

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

INITIAL STATEMENT OF REASONS

Date: April 2, 2010

REG-2010-00001

**STANDARDS AND TRAINING FOR ESTIMATING REPLACEMENT
VALUE ON HOMEOWNERS' INSURANCE**

INTRODUCTION

California Insurance Code Section 1749.85 provides that the California Insurance Commissioner ("Commissioner") shall instruct fire and casualty broker-agents, personal lines broker-agents and applicants for these licenses in proper methods of estimating the replacement value of structures. Further Section 1759.85 requires that if the Department of Insurance ("Department") adopts regulations establishing standards for the calculation of estimates of replacement value of a structure by appraisers, then an appraiser's estimate of the replacement value shall be calculated in accordance with the regulation.

While the underlying labor, building supply costs, and other components considered in estimating replacement value may or may not be accurate, the Department is aware that certain components of replacement value may not have been considered at all, or have not been considered fully, in determining replacement value estimates. These include costs to replace the foundation of the structure; debris removal and demolition expenses, overhead and profit, engineering reports and architects plans. Additionally, full consideration of the type of frame, roof, siding, slope, size, square footage, location, stories, wall heights, materials, and age would provide a more accurate estimated replacement value.

The proposed regulation will: (1) set out requirements applicable to replacement value and replacement cost estimates to create a more consistent, comprehensive and accurate replacement cost calculation; (2) set forth training standards for California resident broker-agents, which shall be part of and not in addition to their continuing education requirements, who sell homeowner's insurance; (3) set forth standards for real estate appraisers who estimate replacement cost for insurance purposes; (4) require the application of certain standards when estimating replacement cost and construction costs; and (5) establish record keeping requirements.

The Commissioner believes that the proposed regulation is necessary to implement, interpret, and make specific Section 1749.85.

The Commissioner proposes the following changes to Chapter 5 of Title 10 of the California Code of Regulations: (1) the addition of new Section 2188.65 to Article 6.5 of Subchapter 1; (2) the amendment of Section 2190.2 of Article 7 of Subchapter 1; (3) the amendment of Section

2190.3 of Article 7 of Subchapter 1; and (4) the addition of new Article 1.3: Valuation of Homes to Subchapter 7.5.

SPECIFIC PURPOSE AND REASONABLE NECESSITY OF REGULATION

The Department and the California Legislature received a significant number of complaints by homeowners who lost their residences in the Southern California wildfires of 2003. Insurance Code section 1749.85 was the Legislature's response. Since 2003, California has experienced significant wildfires in 2007 and 2008 leading to the loss of a high number of residential structures. After each of these fires, fire survivors complained about problems including their experience that after the fire they learned that the replacement value estimates made in setting coverage limits for their homes was too low, causing underinsurance issues to arise during efforts to rebuild or replace their residences.

The significance of the replacement value being accurate is particularly important given that other than a limited number of homeowners who qualify for guaranteed replacement coverage offered by only a small number of insurers, the vast majority of homeowners have one of three kinds¹ of insurance coverage on their home as defined in the California Residential Property Insurance Disclosure Form from Insurance Code Section 10102:

Limited Replacement Cost Coverage With an Additional Percentage which pays replacement costs up to a specified amount above the policy limit;

Limited Replacement Cost Coverage With No Additional Percentage which pays replacement costs up to policy limit only;

Actual Cash Value Coverage which pays the fair market value of the dwelling at the time of the loss, or the cost to repair, rebuild, or replace the damaged or destroyed dwelling with like kind and quality construction up to the policy limit.

Therefore, the necessity of having an accurate estimated replacement value that is updated regularly is paramount. The failure to take into consideration certain factors at all, or to not fully consider other components, as referenced above, is one source of the underinsurance problem.

SECTION 2188.65: BROKER-AGENT TRAINING ON ESTIMATING REPLACEMENT VALUE

2188.65 (a)

This section provides specific definitions applicable to the regulation and to Insurance Code Section 1749.85. Although many of the words and terms defined have a generally understood meaning in the insurance industry, definitions of those words and terms are included to avoid

¹ In conjunction with the coverage options referenced, homeowners may request Building Code Upgrade-Ordinance and Law Coverage which pays up to limits specified in the policy and additional costs required to bring the dwelling up to code.

any ambiguity or uncertainty in the application of the regulation. For example, under paragraph (a)(3) the term “fire and casualty broker-agent” includes a “fire and casualty licensee” as defined in Insurance Code section 1625 and a “personal lines broker-agent” includes a “personal lines licensee” as defined in section 1625.5. However, certain of the definitions are used to encompass concepts that may not be readily apparent from the word or term used. These definitions are discussed below.

(1) “Homeowners’ insurance policy” is given the same meaning as a “policy of residential property insurance” as defined in subdivision (a) of Insurance Code section 10104, except that a policy covering an individually owned mobile home shall constitute a homeowner’s insurance policy. The Insurance Code does not define “homeowner’s insurance” though it is used in Insurance Code section 1749.85. This clarifies that this term means a policy insuring individually owned residential structures of not more than four dwelling units, individually owned condominium units, and individually owned mobile homes. It limits the application to the purpose of the statute and the regulation to address replacement cost of residential structures. This definition provides that use of the term does not include a tenant’s policy for personal contents or a policy for real property or its contents used for commercial, industrial or business purpose, except a structure of not more than four dwelling units rented for individual residential purposes.

(2) “Replacement value” and “replacement cost” are given the same meaning: the amount it would cost to repair, rebuild or replace a completely damaged or destroyed structure, without a deduction for physical depreciation. Insurance Code section 1749.85 uses the term “replacement value” while Insurance Code section 2051.5 (a) uses the term “replacement cost.” One of the purposes of section 1749.85 is to provide licensees with training on how to estimate the amount that it would cost the insured to repair, rebuild, or replace without a deduction for physical depreciation. While this concept is described as Replacement Value in section 1749.85, the same concept is described as Replacement Cost in section 2051.5 (a). The definition in this regulation prevents any misunderstanding, ambiguity or uncertainty as to what is meant when either term is used. Further, Section 10102, which includes disclosure requirements for residential property insurance, defines different policies as: Guaranteed Replacement Cost Coverage With Full Building Code Upgrade; Guaranteed Replacement Cost Coverage With Limited or No Building Code Upgrade; Limited Replacement Cost coverage with an Additional Percentage, and Limited Replacement Cost coverage with no additional percentage. These are definitions of policies; they are not defining “replacement cost” or “replacement value” as those terms are to be used in section 1749.85 or this regulation. By so defining the terminology, the Department seeks to avoid any confusion with how the terms might be used in other contexts.

