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CONNECTICUT INSURANCE LAW JOURNAL

VOLUME 31 **2024–2025** **NUMBER 1**

CONTENTS

ARTICLES

RETHINKING PROP 103'S APPROACH TO INSURANCE REGULATION	*Lars Powell* *R.J. Lehmann* *Ian Adams*	1
FLORIDA'S HOMEOWNERS INSURANCE PROBLEMS	*Peter Molk*	40

RETHINKING PROP 103'S APPROACH TO INSURANCE REGULATION

LARS POWELL
R.J. LEHMANN
& IAN ADAMS*

EXECUTIVE SUMMARY

California voters passed Proposition 103 ("Prop 103") in 1988. Since that time, California's insurance market has struggled to keep pace with national trends and product innovations. The problems with the regulatory regime Prop 103 created most recently came to a head with the September 21st announcement by Governor Gavin Newsom that he had issued an emergency executive order to stabilize the state's rapidly deteriorating market for property insurance.

As other states consider the adoption of reforms inspired by Prop 103, it is necessary to revisit the law's genesis and recent history, as well as to examine the problems that it has fostered.

This paper outlines how the Prop 103 rating system is slow, imprecise, and inflexible relative to other jurisdictions; examines the ways in which the ratemaking system has been rendered unpredictable; and details the form, function, and questionable value proposition of the rate-intervenor system. In so doing, the paper demonstrates that Prop 103 has created an insurance market that struggles to work efficiently even in the best of times and is virtually impossible to sustain in periods of acute stress.

Despite the current problems in California's insurance market, industry critics argue that other states would be better off with regulations similar to those contained in Prop 103. A clear view of the results from California demonstrate that these arguments are false and misleading. Contrary to claims that Prop 103 saved Californians as much as $154 billion in auto insurance premiums from 1989 to 2015, we find that Californians would have saved nearly $25 billion if they had not passed Prop 103.

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The paper concludes with a series of policy recommendations designed to inform both the ongoing implementation of Prop 103 by the California Department of Insurance, as well as other jurisdictions considering elements of a Prop 103 approach.

TABLE OF CONTENTS

I. INTRODUCTION 4
II. THE RECENT HISTORY OF CALIFORNIA INSURANCE MARKET 7
A. PROBLEMS WITH RATE REGULATION UNDER PROP 103 11
B. CATASTROPHE MODELS AND REINSURANCE 14
C. AN INFLEXIBLE SYSTEM 16
III. PROP 103 RATE REVIEW IN PRACTICE 19
A. RATEMAKING AS MARKET-CONDUCT EXAMINATION 19
1. Rulemaking by ratemaking proceeding 19
2. Corporate governance by ratemaking proceeding 21
B. PROP 103'S DEAD LETTER DEEMER 21
C. THE INTERVENOR PROCESS 24
D. RATE SUPPRESSION UNDER PROP 103 26
IV. THE IMPACT OF PROP 103 ON OTHER STATES 28
V. ESTIMATING THE COST OF PROP 103 IN CALIFORNIA AND OTHER STATES 32
VI. RECOMMENDED REFORMS 35
A. INTERPRETIVE REFORMS 35
1. Fast-track noncontroversial filings 35
2. Refocus rate proceedings 36
3. Transparency 36
4. Embracing catastrophe models 37
B. LEGISLATIVE REFORMS 37
1. Insurance Market Action Plan 38
2. Telematics 38
VII. CONCLUSION 39

I. INTRODUCTION

The 1980s were a period of chaotic dislocation in the California automobile insurance market.[1] The California Supreme Court's 1979 decision in Royal Globe Insurance created precedent that third parties could bring action against a tortfeasor's insurer, even if they were not party to the insurance contract in question.[2] What followed was an explosion in insurance-related litigation, as the number of auto-liability claim filings in California Superior Court rose by 82% between 1980 and 1987, and the severity of claims rose by a factor of four.[3] As would be expected, the state's auto insurance premiums followed suit, rising 69.8% from $4.3 billion in 1984 to $7.3 billion in 1987.[4]

This crisis in auto insurance affordability came to a head in 1988 when the twenty-nine ballot initiatives presented to California voters in that November's election included five separate questions dealing specifically with insurance issues.[5] Two of these were broadly supported by the insurance industry: Proposition 104,[6] which would establish a no-fault system for auto insurance and limit damage awards against insurers, and Proposition 106, which would set percentage-based caps on attorneys' contingency fees.[7] Proposition 100, backed by the California Trial Lawyers Association, was proposed as a counter to Props 104 and 106 and if it received more votes that those initiatives it would have canceled the limits on both damage awards and contingency fees, as well as the proposed no-fault system.[8] Proposition 101

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1. W. Kip Viscusi & Patricia Born, *The Performance of the 1980s California Insurance and Liability Reforms*, 2 RISK MGMT. INS. REV. 14–33 (1999).

