

NORTH CAROLINA DEPARTMENT OF INSURANCE
RALEIGH, NORTH CAROLINA

STATE OF NORTH CAROLINA
COUNTY OF WAKE

BEFORE THE COMMISSIONER
OF INSURANCE

IN THE MATTER OF:

THE FILING)
DATED JANUARY 3, 2024 BY)
NORTH CAROLINA RATE BUREAU)
FOR THE REVISION OF)
HOMEOWNERS INSURANCE RATES)

NOTICE OF HEARING

Docket Number 2157



TO THE NORTH CAROLINA RATE BUREAU:

I. Pursuant to the North Carolina General Statutes Chapter 58, Article 36, and other pertinent North Carolina General Statutes, Mike Causey, the North Carolina Commissioner of Insurance, hereby gives notice that a hearing will be held beginning October 7, 2024, at 10:00 a.m., in the hearing room of the North Carolina Department of Insurance (hereinafter “the Department”), Second Floor, 3200 Beechleaf Court, Raleigh, North Carolina, to consider the filing dated January 3, 2024 (hereinafter “the filing”) of the North Carolina Rate Bureau (hereinafter “the Bureau”) for the revision of North Carolina homeowners’ insurance rates.

II. At the hearing, the Department will present its objections to the Bureau’s filing because the Department contends the requested increases in homeowners’ premium rates are excessive and unfairly discriminatory. The Department contends that the Bureau’s filing significantly overstates both the prospective losses and profits that the Bureau is entitled to obtain on behalf of its insurance-company members. The Department asserts that the Bureau’s filing significantly overstates prospective losses, expenses, and profits to try to justify rate increases for

the Bureau's insurance-company members. The Department contends that, if the Bureau's filing were accepted as is, it would unlawfully prejudice and burden the consumers of the state. The Department will present at the hearing its own analysis of those homeowners' rates that are fair, equitable, and in compliance with North Carolina laws for both consumers and homeowners' insurance companies.

III. At the hearing, the Commissioner or his designated hearing officer will consider the Bureau's filing under the standards specified in the North Carolina General Statutes Chapter 58, Article 36, and all other applicable standards as set forth in the North Carolina General Statutes for the making of property insurance rates.

IV. Among other things, the Department contends that the filing suffers from significant deficiencies of the following character:

A. The data contained therein are so questionable that a proper evaluation of this filing, including its various components and methodologies, to determine whether it satisfies the rate standards specified in N.C.G.S. §§ 58-36-10 and 58-36-15 is obstructed. In many instances, the filing lacks the necessary data, documentation, and explanations of methodology to meet the Bureau's statutory burden of proof. As a result, significant further data and information will be requested from the Bureau by the Department. Prior to the date of this notice, however, such data and information has not yet been formally requested and, as a result, biases, and deficiencies beyond those evident at present may yet be detected.

B. The filing is not clear, concise, internally consistent, or readily understandable. There is a pervasive lack of documentation, explanation, and justification of both the data used, as well as the procedures and methodologies utilized in the filing.

C. As a consequence of the deficiencies described herein, the proposed rates appear in their entirety to be excessive and unfairly discriminatory in violation of N.C.G.S. § 58-36-10(1).

V. The Department contends, on information and belief, that the filing fails to comply with the requirements of Article 36 of Chapter 58 of the North Carolina General Statutes at least in the following respects and at least to the following extent:

A. Due consideration has not been given to actual loss and expense experience within this State for both the most recent three-year and five-year periods for which such information is available in that:

1. The use of combined experience for the voluntary market, consent to rate and Beach Plan, is inappropriate and lacks adequate explanation or justification. Further, the loss, expense, and exposure experience provided on, for example, RB-1, pages C-2, C-3, and C-4 and elsewhere in the filing are outdated as the latest data included in the filing is only through 2021. More recent data should be available and included in the analysis.

