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SFA



BILL ANALYSIS

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Senate Bill 991 (Substitute S-1 as passed by the Senate)
Sponsor: Senator Alan Sanborn
Committee: Financial Services

Date Completed: 3-28-02

RATIONALE

In the late 1970s and early 1980s, the Legislature passed a series of bills that extensively reformed the statutes governing home and automobile insurance. Some of these reforms constituted what is commonly called the "Essential Insurance Act", and created underwriting and rating standards for all home and auto insurance companies conducting business in Michigan. These standards addressed Michigan citizens' need to find and purchase adequate car and home insurance. Because it has been more than 20 years since the legislation was enacted, Michigan insurance companies that believe some of the provisions should be updated.

CONTENT

The bill would amend the Insurance Code to revise certain eligibility requirements for insurance policies. Specifically, the bill would:

- Render ineligible for home insurance any person who had been denied a claim based on evidence of arson or fraud.**
- Increase the minimum required insured value for a home repair cost policy from \$7,500 to \$20,000, and a replacement policy from \$15,000 to \$35,000.**
- Specify that a dwelling in a physical condition that clearly presented an extreme likelihood of a significant loss would be ineligible for insurance.**
- Include as a criterion for establishing underwriting rules an insured's failure to correct a physical condition that would present a risk of repeated loss.**
- Increase the acceptable required deductible for comprehensive**

automobile insurance from \$150 to \$500.

- Establish as a criterion for underwriting rules in home or auto insurance an insured's or applicant's threats, harassment, or assault on an insurance employee.**
- Require the Michigan Basic Property Insurance Association (the "pool") to offer HO-3 and repair cost premiums and policies equivalent to those provided by a licensed rating organization.**

Currently, the Code renders ineligible for home insurance any person who has successfully been denied, within the last five years, a claim under a home insurance policy in excess of \$2,000 based on evidence of arson, conspiracy to commit arson, misrepresentation, fraud, or conspiracy to commit fraud by or on behalf of the person. The amount of the denied claim must be greater than either 15% of the amount of insurance in force, if the claim is under a repair cost policy; or 10% of the amount of insurance in force if the claim is under a replacement cost policy. The bill would delete the \$2,000 claim requirement, as well as the percentage amounts of the denied claims.

The Code renders ineligible for home insurance a person who seeks to buy a repair cost policy on a dwelling with an insured value of less than \$7,500, or who seeks to buy a replacement policy on a dwelling with an insured value of less than \$15,000. The bill would increase those amounts to \$15,000 and \$35,000 respectively. The Code further renders ineligible a person who insurers or seeks to insure a dwelling that does not meet minimum standards of insurability as

established by the Commissioner of the Office of Financial and Insurance Services. The bill instead would make ineligible for insurance a person who insured or sought to insure a dwelling that had physical conditions that clearly presented an extreme likelihood of a significant loss under a home insurance policy.

Under the Code, the underwriting rules an insurer may establish for home and automobile insurance must be based on specific, listed criteria. The bill would delete from the homeowner's criteria the physical conditions of a house that clearly present an extreme likelihood of a significant loss under the liability coverages of a home insurance policy. This criterion applies only to new policies. In addition, one basis for automobile underwriting rules specifies that, for the purposes of requiring comprehensive deductibles of not more than \$150, or for refusing to insure if the person refuses to accept a required deductible, the claim experience of the person with respect to comprehensive coverage may be taken into account. The bill would increase the acceptable required deductible to \$500.

Under the bill, in both home and automobile insurance underwriting rules, a new basis for an underwriting rule would be established: evidence that the insured or applicant for insurance was involved in one or more incidents involving a threat, harassment, or physical assault on an insurer employee, agent, or agent employee while acting within the scope of his or her employment, as long as a report of the incident was filed with a law enforcement agency.

The Code establishes the Michigan Basic Property Insurance Association, or the pool, which covers property owners who are ineligible for insurance provided by a private insurer. Currently, the premium for basic property insurance of any risk by the pool must be equal to the rate for identical insurance established by the principal rating organization for identical insurance, plus a uniform surcharge approved by the Commissioner. The bill instead would require that the basic rate be equal to the rate for identical insurance established by a *licensed* rating organization.