2188.65 (b)

Provides that after the day that is ninety days after every California resident fire and casualty broker-agent and personal lines broker-agent must satisfactorily complete one three-hour training course on homeowners’ insurance valuation prior to soliciting individual consumers in order to sell dwelling fire or homeowners’ insurance. Insurance Code sections 1749 through 1749.9 give the Department of Insurance and the commissioner the authority to establish, oversee and implement pre-licensing education and continuing education standards for licensees. Section

1749.1 (a) requires that the commissioner appoint a curriculum board to develop the prelicensing and continuing education curriculum. Section 1749.85 provides that the curriculum committee shall, in 2006, make recommendations to the commissioner broker-agents and broker-agent applicants in proper methods of estimating the replacement value of structures, and of explaining various levels of coverage under a homeowners' insurance policy. Section 1749.7 provides that the commissioner may adopt reasonable regulations necessary for the convenient administration of the article. With this regulation, the commissioner is establishing the curriculum and the extent of training required so that licensees and applicants will be equipped to estimate the replacement value of structures. Additionally, by providing a ninety-day time period in which to satisfy the requirement, the regulation does not impair of ability of broker-agents to earn a livelihood. At the same time, the need for broker-agents to receive the knowledge to be imparted by the training is pressing enough so that requiring the them to take the class within 90 days after the effective date of the regulations is fair and reasonable.

The three-hour course was determined by the curriculum board's Senate Bill (SB) 2 subcommittee which met on several occasions to establish the topics to be included in the homeowners' insurance valuation training. During these meetings the SB 2 subcommittee reviewed the topics and identified the amount of time necessary to provide adequate instruction for each topic listed in Section 2188.65 (d) and (e). As stated on the Homeowners' Insurance Valuation Outline, which is available on the Department's Web site, the specific amount for each topic equals the three hours for this course.

2188.65 (c)

Provides that the training required under this regulation shall be first approved by the commissioner and shall consist of topics related to homeowners' insurance. This section establishes that any course taken to satisfy the requirements stated in Section 1749.85 of the Insurance Code shall comply with section 2188.65(d). This is necessary to assure that agent-brokers who estimate replacement value receive training on those elements of replacement value estimation as stated in the regulation.

2188.65 (d)

Provides the scope of training for broker-agents. It includes training the broker-agent on the differences between homeowners' insurance coverage and other Fire and Dwelling policies. This training is necessary because Fire Dwelling policies typically covered fewer perils than a homeowners' insurance policy, which is an all-risk policy. Also, the Fire Dwelling coverage is usually on an Actual Cash Value basis, not a replacement cost basis. Further, beyond the issue of coverage on the structure, the homeowners policy is a package policy with multiple coverages included, most notably liability coverage, while a fire policy is generally limited to losses directly or related to the structure.

The section requires that training be provided on basic concepts and estimating replacement value:

(1) The broker agents will be trained on how the loss settlement provisions apply to major claims and the cause and effect that underinsurance may have on settlement. This is necessary so that

agent-brokers will understand the consequences of inadequate coverage on an insured's ability to repair, replace or rebuild.

(2) The broker agents will be trained on the differences in indemnity between Actual Cash Value, Replacement Cost coverage, as summarized in California Insurance Code sections 2051, 2051.5, and 10102 including:

(A) California Residential Property Insurance Disclosure, as described in California Insurance Code section 10102; The broker-agents, shall be trained on California Residential Property Insurance Disclosure as stated in California Insurance Code section 10102. This is necessary so that broker-agents can fully explain the different available policies and levels of coverage to the insureds and applicants. The disclosure is provided to every residential policyholder at issuance and every other year thereafter. The Disclosure briefly identifies some of the most significant concerns an insured should have regarding her coverage. At several points in the Disclosure the insured is instructed to contact the producer or insurer to deal with specific concerns.

(B) Depreciation and how it is applied under a homeowners' insurance policy. The broker-agents shall be given training on how depreciation is applied under a homeowners' insurance policy. This is necessary so that broker-agents will have the information to communicate the concept to the insureds and applicants. Additionally, the training will provide information to broker-agents for their use in understanding how the limits of coverage may impact the insured when depreciation is taken into consideration.

(3) There will be training on components of a structure which are necessary to estimate replacement cost, including but not limited to:

(A) Type of foundation

When estimating replacement cost, it is necessary for broker-agents to consider the type of foundation because the cost to repair, replace or rebuild a structure is dependent upon an accurate description of the type of foundation.

(B) Type of frame

When estimating replacement cost, it is necessary for broker-agents to consider the type of frame because the cost to repair, replace or rebuild the structure is dependent upon an accurate description of the type of framing.

(C) Roofing materials and type of roof

When estimating replacement cost, it is necessary for broker-agents consider the roofing materials and type of roof because the cost to repair, replace or rebuild a structure is dependent upon an accurate description of the type of roof.

(D) Siding materials and type of siding

When estimating replacement cost, it is necessary for broker-agents to consider the type of siding materials and type of siding because the cost to repair, replace or rebuild the structure is dependent upon an accurate description of the type of siding materials and siding.

(E) Whether the structure is located on a slope

When estimating replacement cost, it is necessary for broker-agents to consider whether the structure is located on a slope because the cost to repair, replace or rebuild a structure on a slope is a function of the whether the structure is located on a slope.

(F) Size of the entire structure and, separately, the square footage of the living

space.

When estimating replacement cost, it is necessary for broker-agents to determine accurately the size of the entire structure and separately the square footage of the living space because the cost to repair, replace or rebuild a structure is dependent upon the size of structure and square footage of living space.

(G) Geographic location of property;

Building supplies and construction labor have different costs based upon the location (or Zip code).

(H) Number of stories and any nonstandard interior wall heights;

When estimating replacement cost, it is necessary that broker-agents consider the number of stories and nonstandard interior wall heights because the cost to repair, replace or rebuild to a certain number of stories, and or to replace nonstandard wall heights, is dependent on an accurate description of these components.

(I) Materials used in, and types of, interior features and finishes

When estimating replacement cost, it is necessary that broker-agents consider the materials used and the types of interior features and finishes, because the cost to repair, replace or rebuild the structure is a function of the materials used to construct the dwelling and the types of interior features and finishes.

(J) Cost of demolition and debris removal

When estimating replacement cost, it is necessary that broker-agents consider the cost of demolition and debris removal because in the event of a total loss the costs to repair, replace or rebuild the structure will necessarily include costs associated with demolition and debris removal.

