on rate adequacy some of TWIA's larger expenditures would need to be decreased. Commissions paid to insurance agents are 16 percent of TWIA's annual expenditures, and because commissions are based on a percentage of premiums, any increase in premiums is limited by the 16 percent that must be paid to insurance agents. As discussed in Issue 2, TWIA's insurance agent commissions are higher than other insurance companies. Reducing TWIA's insurance agent commissions to align with those of the Texas FAIR Plan — an insurer of last resort for residential property insurance in Texas similar to and administered by TWIA — would decrease TWIA's costs by approximately $23.4 million every year.

Texas Windstorm Insurance Association Expenditures – 2016



Allow TWIA to purchase reinsurance to protect some premium revenue. Statute requires TWIA to purchase reinsurance to cover claims, but TWIA can only use its reinsurance after all other funding sources have been exhausted.[23] In effect, TWIA pays more than $100 million for reinsurance coverage every year but is unlikely to ever make use of its reinsurance. Other insurance companies have reinsurance coverage that protects a portion of their reserves rather than only providing coverage once all funds have been spent on claims.

- **The following strategies would structure TWIA to operate more effectively as an insurer of last resort for those who cannot purchase insurance elsewhere**.

Supplement premium revenue with other dedicated revenue. If premiums are insufficient, TWIA's two main sources of revenue to fund claims after a hurricane are bonds repaid by future premiums and assessments paid by insurance companies.[24] Introducing other forms of funding could increase TWIA's revenue and decrease reliance on premiums, making TWIA more fiscally sound and keeping TWIA affordable for those who cannot purchase insurance elsewhere.

Pay off debt before issuing new debt. After paying the claims for Hurricane Harvey, TWIA has exhausted its Catastrophe Reserve Trust Fund. If TWIA receives more than $200 million in claims in the coming years, it is likely to need to use funding beyond its earned premiums. In the event of another hurricane or hailstorm, statute would require TWIA to issue additional bonds against future premiums, and TWIA policyholders would be paying off Hurricane Harvey claims and this new set of potentially more expensive bonds, with little savings for the next year's claims.[25] Instead, the funding mechanism could be adjusted to allow TWIA to use member assessments before issuing bonds in years when the Catastrophe Reserve Trust Fund is low and TWIA is paying back previously issued bonds.

In the event of another hurricane, TWIA will likely have to issue additional bonds.

Limit the risk pool. By effectively requiring TWIA to provide insurance to everyone who sought but failed to obtain coverage elsewhere, statute has failed to limit the number of TWIA policyholders and thereby increased the amount of funding TWIA will need in the event of a storm. Statute currently requires insurance agents to provide TWIA with proof once every three years that each TWIA policyholder sought windstorm insurance elsewhere.[26] This declination letter is easy to get, since many insurance companies refuse to sell windstorm insurance coverage on the coast for all but a few policyholders. The declination letter also may be issued if an insurance company refuses to provide substantially equivalent coverage — meaning the policyholder may refuse private insurance if the rates are significantly higher or if the insurer does not cover as much as TWIA would. Strengthening the declination letter requirements by requiring policyholders acquire a declination letter from companies that actively sell windstorm insurance within the applicant's county and increasing the number of letters from one to two would help limit TWIA's risk pool.

In effect, TWIA must provide windstorm insurance to everyone who failed to obtain coverage elsewhere.

The depopulation program could also be adjusted to limit TWIA's risk pool. Currently, both the policyholder and the policyholder's insurance agent must approve an offer from a depopulation insurance company to move from TWIA to the depopulation insurance company. Policies from these insurance companies must be substantially similar to TWIA's policies — in both coverage and price — and maintain those terms for three years. Rather than allowing the policyholder and agent to approve the policy transfer, the depopulation programs could be mandatory, requiring TWIA to transfer any policy an insurance company makes an offer on.

Other alternative approaches to providing insurance to TWIA's high-risk policyholders could help TWIA fulfill its mission while remaining financially stable.

These alternative approaches to providing insurance to TWIA's high-risk policyholders would fundamentally change the current functions and operations of TWIA, while potentially still meeting the Legislature's goals. However, these alternatives have not been tested in the property insurance market, and other states' structures do not provide helpful comparative analysis.

- **Restructure TWIA as a reinsurance provider for private insurance companies**. The state would further incentivize private insurance companies to provide windstorm insurance coverage along the coast at a reasonable cost to policyholders by acting as a reinsurer. As a reinsurer, TWIA would receive a portion of the premiums insurance companies collected and invest the funds. In the event of a catastrophic storm, TWIA would help insurance companies pay for claims once claims exceed a certain cost threshold. For example, TWIA could provide funding to insurance companies on any individual claim exceeding $250,000 or once total claims in one year exceeded $1.5 billion.

While alternatives to TWIA's model exist, they largely have not been tested in the property insurance market.

- **Restructure TWIA to be an assigned risk pool**. Windstorm insurance along the coast would operate similarly to the assigned risk pool that ensures everyone in the state can receive car insurance. The Legislature created an assigned risk pool for car insurance, which assigns Texans who cannot get insurance from the private market to an insurer. This program requires all companies who sell car insurance in Texas to participate in the Texas Automobile Insurance Plan Association (TAIPA).[27] Through TAIPA, Texans who have been rejected by at least two car insurers may apply for car insurance. TAIPA prescribes a standard plan of coverage and rate for all policyholders. TAIPA then assigns each applicant to a car insurance company, based on that company's share of the car insurance market in the state. The insurance company provides car insurance for the policyholder based on TAIPA's standard plan and rates and handles any claims that arise.

- **Abolish TWIA and require insurance companies to provide windstorm insurance on the coast**. Under this model, all 143 property insurance companies in Texas that participate in TWIA would decide to cover windstorm insurance on the coast or no longer sell insurance in Texas' $51 billion property insurance market. Depending on how the Legislature implemented this model, the rates insurance companies charge policyholders on the coast may be subject to the insurance commissioner's review.

- **Other states' models**. Other states' approaches to ensuring adequate windstorm insurance coverage vary, but most states that offer windstorm coverage either focus on having a more diverse or smaller risk pool.

Most states that offer windstorm coverage either focus on having a more diverse or smaller risk pool.

<u>Diverse risk pool</u>. Florida and Louisiana combine their state's version of TWIA with their state's Fair Access to Insurance Requirements (FAIR) Plan. FAIR Plan associations provide residential property insurance throughout the state when no private company will provide coverage. Combining these insurance plans means the states' policyholders have one insurance policy that covers both windstorm and other homeowners insurance like fire and theft. Combining the plans also means the insurance company collects premiums on all of these possible perils, diversifying their risk pool.

Smaller risk pool through high rates. Louisiana's plan assesses the market rate for insurance in each parish and then charges its policyholders 10 percent above the parish's market rate. Keeping rates high incentivizes policyholders to continuously seek other insurance options ensuring fewer policyholders and therefore a smaller pool of risk. Louisiana's plan also does not undercut private insurance rates.

North Carolina limits the amount of risk it takes on by capping its maximum coverage.

Limit maximum coverage. North Carolina limits its maximum coverage to $750,000 for residential properties and $3 million for commercial. By comparison, TWIA covers up to $1.8 million for residential properties and $4.4 million for commercial buildings. Properties that need more coverage can purchase a second insurance policy for damages above the maximum coverage provided by the state. By lowering its maximum coverage, North Carolina limits the amount of risk it takes on and therefore needs less funding to pay claims.

Recommendations

TWIA is subject to review, but not abolishment, under the Texas Sunset Act.[28] Normally, as part of such a review, Sunset staff presents its findings and makes recommendations to the Sunset Advisory Commission to improve the efficiency and effectiveness of an agency's operations, performance, and structure. Sunset staff determined TWIA's current structure is fundamentally unsustainable and does not best serve the state, primarily due to the fundamental conflict at TWIA's core — should it be the insurer of last resort or a true insurance carrier. However, given the unique nature of TWIA, its competing statutory mandates, and the recent impetus of the governor's request for legislative review of TWIA's actuarial soundness, Sunset staff cannot make recommendations to address TWIA's performance, operations, and structure without endorsing one policy direction over another, which is a matter for the Legislature to decide.

Unlike Sunset staff, the role of the Sunset Commission is to make recommendations to the Legislature for consideration regarding the agency's operations, performance, and structure.[29] Recognizing that as currently structured TWIA's long-term health is substantially impeded by its limited funding options and reliance on debt, and the governor's indication the Legislature should consider and have the opportunity to fully address this issue during the 86th Session, the Sunset Commission could adopt one of the following recommendations, which would be drafted into TWIA's Sunset bill, as a starting point for these discussions.

Alternatively, since TWIA is not subject to abolishment, the Sunset Commission could choose to simply forward the findings of this review to the Legislature for consideration. TWIA would continue under its current statutory authority and structure and the statutory provision requiring a Sunset review of TWIA would expire on September 1, 2019.

Change in Statute

1.1 Continue TWIA as an insurer of last resort.

- Restructure TWIA's funding to rely less on premium-funded debt while TWIA is still paying off debt. To reduce TWIA policyholders' exposure after a catastrophe year, require TWIA to issue $500 million in member assessments before issuing $500 million in bonds, effectively reversing the funding to alternate between member assessments and then bonds.

- Limit TWIA's risk pool by strengthening its depopulation and declination programs. This recommendation would require TWIA policyholders and applicants to receive two letters declining to provide windstorm insurance coverage from insurance companies that are actively writing windstorm insurance on the coast that year. This recommendation would also transition the depopulation programs to require TWIA to transfer any policy that receives an offer through the depopulation program to the offering insurance company.

1.2 Continue TWIA as an insurance company reliant primarily on premium funding.

- Require TWIA to recommend and the Texas Department of Insurance to approve actuarially sound rates within five years.
- Direct TWIA and the Texas Department of Insurance to adopt an investment plan for the Catastrophe Reserve Trust Fund.
- Amend TWIA's statute to allow TWIA to purchase reinsurance to protect a portion of its Catastrophe Reserve Trust Fund, in line with the operations of many private insurance companies.
- Direct the Texas Department of Insurance to reduce TWIA's commission rates paid to insurance agents to align TWIA's commission rates with the commission rates paid by the Texas FAIR Plan.
- Remove requirements in statute that TWIA not compete with private industry and that TWIA function only as an insurer of last resort.
- Abolish the depopulation programs required in statute and the declination requirement to qualify for coverage, effectively allowing TWIA to increase its revenue pool.

Fiscal Implication

Neither recommendation would have a direct fiscal impact on the state, as TWIA does not receive any state funding. However, either recommendation would have a significant impact on ensuring TWIA is financially solvent and able to provide windstorm and hail insurance on the Texas coast.

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[1] S.B. 31, 62nd Texas Legislature, Regular Session, 1971; $500 million in losses in 1970 adjusted based on the average inflation rate since 1970; Texas Windstorm Insurance Association, *Self Evaluation Report for the Sunset Advisory Commission September 1, 2017*, accessed October 1, 2018, https://www.sunset.texas.gov/public/uploads/files/reports/Texas%20Windstorm%20Insurance%20Association%20Self-Evaluation%20Report.pdf, 16.

[2] All citations to Texas statute are as they appear on http://www.statutes.legis.texas.gov/. Section 2210.001, Texas Insurance Code.

[3] Ibid.