2. The failure to use actual data in various calculations, including but not limited to the modeled “compensation for assessment risk,” the modeled “net cost of reinsurance,” and the “trended modeled hurricane base-class loss costs,” lacks adequate explanation or justification. The data, assumptions, and methodology underlying the modeled values were not provided.

3. The filing contains data and information that appear inconsistent, outdated, irrelevant, incomplete, or not in compliance with the statutory requirements of N.C.G.S. §§ 58-36-10 and 58-36-15.

4. The derivations and/or selections of the loss development factors used in the filing are not properly documented, explained, or justified.

5. The filing fails to adequately document, explain, or justify the provisions for general expenses, other acquisition expenses, commissions and brokerage, taxes, licenses and fees, and loss adjustment expenses.

6. The treatment of dividends and deviations in the derivation of manual rates is unsupported by either theory or practice and is contrary to N.C.G.S. § 58-8-25 and to the decisions of the appellate courts of North Carolina.

7. The filing fails to give due consideration to observed changes in the loss costs in establishing loss trends. The filing fails to provide proper data for calculating trends. Only five annual data points were provided whereas quarterly data points should have been provided. Further, the data that was provided was only through 2021 but more recent data should be available and included in the analysis. Additional ratemaking data, trend data, and other relevant data should be available. Appropriate consideration was not given to actual insurance loss trends. Fast Track trend data is available and should be considered. The filing fails to support the numerical magnitude of the trends used, as well as the basis for using different selected trends on a prospective basis compared to the selected historical trends.

8. The filing fails to adequately explain (a) how the common deductible was selected to which various data, including but not limited to data on RB-1, pages C-2, C-3, and C-4, were adjusted, (b) how the adjustment was made including the derivation and support for the loss elimination ratios (LER) used, to

provide any underlying calculations, or (c) to explain its impact on the requested rate level change.

9. The “compensation for assessment risk” in RB-1, pages C-2, C-3, C-4, and elsewhere in the filing does not appear to be an actual value, but, instead, is a calculated hypothetical value that is inappropriate and lacks adequate explanation or justification, among other reasons because:

a. The filing does not support the numerical value of the provision for the “compensation for assessment risk” included in the filing;

b. With regards to the provision for “compensation for assessment risk,” the filing appears to disregard the actual relevant assessment experience for North Carolina;

c. The “compensation for assessment risk” is, effectively, largely an additional profit provision. The filing has not justified the large profit component of the “compensation for assessment risk” and furthermore does not explain why this extra hidden profit provision is needed in addition to the explicit underwriting profit provision included in the filing;

d. The “compensation for assessment risk” is based upon unsupported and undocumented computer model calculations which have been previously rejected by the Commissioner of Insurance;

e. The “compensation for assessment risk” is based on simulated hurricane models, as well as derived profit multiples,

neither of which have been shown to be accurate or reliable, and both of which have previously been rejected by the Commissioner of Insurance; and

f. The “compensation for assessment risk” is based on a 50% value for the impact of reinsurance, which is not supported by any actual information, but instead is merely an assumption of the Bureau.

10. The “net cost of reinsurance” on RB-1, pages C-2, C-3, C-4, and elsewhere in the filing does not appear to be an actual value, but instead is a calculated hypothetical value that is inappropriate and lacks adequate explanation or justification, including because:

a. The filing does not support the numerical value of the provision for the “net cost of reinsurance” included in the filing;

b. The “net cost of reinsurance” provision in the filing appears to disregard the actual reinsurance experience in North Carolina;

c. The filing lacks relevant information for evaluating the provision for the “net cost of reinsurance,” including because: (i) amounts actually paid or to be paid to reinsurers, (ii) ceding commissions paid or to be paid to insurers by reinsurers, (iii) expected reinsurance recoveries from actual, as opposed to hypothetical, reinsurance, (iv) North Carolina exposure to catastrophic events, (v) the basis and the results from unsupported and undocumented models, (vi) reinstatement premium, and (vii)

actual reinsurance provisions and structure applicable to North Carolina homeowners' insurance;