(K) Architect's plans, engineering reports, and permits

When estimating replacement cost, it is necessary that broker-agents consider that the cost to repair, replace or rebuild the structure will include costs associated with architect's plans, engineering reports and or permits.

(L) Age of the structure or the year it was built

When estimating replacement cost, it is necessary that broker-agents consider the age of the structure and the year it was built. This may have an impact on the cost to repair, replace or rebuild the structure including but not limited to factors such as code upgrade requirements and availability of materials.

(M) Additional costs associated with building a single or custom home

When estimating replacement cost, it is necessary that broker-agents consider that there may be additional costs to repair, replace or rebuild a single or custom home that might not be incurred in repairing, replacing or rebuilding a tract home. The key to this provision is to prohibit the use of a tract home cost, which has economies of scale of labor and supply associated with it. Also, the third party a replacement cost calculator which real estate appraisers use, currently uses a "tract home" basis, which lowers the replacement cost. Also, if the goal is to provide as sufficient coverage, after a loss, to rebuild a single home, the RC value should not be based upon a lower tract home basis.

(4) The broker-agents will be trained to consider the effects of catastrophes on replacement cost. After a catastrophe the Department has seen "demand surges" and the costs of construction, including labor, fuel, transportation and permit restrictions increase. Training is necessary so broker-agents will have the information necessary to factor in these potential increased costs and

in turn, understand how the levels of coverage including the availability of an additional percentage above replacement cost may be required to provide coverage for demand surge costs.

(5) The broker-agents will be trained on the different homeowner insurance coverage and policies including enhancements and endorsements. It is necessary that broker-agents be well versed in this area so that they can communicate options to insureds and applicants. The purpose is that broker-agents, and in turn, insureds and applicants, will have an understanding of how these insurance coverage and policy options are available to help protect against underinsurance. The review is to include:

(A) what is included and excluded in Building Code Upgrade (Ordinance and Law) Coverage, as defined in California Insurance Code section 10102

In certain circumstances the cost to repair, rebuild or replace will be impacted by costs associated building code requirement. This occurs when building codes may have changed between the time the structure was first constructed and the time after a loss when the structure is to be repaired, rebuilt or replaced. It is necessary that broker-agents understand the availability of this coverage, what is covered under the upgrade and what is not, so that the information can be made known to insureds and applicants.

(B) the various types and levels of replacement cost, as defined in California Insurance Code section 10102

It is important that broker-agents be well versed in the different levels of replacement cost policies as defined in section 10102. This decision regarding which policy level to purchase is often the most important one an insured or applicant will make in determining how best to insure the structure. The replacement cost levels are significantly different from one another, and some may be available to a particular insured or applicant and some might not be, depending on a number of factors including whether a specific carrier offers the coverage and whether the property to be insured so qualifies. The levels of coverage for replacement cost policies are: Guaranteed Replacement Cost Coverage with Full Building Code Upgrade; Guaranteed Replacement Cost Coverage with Limited or No Building Code Upgrade pays replacement costs without regard to policy limits but limits or excludes costs resulting from code changes; Limited Replacement Cost Coverage With an Additional Percentage which pays replacement costs up to a specified amount above the policy limit; and Limited Replacement Cost Coverage With No Additional Percentage which pays replacement costs up to policy limit only. The training will enable the broker-agents to communicate effectively to insureds and applicants the features of each policy level and the kind of protection afforded. This will assist insureds and applicants in making an informed choice.

(6) Broker-agents will receive training on the California Standard Form Fire Policy and FAIR Plan coverages, as described in California Insurance Code sections 2071 and 10090, respectively.

The Standard Form Fire Policy is required in California. It includes information on the insurer, the structures to be insured, the policy effective dates, the coverage, and sections regarding concealment and fraud, uninsurable and excepted property, perils not included, other insurance, conditions suspending or restricting insurance, other perils or subjects, added provisions, waiver provisions, cancellation of policy, mortgagee interests and obligations, pro rata liability, requirements in case loss occurs, appraisal, adjusters, company's options, abandonment, when loss payable, suit and subrogation. As broker-agents are selling this product, training is required

so that they will have a full understanding of the policy and how it functions.

Pursuant to Section 10090, The FAIR Plan (Fair Access to Insurance Requirements) was established to “provide for the equitable distribution among admitted insurers of the responsibility for insuring qualified property for which basic property insurance cannot be obtained through the normal insurance market.” The FAIR Plan offers a standard fire insurance policy and no coverage is provided for liability or coverage for other perils such as burglary. Further, no levels of replacement cost coverage as defined in section 10102 are available other than Limited Replacement Cost Coverage with No Additional Percentage which pays replacement costs up to policy limit only. Additionally, the FAIR plan does not provide an estimated replacement cost to its insureds or applicants. Training is necessary so that broker-agents selling FAIR plan policies will understand that the FAIR plan issues insurance as a last resort to homeowner and will have information on the extent of the coverage and limitations. In this regard, broker-agents will be equipped to communicate this information to insureds and applicants when necessary.

(7) Training will be provided to review of the types of basic building construction, including tilt-up, cinderblock, wood frame, brick and masonry, and metal frame. In order for broker-agents to estimate replacement costs, as referenced in this section at (3), it is necessary that they take into consideration components of a structure. In this regard, it is necessary that broker-agents have an understanding of very basic types of building construction. This will enable them to recognize the components, to ask the insureds and applicants the correct questions to ascertain the information necessary to factor into an estimated replacement cost. Replacement cost estimates require an understanding of Tilt up, cinderblock, conventional frame, brick and masonry and metal frames as the cost will differ depending upon the type of basic building construction.

(8) There will be training to review of the various methodologies of estimating replacement cost including:

- (A) Proprietary replacement cost valuation tools;
- (B) Real estate appraisals;
- (C) Insurance company’s valuation software;
- (D) Contractor’s and architect’s estimates or opinions;
- (E) Cost per square footage estimates; and
- (F) Insured’s opinion.

There are various methods used to estimate replacement cost. It is important for broker-agents who are estimating replacement cost to understand that there are several different methods that can be utilized to estimate replacement cost. This is so that they are aware that there is more than one method that is and can be used.

(9) Review of fire mitigation and how it affects insurance costs, to include:

- (A) Define, recognize, and describe the fire problem in the wild land urban interface;
- (B) Discuss the areas that affect the risk and hazard such as topography, fuels type and locations, weather, and construction; and

(C) Discuss current state regulations that address efforts to mitigate and indicate that local codes may also apply. These include importance of defensible space and fire-resistant building construction.