[4] The commissioner of insurance determines the counties TWIA covers, which currently includes 14 counties and parts of Harris County. Section 2210.005, Texas Insurance Code; State Board of Ins., *TX Catastrophe Property Insurance Pool Act – Designation of Catastrophe Areas*, No. 168789 (June 2, 1971).

[5] Texas Windstorm Insurance Association, *TWIA Board of Directors Meeting Materials July 2018*, accessed October 1, 2018, https://www.twia.org/wp-content/uploads/TWIA-Board-of-Directors-Meeting-Materials-July-2018.pdf, 32.

[6] Subchapter B-1, Chapter 2210, Texas Insurance Code.

[7] Section 2210.0715, Texas Insurance Code.

[8] Ibid.

[9] Section 2210.452(c), Texas Insurance Code.

[10] Section 2210.072, Texas Insurance Code; Statute requires TWIA to issue up to $500 million in bonds, but does not provide another means to obtain this funding if bonds cannot be issued.

[11] Section 2210.612, Texas Insurance Code.

[12] Section 2210.0725, Texas Insurance Code.

[13] Section 2210.073, Texas Insurance Code.

[14] Section 2210.6132, Texas Insurance Code.

[15] Section 2210.453(c), Texas Insurance Code.

[16] Section 2210.453(b), Texas Insurance Code.

[17] Only $448 million of the bond revenue will pay Hurricane Harvey claims, TWIA retained $51 million for debt reserve funds.

[18] Section 2210.001, Texas Insurance Code.

[19] Letter from Governor Greg Abbott to Commissioner of the Texas Department of Insurance Kent Sullivan, October 11, 2018.

[20] Based on 43 hurricanes occurring in a 118 year span; Texas Department of Insurance, *Texas Windstorm Insurance Association Overview for Quarter Ending March 31, 2018*, accessed September 15, 2018, https://www.tdi.texas.gov/pubs/pc/pctwiabrief.pdf, 17.

[21] Section 2210.452, Texas Insurance Code.

[22] TWIA largely spent the balance of the Catastrophe Reserve Trust Fund to pay Hurricane Harvey claims. As of June 2018, the fund holds $3.4 million.

[23] Section 2210.453(c), Texas Insurance Code.

[24] Bonds may also be repaid by premium surcharges if premiums are insufficient. Section 2210.609, Texas Insurance Code.

[25] Section 2210.072, Texas Insurance Code.

[26] Section 2210.202, Texas Insurance Code.

[27] Chapter 2151, Texas Insurance Code.

[28] Section 2210.002(b), Texas Insurance Code.

[29] Section 325.012, Texas Government Code.

Issue 2

Inefficient Renewal Requirements and Payment Policies Increase Costs for Policyholders.

Background

Like most insurance companies, the Texas Windstorm Insurance Association (TWIA) issues insurance policies that are effective for one year. Unlike other insurance companies, TWIA requires a complete application each year to continue coverage rather than automatically renewing policies.[1] At renewal, TWIA checks to ensure the policyholder has been declined coverage by a private insurance company within the last three years through a declination letter.[2] Unless the policyholder has changes to declare at the time of renewal, TWIA does not collect any new information.[3]

Annual premiums are the payment that customers owe to the insurance company for policy coverage. Insurance companies calculate premiums by multiplying the insured value of the property by the insurance rate. Insurance rates are based on the expected costs the insurance company will have to incur to insure a property, including anticipated claims, commissions paid to insurance agents, state taxes, and operation costs. The table, *TWIA Premiums and Coverage*, shows the average and median levels of policy coverage and premiums for policyholders in 2017.

TWIA Premiums and Coverage – 2017

		Coverage	Annual Premium
Residential	Average	$265,328	$1,625
	Median	$234,600	$1,446
Commercial	Average	$822,383	$6,017
	Median	$300,000	$2,568

Findings

The insurance policy renewal process is unnecessarily burdensome, increasing costs for policyholders and workloads for insurance agents.

- **Costly and unnecessary annual applications**. Unlike most other insurance companies, TWIA cannot allow for automatic renewal of its insurance policies.[4] In 2011, the Legislature required TWIA to develop a simplified insurance policy renewal process.[5] In response, TWIA created an improved electronic policy management system allowing for auto-population of data fields for insurance agents and online payments.[6] However, TWIA still cannot allow for automatic policy renewals.[7] Instead, rather than allowing policyholders to declare any major changes to the property and send in a premium payment to automatically renew their policy and continue coverage, TWIA requires submission of a full application each year to continue insurance coverage, even if nothing about the property or policy has changed. Further, proof of declination from a private insurance company is only required every three years and does not need to be resubmitted annually.[8]

TWIA cannot allow for automatic renewal of its policies.

- **Higher than average insurance agent commissions for renewals**. Statute authorizes the commissioner of insurance, on recommendation by TWIA's board of directors, to set a commission structure for insurance agents writing TWIA policies.[9] Statute requires the commission structure to be fair and reasonable, based on the amount of work an insurance agent must do to submit an application, and take prevailing private market rates into consideration.[10] TWIA's insurance agent commission rate is set at 16 percent annually for all policies, and commissions paid to insurance agents make up a significant portion of TWIA's expenses. In 2017, TWIA paid insurance agents $67.3 million in commissions. While TWIA paid a full commission on more than 230,000 policies, only 32,062 were first-time applications necessitating full processing of new information. As shown in the table, *Texas Insurance Agent Commission Rates*, TWIA's 16 percent commission rate is much higher than the rates for both the voluntary market and Texas FAIR Plan, another state-created insurer of last resort.[11] If TWIA were to propose and the commissioner of insurance approve renewal commission rates commensurate with Texas FAIR Plan renewal commission rates at 10 percent rather than 16 percent, TWIA could save approximately $23.3 million per year on the 198,000 applications that were for renewal rather than a new policy. With these savings, TWIA would be closer to achieving actuarially sound rates, without raising premiums as much.

Texas Insurance Agent Commission Rates – 2017

Texas FAIR Plan	New: 12.5% Renewal: 10%
Other insurance companies in Texas – Residential and Commercial Fire and Allied Lines	Average: 11.5%
Other insurance companies in Texas – Homeowners	Average: 12.3%
TWIA	16%
Federal Flood	17.2%

Many TWIA customers incur additional costs due to statutory barriers to installment payments.

Financing companies charge policyholders up to 20 percent interest for premium financing.

Statute requires policyholders to pay the annual premium in full before a TWIA policy can go into effect, essentially prohibiting installment payments.[12] Because TWIA is not able to accept monthly or quarterly installment payments, some policyholders use third-party financing companies to pay their annual premiums upfront. These financing companies charge up to 20 percent interest, significantly increasing the cost of a TWIA policy to the policyholder. While less than 10 percent of TWIA's 240,000 policyholders use premium financing companies, allowing TWIA to accept installment payments would lower the cost of obtaining a TWIA policy for these customers and would be a consumer-friendly change. Statute authorizes Texas FAIR Plan to accept installment payments, which are also standard in the insurance industry.[13]

The lack of direct payment options increases insurance agent workload and red tape for policyholders.

TWIA bills its policyholders for both new applications and renewals through the insurance agent, even though statute does not prohibit TWIA from billing policyholders directly. Requiring agents to be directly involved creates an unneeded step in the billing process. TWIA also does not accept credit card payments due to associated merchant fees, but instead requires mailed checks or electronic bank transfers. While companies in Texas cannot pass along credit card costs to consumers, TWIA is authorized as a governmental entity to levy a surcharge or convenience fee on credit card payments to help recoup those costs.[14] Paired with automatic renewal, providing more direct payment options to consumers would make TWIA policies easier to purchase and improve the customer experience while reducing agent workloads.

Recommendations

Change in Statute

2.1 Require TWIA to automatically offer policy renewal unless new information is necessary.

This recommendation would require TWIA to establish an automatic renewal process, reducing the extent of insurance agent involvement. A policy would automatically be offered to a policyholder and renewal would be issued if payment is received, as long as TWIA does not require a new declination letter or new information on the insurability of the property and the policyholder does not opt to cancel the policy at the time of renewal. This recommendation would streamline the process for the majority of renewals when no new information is necessary to continue coverage, while still ensuring policyholders fulfill statutory requirements to seek private market options. Automatic renewals would make it easier for policyholders to maintain continuity of coverage and reduce the workload of insurance agents.

2.2 Authorize TWIA to accept installment premium payments.

This recommendation would allow TWIA to provide premium installment payment plans and remove the requirement that premiums must be paid in full before a policy goes into effect. This statutory change would allow TWIA to administer its policies in a manner similar to those under the Texas FAIR Plan and private market, helping reduce costs for customers who cannot pay the full annual premium upfront.

2.3 Authorize TWIA to accept credit card payments.

This recommendation would authorize TWIA to accept credit card payments and would authorize TWIA, like other governmental entities, to pass credit card processing costs forward through a surcharge.[15] Many private insurance companies and other governmental entities accept credit card payments to improve customer service and provide more payment options. While not all TWIA customers would benefit from credit card payment, having several payment options would make premium payment easier for many policyholders.

Management Action

2.4 Establish separate insurance agent commission rates for new applications and automatic renewals.

This recommendation would require TWIA to propose separate commission rates for new applications and renewed policies to the commissioner of insurance for approval. Like the insurance agent commission rates for new applications, commission rates for renewed policies should be fair and reasonable and take into consideration the work required of insurance agents and prevailing market rates for renewals. The

Texas FAIR Plan sets insurance agent commission rates separately for new applications and renewals, and this recommendation would follow standard practice for other insurance companies. Separate rates for new applications and renewals would better allow TWIA to compensate insurance agents in a manner commensurate with the work required. Along with the streamlined automatic renewal process outlined in Recommendation 2.1, TWIA would significantly reduce the workload for insurance agents when renewing TWIA policies.

2.5 Direct TWIA to directly bill customers for premiums for automatic renewal.

This recommendation would direct TWIA to bill customers eligible for automatic renewal directly, removing the need for insurance agents to act as middlemen in processing payments. Direct billing would make it easier and more straightforward for policyholders to pay their premiums and help to reduce unnecessary workload for insurance agents.

Fiscal Implication

These recommendations would have no fiscal impact to the state because TWIA does not receive any state funding. TWIA may have increased costs from credit card processing, but the costs cannot be estimated because they depend on the number of policyholders who would pay by credit card and the surcharge TWIA charges to recover costs for credit card payments. TWIA could reduce its costs if renewal commissions were set at a rate lower than the regular commission rate, but the exact savings cannot be estimated at this time.

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[1] All citations to Texas statutes are as they appear on http://www.statutes.legis.texas.gov/. Section 2210.203(c), Texas Insurance Code.

[2] Section 2210.202(a), Texas Insurance Code.

[3] Policyholders should report any changes or improvements to their property to their insurance company as the changes occur to ensure adequate coverage throughout the year.

[4] 28 T.A.C. Section 5.4902(b).

[5] H.B. 3, 83rd Texas Legislature, Regular Session, 2011.

[6] Section 2210.202(b), Texas Insurance Code.

[7] 28 T.A.C. Section 5.4902(b).

[8] Section 2210.202(a), Texas Insurance Code.

[9] Section 2210.203(d), Texas Insurance Code.

[10] Section 2210.203(c), Texas Insurance Code.