Under the Code, rates charged in each territory by the pool for home insurance must

be equal to the weighted average of the 10 voluntary market insurer groups with the largest premium volume in the State. Rating territories for home insurance established by the pool must be the same as those used by the largest number of insurers by premium volume writing home insurance in the State. Any change in the rates of those insurers that would produce a change in excess of 5% in the HO-2 pool rates for any territory must be reflected as soon as reasonably practicable in the HO-2 pool rates. The bill would retain these provisions, but specify that any change in the rates for *an HO-2 form replacement cost policy* in excess of 5% would have to be reflected as soon as practicable. (An HO-2 form replacement cost policy is known as a "named peril" policy, which insures holders against specific, named hazards, such as fire, theft, or windfall damage.)

The Code requires that the pool offer certain policies to its insureds. Currently, the pool must offer HO-2 replacement cost policies and repair cost policies equivalent to the same policies filed and in effect in the State for the principal rating organization. The bill instead would require that the HO-2 and repair policies be equivalent to ones filed and in effect for a *licensed* rating organization. In addition, the bill would add to the list of mandatory policies offered by the pool an HO-3 form replacement cost policy equivalent to an HO-3 policy filed and in effect for a licensed rating organization. (An HO-3 policy, known as an "all perils" policy, insures holders against all perils except those specifically exempted.) Under the bill, rates established by the pool for HO-3 policies could not be based on the weighted average methodology used to calculate other rates charged by the pool.

MCL 500.2103 et al.

ARGUMENTS

(Please note: The arguments contained in this analysis originate from sources outside the Senate Fiscal Agency. The Senate Fiscal Agency neither supports nor opposes legislation.)

Supporting Argument

The home and auto insurance market has changed in the past couple decades, and it is time to update the law's essential insurance provisions. The bill would reflect current market conditions by increasing the minimum

required insured value for coverage of a home, increasing the acceptable required deductible for comprehensive auto insurance, and making a person ineligible for home insurance if a previous claim had been denied due to arson or fraud, regardless of the dollar amount or percentage level of the denied claim. In addition, the bill would enable insurance companies to control their losses by allowing insurers to refuse to cover or renew those insureds who do not maintain their property at an acceptable level. Reducing losses should, of course, lower the premiums for insureds. Further, the bill would permit insurers to refuse insurance to anyone who threatened or physically assaulted an insurance agent or employee. This would provide a reasonable measure of protection for agents, who have been victims of harassment and threats in the past.

Opposing Argument

Under the bill, homeowners whose dwellings did not meet the proposed minimum coverage amounts could become ineligible for coverage in the regular insurance market, and be forced to seek coverage in the Michigan basic pool. Since the pool's rates might be slightly higher than the regular market policy rates, this amendment could force those who can least afford it to pay more for insurance.

Response: The bill would require the pool to offer an additional, higher level of homeowners' coverage in the form of an HO-3, all-perils policy. This could help compensate those who were forced into the pool by offering them an option for more comprehensive coverage.

Opposing Argument

It appears that the bill would remove the current ability of the Commissioner to promulgate rules setting minimum standards of insurability for a dwelling. Under the proposed language, a dwelling would be ineligible for coverage if it had a physical condition that clearly presented an extreme likelihood of a significant loss under a home insurance policy, language that currently is found in the underwriting rules section of the Code. The proposed revision would allow insurers to use the significant loss language to refuse to renew an existing policy, instead of using it only as a condition for refusing to issue a new insurance policy. This change could result in more homeowners' losing their regular market coverage and being forced into

the Michigan basic pool. At least, "physical conditions that clearly present an extreme likelihood of significant loss" should be defined as they have been in the past, with sample underwriting rules.

Response: The Commissioner still could use his or her general rule-making authority to clarify this provision, if necessary.

Legislative Analyst: Claire Layman

FISCAL IMPACT

The bill would have no fiscal impact on State or local government.

Fiscal Analyst: Elizabeth Pratt

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This analysis was prepared by nonpartisan Senate staff for use by the Senate in its deliberations and does not constitute an official statement of legislative intent.