It is necessary that broker-agents transacting in homeowners' insurance have a working knowledge of the fire risks posed when urban areas are built up against wild lands. In this regard, training will be provided so that broker agents will recognize the risk when transacting in the sale of homeowners' insurance. The training will include how topography, fuels, locations and constructions can either lessen or increase the risk of fire damage to homes built in these areas. Of great importance, as well, is an understanding of current statutes, regulations and local ordinances and codes which address efforts to militate against the risks including the importance of preventive measures. These include but are not limited to an understanding of zones around buildings requiring brush clearance and firebreaks. The applicable statutes include Public Resources Code Section 4291 and Government Code Section 51175; and the applicable regulations include Section 1299 of Division 1.5, Chapter 7, Subchapter 3, Article 3 of Title 14 of the California Code of Regulations and Section 2696.1 et seq. of Chapter 5, Subchapter 7.6 of Title 7.6 of Title 10 of the California Code of Regulations. The codes and regulations are not cited in the proposed regulation as these citation references would need to be changed in the event these codes and regulations changed. The goal is to assure that the broker-agent has an understanding of the zones and brush clearance firebreaks in place at the time the training is provided. The laws, regulation and ordinance instruction will provide broker-agents with information on the consequences of types of vegetation, trees, fuel breaks, fire hazard zones, building materials and how they might mitigate against fire risks. and the use of defensible space to mitigate these risks.

2188.65 (e) The training shall ensure that the broker-agent is aware of the provisions of sections 2695.182 and 2695.183.

As is fully delineated therein, section 2695.182 states that if a licensee provides an estimate of replacement cost or construction costs, the licensee shall document and maintain certain records. It is necessary that as part of their training, broker-agents be made aware of these record-keeping requirements so that they understand their obligation to be in compliance with the regulation.

As is fully delineated therein, section 2695.183 sets forth the standards to be used when a licensee estimates replacement cost. It is necessary that as part of their training, broker-agents be made aware of these standards so that they understand their obligation to estimate replacement cost in compliance with the regulation

2188.65 (f) Any course or seminar that is disapproved under the provisions of this section shall be presumed invalid for credit towards the continuing education requirement of this section unless it is approved in writing by the commissioner. Insurance Code sections 1749 through 1749.9 give the commissioner the authority to establish continuing education standards for licensees. Section 1749.7 provides that the commissioner may adopt reasonable regulations necessary for the convenient administration of the article. Pursuant to this statutory authority, and based upon the regulation, if the commissioner does not approve in writing a course or seminar, then it presumed invalid.

AMENDMENT OF SECTION 2190.2: REQUIRED RECORDS

This section provides that certain records are to be maintained by every agent or broker or surplus lines broker or special lines' surplus lines broker. The records that must be maintained for at least five years are identified in provisions (a) through (p). It is necessary to amend this section by adding provision (q) to read:

Any documents required to be maintained pursuant to Section 2695.182 except that documents to which the last sentence of Section 2695.182 applies must be maintained for the three-year period specified in that sentence.

This is important as new section 2695.182 states that if a licensee provides an estimate of replacement cost or construction costs, the licensee shall document and maintain certain records, records that are not identified in Section 2190.2 (a) through (p). Because agents, brokers, surplus lines brokers and special lines' surplus lines brokers will have new record keeping requirements pursuant to section 2695.182, these requirements are cross-referenced to the Required Records Section 2190.2. This makes clear that these records are now subject to record keeping requirements, and provides notice to those licensees who will be affected by the new record keeping requirements.

AMENDMENT OF SECTION 2190.3: RECORDS BY FILE

This section provides that certain records are to be maintained by every agent or broker or surplus lines broker or special lines' surplus lines broker. The records that must be maintained are identified in provisions (a) through (e). It is necessary to amend this section by adding provision (f) to read:

An agent or broker who provides an estimate of replacement cost or any estimate of construction costs to an applicant or insured with respect to a policy of homeowner's insurance shall maintain records as mandated by Section 2695.182.

This is necessary as new section 2695.182 states that if a licensee provides an estimate of replacement cost or construction costs, the licensee shall document and maintain certain records, records that are not identified in Section 2190.3 (a) through (e). Because agents, brokers, surplus lines brokers and special lines' surplus lines brokers will have new record keeping requirements pursuant to section 2695.182, it is important that these requirements be cross-referenced to the Records by File Section 2190.3 so as to make clear that these records are now subject to record keeping requirements, and to give notice to those licensees who will be affected by the new record keeping requirements.

ARTICLE 1.3: VALUATION OF HOMES

SECTION 2695.180: DEFINITIONS

This section provides specific definitions applicable to the regulation and to Insurance Code

Section 1749.85. Although many of the words and terms defined have a generally understood meaning in the insurance industry, definitions of those words and terms are included to avoid any ambiguity or uncertainty in the application of the regulation. For example, under subdivision (c) the term “fire and casualty broker-agent” includes a “fire and casualty licensee” as defined in Insurance Code section 1625 and a “personal lines broker-agent includes” a “personal lines licensee” as defined in section 1625.5. However, certain of the definitions are used to encompass concepts that may not be readily apparent from the word or term used. These definitions are discussed below.

(a) “Homeowners’ insurance policy” is given the same meaning as a “policy of residential property insurance” as defined in subdivision (a) of Insurance Code section 10104, except that in this article a policy covering an individually owned mobile home shall constitute a homeowner’s insurance policy.

The Insurance Code does not define “homeowner’s insurance” though it is used in section 1749.85. This clarifies that this term means a policy insuring individually owned residential structures of not more than four dwelling units, individually owned condominium units, and individually owned mobile homes. It limits the application to the purpose of the statute and the regulation to address replacement cost of residential structures. This definition provides that use of the term does not include a tenant’s policy for personal contents or a policy for real property or its contents used for commercial, industrial or business purpose, except a structure of not more than four dwelling units rented for individual residential purposes.