[11] The average rates for other insurance companies in Texas are averages across companies and across new applications and renewal business. Certain insurance companies may have commission rates more similar to TWIA's rates, as the inclusion of renewal commission rates lowers the overall averages.

[12] Section 2210.203(a), Texas Insurance Code.

[13] Section 2211.054(5), Texas Insurance Code.

[14] Section 604A.002(b)(1), Texas Business and Commerce Code.

[15] Ibid.

Issue 3

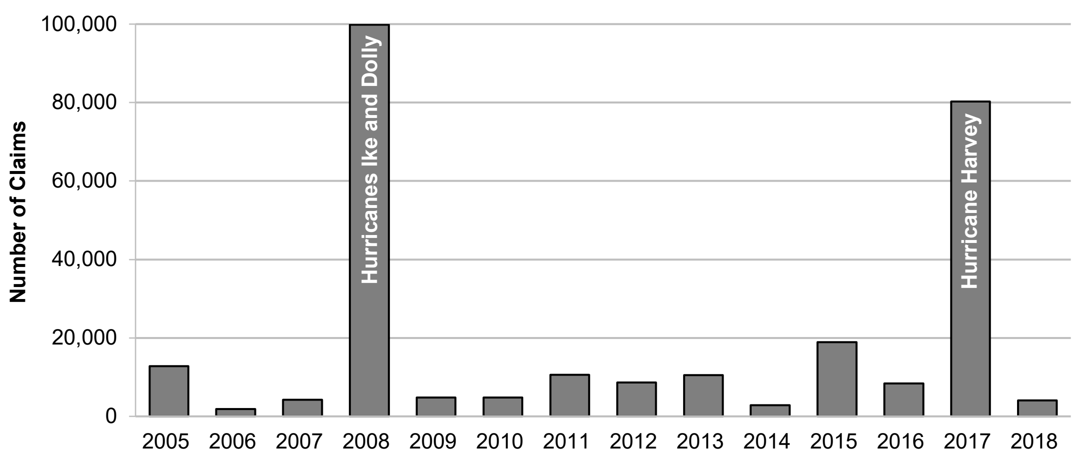
Despite Improvements in Claims Handling, TWIA's Hurricane Harvey Response Highlights Difficulties for Policyholders.

Background

The Texas Windstorm Insurance Association (TWIA) provides wind and hail insurance coverage for residential and commercial coastal property owners unable to buy insurance through the private market. Insurance policies from TWIA supplement traditional property insurance and do not cover fire, theft, flood, or other threats, but may cover wind-driven rain if the policyholder elects to purchase the additional coverage.

Like most insurance companies, TWIA assesses damage, pays policyholder claims, and handles disputes over insurance coverage and claim payouts. Coverage for a claim typically includes the replacement costs and living expenses while the policyholder's home is being repaired. In 2017, TWIA processed 80,257 claims, including 76,056 claims related to Hurricane Harvey. In a year without a hurricane, TWIA processes an average of 7,000 claims. Like most insurance companies, TWIA contracts for additional temporary claims staff to meet demand during a hurricane, as shown in the flowchart, *TWIA Claims Process*, in Appendix C. The chart below, *TWIA Claims Filed*, shows the annual volume of claims from 2005–2018 to date.

TWIA Claims Filed 2005–2018



By statute, TWIA has 60 days to accept or deny a policyholder's claim and 10 additional days to issue a payment on that claim.[1] The insurance commissioner may extend these deadlines to a total of 180 days during a catastrophe.[2] In 2016, the latest complete year without a hurricane, TWIA received 8,393 claims, resolved residential claims in 5.8 days, and handled 143 (1.7 percent) disputes.

After TWIA assesses any damage and issues the first payment for a claim, policyholders can dispute TWIA's decision regarding damages, coverage, and repair costs through three main methods:

- Appraisal: TWIA and the policyholder each hire an appraiser and jointly hire an "umpire" to re-evaluate the claim and make binding decisions.[3]

- Legal action: A policyholder files a lawsuit against TWIA to receive any denied coverage on a claim, but statute limits how much can be recovered.[4]
- Supplemental payment process: An alternative, informal resolution process where policyholders provide TWIA additional information on a claim that may change TWIA's assessment of loss or repair costs.

TWIA improved claims performance following criticisms of slow claims response after Hurricane Ike in 2008, as shown in the table below, *TWIA Improvements to Claim Handling Performance After Hurricanes*. TWIA also added a claims quality assurance department; created an online claims center for policyholders and agents to file a claim electronically and check the status of a claim, including claim payments; and implemented a claims triage process to route complicated claims to specialized staff.

TWIA Improvements to Claim Handling Performance After Hurricanes

	Hurricane Ike 2008	Hurricane Harvey 2017
Claims received	93,065	76,532
Average number of days to process residential claims	257	35
Disputed claims to date	10,761 (11.6%)	1,235 (1.6%)
Policyholder complaints to the Texas Department of Insurance (TDI)	1,738 (1.9%)	232 (0.3%)

Findings

TWIA's supplemental claims payment process creates confusion for policyholders.

Although TWIA has greatly improved its claims handling since Hurricane Ike, confusion over TWIA's claims process has led some policyholders to protest what they see as delayed claims processing and low claims payments. Much of this confusion relates to TWIA's process for issuing supplemental payments after the initial assessment of damage and claim payment. As described further in the textbox below, supplemental payments benefit both policyholders and TWIA.

Supplemental Payments

The supplemental payment process allows insurance carriers, like TWIA, and policyholders to resolve disputes over the value of a claim without incurring the cost of the statutory appraisal process.

Insurance carriers commonly receive additional information after the first damage assessment. After a hurricane, a region may experience a high demand for building materials, increasing the cost of repairs while the policyholder tries to hire an available contractor, which can take months following a hurricane. TWIA and most insurance companies understand that price estimates after hurricanes are not exact, and will work through the supplemental payment process to pay the market rates for repairs. Policyholders also commonly discover additional damage to a property once the contractor starts repairs, resulting in additional covered losses.

While statute provides deadlines for TWIA to initially approve or deny a claim, TWIA, like other insurers, commonly accepts additional claim information after that deadline and issues additional payments on a claim in response to new information from policyholders.[5] Supplemental payments are a standard tool for private insurers and the National Flood Insurance Program, because claims can be settled more quickly and efficiently for policyholders and insurers, particularly after hurricanes.[6] TWIA issued supplemental payments for an estimated 29 percent of claims related to Hurricane Harvey.

Supplemental payments allow insurance carriers to resolve claims disputes more quickly and efficiently.

However, because the supplemental payment process is not clearly laid out in statute, TWIA struggles to explain the process and does not provide policyholders and insurance agents with sufficient information. Without clear information, policyholders may believe the initial payment is the final payment and that their only recourse is through either the statutory appraisal process or legal action.

Assessing the replacement cost of a property at the time of loss creates confusion and uncertainty for TWIA policyholders.

When a policyholder applies for a TWIA policy, the policyholder works with an insurance agent to calculate the property's replacement value and purchase insurance to cover that cost. When the policyholder files a claim, statute requires TWIA to calculate the replacement value of the property again at the time of the loss.[7] Establishing the replacement cost twice, particularly at the time of loss, is not a standard practice in the insurance industry and does not benefit policyholders or TWIA.

The differences in calculations can surprise and frustrate policyholders if they receive lower payouts from TWIA because the property's value at the time of loss is different from the value when the policyholder purchased the policy. Under statute, if at the time of loss the insurance coverage on a property is less than 80 percent of the property's full replacement cost, TWIA may not pay more than the replacement cost of the part of the property that was damaged or destroyed minus depreciation.[8] Receiving the replacement cost for covered damages minus depreciation would mean that the policyholder receives what is called the actual cash value payment of the claim, which can be significantly less than the cost to repair or rebuild a property as it was before the storm. Recalculating the replacement cost at the time of loss also creates inefficiencies for TWIA, because insurance adjusters and claims examiners must redo the replacement cost calculation when a policyholder files a claim, delaying claim resolution.

Establishing replacement cost twice is not standard practice in the insurance industry.

TWIA closes claims timely, but tracks and reports data in a way that fails to communicate the full story.

After a hurricane, policyholders, legislators, community groups, and TWIA board members rely on data from TWIA to know how quickly TWIA is responding to claims, and to estimate when residents and businesses along the coast will have the funds to begin rebuilding. After Hurricane Harvey, TWIA successfully met the deadline in statute to approve or deny a claim and reported that it averaged 35 days to make a first payment for the vast majority of its residential claims.[9] However, the way TWIA captures data may not provide an accurate picture of how quickly TWIA closed claims.

TWIA potentially undercounts how long it takes to finally resolve claims.

Similar to the insurance industry at large, TWIA tracks and reports the average number of days to close a claim based on the number of days from when TWIA received the claim to the day TWIA most recently considered the claim resolved, meaning that TWIA had made a final payment on the claim or made a final coverage decision on the claim. However, this tracking method inflates the average number of days TWIA takes to reach a first claim decision, because this method may include any supplemental payment time beyond the first claim decision. TWIA also includes only closed claims in its reporting, potentially undercounting how long TWIA takes to finally resolve claims by excluding claims that are still open. For example, if TWIA included claims that were still open when calculating the average number of days to close a residential claim in 2017, the average would increase from 35 days to 36 days. Although TWIA's measures are largely accurate, the measures could include more information to meet the needs of TWIA's stakeholders.

TWIA increased communication and outreach after Hurricane Harvey, but ultimately failed to fully address policyholder concerns.

Policyholders report not knowing where to complain about TWIA.

Although educating consumers and addressing misinformation is difficult after a hurricane, confusion surrounding the claims handling process increases frustrations for policyholders. For example, of the more than 70,000 claims filed after Hurricane Harvey, 19,340 resulted in no payment because either the complainant did not have a TWIA policy or the claim amount was below the policyholder's deductible. Despite TWIA's efforts, policyholders may not understand they do not have a policy with TWIA because TWIA's depopulation program is extremely complex, as discussed in Issue 4. Policyholders also may not understand how TWIA calculates deductibles, although TWIA calculates deductible payments like other insurers. TWIA's inability to adequately mitigate confusion in both areas through better communication and education left policyholders frustrated. Further, as previously discussed, TWIA does not fully or clearly explain the supplemental payment process to policyholders. Policyholders also continue to report not knowing where to complain when they have concerns about a TWIA claim, even though the Legislature has established a full-time TWIA ombudsman employed by the Texas Department of Insurance (TDI), which is the appropriate outlet for policyholders to submit complaints.[10]

TWIA has identified these concerns and is taking steps to better communicate to its stakeholders. For example, TWIA has implemented customer service surveys, quality assurance programs, coastal town halls and other community outreach, mobile claims centers, and an insurance agent focus group. However, TWIA does not systematically gather input and feedback from policyholders to ensure the new communication strategies effectively address problems identified. For instance, TWIA created an explanation sheet about the claims process to leave with policyholders when TWIA assesses the extent of damage at a property. Although creating an explanation sheet is a good step, the sheet does not clearly explain how the supplemental payment process works in detail, or provide the contact information for TWIA's ombudsman if the policyholder has a complaint about how TWIA handled their claim. Similarly, TWIA's website also does not provide clear and easily accessible information about how to file a complaint about TWIA with TDI, outreach events on the coast, or the timeline of the anticipated claim resolution process after a hurricane. The website should not be the only source of information about the claims process, because policyholders and insurance agents may lack internet access after a hurricane.