d. The "net cost of reinsurance" is, in large part, additional transfer of profit from policyholders to the industry. The net cost of reinsurance is more than 31% of the Bureau's "Required Base Rate Per Policy" for the owners' forms. This is more than triple the explicit underwriting profit provision of 9.0 % included in the filing. These two profit provisions included in the filing result in over 40% of the Bureau's "Required Base Rate per Policy" for owners' insurance being allocated to insurance industry underwriting profits (this does not include other provisions for underwriting profit included in the Bureau's rate calculation under the names of "Compensation for Assessment Risk per Policy" and "Contingencies");

e. Documentation and justification were not provided showing that the calculations underlying the "net cost of reinsurance" provision are based upon the data and experience for the relevant set of insurance companies;

f. The Bureau's contention that "It is not possible to measure reinsurance costs of the various insurance companies applicable specifically to homeowners' insurance written in North Carolina" is not supported; and

g. The alleged justification for the “net cost of reinsurance” is based on hearsay and purported proprietary data and information without any underlying support.

11. The “trended modeled hurricane base-class loss cost” in RB-1, pages C-2, C-3, C-4, and elsewhere in the filing does not appear to be an actual value but instead is a calculated hypothetical value that is inappropriate and lacks adequate explanation or justification because, among other reasons:

a. The alleged justification for the “modeled hurricane base-class loss cost” is based on hearsay and purported proprietary data and information without any underlying support; and

b. The filing appears to disregard the actual hurricane loss experience in North Carolina.

12. The filing does not demonstrate that various values—including but not limited to, the loss, expense, exposure, hurricanes, other catastrophes, reinsurance, assessments, and average rating factor information—contained in the filing accurately and reasonably reflect actual historical experience.

13. The filing does not demonstrate that the data, experience, and values used are accurate, reliable, or relevant.

14. The filing has not adequately provided the basis for the changes to the methodology used by the Bureau and the impact those changes have on the calculations and results.

B. Due consideration has not been given to prospective loss and expense experience within this State because, among other reasons:

1. Trending procedures are not adequately documented, explained, or justified. Examples include the use of the all items CPI, the all items less energy CPI, compensation cost index, and the respective weights applied to these indices.

Moreover:

a. The historical loss trend selections of 5.5%, -1.0%, and 4.5% and prospective loss trend selections of 6.5%, 4.0%, and 4.5% for Owners, Tenant, and Condominium forms, respectively, were not justified;

b. The data utilized for trend were inappropriate, insufficient, outdated, and incomplete;

c. Only incomplete, limited, and inappropriate five annual data points were provided for the loss trend, whereas quarterly data points should be provided; and

d. Loss data, even when provided, were only through 2021 when more recent data should be available and included in the analysis. Fast Track trend data more recent than the trend data included in the filing are available and should be considered.

2. The filing fails to consider the effects on experience of past and prospective changes in relevant economic and other causal variables in selecting various trends, including but not limited to the trends for losses and expenses. Further, the filing fails to give due consideration to observed trends in loss costs in establishing expense trends.

3. The filing fails to provide the proper derivation of various factors, for example, on RB-1, pages C-2, C-3, and C-4 in the filing.

4. The filing has not supported the exposure trends used and has not considered the impact of insurance company procedures, including but not limited to, insurance-to-value initiatives that would impact the exposure trend.

5. The filing does not adequately justify the projected expense provisions used in the rate level calculation. The external Bureau of Labor Statistics indices utilized to calculate expense trend were not substantiated for their relevance. The 5.0% selected expense trend was not justified or supported.