(b) “Replacement value” and “replacement cost” are given the same meaning: the amount it would cost to repair, rebuild or replace a completely damaged or destroyed structure. Insurance Code section 1749.85 uses the term “replacement value” while Insurance Code section 2051.5 (a) uses the term “replacement cost.” One of the purposes of section 1749.85 is to provide licensees with training on how to estimate the amount that it would cost the insured to repair, rebuild, or replace without a deduction for physical depreciation. While this concept is described as Replacement Value in section 1749.85, the same concept is described as Replacement Cost in section 2051.5 (a). The definition in this regulation prevents any misunderstanding, ambiguity or uncertainty as to what is meant when either term is used. Further, Section 10102, which includes disclosure requirements for residential property insurance, defines different policies as: Guaranteed Replacement Cost Coverage With Full Building Code Upgrade; Guaranteed Replacement Cost Coverage With Limited or No Building Code Upgrade; Limited Replacement Cost coverage with an Additional Percentage, and Limited Replacement Cost coverage with no additional percentage. These are definitions of policies; they are not defining “replacement cost” or “replacement value” as those terms are to be used in section 1749.85 or this regulation. By so defining the terminology, the Department seeks to avoid any confusion with how the terms might be used in other contexts.

(d) "Licensee" is defined to mean (1) any person or entity that holds a license or certificate of authority issued by the Department of Insurance; (2) a broker-agent; or any other entity for whom the Insurance Commissioner's consent is required before transacting business in the State of California or with California residents. This regulation is designed to encompass all persons and entities regulated by the Insurance Commissioner. By defining a licensee to include not only broker agents, but also insurance carriers (who hold certificates of authorities) and any other

entity requiring Insurance Commissioner consent before transacting insurance business, there can be no uncertainty as to whom the regulation applies. As broker agents and insurers are each involved in estimating replacement cost, it is essential that the regulation be clear that it applies to both.

2695.181. Standards for Real Estate Appraisers.

Insurance Code 1749.85 provides that if the Department of Insurance adopts a regulation establishing standards for the estimating replacement value of a structure by real estate appraisers, then an appraiser's estimate of replacement cost shall be calculated in accordance with the regulation. With this section the Department is requiring that a real estate appraiser, whether or not a licensee, shall not estimate the replacement cost of a structure for use in connection with a homeowner's insurance policy unless the estimate of replacement cost complies with the provisions of subdivisions (a) through (e) of Section 2695.183. Real estate appraisers typically are used by the lending industry to assure that the property's value supports the loan applied for by purchasers or those refinancing their homes. This regulation does not mandate that real estate appraisers comply with section 2695.183 unless the appraisal is going to be used for insurance purposes. One of the purposes of the regulation is to make more consistent and accurate estimated replacement cost calculations used in establishing homeowner insurance coverage. The regulation is designed to assure that certain factors, features and components are used in calculating estimated replacement cost. It is necessary that real estate appraisers be held to the same requirements and standards should their calculations be used for insurance purposes. This regulation makes this concept clear.

The section states that appropriate licensure by the Department of Insurance is required in order to lawfully explain levels of coverage. If a real estate appraiser does estimate replacement cost for purposes of insurance, he or she may do so, but may not explain how the use of the estimate interacts with levels of coverage unless the appraiser is a licensee of the Department of Insurance. It is necessary to make this clear for the benefit of real estate appraisers, who though licensed by the Office of Real Estate Appraisers may not otherwise know the requirements of licensure by the Department of Insurance.

Section 2695.182. Documentation of Person Making Estimate.

Section 2695.182(a) provides that if an estimate of replacement cost or any estimate of construction costs is provided by a licensee to an applicant or insured, the following records are to be maintained in the applicant's or insured's file. The purpose and necessity of the record keeping requirement is to enable the licensee, the applicant or insured, and the regulator, to have a record of how the replacement cost estimate or construction cost estimate was created. It has been the Department of Insurance experience that after a catastrophic wildfire consumer complaints on underinsurance often are based upon how the estimates were arrived at, what was considered, what was not considered, what was said and by whom. Not uncommonly, there is little if any documentation in the insured's file reflecting the steps taken to arrive at the estimated replacement or construction costs. With this regulation, the Department seeks to assure that adequate records are kept reflecting the course of business events that transpired leading to and supporting the estimate and that there is a clear record that only those permitted to estimate

replacement cost by CIC Section 1749.85 are doing so. Additionally, this record keeping requirement will assist the Department's enforcement efforts, and the resulting accountability will lead to improved compliance.

(1) This record is to identify the status of the person providing the estimate of replacement value. It is to identify if it was an insurer underwriter or actuary or other person identified by the insurer, a broker-agent, a contractor, an architect, a real estate appraiser, or other person or entity permitted to make such an estimate. This will enable one to ascertain the source of the calculation and provide that there is a clear record that only those permitted to estimate replacement cost by CIC Section 1749.85 are doing so.

(2) The name, job title, address, telephone number, and license number, if applicable, of the person providing the estimate of replacement value or construction costs. This is necessary so that the person who communicates the estimate, as opposed to the person who calculated it, in the event they are not the same person, can be identified. This will assure that there is a clear record that only those permitted to estimate replacement cost pursuant to Insurance Code Section 1749.85 are doing so.

(3) The source from which or method by which replacement value was determined, to include any replacement cost calculator, contractor's estimate, architectural report, real estate appraisal, or other source or method. This is necessary so that the method can be identified so as to assure that the standards required to be considered in estimating replacement cost are so considered. This will assure that there is a clear record that only those permitted to estimate replacement cost pursuant to Insurance Code Section 1749.85 are doing so and that they are using source methods that are consistent with the standards so established.

(4) A copy of any reports, inspection reports, contractor's estimates, or other documents used to estimate replacement value. This is necessary so that all of the information being used to estimate replacement cost is maintained to assure that there is a clear record as to how replacement cost was estimated.

Section 2695.182 (b) requires that a licensee shall maintain in the insured's file the records specified in subdivision (a) of this section for the entire term of the insurance policy or the duration of coverage, whichever terminates later in time, and for five years thereafter. Additionally, if the estimate is provided to an applicant and a policy is not issued, a licensee shall maintain in the applicant's file the records specified in subdivision (a) of this section for a period of three years following the time the estimate is generated. The five-year requirement is based on the standard for record retention under Sections 2190.2 and 2190.3 (b) of Article 7 of Subchapter 1 of Chapter 5 of Title 10 of the California Code of Regulations.

This provision is necessary to permit the Department to exercise its regulatory obligation to investigate consumer inquiries and to conduct market conduct examinations that involve issues including underinsurance matters. The Department may seek documents establishing whether the insured provided the correct information to the licensee and, at the same time, be able to review a copy of the replacement cost estimated for the same purpose. As to documentation regarding policies that are not issued, again, the purpose is to assure that there are records maintained which will permit the Department to exercise its regulatory obligation to assure compliance with applicable statutes and regulations. The requirement that documents for issued policies be kept for the longer five-year period is because there is a much greater possibility they might be a source document should a dispute arise in the handling of a partial or total loss. The three-year

document retention requirement for non-issued policies is to permit the Department to ascertain whether the underwriting process was consistent. It provides an opportunity to evaluate if estimates generated for applicants comply with the regulations. The documents would be available to sample during a market conduct exams to verify compliance with the regulations. In general, the record-keeping requirement is to assure that documentation is available so that the Department can meet its statutory obligation to regulate producers and perform market conduct exams to ensure compliance.