TWIA's website does not provide a timeline of the anticipated claims resolution process after a hurricane.

TWIA's oversight of contracted insurance adjusters does not focus resources on the highest risk areas.

When a policyholder files a claim, TWIA usually sends an insurance adjuster to the property to assess the level of damage. TWIA does not employ its own insurance adjusters and instead contracts with independent adjusting firms to provide insurance adjusters when TWIA needs them, a common insurance industry practice for entities that respond to disasters. TWIA used 1,859 insurance adjusters during Hurricane Harvey. All insurance adjusters must be licensed by the Texas Department of Insurance and must go through TWIA's certification training and exam.[11]

In response to past problems with insurance adjusters, TWIA implemented insurance industry best practices for managing independent adjusters, including creating a quality assurance department to improve insurance adjuster oversight. The department added several controls, such as claims sampling, claims audits, re-inspections, and training and testing insurance adjusters based on TWIA's claims guidelines. While TWIA's quality assurance department has improved oversight of contracted insurance adjusters, TWIA could benefit from implementing a more risk-based approach to sampling claims to measure insurance adjuster performance. TWIA currently samples at least 10 percent of all claims for quality assurance without regard to county, claim amount, claim volume, or other factors. Where negative trends are identified, TWIA reviews additional claims and takes corrective action as needed, including removing adjusters or adjuster firms from future work.

More risk-based oversight of insurance adjusters could improve performance on TWIA's most complex claims.

Implementing a more risk-based approach, such as sampling the claims most affected by negative insurance adjuster performance, could improve TWIA's ability to know how well contracted insurance adjusters are performing on the most complex claims and in the counties that were hardest hit by a storm. Currently TWIA includes the most complex claims in its sample, but may miss the highest risk claims by failing to stratify their sampling within the entire claims pool.

Recommendations

Change in Statute

3.1 Authorize TWIA to issue supplemental payments.

This recommendation would clearly authorize TWIA to implement a supplemental payment process for claims disputes and would authorize the commissioner of insurance to adopt all necessary rules. This recommendation would require TWIA to inform policyholders of the process to request supplemental payments but would not prohibit or in any way limit policyholders' existing rights to seek appraisal or legal remedies. This recommendation would ensure that the policyholder's right to appraisal does not expire while the policyholder is going through the supplemental payment process. This recommendation also would require the commissioner of insurance, with input from TWIA and stakeholders, to clarify the timeline for a policyholder to seek supplemental payments in rule. Authorizing TWIA to issue supplemental payments and requiring the commissioner of insurance to adopt rules for that process would align statute with TWIA's current practice and create more clarity for policyholders regarding how TWIA can pay a claim. The commissioner of insurance should adopt rules to implement this recommendation by January 1, 2020.

3.2 Require TWIA to assess the replacement cost of a property only at the time TWIA issues or renews the policy.

This recommendation would remove the requirement for TWIA to establish the replacement cost of a property at the time of loss and would instead require TWIA to establish the replacement cost of a property on the effective date of a TWIA policy. Making this change would reduce duplication of effort by TWIA staff, increase TWIA's efficiency during catastrophes, and reduce uncertainty for policyholders around the coverage of their policies.

Management Action

3.3 Direct TWIA to track and report more comprehensive information regarding claims handling performance.

This recommendation would supplement TWIA's extensive existing claims tracking and reporting to ensure claims handling performance data is tailored to TWIA's diverse stakeholder groups. Under this recommendation, at a minimum, TWIA should track and report

- the average amount of time it takes to issue a first disposition on a claim, from the date when TWIA receives the claim to the date TWIA sends the letter to inform the policyholder what TWIA will cover;
- the average amount of time it takes to finally close a claim;
- data on the number of open claims, including, on average, how long claims are open after the first disposition letter; and
- how many times a claim was re-opened due to receiving additional information from parties outside TWIA — such as the policyholder or the policyholder's representative.

Tracking and reporting additional information to the TWIA board of directors and on TWIA's website through its existing data reporting mechanisms would provide a more complete picture of TWIA's claims handling performance. While TWIA currently tracks and reports considerable data, TWIA uses methods in line with private insurance companies. TWIA should continue using industry standards because they are best practices for the insurance industry, but should additionally track and report data in a way that makes sense for policyholders, legislators, and the public.

3.4 Direct TWIA to develop a post-hurricane communication plan with more input from stakeholders.

To address concerns highlighted after Hurricane Harvey, this recommendation would direct TWIA to develop a communication plan using input from policyholders, insurance agents, and local governments. Under this recommendation, TWIA should work to continue including more information in layman terms on its website and written materials about how deductibles are calculated, what is covered under standard TWIA policies, the claims process and anticipated timelines, and how policyholders can file a complaint against TWIA. TWIA's communication plan would also include communication strategies after a hurricane beyond those that require internet access or mail access, as these avenues can be disrupted after a hurricane.

To ensure TWIA continues to solicit regular feedback, TWIA would be directed to create a working group of policyholders, similar to TWIA's insurance agent advisory group. TWIA should publish information on its website about how policyholders and insurance agents can participate in either working group, when the groups meet, and how TWIA has implemented changes in response to feedback gathered from stakeholders. TWIA would use the working groups to gather feedback on TWIA's communications and operations both after hurricanes and ongoing strategies TWIA can implement to increase transparency.

Although TWIA is not a state agency, TWIA is accountable to the Legislature and should work to be more accessible and accountable to its policyholders. This recommendation would ensure TWIA's future communication strategies better address stakeholders' concerns and increase transparency in TWIA's interactions with policyholders and insurance agents.

3.5 Direct TWIA to fully implement a risk-based approach to monitoring insurance adjusters.

Under this recommendation, TWIA would implement a more risk-based approach to monitoring insurance adjusters and all hired claim experts. At a minimum, TWIA should sample claims for insurance adjuster performance according to county, claim volume, or claim amount to help ensure that the quality assurance sample represents the properties that were most affected by a storm. As part of this recommendation, TWIA would also include building consultants, engineers, and other claims experts it hires in its quality assurance reviews to ensure TWIA has information on the day-to-day performance of all individuals involved with claims, not just insurance adjusters. This additional information would improve TWIA's ability to quickly respond to problems and policyholder concerns.

Fiscal Implication

These recommendations would have no cost to the state because TWIA receives no funding from the state. Clarifying the supplemental payment process for policyholders may have a fiscal impact to TWIA, as more policyholders may take advantage of this process to seek additional claims payments. However, the impact cannot be determined at this time, as costs to TWIA and policyholders may also decrease as fewer policyholders seek appraisal or litigation. Removing the requirement that TWIA establish the replacement cost at the time of loss would decrease workload for TWIA. However, TWIA may face higher claims amounts due to more policyholders qualifying for replacement cost of the property at the time of loss, rather than actual cash value of the property.

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1 All citations to Texas statutes are as they appear on http://www.statutes.legis.texas.gov/. Section 2210.573, Texas Insurance Code.

2 Section 2210.581, Texas Insurance Code.

3 Sections 2210.574(d) and 2210.574(e), Texas Insurance Code.

4 As a prerequisite to filing legal action against TWIA, TWIA may require the claimant to submit to alternative dispute resolution by mediation or moderated settlement conference. If the claimant is not satisfied after the alternative dispute resolution, the claimant may bring an action against TWIA in district court. Sections 2210.575–.576, Texas Insurance Code.

5 Section 2210.573, Texas Insurance Code.

6 "Preparing for an Insurance Adjuster: An Important Step in Recovery," Insurance Journal, September 1, 2010, https://www.insurancejournal.com/news/southcentral/2010/09/01/112925.htm; "FEMA's National Flood Insurance Program Enhances the Flood Claims Process and Extends Grace Period for Policy Renewals," Federal Emergency Management Agency, September 4, 2017, https://www.fema.gov/news-release/2017/09/04/femas-national-flood-insurance-program-enhances-flood-claims-process-and.

7 Section 2210.207, Texas Insurance Code.

8 Section 2210.207(d), Texas Insurance Code.

9 Section 2210.573(d), Texas Insurance Code.

10 Section 2210.582, Texas Insurance Code.

11 "Adjuster: property and casualty," Texas Department of Insurance, accessed October 16, 2018, https://www.tdi.texas.gov/agent/adjuster-property-casualty-apply.html.

ISSUE 4

TWIA's Assumption Reinsurance Depopulation Program Is Unnecessarily Complicated and Inefficient.

Background

In 2015, the Legislature required the Texas Windstorm Insurance Association (TWIA) to start depopulation programs to encourage private insurance companies to take over TWIA policies and provide windstorm coverage along the coast.[1] TWIA runs two depopulation programs: the Assumption Reinsurance Depopulation Program and the Voluntary Market Depopulation Program. About 15,800 policies have transferred out of TWIA to private insurance companies under the two programs since 2015, and about 190 of those have returned. Because TWIA's financial position is dependent on expected future premiums, based on current projections, only about 2,000 policies can be depopulated in 2018 before negatively impacting TWIA's financial status.

- **Assumption Reinsurance Depopulation Program**. Participating private insurance companies review TWIA's policies and make offers to acquire a large number of policies all at once. This program is loosely modeled after the depopulation program for Louisiana Citizens, that state's insurer of last resort. Participating insurance companies must sign a confidentiality agreement to review policy information, which includes names, building characteristics, and addresses, but no financial information.[2] In the program, insurance agents must approve any offer from another insurance company before it goes to the policyholder, and the policy will transfer to the new insurance company unless the policyholder opts out. The textbox, *Assumption Reinsurance Depopulation Program Timeline*, summarizes the process. Once a policy is transferred, the new insurance company must maintain substantially similar coverage, insurance agent commissions, and premiums for three years.[3] After three years, the new insurance company can treat the policy as any other and set its own terms. Because the first set of policies transferred out of TWIA in 2016, restrictions on coverage, premiums, and commissions have yet to expire on any transferred policies. About 12,800 policies have transferred under this program.

> **Assumption Reinsurance Depopulation Program Timeline**
>
> ***August 25***: Final day for participating insurance companies to review TWIA's policies and identify which ones they will make offers on.
>
> ***September 1***: Insurance agents receive notice of offers from participating insurance companies.
>
> ***October 31***: Final day for insurance agents to approve offers from participating insurance companies.
>
> ***December 1***: TWIA notifies policyholders about approved offers to take over policies. The policies transfer to the new insurance company unless the policyholder proactively opts out of the offer.
>
> ***May 31***: Deadline for policyholders to opt out of the transfer of their policy to the new insurance company.

- **Voluntary Market Depopulation Program**. Participating insurance companies review and select TWIA policies they would be interested in acquiring as the individual policies renew throughout the year. Insurance companies do not have any restrictions on the coverage and premiums of the policies they obtain through this program. About 3,000 policies have transferred under this program.

Findings

The Assumption Reinsurance Depopulation Program is administratively complex, creating unnecessary confusion.

The process of transferring TWIA policies to a new insurance company is extremely complicated, creating additional work for TWIA and confusion for policyholders and insurance agents. In 2013, TWIA performed a study of various methods of depopulation and ways to encourage the private market to insure against windstorms along the coast, concluding that an assumption reinsurance program was among the most administratively expensive and complex types of depopulation programs.[4]

TWIA received 1,500 claims from policyholders who did not realize their policy had transferred.

