

DEPARTMENT OF INSURANCE

Legal Division, Rate Enforcement Bureau
45 Fremont Street, 21st Floor
San Francisco, CA 94105



INVITATION TO PRENOTICE PUBLIC DISCUSSIONS REGARDING LENDER PLACED INSURANCE AND AMENDMENTS TO COMMODITY AND SPECIALTY INSURANCE CLASSIFICATIONS

REG-2012-00013**Notice Date: September 28, 2012**

BACKGROUND INFORMATION

As set forth in this Notice, the California Department of Insurance ("Department") has scheduled a workshop to consider possible changes to lender placed insurance and commodity and specialty classifications for **Thursday, October 25, 2012** at 10:30 a.m.

Lender placed or force placed insurance is insurance that a lender places on real or personal property to protect its interest in that property. For example, when a bank lends an individual money to buy a home or a car it retains a security interest in that home or car and requires the individual to maintain homeowners or automobile insurance. If the individual fails to maintain the required insurance, the lender will then place insurance on the home or car to protect its security interest.

Lender placed homeowners insurance has been the focus of recent attention due to allegations that lenders are charging homeowners high premiums when the homeowners could purchase the same insurance for much less. The Department is seeking input on whether lender placed insurance should be considered specialty or commodity insurance for rate regulation purposes.

California Code of Regulations (CCR), title 10, section 2642.7 provides that certain identified lines may be disaggregated for ratemaking purposes into subcategories for "commodity" and "specialty" insurance. It also provides that specialty insurance shall be reviewed using the "most sound actuarial method." Commodity insurance is reviewed using the standard regulatory formula.

Specialty insurance generally involves a large premium and/or a special, unique or unusual risk. Examples of specialty insurance include nuclear risks, kidnap and ransom, political risks, or product tampering. CCR section 2642.7 lists the lines, sublines and risks that shall be considered specialty insurance by name, such as those set forth above. It also provides that specialty insurance shall include "any single policy having an annual premium over \$75,000." Conversely, commodity insurance insures standard or common risks that do not require special underwriting and rating. Examples of commodity insurance include homeowners and automobile insurance.

Lenders typically purchase lender placed insurance via a master policy. The lender subsequently adds individual homes and cars to the master policy and charges the cost of insurance for each home or car to the individual owner. While the total premium paid by the lender for all property added to the master policy may be over the current regulatory threshold of \$75,000, the premium

charged to the individual property owner is well under \$75,000. Some insurers assert that master policies are single policies with premiums over \$75,000 and should be rated as specialty insurance, even though the premium for any given certificate holder is well below \$75,000.

The Department is considering amending the regulation to require that lender placed insurance should be filed as commodity insurance. The Department is also considering whether to:

- (1) raise the \$75,000 premium threshold to \$1,000,000;
- (2) raise the \$100,000 deductible threshold to \$500,000;
- (3) clarify that group policies and master policies are not considered "single" policies for the purpose of qualifying as specialty insurance;
- (4) clarify that excess and/or umbrella policies written over personal lines do not qualify as specialty insurance;
- (5) clarify that an underlying policy must cover a commercial exposure before the excess/umbrella policy can be considered specialty insurance;
- (6) raise the \$500,000 underlying limit threshold to \$1,000,000 for excess/umbrella policies to qualify as specialty insurance;
- (7) clarify that while certain lines, sublines and risks qualify as specialty insurance under subsection (d) they may also be filed as commodity insurance; and
- (8) expressly provide that lender placed insurance does not qualify as specialty insurance.

Attached is a copy of the changes proposed for discussion at these prenotice public discussions. Proposed additions to the existing regulations are indicated in underline; proposed deletions are indicated in ~~strikeout~~.

INVITATION TO PRENOTICE PUBLIC DISCUSSIONS

The Department hereby invites all interested persons to attend the prenotice public discussions and to provide input regarding the Department's proposed amendments to CCR section 2642.7. These discussions will satisfy the prenotice public discussions requirements of California Government Code (CGC) 11346.45. The purpose of these discussions is to receive input and comments from interested persons.

In these discussions, the Department will seek input and comments regarding the following issues and other issues, concerns or suggestions from interested parties regarding CCR section 2642.7:

- Should the Department treat lender placed insurance as "specialty" or "commodity" insurance?
- Should the Department review lender placed insurance under the standard regulatory rate making formula?
- Should the Department raise the threshold limits set forth above? If so, by how much?
- Will the proposed amendments affect the creation or elimination of jobs within the State of California? If so, how?

- Will the proposed amendments affect the creation of new businesses or the elimination of existing businesses within the State of California? If so, how?
- Will the proposed amendments affect the expansion of businesses currently doing business within the State of California? If so, how?
- The benefits of the proposed amendments to the health and welfare of California residents, worker safety, and the state's environment.

The content of these prenotice public discussions is limited to the potential changes and topics set forth above.

WRITTEN COMMENTS

The Department invites written comments regarding the issues identified above in advance of the workshop. Written comments should be submitted by e-mail to REBRegComments@insurance.ca.gov **before the close of business on Monday, October 22, 2012**. The Department will also accept oral comments at the workshop.

TIME AND PLACE OF WORKSHOP

October 25, 2012, 10:30 a.m.
California Department of Insurance
45 Fremont Street, 22nd Floor Hearing Room
San Francisco, CA 94105

RSVP REQUESTED / CDI CONTACT PERSON

If you plan to attend this workshop please RSVP by sending your name, the name of the organization (if any) which you represent, your mailing address, telephone number, and email address to REBRegComments@insurance.ca.gov no later than October 22, 2012.

Because of building security procedures, gaining access to the workshop may be more difficult for people who have not given their information to the CDI contact person listed below.