C. Due consideration has not been given to the hazards of conflagration and catastrophe because, among other reasons:

1. The use of simulated data in the calculation of various values—including but not limited to catastrophe losses, hurricane losses, net cost of reinsurance, compensation for assessment risk, and excess losses—is not adequately explained or justified and may be incorrectly calculated;

2. The use of the AIR Worldwide (hereinafter “AIR”) and Risk Management Solutions (hereinafter “RMS”) computer simulation models in the filing to derive the provisions for hurricane losses, the “net cost of reinsurance,” and the “compensation for assessment risk,” as well as other provisions elsewhere in the filing, is inappropriate and lacks adequate explanation or justification. In addition, the filing fails to include adequate and complete testimonies, data, assumptions, documentation, background information, and analyses underlying the models from AIR and RMS. Instead, the Bureau utilized Aon, a reinsurance broker,

to run the models and to present undocumented and unsupported results and conclusions;

3. The calculation in the filing of the excess loss factor (described as the “excess factor”) on RB-1, page D-32 is inappropriate and lacks adequate explanation or justification;

4. The filing does not demonstrate that various provisions for hazards of conflagration and catastrophe—such as the excess loss factor and the AIR and RMS modeled losses—do not overlap and result in an inflated overall rate provision;

5. The AIR and RMS computer model results are based upon unidentified and, possibly, outdated data and experience;

6. Documentation and justification were not provided showing that the data and experience relied upon in the AIR and RMS computer model results are accurate and reliable;

7. Documentation and justification were not provided showing that the various assumptions, parameters, formulas, and other components underlying the AIR and RMS computer models are reasonable and appropriate for North Carolina;

8. Evaluating the validity of the AIR and RMS models is impeded by the fact that numerous assumptions, parameters, formulas, data, and other components underlying the models have not been disclosed. Support has not been provided that demonstrate that the AIR and RMS models are based upon the best available scientific information for assessing hurricane frequency, severity, damage

and loss, and that the projected losses derived from the models meet all applicable standards;

9. Documentation was not provided regarding how the modeled losses from the AIR and RMS computer models compare to actual catastrophe losses in North Carolina;

10. Documentation was not provided which appropriately supports the changes in the AIR and RMS computer models over time and how those changes impact the numerical value of the modeled losses;

11. Documentation was not provided to adequately explain or justify why two different AIR models and two different RMS models were used in the filing. The AIR standard model and the RMS historical model were used to derive the provision for hurricane losses in RB-1, pages C-2, C-3, and C-4, while AIR WSST model and the RMS Medium-Term Rate model were used in the calculation of the “net cost of reinsurance” provision;

12. Documentation was not provided to adequately quantify, explain, justify, or reconcile the different values resulting from the AIR and RMS models;

13. Documentation was not provided to adequately explain or justify the blending procedure applied to the AIR and RMS models;

14. The inclusion of the Beach Plan and consent to rate data in the calculations is unsupported;

15. Actual conflagration and catastrophe experience and data for North Carolina homeowners’ insurance was not provided or used in the filing;

16. Documentation was not provided to adequately demonstrate that the allocation of the net cost of reinsurance to territory was appropriate;

17. The excess factor, excess loss, and excess procedures used in the filing are not supported or justified;

18. The filing has not provided annual historical exposure and hurricane loss data by territory for 1987 through 2000 and has not shown that this data is not reasonably available; and

19. Despite being requested by the Department in connection with prior filings, the current filing does not contain data required by subdivision (2) of this subsection [N.C.G.S. 58-36-15 (d2)(2)].

D. Due consideration has not been given to (a) a reasonable margin for underwriting profit and to contingencies, (b) dividends, savings, or unabsorbed premium deposits allowed or returned by insurers to their policyholders, members, or subscribers, or to (c) investment income earned or realized by insurers from their unearned premium, loss, and loss expense reserve funds generated from business within the State because, among other reasons:

1. The profit model employed by the Bureau in the calculation of the filed underwriting profit provisions has been previously rejected by the North Carolina Court of Appeals and, therefore, cannot be used to calculate the profit provisions in this filing;

2. The test employed by the Bureau to compare its calculation of projected returns to the alleged cost of capital required by industries of comparable

risks-uses investment income from capital and surplus in violation of numerous court decisions;

3. The profit calculations in the filing are made using GAAP based accounting. However, decisions by the Court of Appeals have held that SAP based accounting is appropriate for ratemaking purposes in North Carolina;