- **Policyholder confusion delays claim payments**. In the wake of Hurricane Harvey, TWIA received 1,500 claims from former policyholders who either did not realize their policy had already transferred or did not realize their policy would transfer at all. This misunderstanding delayed the claims process for these individuals. Policyholders' confusion is understandable given that, depending on the renewal date, TWIA's name may remain on the insurance policy for up to a year after the new insurance company has assumed responsibility.

  Depopulation also can cause confusion between insurance agents and policyholders, such as when the policyholder does not notify their insurance agent about opting out of the depopulation program. Further, in some cases, multiple insurance companies made offers on the same policy and were later confused about which company had taken over the depopulated policy. When the policyholder filed a claim, multiple insurance companies attempted to handle it, requiring TWIA to step in, search its records, and determine which insurance company took over the policy.

Policyholders may still see TWIA's name on their policy, even though a new insurer has taken over.

- **The complexity of the program requires logistical and financial gymnastics**. For the six months between December and June, when the policyholder can opt out of the program, TWIA and the new insurance company split financial and legal obligations through an assumption reinsurance model.[5] If a policyholder has a claim during this time, TWIA operationally handles the claim but charges the new insurance company for the loss. If a policyholder were to sue during the first six months, TWIA would be the subject of the lawsuit.

  After the opt-out period, the policy, operations, and claims liability transfer to the new insurer, but TWIA still handles underwriting for the policy until it renews, at which point the new insurance company takes over underwriting and claims servicing responsibilities. The policyholder would still see TWIA's name on their insurance policy, even though the new insurance company has taken over; the new insurer's information does not appear on the policy until it has been renewed. TWIA holds premiums earned on the policy until the opt-out period is over and then transfers the premium income to the new insurance company minus a 24 percent commission paid to TWIA.[6] The commission paid to TWIA covers administrative overhead, state taxes, and the commission for the insurance agent. If a policyholder opts out of the transfer, TWIA has to adjust their accounting and re-absorb the premiums.

The industry's interest in the Assumption Reinsurance Depopulation Program is limited and the benefits to policyholders are questionable.

A key component of any depopulation program is the willingness of the private market to participate. However, only five insurance companies have participated in TWIA's Assumption Reinsurance Depopulation Program, and the number has decreased each year of the program, as seen in the table, *Assumption Reinsurance Depopulation Program Statistics*. In contrast, more than 140 insurance companies sell property insurance in Texas and are subject to TWIA's member assessments. Further, while all participating insurance companies must be approved by the Texas Department of Insurance, many are not highly rated by independent national insurance company evaluators, raising concerns for insurance agents and policyholders.

Only five companies have participated in the Assumption Reinsurance Depopulation Program.

Assumption Reinsurance Depopulation Program Statistics

Year	Number of Companies Participating	Number of Unique Offers	Offers Accepted by Agent	Policies Transferred on June 1
2016–2017	4	102,171	18,047	11,164
2017–2018	3	109,356	3,091*	1,634
2018–2019**	2	75,039	—	—

* The number of approved offers in the 2017–2018 program year was likely impacted by the timing of Hurricane Harvey, which hit the same week insurance agents were notified of offers.

** The 2018–2019 program year was not complete at the time of this publication.

Although several participating insurers are familiar with other states' depopulation programs, many are new to Texas and unfamiliar with TWIA's limited coverage and policy terms.[7] Because TWIA only covers hail and windstorm damage rather than providing whole house policies, participating companies must change their standard coverage to offer plans for just wind and hail to participate in the Assumption Reinsurance Depopulation Program. TWIA policyholders each have standard homeowners insurance from another carrier and, while they may eventually purchase a whole house policy that includes windstorm coverage from the new insurance company, they cannot automatically be transferred into one. Once the restrictions expire on the first round of depopulated policies in 2019, insurance companies can change the type of coverage they offer, and the impact this may have on policyholders is unclear.

Insurance agent interest in and ability to participate in the Assumption Reinsurance Depopulation Program is limited.

Insurance agents must first agree for policyholders to participate in the program.

- **Insurance agents have expressed concerns about the program's viability**. Some independent insurance agencies have opted out of participating in the Assumption Reinsurance Depopulation Program, citing uncertainty about the quality and financial soundness of the participating companies, and discomfort with making such a decision on their clients' behalves. Insurance agents help their clients understand available insurance options and make decisions about what coverage to purchase. Because notice that a new insurance company has selected a policy for depopulation is sent directly to the insurance agent, the agent, and not the policyholder, makes the initial decision whether to participate in the depopulation program. The policyholder, on the other hand, is enrolled in the program upon their insurance agent's approval and must proactively opt out if they do not wish to participate.

- **Many insurance agents contractually cannot sell depopulation policies**. All insurance agents can sell TWIA policies, including captive insurance agents under contract to sell policies for only a specific insurance company. However, because of that contractual obligation, these captive insurance agents cannot participate in the depopulation program because the insurance agent would need to contract with the new insurance company to participate. Therefore, a number of depopulation offers will never have the opportunity to reach policyholders.

Recommendation

Change in Statute

4.1 Eliminate the Assumption Reinsurance Depopulation Program.

This recommendation would remove TWIA's Assumption Reinsurance Depopulation Program from statute, but would maintain the Voluntary Market Depopulation Program and the confidentiality requirements for insurance companies who access information about TWIA policies. The Assumption Reinsurance Depopulation Program is complicated and inefficient, while the Voluntary Market Depopulation Program achieves the same goals without policyholder confusion. Discontinuing the Assumption Reinsurance Depopulation Program would also reduce the administrative burden on TWIA and the potential for misunderstanding by insurance agents and policyholders.

Fiscal Implication

This recommendation would not have a fiscal impact to the state because TWIA is not a state agency and does not receive any state funding. This recommendation also would not have a cost to TWIA or TWIA policyholders, but could result in some administrative savings.

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[1] All citations to Texas statutes are as they appear on http://www.statutes.legis.texas.gov/. Section 2210.701, Texas Insurance Code.

[2] 28 T.A.C. Section 5.4309.

[3] Section 2210.703, Texas Insurance Code.

[4] "Texas Windstorm Insurance Association Clearinghouse Feasibility Study," December 2013, https://www.twia.org/wp-content/uploads/2015/03/TWIA-Clearinghouse-Feasibility-Study1.pdf.

[5] Section 2210.705, Texas Insurance Code.

[6] Section 2210.705(3), Texas Insurance Code.

[7] Florida Citizens is the State of Florida's insurance provider of last resort. Unlike Texas, Florida combined their FAIR Plan with their windstorm and hail insurance provider to sell whole house insurance policies, which are easier to transfer to the private market. See "Texas Windstorm Insurance Association Clearinghouse Feasibility Study" for more information about Florida's depopulation program and key differences between Florida Citizens and TWIA.

Issue 5

TWIA's Process for Issuing Windstorm Certificates of Compliance Is Duplicative and Poses Risks to Public Safety.

Background

The Texas Department of Insurance (TDI) sets windstorm building code requirements based on international standards for buildings likely to encounter high wind speeds. To purchase windstorm insurance from the Texas Windstorm Insurance Association (TWIA), statute requires most property owners get a certificate of compliance to verify the building and any updates or extensions were built in compliance with the windstorm code.[1] Buildings that do not meet windstorm code may not only result in damage to people or other structures, but could also hinder TWIA's ability to accurately measure its liability and set insurance rates at appropriate levels. The state issues certificates of compliance both for entire buildings and for specific repairs, updates, or expansions, such as new roofs and screened-in porches.[2]

In addition to setting windstorm code, TDI issues a certificate of compliance with windstorm code called a WPI-8. TDI's process confirms that construction projects meet the windstorm code and identifies any issues with building materials or installation at the point when problems can be easily fixed. TDI issued 33,251 WPI-8s in 2017 and an additional 23,316 in the first half of 2018.

However, not all insured structures are newly constructed. Before 2017, the only way to get a certificate of compliance if construction was already completed was for an engineer to deconstruct portions of walls and roofs to inspect internal structural elements. Creating an alternative path to certification that did not require deconstruction, the Legislature tasked TWIA with issuing a certificate of compliance for completed projects that were not inspected throughout construction, known as a WPI-8-C. TWIA issued 4,422 WPI-8-Cs in 2017 and an additional 8,984 in the first half of 2018. The textbox, *Certificate of Compliance Options*, has more information about the two windstorm code compliance certificates.[3]

Certificate of Compliance Options

The state provides two types of certificates of compliance with windstorm code: the WPI-8 and the WPI-8-C.

During construction – WPI-8

To certify that a structure was built to windstorm code, TDI requires inspections throughout the construction process to ensure internal framing and structural supports meet windstorm code. TDI provides licensed engineer inspectors to property owners at no cost or, for larger or more complicated projects, property owners can hire inspectors or engineers pre-approved by TDI. Once the project is completed and all inspection documentation has been submitted and evaluated, TDI issues a WPI-8.

Post-construction – WPI-8-C

TWIA issues certificates of compliance for completed projects, where a constructed building did not receive inspections throughout the construction process. Statute provides two paths to get a WPI-8-C:

1. *Engineer-Designed Projects*: TWIA will issue a WPI-8-C after receiving documentation that a licensed professional engineer designed the construction project.
2. *Engineer-Inspected Construction*: TWIA will issue a WPI-8-C after receiving documentation that a licensed professional engineer completed a post-construction inspection confirming windstorm code compliance.

Findings

TWIA is ill-suited to ensure windstorm code compliance.

Regulatory activities, such as issuing WPI-8-Cs, are outside of TWIA's scope and do not fit within its mission to be an insurer of last resort.[4] The windstorm code ensures buildings are designed to withstand storms, limiting the amount of flying debris that can cause additional harm to people or other buildings and reducing damage and costs for both policyholders and TWIA. Proper verification of windstorm code compliance is important, because no clear signs of windstorm code violations are likely to arise until a major storm hits.

TWIA focuses on its primary functions of offering insurance and handling claims.

However, as an insurance provider, TWIA is not well suited to administer windstorm code compliance. TWIA's employees and processes focus on its primary functions of offering insurance and handling claims. TWIA does not employ engineers to evaluate certificate applications or inspectors to visit or inspect buildings; instead, TWIA relies on TDI's regulatory functions to set windstorm code and verify compliance.

TDI has an existing regulatory process to issue windstorm certificates of compliance.

Because TDI has long been the issuer and regulator of windstorm certificates of compliance, TDI has an existing, proven structure for oversight. TDI, unlike TWIA, has staff expertise and fully developed processes for responding to complaints and conducting audits, approving inspectors, and providing information to the public.

TWIA has no capacity or authority to ensure the quality of compliance certificates or respond to complaints.

- **Responding to complaints and conducting audits**. TDI responds to consumer complaints related to TDI-approved windstorm code compliance inspectors and audits WPI-8s. TDI revokes approval for any inspectors whose work repeatedly fails audits. Additionally, TDI engineering staff randomly sample WPI-8 applications and double check that all documentation is accounted for and accurate. TWIA has no program, capacity, or authority to provide quality assurance audits for WPI-8-Cs or to respond to consumer complaints.