Section 2695.183. Standards to Be Used when a Licensee Estimates Replacement Cost.

While the underlying labor, building supply costs, and other components considered in estimating replacement value may or may not be accurate, the Department is aware that certain components of replacement value may not have been considered at all, or have not been considered fully, in determining replacement value estimates. The purpose of this regulation is to assure that when replacement cost is estimated, that certain criteria are followed and that specific components and features are used in making the estimate regarding replacement cost.

Section 2695.183 (a)

This subsection provides that an estimate of replacement cost shall include all expenses that would reasonably be incurred to rebuild the structure(s) in its entirety, including but not limited to:

(1) Cost of labor, building materials and supplies

Failure to account for current labor, building material and supply costs will lead to a low estimated replacement cost. The necessity of accounting for these costs accurately is necessary to achieve a realistic estimated replacement cost.

(2) Overhead and profit

Contractors who repair and rebuild homes destroyed by fire factor in overhead and profit to their estimates. In this regard, any failure by a licensee to account for the overhead and profit in the rebuilding stage when estimating replacement cost will result in an insufficient estimated replacement cost. Accounting for these costs accurately is necessary to achieve a realistic estimated replacement cost.

(3) All components and features of the insured structure, as well as all other costs incident to reconstruction, including, but not limited to:

(A) Type of foundation

When estimating replacement cost, it is necessary for broker-agents to consider the type of foundation because the cost to repair, replace or rebuild a structure is dependent upon an accurate description of the type of foundation. There can be extreme differences between the cost of replacing one kind of foundation as compared to a different type of foundation. In this regard, when estimating replacement cost, it is necessary to consider the foundation component generally, and to account for the type of foundation as well, so as to accurately estimate the cost.

(B) Type of frame

When estimating replacement cost, it is necessary for broker-agents to consider the type of frame because the cost to repair, replace or rebuild the structure is dependent upon an accurate description of the type of framing. There can be extreme differences between the cost of replacing one kind of framing as compared to a different type of framing. In this regard, when

estimating replacement cost, it is necessary to consider the framing component generally, and to account for the type of framing as well, so as to accurately estimate the cost.

(C) Roofing materials and type of roof

When estimating replacement cost, it is necessary for broker-agents consider the roofing materials and type of roof because the cost to repair, replace or rebuild a structure is dependent upon an accurate description of the type of roof. There can be extreme differences between the cost of replacing one kind of roof as compared to a different type of roof. In this regard, when estimating replacement cost, it is necessary to consider the roof component generally, and to account for the type of roof as well, so as to accurately estimate the cost.

(D) Siding materials and type of siding

When estimating replacement cost, it is necessary for broker-agents to consider the type of siding materials and type of siding because the cost to repair, replace or rebuild the structure is dependent upon an accurate description of the type of siding materials and siding. There can be extreme differences between the cost of replacing one kind of siding as compared to a different type of siding, including the siding materials used. In this regard, when estimating replacement cost, it is necessary to consider the type of siding, and the siding materials as well, so as to accurately estimate the cost.

(E) Whether the structure is located on a slope

When estimating replacement cost, it is necessary for broker-agents to consider whether the structure is located on a slope because the cost to repair, replace or rebuild a structure on a slope is a function of the whether the structure is located on a slope. There can be extreme differences between the cost of replacing a structure on a slope as compared to replacing a structure that is not located on a slope. In this regard, it is necessary for this component to be considered when estimating replacement cost.

(F) Size of the entire structure and, separately, the square footage of the living space

When estimating replacement cost, it is necessary for broker-agents to determine accurately the size of the entire structure and separately the square footage of the living space because the cost to repair, replace or rebuild a structure is dependent upon the size of structure and square footage of living space.

(G) Geographic location of property;

Building supplies and construction labor have different costs based upon the location of the property. There can be extreme differences between the cost of replacing a structure in one geographic location as compared to another. In this regard, it is necessary for this component to be considered when estimating replacement cost.

(H) Number of stories and any nonstandard interior wall heights;

When estimating replacement cost, it is necessary that broker-agents consider the number of stories and nonstandard interior wall heights because the cost to repair, replace or rebuild to a certain number of stories, and or to replace nonstandard wall heights, is dependent on an accurate description of these components. There can be extreme differences between the cost of

replacing a structure depending on these components and it is necessary for them to be considered when estimating replacement cost.

(I) Materials used in, and types of, interior features and finishes

When estimating replacement cost, it is necessary that broker-agents consider the materials used and the types of interior features and finishes, because the cost to repair, replace or rebuild the structure is a function of the materials used to construct the dwelling and the types of interior features and finishes. There can be an extreme difference in the cost of replacing a structure with one kind of materials used in construction and the types of interior finishes as compared to a structure which does not make use of those materials and interior features and finishes. In this regard, it is necessary for these components to be considered when estimating replacement cost.

(J) Cost of demolition and debris removal

When estimating replacement cost, it is necessary that broker-agents consider the cost of demolition and debris removal because in the event of a total loss the cost to repair, replace or rebuild the structure will necessarily include costs associated with demolition and debris removal.

(K) Architect's plans, engineering reports, and permits

When estimating replacement cost, it is necessary that broker-agents consider that the cost to repair, replace or rebuild the structure will include costs associated with architect's plans, engineering reports and or permits. These costs can and do occur on partial losses, but do not result in underinsurance (if omitted) on a partial loss, as the coverage limits will be sufficient.

(L) Age of the structure or the year it was built

When estimating replacement cost, it is necessary that broker-agents consider the age of the structure and the year it was built. This may have an impact on the cost to repair, replace or rebuild the structure including but factors such as code upgrade requirements and availability of materials.

Section 2695.183 (b) The estimate of replacement cost shall be based on an estimate of the cost to rebuild or replace the structure taking into account the cost to reconstruct the single property being evaluated, as compared to the cost to build multiple, or tract, properties. This is necessary because in tract housing labor costs are reduced because the home-builders need not be skilled craftsmen and material costs are reduced because the builder is buying and transporting materials in bulk amounts. The repetitive nature of the plans, and the large number of units produced, are the most significant factors in reducing the cost of these houses.