2. Royal Globe Ins. Co. v. Superior Court, 592 P.2d 329, 332 (1979), *overruled by* Moradi-Shalal v. Fireman's Fund Ins. Cos., 758 P.2d 58 (1988).

3. DAVID APPEL, REVISITING THE LINGERING MYTHS ABOUT PROPOSITION 103: A FOLLOW-UP REPORT (2004), https://www.namic.org/wp-content/uploads/legacy/040921AppelFinalRpt.pdf.

4. Viscusi & Born, *supra* note 1, at 18.

5. Jerry Gillam & Leo C. Wolinsky, *State's Voters Face Longest List of Issues in 66 Years: Nov. 8 Ballot to Carry Maze of 29 Propositions*, L.A. TIMES (July 7, 1988, 12:00 AM), https://www.latimes.com/archives/la-xpm-1988-07-07-mn-8306-story.html.

6. *Provisions of the Insurance Measures: Proposition 104 No-Fault Insurance*, L.A.TIMES (Oct. 10, 1988, 12:00 AM), https://www.latimes.com/archives/la-xpm-1988-10-10-mn-2779-story.html.

7. Gillam & Wolinsky, *supra* note 5.

8. Kenneth Reich, *Prop. 100 Evokes Unrestrained Claims From Insurers, Lawyers*, L.A. TIMES (Sept. 14, 1988, 12:00 AM), https://www.latimes.com/archives/la-xpm-1988-09-14-mn-1907-story.html.

would cap insureds' ability to recover bodily injury damages, paired with a promised 50% reduction in the bodily injury portion of insurance premiums.[9]

In the end, however, only one of the insurance measures was approved in the November 8th election: Proposition 103, also known as the "Insurance Rate Reduction and Reform Act."[10] Authored by Harvey Rosenfield of the Santa Monica-based Foundation for Taxpayer and Consumer Rights (now known as Consumer Watchdog) and sponsored by Rosenfield's organization Voter Revolt, Prop 103 carried narrowly with 51.1% yes votes to 48.9% against.[11]

Prop 103's stated purpose was "to protect consumers from arbitrary insurance rates and practices, to encourage a competitive insurance marketplace."[12] Proponents of the measure claim they have achieved that, touting $154 billion in consumer savings over the first 30 years it was in effect.[13]

Among the specific changes mandated by the law were:

- California's insurance commissioner, previously appointed by the governor, was made an elected position, chosen in the same cycle with the other state officers for a term of four years.[14]
- Beginning in November 1988, all automobile and other property and casualty insurance rates were to be rolled back to 80% of their levels as of November 8th, 1987, and were to be held at such levels until November 1989.[15]
- Rate increases and decreases were to be subject to prior approval of the elected insurance commissioner, replacing the "open competition" system that had previously prevailed for forty years under the McBride-Grunsky Insurance Regulatory Act of 1947, which required only that insurers submit rate manuals to the California Department

9. Kenneth Reich, *Prop. 101: It's 'Not Perfect,' Measure's Sponsors Concede*, L.A. TIMES (Sept. 21, 1988, 12:00 AM), https://www.latimes.com/archives/la-xpm-1988-09-21-mn-2241-story.html.

10. *Text of Proposition 103*, CONSUMER WATCHDOG (Jan. 1, 2008), https://consumerwatchdog.org/insurance/text-proposition-103.

11. Steve Geissinger, *Californians Approve Auto Insurance Cuts, Insurer Files Lawsuit,* ASSOCIATED PRESS (Nov. 9, 1988).