- **Inspector regulation**. For smaller projects and repairs, TDI employs inspectors to conduct construction site visits for WPI-8s at no cost to the property owner. Further, TDI pre-approves independent inspectors that property owners can hire to provide the required inspections for WPI-8s. TWIA's WPI-8-C process requires property owners hire independent engineers to certify that construction meets windstorm code, but statute requires TWIA to issue WPI-8-Cs to anyone submitting the completed forms without any sort of evaluation.[5] TWIA also cannot prohibit professional engineers licensed in Texas from submitting WPI-8-Cs, even engineers that TDI has removed from its list of approved inspectors.

- **Staff expertise**. To provide necessary knowledge and information about windstorm building codes and WPI-8s, TDI employs several engineers who evaluate applications, certify compliance, investigate complaints, and conduct audits. Engineering expertise is a key component of TDI's ability to provide oversight of the WPI-8 process and ensures buildings seeking windstorm insurance are actually windstorm code compliant. TWIA, as an insurance provider, does not have any engineers on staff or any other way to evaluate the information provided in applications for WPI-8-Cs.

- **Information for the public**. TDI works to provide information to the public about meeting windstorm code and to make WPI-8 records easily accessible. TDI hosted training sessions after Hurricane Harvey to explain windstorm certification requirements for property owners and contractors and worked with construction materials stores to identify products that meet windstorm code. Many different people require access to records about windstorm code compliance, such as property owners, construction and engineering companies, and real estate agents. TDI has an easily searchable online portal where WPI-8s are accessible by property address or certificate number. If someone wishes to verify WPI-8-Cs, they have to call TWIA and have employees search the internal database. While TWIA provides information on its website about meeting windstorm code, their public education focus is on the claims process and creating a duplicative online portal would increase TWIA's costs to administer the program.

TDI has an online portal to search compliance certificates.

Issuing certificates of compliance based on building design alone exposes TWIA to additional potential liability.

Providing insurance on a home that was designed to meet windstorm code, but may not have been built to code, places TWIA and property owners at risk. The goal of the windstorm code certification processes is to ensure the windstorm code is met. While building designs are an important component of meeting windstorm code, some inspection of the completed building is necessary to ensure compliance. Currently, statute provides two methods to qualify for a WPI-8-C: submit a verified design or have an engineer inspect the building, using designs and other documentation as additional proof.

Having an engineer certify that a property's design meets windstorm code may not be sufficient to conclude the building actually meets windstorm code after construction. No matter how well a project is designed, compliance with windstorm code depends on the choices made during construction. For example, a design may call for windstorm-certified windows, but the homebuilder or the homeowner may purchase a different window to cut costs. Alternatively, the homeowner may purchase the correct windstorm-certified window but install it improperly, negating the safety effects of the window's design. An inspection would be necessary to identify either of these windstorm code violations. However, requiring an inspection to improve the validity of the design-only option would exactly recreate and duplicate the other method for getting a WPI-8-C.

No matter how well a project is designed, windstorm code compliance depends on choices made during construction.

Recommendations

Change in Statute

5.1 Transfer the issuance of WPI-8-Cs from TWIA to TDI.

This recommendation would transfer the WPI-8-C certification process to TDI. With the transfer, this recommendation would clarify that TDI must first receive proper documentation supporting the engineer's evaluation and the form would require the engineer's seal. TDI would be authorized to deny certificate applications if documentation is incomplete. If TDI has any concerns with the work of the engineer, TDI would be authorized to refer the matter to the Texas Board of Professional Engineers as a formal complaint subject to enforcement actions by the board. This recommendation would ensure WPI-8-Cs are issued under proper oversight to guarantee TWIA-insured buildings can withstand strong winds, limiting damage and debris during and after major storms. Transferring the WPI-8-C process to TDI would also provide better customer service by allowing electronic access to filed WPI-8s and WPI-8-Cs, and providing comprehensive and consistent information about windstorm code compliance. This recommendation would also allow TWIA to better focus on its core insurance functions.

5.2 Remove the ability to obtain a WPI-8-C based on design alone.

This recommendation would eliminate the ability of a property owner to get a WPI-8-C based on engineer-sealed design plans alone. Some inspection of a completed building is necessary to ensure the design was properly constructed and that the building meets windstorm code. By removing a path that does not provide sufficient evidence of compliance, this recommendation would help strengthen the integrity of the WPI-8-C process and better protect public safety. Property owners would still be able to get a WPI-8-C following the inspection of their property by a licensed engineer or a WPI-8 by getting inspections throughout the construction process. This recommendation would only apply to applications for certificates filed after September 1, 2019; TDI would be required to accept any WPI-8-Cs issued by TWIA prior to this date.

Fiscal Implication

These recommendations would have a minimal fiscal impact to the state. TWIA does not receive any state funding, but would see reduced costs with the transfer of the WPI-8-C process to TDI, which already has processes in place for issuing and managing WPI-8s that would be used for issuing WPI-8-Cs. The increased costs for TDI to issue and oversee WPI-8-Cs cannot be estimated, because the number of policyholders who might request WPI-8-Cs is unknown. However, while TDI currently provides certificates of compliance at no cost, statute authorizes TDI to charge a fee for certificates of compliance, and TDI could ensure the fee covers the cost of issuing the additional certificates if necessary.[6]

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[1] All citations to Texas statutes are as they appear on http://www.statutes.legis.texas.gov/. Sections 2210.251(d) and 2210.251(e), Texas Insurance Code. TWIA policyholders with structures built between 1988 and 2009 pay a 15 percent surcharge if they do not have a windstorm certificate. Policyholders with structures built before 1988 are exempt from the surcharge, and structures built after 2009 must have a certificate.

[2] TDI lists certain building improvements and repairs that do not require a windstorm code compliance certificate. Examples of repairs falling into this category include repairs to roof coverings with an area of less than 100 square feet, replacing gutters, replacing decorative shutters, fence repair, plumbing and electrical repairs, and painting and carpeting.

[3] Section 2210.2515(c), Texas Insurance Code.

[4] Section 2210.001, Texas Insurance Code.

[5] Section 2210.2515(c), Texas Insurance Code.

[6] Section 2210.2515(h), Texas Insurance Code.

ISSUE 6

TWIA Lacks Certain Good Government Standards That Would Enhance Responsiveness, Transparency, and Accountability.

Background

Like private insurance companies, the Texas Windstorm Association (TWIA) operates with regulation and oversight from the Texas Department of Insurance (TDI). TWIA is also governed by a nine-member board of directors comprised of

- three industry representatives from companies actively writing and renewing windstorm and hail insurance across the coast;
- three members living in the coastal counties TWIA serves, one of whom must be an independent property and casualty insurance agent; and
- three members who live more than 100 miles from the coast.[1]

TWIA's board operates according to a plan of operation adopted in rule by TDI, which sets out the board's responsibilities and basics of TWIA's administration, including underwriting standards, procedures for paying claims, and processes for issuing and repaying bonds.[2]

TDI initiates the rulemaking process for all rules related to TWIA, including the plan of operation, and holds public hearings on proposed rules.[3] TWIA may present recommendations for its rules and plan of operation at TDI's hearings, similar to any other stakeholder.[4] TWIA's board does not have rulemaking authority, and TDI does not have to take action on TWIA's proposals.[5] As a nonprofit insurance provider created by the Legislature, TWIA is not a state agency and does not receive any appropriations from the General Revenue Fund or any tax dollars.

Findings

The current rulemaking process impedes TWIA's ability to quickly implement statutory changes and respond nimbly to stakeholder needs.

Relying on TDI to proactively adopt necessary rules leaves TWIA with rules that are out of step with legislative changes and current practice. Although TDI has recently expedited issuance of rules, TDI does not always adopt rules in a timely manner. For example, TDI has yet to fully update TWIA's rules to implement statutory changes adopted in 2015 related to disbursements from the Catastrophe Reserve Trust Fund.[6] TDI also has yet to update TWIA's rules to implement changes from legislation enacted in 2011 that directed TDI to adopt rules defining the term "actuarially justified" as it relates to premium discounts and surcharge credits on TWIA policies, instead deferring to TWIA to define this internally.[7] TDI concluded that no rules were necessary, but adopting a clear definition in rule would have provided TWIA with clearer guidance and ensured compliance.

TDI has not fully updated TWIA's rules to implement statutory changes passed in 2015.

TWIA currently has no real role or standing during TDI's rulemaking process. Despite having a governing board appointed by the commissioner of insurance and extensive, detailed statutory oversight, TWIA submits comments on TDI's proposed rules like any other third party and does not participate in the drafting of rules or public hearings soliciting comments on the rules. Given that statute requires so much of TWIA's day-to-day processes be set out in rule, TWIA cannot innovate or respond to feedback from stakeholders without appealing to TDI and waiting for its response.

TWIA has no real role or standing during TDI's rulemaking process.

Expressly authorizing TWIA to propose rules that require TDI to take action would give TWIA's stakeholders another forum to provide feedback on proposed changes and allow TWIA to react to pressing matters in between legislative sessions. Since TWIA is not a state agency it cannot have rulemaking authority, but it could operate in a manner similar to an advisory board under a regulatory agency. TWIA has the expertise of its day-to-day operations necessary to detail how it would implement legislative and customer service changes, while TDI would retain rulemaking authority and regulatory oversight.

TWIA's statute does not reflect good government principles typically applied during Sunset reviews.

The Sunset Advisory Commission has developed a set of standard recommendations it applies to all state agencies reviewed unless an overwhelming reason exists not to do so. These across-the-board recommendations (ATBs) reflect an effort by the Legislature to place policy directives on agencies to prevent problems from occurring instead of reacting to problems after an issue arises. ATBs are statutory administrative policies adopted by the Sunset Commission that contain "good government" standards and reflect review criteria contained in the Sunset Act designed to ensure open, responsive, and effective government. While TWIA is not a state agency, certain ATBs are still applicable to TWIA as a governmental entity, though they may need modification to match TWIA's unique structure and function.

- **Board member training**. TWIA's statute does not specify the type of training and information board members need for them to properly discharge their duties. Additionally, statute does not require TWIA to create a training manual for all board members or specify that the training must include a discussion of the scope of the board's authority.

- **Public members and conflicts of interest**. Having public membership on the board ensures an effective balance between represented industry interests and public interests. Statute requires the TWIA board to consist of three members who represent insurance companies; three members who reside in the coastal counties, one of whom must be an independent insurance agent; and three members who reside 100 miles from the coast.[8]

By specifying certain members should represent insurance interests — three representatives from insurance companies and one coastal member who is an independent insurance agent — statute appears to indicate the remaining five members should represent the interests of the public from the areas they represent. However, statute does not prohibit these public members representing coastal counties or counties 100 miles from the coast from being involved in the insurance industry or from receiving compensation for work performed for windstorm repair. Without this prohibition, the board could be comprised of a majority of members who represent or benefit from insurance interests, undermining the board's membership diversity. For example, two current non-industry TWIA board members receive funds from TWIA or have ties with professional trade organizations involved in the insurance industry.

Statute does not prevent public members from being involved in the insurance industry.

Statute also does not require board members to disclose potential conflicts of interest. Although the statutory design of the board necessarily means that some members will have a conflict of interest, the board could benefit from a requirement to disclose certain conflicts. For example, disclosing when an agenda item directly affects or benefits the board member's affiliated company or personal windstorm insurance policy would provide some measure of accountability to ensure board members do not take advantage of their official positions. By comparison, general law effectively requires members of all other boards in the state to disclose their conflicts of interest and abstain from voting on items that may present a conflict.[9]

All but one of TWIA's reporting requirements continue to be needed.