4. The filing appears to inappropriately evaluate various items, including but not limited to the investment rate of return, investment expenses, taxes, investable funds, policyholder supplied funds, insurance company supplied funds, installment and other fees, and target profit;

5. The cost of capital standard employed in the filing as the basis for selecting the statewide provision for underwriting profit is inappropriate because it inherently contains income earned and realized from capital and surplus funds, and thus it violates North Carolina law;

6. The cost of capital, even if it were relevant and could be used in the profit calculation, appears to have been calculated improperly in the filing and is not adequately justified;

7. The filing fails to justify the 9.0% statewide underwriting profit provision. Support and documentation were not provided for the 9.0% value for the underwriting profit provision;

8. The filing fails to justify and demonstrate how the 1.0% contingency provision was determined. The filing uses a completely unsupported and arbitrary value. The contingency provision is effectively an additional profit provision. The

calculations and assumptions used by the Bureau in purported support of the contingency provision were not adequately justified and appear to be inappropriate;

9. The filing does not explain why, in addition to the underwriting profit contingency provisions, additional profit loadings are effectively included elsewhere in the filing, including but not limited to “net cost of reinsurance” and “compensation for assessment risk”;

10. The filing appears to include profit loading from multiple factors within the filing including at least: (i) the explicit underwriting profit provisions, (ii) the contingency provision., (iii) the “net cost of reinsurance” provision, and (iv) the “compensation for assessment risk” provision. The inclusion of these multiple profit factors results in excessive and unfairly discriminatory rates;

11. The filing fails to justify various assumptions made by Dr. Zanjani, including but not limited to the: (i) risk of the insurance business, (ii) appropriate target profit, and (iii) projected revenue for insurance companies;

12. The filing fails to follow the 1999 North Carolina Supreme Court's decision that rejected the Bureau's methodology of adding an explicit additional factor into the rates for policyholder dividends and deviations;

13. The filing fails to treat dividends and deviations as savings and instead negates whatever savings they reflect in that the dividends and deviations are used to justify raising the rate level to offset their impact. The filing provides inadequate documentation and explanation as to how savings have been given due consideration in the filing;

14. The filing does not adequately support the projected magnitude of policyholder dividends and deviations;

15. The filing treats dividends and deviations inappropriately;

16. The filing does not reflect the payment of dividends from surplus as required by N.C.G.S. § 58-8-25; and

17. The Bureau's treatment of policyholder dividends and deviations results in unfairly discriminatory and excessive rates.

E. Due consideration has not been given to past and prospective expenses specifically applicable to this State because, among other reasons:

1. The filing fails to adequately document, explain, or justify (a) the method by which insurance companies determined the amount of expenses to report as being applicable to North Carolina homeowners' insurance or (b) the assumed split of those expenses between the various coverage forms;

2. The filing fails to justify the distribution of the selected relativities for General Expense and Other Acquisition Expense dollars per policy between the various forms; and

3. The filing does not adequately justify the past or projected expense provisions used in the rate level calculation.

F. Due consideration has not been given to all other relevant factors within this State because, among other reasons:

1. The filing inappropriately reflects the data and experience of the Beach Plan and consent to rate;

2. The filing fails to provide adequate justification to support the distribution of the rate changes by territory;

3. The filing fails to provide adequate justification to support the base class rate by territory;

4. The filing fails to adequately document and justify the average policy amount relativity, average rating factor, current amount factors, average exposure per policy, premium trend factors, expense trend factors, exposure trend factors, loss trend factors, and base class loss cost and base class rates used in the rate level calculation;

5. The windstorm or hail exclusion credits and windstorm mitigation credits set forth in the filing are not adequately documented or supported;

6. The filed and indicated rate level changes and rates on pages A-2, A-3 and A-4 are not supported, are based upon unsound actuarial procedures and unsound ratemaking calculations, are contrary to the applicable statutory standards and inconsistent with relevant court decisions, and would result in excessive and unfairly discriminatory rates;