Please direct any questions regarding this notice to:

Jennifer McCune
California Department of Insurance
Rate Enforcement Bureau
45 Fremont Street, 21st Floor
San Francisco, CA 94105
(415) 538-4148
jennifer.mccune@insurance.ca.gov

ADVOCACY OR WITNESS FEES

Persons or groups representing the interests of consumers and who are otherwise in compliance with California Code of Regulations (CCR) Title 10, section 2661.4, may be entitled to reasonable advocacy fees, witness fees, and other reasonable expenses, in accordance with the provisions of CCR Title 10, Chapter 5, Subchapter 4.9, Article 13, in connection with their participation in this matter. Persons interested in inquiring about the appropriate procedures should contact the Office of the Public Advisor at the following address:

Edward Wu
Attorney/Public Advisor
California Department of Insurance
Office of the Public Advisor
300 South Spring Street, South Tower, 12th Floor
Los Angeles, CA 90013
(213) 346 – 6635
edward.wu@insurance.ca.gov

PRENOTICE PUBLIC DISCUSSIONS FACILITY

The facility to be used for these prenotice public discussions is accessible to persons with mobility impairments. Persons with sight or hearing impairments are requested to notify the CDI Contact Person listed above, before the close of business on October 22, 2012 in order to make special arrangements.

ADDITIONAL INFORMATION

Please be advised that participation in these prenotice public discussions will be in addition to, and not in substitution for, any participation in the formal rulemaking process. This Invitation to Prenotice Public Discussions does not constitute a Notice of Proposed Action under the Administrative Procedure Act. Consequently, comments (oral or written) received in connection with these prenotice public discussions will not be included in the rulemaking file, which will not be opened until the time formal notice is issued. Similarly, the Department is not required to respond to comments received before the Notice of Proposed Action has been issued and the rulemaking file opened. For this reason, if you wish to have comments included in the rulemaking file, or to require the Department to respond to them as part of the process by which it adopts this regulation, you must present your comments during the formal public comment period according to the procedures outlined in the Notice of Proposed Action at the time that document is issued, regardless of whether the comments have been made in connection with this workshop. The Commissioner nonetheless welcomes your participation in these discussions, and hopes that the amended regulation that may subsequently be proposed will benefit from your input.

STATE OF CALIFORNIA
DEPARTMENT OF INSURANCE
45 Fremont Street, 21st Floor
San Francisco, California 94105

REG-2012-00013

September 28, 2012

PROPOSED REGULATION TEXT¹

§ 2642.7. ~~Lines of Insurance.~~ Filing Categories.

(a) Wherever in this subchapter insurance is required to be classified by line, the classification shall be into one of the following categories:

- (1) Fire
- (2) Allied Lines
- (3) Farmowners multiple peril
- (4) Homeowners multiple peril
- (5) Commercial multiple peril liability
- (6) Commercial multiple peril non-liability
- (7) Inland marine
- (8) Medical malpractice
- (9) Earthquake
- (10) Other liability
- (11) Products liability
- (12) Private passenger automobile liability
- (13) Private passenger automobile physical damage
- (14) Commercial automobile liability
- (15) Commercial automobile physical damage
- (16) Aircraft
- (17) Fidelity
- (18) Surety
- (19) Burglary and theft
- (20) Boiler and machinery.

¹ Proposed additions to existing regulation text are in underline; proposed deletions to existing regulation text are in ~~strikethrough~~.

(b) For purposes of this subchapter, mechanical breakdown and similar insurance covering loss caused by the failure or malfunction of a component or system of a motor vehicle, as described in California Insurance Code Section 116(c), shall be classified as other liability occurrence.

(c) Any insurer or the Commissioner may disaggregate any of the foregoing lines, except homeowners multiple peril, private passenger automobile liability, and private passenger automobile physical damage, into two subcategories, "commodity" and "specialty." Rates for specialty insurance shall be approved or disapproved using the most sound actuarial method, consistent with California law, in accordance with the Actuarial Standards of Practice, and relevant and accepted actuarial principles, guidelines, and literature.

(d) ~~Specialty insurance shall include:~~ Only the following lines, sublines and risks may be filed as specialty insurance:

(1) Any single policy having an annual premium over ~~\$75,000-1,000,000~~. For the purposes of this subsection, a single policy does not include a group policy or a master policy.

(2) Any single policy having a deductible or self-insured retention of ~~\$100,000-500,000~~ or more;

(3) Any excess property, excess liability, or umbrella policy, where none of the underlying policies include private passenger automobile liability, private passenger automobile physical damage, or homeowners coverage, ~~or and~~ where the underlying policy is written by an unaffiliated insurer and covers at least the first \$500,000 \$1,000,000 in losses;

(4) All policies for

(A) nuclear risks,

(B) pollution legal liability,

(C) product-tampering, product impairment, or product recall,

(D) kidnap and ransom,

(E) political risks,

(F) directors' and officers' liability,

(G) boiler and machinery insurance,

(H) fidelity insurance,

(I) mortgage guaranty insurance,

(J) employer liability under the United States Longshoremen's and Harbor Workers' Compensation Act (33 U.S.C. section 901 et seq.), the Jones Act (46 U.S.C. section 688), the Federal Employer Liability Act (45 U.S.C. section 51 et. seq.), or any similar statute,

(K) excess employer's liability over workers' compensation insurance,

(L) differences in conditions coverage,

(M) surety,

(N) credit, and

(O) aviation.

(e) Specialty insurance shall not include lender-placed insurance. Lender-placed insurance is insurance placed by a lending institution or servicer on a borrower's property, whether real or personal, when the borrower does not maintain coverage on the property as required by contract.

(e)(f) Commodity insurance shall include all policies in the line that are not defined in this section as specialty. All lines, sublines and risks not filed as specialty insurance shall be filed as commodity insurance.