The Sunset Act establishes a process for the Sunset Commission to consider if reporting requirements of agencies under review need to be continued or abolished.[10] The Sunset Commission has interpreted these provisions as applying to reports required by law that are specific to the entity and not general reporting requirements that extend well beyond the scope of the entity under review. Reporting requirements with deadlines or that have expiration dates are not included, nor are routine notifications or notices, posting requirements, or federally mandated reports.

TWIA's Bimonthly Report Card *duplicates another report.*

State law requires TWIA to produce three reports, listed in the chart on the following page, *TWIA Reporting Requirements*. The *Bimonthly Report Card* is substantially similar to the *Annual Report Card* TWIA provides to the board at its quarterly meetings creating unnecessary duplication. Sunset staff analysis determined the other two reports continue to provide useful information and should be continued.

TWIA Reporting Requirements

Report Title	Legal Authority	Description	Recipient	Sunset Evaluation
1. Annual Report Card	Section 2210.107(c), Texas Insurance Code	Annual report on whether TWIA met the primary objectives of its board of directors.	Governor, Lieutenant Governor, Speaker of the House, Commissioner of Insurance, and TWIA Legislative Oversight Board	Continue
2. Biennial Report	Section 2210.0025, Texas Insurance Code	Proposed changes to TWIA's laws and information requested by TDI regarding TWIA operations or procedures.	Appropriate committees of each house of the Legislature, Insurance Commissioner, and Sunset Advisory Commission	Continue
3. Bimonthly Report Card	Section 2210.107(b), Texas Insurance Code	Bimonthly report on whether TWIA met the primary objectives of its board of directors.	TWIA Board of Directors	Eliminate

TWIA should continue to implement cybersecurity requirements and industry best practices.

The 85th Legislature tasked the Sunset Commission with assessing cybersecurity practices for entities under review.[11] The assessment of TWIA's cybersecurity practices focused on identifying whether TWIA complied with industry cybersecurity best practices. Sunset staff did not perform technical assessments or testing due to lack of technical expertise, but worked closely with the Department of Information Resources to gather a thorough understanding of TWIA's technical infrastructure. Sunset staff found no issues relating to TWIA's cybersecurity practices that require action by the Sunset Commission or the Legislature, and communicated the results of this assessment directly to TWIA.

Recommendations

Change in Statute

6.1 Authorize TWIA to formally propose rules to the Texas Department of Insurance.

This recommendation would authorize TWIA to propose rules directly to TDI. Under this recommendation, TWIA would propose rules to TDI, which would retain ultimate rulemaking authority. This recommendation would specify that TDI must initiate the formal rulemaking process within 30 days of receiving TWIA's proposed rules, and adopt or reject TWIA's proposed rules within the timeframes established by the Administrative Procedure Act. TDI would also be required to include TWIA in public hearings and other stakeholder processes for adopting rules. Authorizing TWIA to propose rules to TDI would ensure the timely implementation of statute and facilitate TWIA's continued process improvements.

6.2 Apply the standard across-the-board requirement related to board member training.

This recommendation would require TWIA to provide training to its board members and would clearly establish the type of information to be included in the training. The training would need to provide board members with information regarding the legislation that created the board and legislation that affects TWIA; its programs, functions, rules and budget; its role in TDI's rulemaking process; the results of its most recent formal audit; the requirements of laws relating to open meetings, public information, administrative procedure and conflicts of interest; and any applicable ethics policies. This recommendation also would require the agency to develop a training manual that each TWIA member attests to receiving annually. Requiring this training and the training manual would provide board members with adequate information to allow them to properly discharge their duties.

6.3 Apply standard across-the-board requirements related to public membership.

This recommendation would prohibit a person from serving as a public member of the board if the person or the person's spouse uses or receives a substantial amount of tangible goods, services, or money from TWIA, other than insurance claim payments or, compensation or reimbursement authorized by law for TWIA membership, attendance, or expenses. In addition, this recommendation would prohibit a person employed by or participating in the management of a business entity or other organization in the insurance industry, or receiving money from TWIA, from being a public member on its board. Adding this prohibition would help ensure that public members of TWIA's board of directors represent public interests rather than a personal or industry interest.

6.4 Require TWIA board members to publicly disclose specific conflicts of interest.

This recommendation would require members of TWIA's board of directors to publicly disclose specific conflicts of interest before discussing or voting on a matter before the board. For example, this recommendation would require board members to disclose if a board member's affiliated company would benefit financially from a vote or a board member's windstorm insurance cost or coverage would be impacted by a vote. While Sunset acknowledges that some conflicts of interest are built into the composition of the board as set in statute, adding the requirement to at least disclose a conflict of interest would improve transparency for stakeholders and board members around board decisions.

6.5 Eliminate the duplicative *Bimonthly Report Card* reporting requirement and continue TWIA's two other required reports.

This recommendation would eliminate TWIA's *Bimonthly Report Card*, since this information is duplicative of the *Annual Report Card* and continue TWIA's two other reports, including the *Biennial Report* and the *Annual Report Card.*

Fiscal Implication

These recommendations would not have a fiscal impact to the state because TWIA does not receive state funds. The recommendations would reduce the workload of TWIA staff by removing the requirement in statute for TWIA to produce the *Bimonthly Report Card*. TWIA already provides information to its board members and could use its existing resources to provide additional training to the board.

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1 All citations to Texas statutes are as they appear on http://www.statutes.legis.texas.gov/. Section 2210.102, Texas Insurance Code.

2 Section 2210.152, Texas Insurance Code; 28 T.A.C. Sections 5.4001, 5.4007–.4011, 5.4101–.4102, 5.411–.4114, 5.4121, 5.4123–.4128, 5.4133–.4136, 5.4141–.4149, 5.4161–.4167, 5.4173, 5.4902–.4908, and 5.4911.

3 Section 2210.151, Texas Insurance Code.

4 Section 2210.153, Texas Insurance Code.

5 Section 2210.151, Texas Insurance Code.

6 Section 2210.452, Texas Insurance Code; TDI reports that the updated rule as required by the 2015 legislation is in the final stages of review as of October, 2018. TDI reports the absence of an updated rule did not adversely impact TWIA's ability to access or disburse funds following Hurricane Harvey.

7 Section 2210.363, Texas Insurance Code.

8 Section 2210.102, Texas Insurance Code.

9 Section 572.058(a), Texas Government Code.

10 Sections 325.0075, 325.011(13), and 325.012(a)(4), Texas Government Code.

11 Section 325.011(14), Texas Government Code.

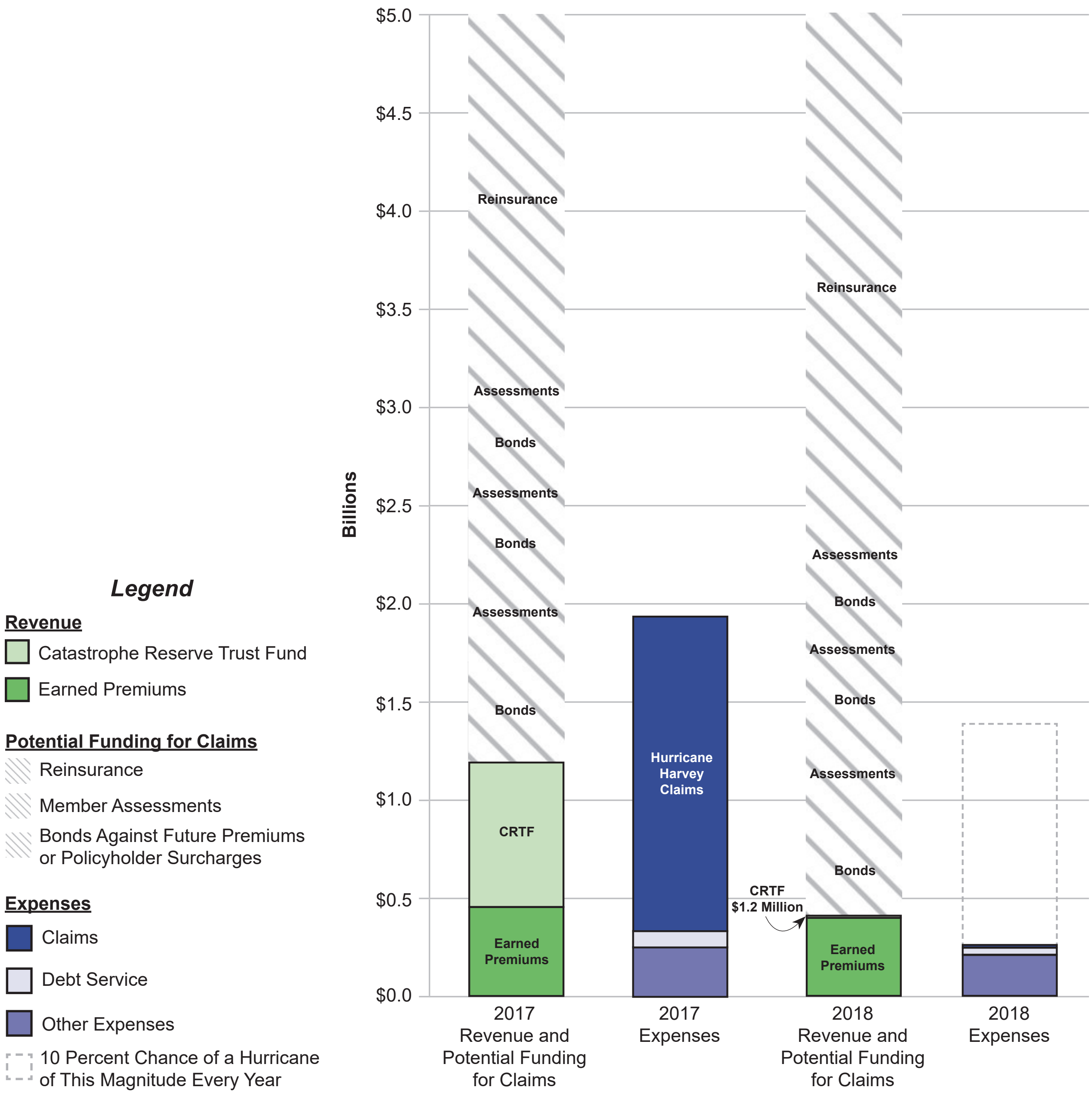
APPENDICES

Appendix A

How TWIA Pays for Claims

The Texas Windstorm Insurance Windstorm Association (TWIA) pays claims and other expenses with revenue from premiums and contributes any excess revenue to the Catastrophe Reserve Trust Fund (CRTF). To pay for claims that exceed that year's premiums, the Legislature requires TWIA to access other sources of revenue, including funds accumulated in the CRTF, bonds repaid by future premiums or policyholder surcharges, assessments on property insurance companies, and reinsurance. The State of Texas does not directly contribute any funds to TWIA, nor does the state back any of TWIA's debt.