7. It has not been demonstrated that the data and procedures in the filing meets acceptable data and ratemaking standards, including those established by the Actuarial Standards Board;

8. It has not been demonstrated that the data, calculations, and analyses included in the filing reflects acceptable claim practices by insurance companies, including but not limited to the distribution of hurricane damage between wind and water causes of loss;

9. The rates and rating factors to be implemented, including but not limited to rules, rates, credits, factors, or referenced in pages B-2 through B-7, are not supported, are based upon unsound actuarial procedures and unsound ratemaking calculations, are contrary to the applicable statutory standards and inconsistent with relevant court decisions, and would result in excessive and unfairly discriminatory rates;

10. The credibility procedures used in the filing are not supported or justified; and

11. The filing reflects various aspects of the Beach Plan inconsistently, including the consideration given to losses, expenses, reinsurance, catastrophes and other components of the rate calculation.

As a consequence of the deficiencies described herein, the proposed rates appear in their entirety to be excessive and unfairly discriminatory in violation of N.C.G.S. § 58-36-10(1).

VI. The Commissioner reserves the right to examine the impact of: any state and federal legislation that will be implemented during the period when these rates are to be in effect; any court decisions that may relate to the calculations or methodologies in the filing; any data related to the filing supplied by the Bureau after the date of this Notice; and the findings of any audit of a statistical agent regarding the Bureau or any insurer writing homeowners' insurance to the extent that any such audit serves to call into question the integrity of any data contained in the filing.

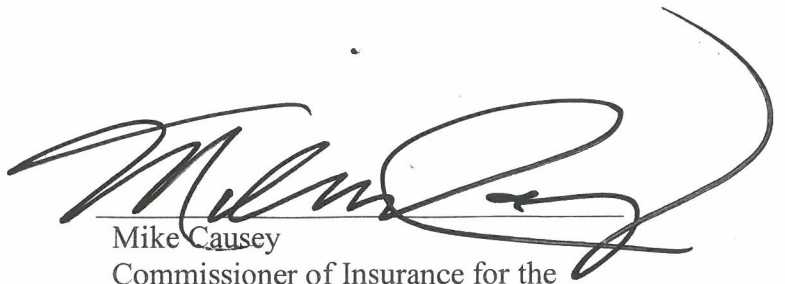
VII. The Commissioner, in accordance with N.C.G.S. Chapter 58, Article 36, directs the staff and consultants of the Bureau and Department to meet for a prehearing conference in the Tenth-Floor conference room at the Department, 3200 Beechleaf Court, Raleigh, North Carolina on September 17, 2024 at 10:00 a.m. The representatives of the Department are directed to obtain

court reporting for the aforementioned prehearing conference and to record all proceedings of the prehearing conference. In accordance with N.C.G.S. Chapter 58, the representatives and consultants of the Bureau and the Department are directed to be prepared at the prehearing conference and to have met prior to the prehearing conference to compile the following information to be presented at that hearing:

- A. List of names of all potential witnesses;
- B. Stipulations as to their qualifications as experts;
- C. Stipulations as to the sequence or appearance of witnesses;
- D. Such information relating to other matters and issues as may arise during the hearing, including but not limited to substantive and evidentiary matters;
- E. The parties for both sides will identify the issues that will be presented at the hearing; and
- F. Both parties will set forth specifically which issues can be eliminated that are included in this notice.

VIII. The Bureau will make newspaper publications of the time and place of this hearing.

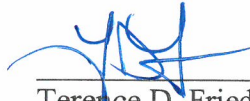
This the  day of February, 2024.


Mike Causey
Commissioner of Insurance for the
State of North Carolina

CERTIFICATE OF SERVICE

I hereby certify that a true and accurate copy of the foregoing **NOTICE OF HEARING** was served on counsel for the North Carolina Rate Bureau, as well as the Bureau itself, by mailing a copy of the same via U.S. Mail, and electronic mail, addressed as follows:

DEPARTMENT OF INSURANCE



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