Section 2695.183 (c) The estimate of replacement cost shall not be based upon the resale value of the land, or upon the amount or outstanding balance of any loan.

This provision is necessary because consumers can be confused and might think the land value is included in replacement cost estimate. Further, this provision is required to make it clear to insurers that they must not include this. They should not include this because the value of the land is not covered by the homeowner policy.

Section 2695.183 (d) The estimate of replacement cost shall not include a deduction for physical depreciation. This provision is required because in replacement cost or actual cash value policies, depreciation is not taken on a total loss to the structure pursuant to the policy, itself. Further, it is clear that what is being estimated is the cost to rebuild the home and depreciation is not rationally related to that cost. In this regard, this provision makes it clear that anytime a replacement cost policy or an actual cash value policy is in place, and an estimate of replacement cost is determined, the estimate must not include depreciation.

Section 2695.183 (e) provides that a licensee who estimates replacement cost, or who relies upon an estimate of replacement cost produced by another, shall take reasonable steps to verify that the sources and methods used are kept current to reflect changes in the costs of reconstruction and rebuilding, including changes in labor, building materials, and supplies, based upon the geographic location of the insured structure. This is necessary for the basic reason that a calculation of the estimate of replacement cost is dependent upon the consideration of accurate and up to date information. If the costs of reconstruction and rebuilding are outdated and inaccurate, the estimated replacement cost will be inaccurate. The purpose of this subdivision is to assure that licensees act reasonably to confirm the accuracy of the data they are using in estimating replacement cost. The purpose is to assure that correct information is used in establishing estimated replacement cost and when the replacement cost estimating tools are required to be used by the insurer, the insurer is in a better position to assure their reliability.

Section 2695.183 (f) “Demand surge” is a phenomenon characterized by a substantial increase in the cost of construction due to unusually high demand for contractors, building supplies and construction labor. Demand surge typically occurs after a disaster, such as a wildfire, earthquake, or other natural disaster, in which large numbers of structures are destroyed within a specific geographic area. A replacement cost estimate, or construction cost estimate, generated by or on behalf of a licensee, shall not include consideration for demand surge. The licensee shall disclose this fact to the applicant or insured in the notice or report provided under subdivision (i) of this Section 2695.183.

The disclosure to the applicant or insured is necessary as every one of the other factors required to be considered in estimating replacement cost or a construction cost may be related to a premium cost, but while the other factors are knowable and have some relation to the individual structure being evaluated, the extent of any disaster and thus the degree of demand surge is unknowable and bears no logical correlation to the structure.

The purpose is to assure that the replacement cost shall be calculated to rebuild or replace a home in a situation where there is no demand surge, and that the additional percentage available in a replacement cost policy would provide coverage in the event the loss was related to a disaster, where demand surge elements might exist.

Section 2695.183 (g) provides that the provisions of this article are binding upon licensees, even if they rely upon information, data or statistical methods obtained through a third party source. In the typical transaction, licensees will use third party cost calculator software to estimate replacement cost. This subsection is required to establish that if the licensee does provide an estimated replacement cost, that licensee is obligated to comply with the standards in this article. This will enable the Department of Insurance to exercise its regulatory authority over its

licensees to assure compliance with this article. Further, the subdivision requires that information received by the Department shall be accorded the degree of confidential treatment required by section 735.5 of the Insurance Code or Chapter 2 of Part 1 of Division 3 of Title 2 of the Government Code, commencing at section 11180. This provision is necessary to make it clear that any vendor information that is considered to be “proprietary” shall be treated as required under section 735.5 of the Insurance Code.

Section 2695.183 (h) If a licensee uses an estimate of replacement cost or construction costs to set or recommend a policy limit on a homeowners’ insurance policy for an applicant or insured, the licensee must provide a copy of the replacement cost estimate to the applicant or insured at the time the policy limit is set or recommended. If the estimate of replacement cost or construction costs is updated or changed by, or on behalf of, the licensee, the licensee shall provide a copy of the revised estimate of replacement cost to the applicant or insured within sixty (60) calendar days from the time the estimate is generated. The estimate of replacement cost must itemize each component specified in subdivision (a) of this Section 2695.183.

This provision is necessary to assure that the applicant or insured knows the replacement cost estimate and how it is calculated. If the applicant or insured knows this information at the outset, he will be in a better position to correct any inaccuracies at the beginning of the transaction process, rather than not finding out until after a loss, that for example, the square footage on the home was inaccurately low when the estimate was formulated and hence he is now underinsured. It has been the Department’s experience that after fire related disasters, insureds have complained that they learned that the replacement cost estimates made in setting coverage limits for their homes were too low, causing underinsurance issues to arise during efforts to rebuild or replace their residences. This subdivision is necessary to make clear to the applicant or insured what is included in the replacement cost estimate. If all of the relevant elements and components necessary to calculate an estimate of replacement cost are not considered, the use of the term “replacement” is inherently misleading. It leads an applicant or insured to expect that the estimate was based on all of the necessary components to effectuate a true “replacement” cost estimate when, in reality, the estimate may, in fact, be low because certain components necessary to rebuild or replace have not been factored into the estimate. Consequently the estimate would have been an estimate of something other than what it would actually take to replace the structure. Further, the purpose of this subsection is to provide the Department of Insurance, pursuant to its regulatory and enforcement authority, the availability of accurate information in assuring that licensees have complied with the with subdivisions (a) through (e) of this Section 2695.183 in calculating estimated replacement cost.

Section 2695.183 (i) Licensees shall maintain (1) a record of the information supplied by the applicant or insured that is used by the licensee to generate the replacement cost estimate or any construction cost estimate and (2) a copy of any replacement cost estimate and any construction cost estimate supplied to the applicant or insured pursuant to subdivision (i) of this Section 2695.183. If a policy is issued, these records and copies shall be maintained in the insured’s file for the entire term of the insurance policy or the duration of coverage, whichever terminates later in time, and for five years thereafter. However, in the event the estimate is provided to an applicant to whom an insurance policy is never issued, the records and copies referred to in the first sentence of this subdivision (i) shall be maintained in the applicant’s file for a period of

three years following the time the estimate is generated.

This provision is necessary to permit the Department to exercise its regulatory obligation to investigate consumer inquiries and to conduct market conduct examinations that involve issues including underinsurance matters. The Department may seek documents establishing whether the insured provided the correct information to the licensee and at the same time be able to review a copy of the replacement cost estimated for the same purpose. As to documentation regarding policies that are not issued, again, the purpose is to assure that there are records maintained which will permit the Department to exercise its regulatory obligation to assure compliance with applicable statutes and regulations.