TWIA Revenue and Potential Funding for Claims Compared to Expenses — 2017–2018

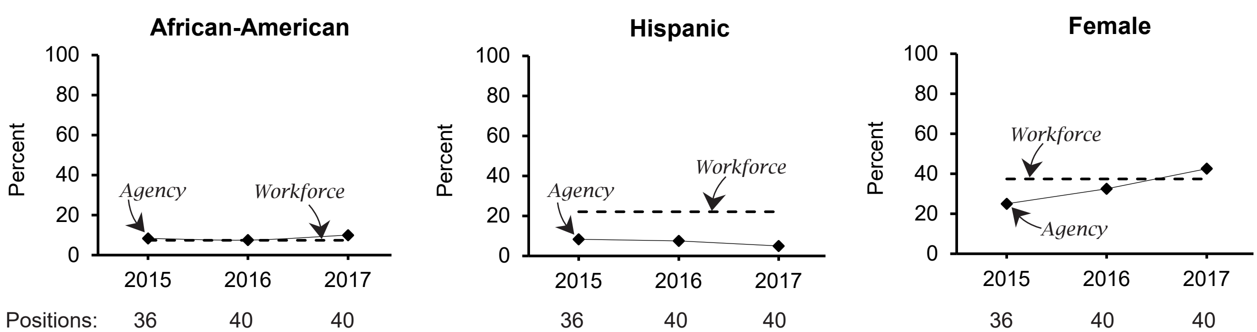


Appendix B

Equal Employment Opportunity Statistics 2015 to 2017

In accordance with the requirements of the Sunset Act, the following material shows trend information for the employment of minorities and females in all applicable categories by the Texas Windstorm Insurance Association (TWIA).[1] The trend information includes data for TWIA and Texas FAIR Plan Association combined because the two associations share staff and this data was not available on an allocated basis for TWIA alone. TWIA maintains and reports this information under guidelines established by the Texas Workforce Commission.[2] In the charts, the dashed lines represent the percentages of the statewide civilian workforce for African-Americans, Hispanics, and females in each job category.[3] These percentages provide a yardstick for measuring agencies' performance in employing persons in each of these groups. The diamond lines represent TWIA's actual employment percentages in each job category from 2015 to 2017. TWIA consistently fell below civilian workforce percentages for African-Americans in the professional and administrative support categories from 2015 to 2017. TWIA also consistently fell below civilian workforce percentages for Hispanics in the administration category for the last three years. TWIA has no employees in the technical, service/maintenance, and skilled craft categories.

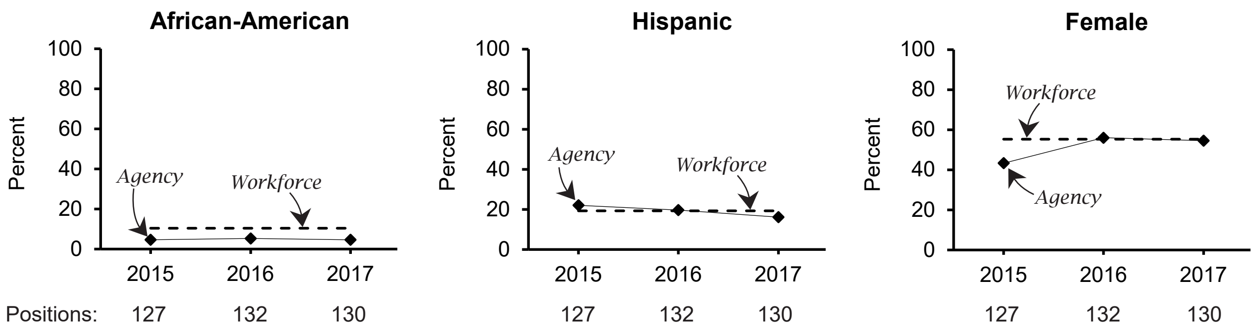
Administration



TWIA exceeded the civilian workforce percentages for African-Americans, but fell below the percentages for Hispanics in the last three years and for females in 2015 and 2016.

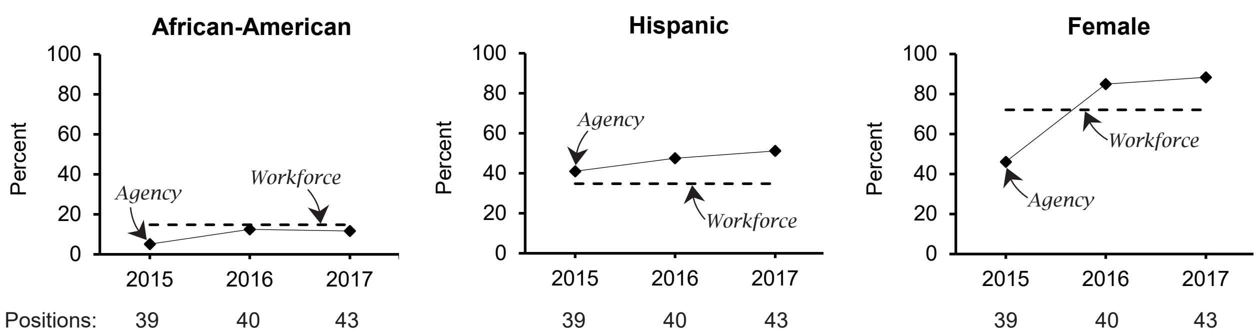
Appendix B

Professional



TWIA fell below the civilian workforce percentages for African-Americans in the last three years. TWIA also fell below the civilian workforce percentages for Hispanics in 2017 and for females in 2015 and 2017.

Administrative Support



TWIA exceeded the civilian workforce percentages for Hispanics in the last three years, but fell below the civilian workforce percentages for African-Americans in that same period and for females in 2015.

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1 All citations to Texas statutes are as they appear on http://www.statutes.legis.texas.gov/. Section 325.011(9)(A), Texas Government Code.

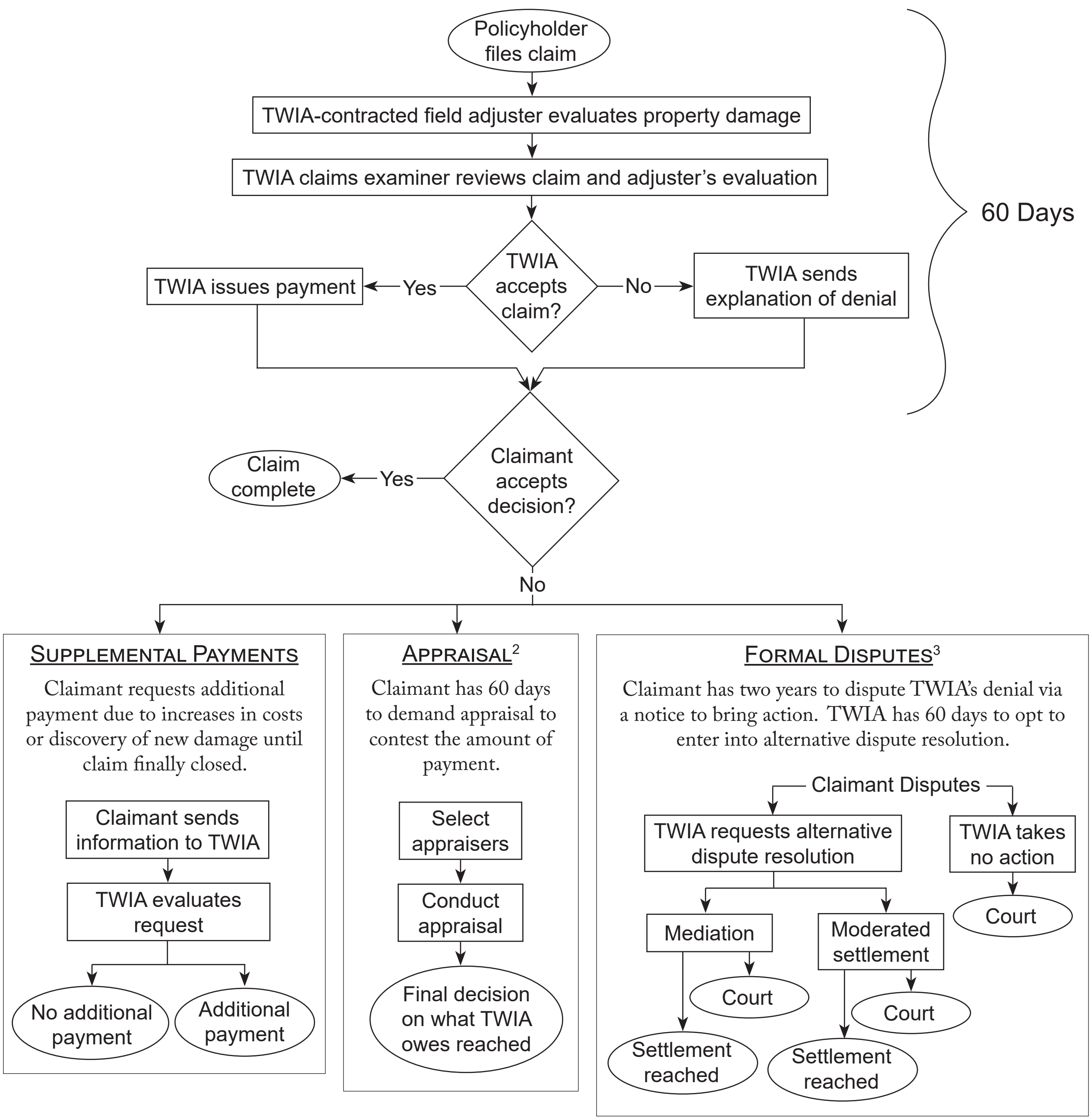
2 Section 21.501, Texas Labor Code.

3 Based on the most recent statewide civilian workforce percentages published by the Texas Workforce Commission.

Appendix C

TWIA Claims Process

When a policyholder files a claim, the Texas Windstorm Insurance Association (TWIA) processes the claim much like a private insurance company but subject to statutory deadlines. The policyholder has a year after the damage occurs to file a claim, and TWIA has 60 days to make a decision on the claim.[1] The Texas Department of Insurance can extend this deadline to up to 180 days. If a claimant disputes TWIA's payment amount, the claimant can pursue additional funds through the appraisal or supplemental payment processes. If a claimant disagrees with TWIA's denial of coverage, the claimant can formally dispute the denial.



Appendix C

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1 All citations to Texas statutes are as they appear on http://www.statutes.legis.texas.gov/. Sections 2210.205(a)(1) and 2210.573, Texas Insurance Code.

2 Section 2210.574, Texas Insurance Code.

3 Sections 2210.575 and 2210.576, Texas Insurance Code.

Appendix D

Staff Review Activities

During the review of the Texas Windstorm Insurance Association (TWIA), Sunset staff engaged in the following activities that are standard to all Sunset reviews. Sunset staff worked extensively with TWIA personnel; attended board meetings; met with staff from key legislative offices; conducted interviews and solicited written comments from interest groups and the public; reviewed TWIA's documents and reports, state and federal statutes, legislative reports, previous legislation, and literature; researched the organization and functions of similar state entities in other states; and performed background and comparative research.

In addition, Sunset staff also performed the following activities unique to this agency:

- Interviewed policyholders, insurance agents, engineers, local government officials, and community groups on the coast
- Interviewed staff from state agencies including the Texas Department of Insurance, Office of Public Insurance Counsel, and Texas Board of Professional Engineers
- Virtually toured the Texas Windstorm Insurance Association's Policy Center and Claims Center portals
- Solicited and reviewed feedback through an online questionnaire of TWIA stakeholders

Sunset Staff Review of the *Texas Windstorm Insurance Association*

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