Section 2695.183 (j) provides that using any form of the word “replace” or “replacement” in any estimate of construction costs not comporting with subdivisions (a) through (e) of this Section 2695.183 constitutes making a statement with respect to the business of insurance which is misleading and which by the exercise of reasonable care should be known to be misleading, pursuant to Insurance Code section 790.03.

Insurance Code Section 790.03 identifies prohibited acts including in its subdivisions (a) and (b) which include misleading statements. With this subdivision, the Department seeks to enunciate clearly that the term “replacement” when used in the context of the kinds of estimates addressed in this article, but not complying with the standards set forth in subdivisions (a) through (e) of Section 2695.183, represents a prohibited act under Insurance Code Section 790.03. To inform an applicant or insured that what is being estimated is what it would take to replace her dwelling is inherently misleading when the estimate fails to take into account each cost element of what it would actually take to replace the dwelling in the event of a total loss. The purpose is to provide necessary guidance to licensees and the Department of Insurance, pursuant to its regulatory and enforcement authority, since it is required to assure compliance with the Insurance Code, including by means of disciplinary action for violations of Insurance Code section 790.03.

Further, a licensee that provides an applicant or insured with any estimate of construction costs that does not satisfy all of the requirements of subdivisions (a) through (e) of this Section 2695.183 shall indicate that it is not an estimate of replacement cost and shall identify and explain in the estimate each of the ways in which the estimate of construction costs that is provided fails to meet the requirements for a replacement cost estimate that are stated in said subdivisions (a) through (e). This is to alert applicants or insureds that they are receiving not a “replacement cost” estimate but rather a “construction costs” estimate, which may not be sufficient to replace or rebuild the residence. Further, the licensee must specify each of the ways in which the estimate that is provided falls short of what can accurately be characterized as a replacement cost estimate; it may be that the applicant or insured is satisfied with coverage that will not replace his foundation, for instance, and understands that that is what he or she is paying for, in which case there would be nothing misleading about the estimate. However, when a licensee provides an estimate that purports to be based on features of a particular structure but knows that the estimate fails to take into account each cost element that could be required in the event of a total loss, the estimate would be inherently misleading unless the licensee observed the requirements of this provision. In this regard, with this subsection, the applicant or insured

cannot be misled into thinking that he is receiving an estimate to replace or rebuild his residence when he is not.

Section 2695.183 (k) When an insurer requires that a broker-agent utilize a specific source or tool to create an estimate of replacement cost or construction costs,

(1) the insurer shall prescribe procedures to be followed by broker-agents when they use the source or tool.

This provision is required to assure that the insurer has in place specific procedures required to be followed when using the source or tool. In order to assure that replacement cost estimating sources are tools are used correctly, there must be in place procedures for how they are to be used. In this regard, the procedures can be communicated to those using the sources or tools, as is proscribed in (2) herein.

(2) the insurer shall provide the broker-agent with the training or training materials necessary to properly utilize the source or tool according to the insurer's prescribed procedures.

This is necessary so that the proper procedures proscribed by insurers are communicated through training to the broker-agents using the sources and tools. The purpose is to assure that not only are there correct procedures to be followed when using the sources or tools to estimate replacement cost or construction costs, but that the broker-agents who are using the sources and tools have the required information so as to implement use of the sources and tools effectively and accurately.

(3) the insurer, and not the broker-agent, shall be responsible for any noncompliance with the provisions subdivisions (a) through (f) of this Section 2695.183, unless that noncompliance results from failure by the broker-agent to follow the insurer's prescribed procedures when using the source or tool.

Because it is not uncommon for an insurer to require that a broker-agent use a specific source or tool to create an estimate of replacement cost or construction costs, in these situations, the insurer shall be responsible if there is any noncompliance. The purpose is to assure that correct information is used in establishing estimated replacement cost and construction costs and when the estimating tools are required to be used by the insurer, the insurer is in a better position to assure their reliability. Without this provision, insurers would be able to escape accountability for decisions that they have made. However, it is necessary not to hold insurers accountable for behavior over which they have no control, for instance, if a producer misuses the software designated by the insurer or fails to use it in accordance with procedures set forth by the insurer.

Section 2695.183 (l) This Section 2695.183 applies to all communications by a licensee, verbal or written, with the sole exception of internal communications within an insurer, or confidential communications between an insurer and its contractor, that concern the insurer's underwriting decisions and that never come to the attention of an applicant or insured. This purpose of this section is to allow insurers to discuss values internally without having to follow the standards and record keeping requirement. The purpose is to exempt insurers from having to follow the regulations when it comes to their internal discussions since in those cases there is no detrimental effect to customers, because no misleading statement will have been made to them.

Section 2695.183 (m) No provision of this article shall be construed as requiring a licensee to estimate replacement cost to set, or recommend to an applicant or insured, a policy limit on a

homeowners' insurance policy, or to advise the applicant or insured as to the sufficiency of such an estimate.

The regulations establish requirements for licensees to follow when estimating replacement cost. The regulations do not require that licensees estimate replacement cost or advise an applicant or insured on the sufficiency of the estimate, nor is it the intention of the regulations to do so, nor may these regulations be construed as establishing this requirement.

IDENTIFICATION OF STUDIES

There are no specific studies relied upon in the adoption of these regulations.

SPECIFIC TECHNOLOGIES OR EQUIPMENT

Adoption of these regulations would not mandate the use of specific technologies or equipment.

ALTERNATIVES

The Commissioner has determined that no reasonable alternative exists to carry out the purpose for which the regulations are proposed. Performance standards were considered but were rejected as an unreasonable and impracticable alternative in the context of regulations that seek efficiently to define specific rules for the protection of service members being sold life insurance policies.

ECONOMIC IMPACT ON SMALL BUSINESS

The Commissioner has identified no reasonable alternatives to the presently proposed regulations, nor have any such alternatives otherwise been identified and brought to the attention of the Department, that would lessen any impact on small business. Although performance standards were considered as an alternative, they were rejected, in part, because the kind of risks from which the regulations seek to protect consumers cannot practicably be gauged by means of a performance standard.

PRENOTICE DISCUSSIONS

Pursuant to Government Code Section 11346.45, the Commissioner conducted prenotice public discussions on February 11, 2010 at 9:30 a.m. at the California Department of Insurance office in Los Angeles.