12. CONSUMER WATCHDOG, *supra* note 10.

13. Press Release, Consumer Fed'n of Am., 30 Years and $154 Billion of Savings: California's Proposition 103 Insurance Reforms Still Saving Drivers Money (Oct. 17, 2018), https://consumerfed.org/press_release/30-years-and-154-billion-of-savings-californias-proposition-103-insurance-reforms-still-saving-drivers-money.

14. CONSUMER WATCHDOG, *supra* note 10.

15. *Id.*

of Insurance (CDI).[16] Under the Act public hearings were mandatory for personal lines increases of more than 7% and commercial lines increases of more than 15%, while others were at the CDI's discretion.[17]

- The law created a role at these hearings for "public intervenors," who are empowered to file objections on behalf of consumers, with fees to be paid by the applicant insurance company.[18]
- Prop 103 also established a rate-setting formula for auto insurance that mandated rates be based on an insured's driving record, number of miles driven, and years of driving experience.[19] While other factors could be considered, the burden would be on insurers to demonstrate they are statistically correlated with risk.
- Drivers with at least three years of driving experience, no more than one violation point during the previous three years, and no fault in an accident involving death or damage great than $500 must be offered a "good driver discount" that is at least 20% below the rate the driver would otherwise have been charged for coverage.[20]
- The business of insurance was deemed subject to California antitrust, unfair business practices, and civil-rights law.[21]

Because the law was subject to immediate and ongoing litigation, some provisions were only fully implemented years after the proposition's passage.[22] But notable among the law's other provisions was Section 8(b), which rendered Prop 103's text extraordinarily difficult to amend:

> "The provisions of this act shall not be amended by the Legislature except to further its purposes by a statute passed in each house by roll call vote entered in the journal, two-thirds of the membership concurring, or by a statute that becomes effective only when approved by the electorate."[23]

16. McBride-Grunsky Insurance Regulatory Act of 1947, CAL. INS. CODE §§ 1850–60.3 (West 2024).

17. *Id.*

18. CONSUMER WATCHDOG, *supra* note 10.

19. *Id.*

20. *Id.*

21. *Id.*

22. *See* Ian Adams, *R Street Policy Study No. 43: The Troublesome Legacy of Prop 103*, R STREET 7 (Oct. 2015), https://www.rstreet.org/wp-content/uploads/2018/04/RSTREET43-1.pdf.

23. CONSUMER WATCHDOG, *supra* note 10.

Much has changed in the world and in California's insurance industry since the passage of Prop 103, but the lion's share of the law remains as it was in 1988.

II. THE RECENT HISTORY OF CALIFORNIA INSURANCE MARKET

The recent story of California's property and casualty insurance market has been one of uncertainty and induced dysfunction.

Prior to the COVID-19 pandemic, California's market was saddled by availability issues stemming from a series of historically costly wildfires. California homeowners insurers posted a combined underwriting loss of $20 billion for the massive wildfire years of 2017 and 2018 alone, more than double the combined underwriting profit of $10 billion that the state's homeowners insurers had generated from 1991 to 2016.[24] Partly in response to those losses, as well as the inability to adjust rates expeditiously, the number of nonrenewals of California residential-property policies grew by 36% in 2019, and new policies written by the state's residual-market Fair Access to Insurance Requirements (FAIR) Plan surged 225% that same year.[25]

To stanch the bleeding of admitted market policies into the FAIR Plan, California's syndicated fire insurance pool that acts as a provider of last resort, and the surplus-lines market, CDI, in December 2019, invoked recently enacted statutory authority to issue moratoria barring insurers from nonrenewing roughly 800,000 policies in ZIP codes adjacent to specified major wildfires.[26] As of November 2022 nearly 2.4 million policies statewide were in ZIP codes under nonrenewal moratoria, many of them added following additional catastrophic wildfires in 2020.[27]

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24. Eric J. Xu, Cody Webb & David D. Evans, *Wildfire Catastrophe Models Could Spark the Change California Needs*, MILLIMAN (Oct. 2019), https://fr.milliman.com/-/media/milliman/importedfiles/uploadedfiles/wildfire_catastrophe_models_could_spark_the_changes_california_needs.ashx.

25. CAL. DEP'T OF INS., DATA ON INSURANCE NON-RENEWALS, FAIR PLAN AND SURPLUS LINES (2015-2019) 1 (2020), https://www.insurance.ca.gov/0400-news/0100-press-releases/2020/upload/nr104Charts-NewRenewedNon-RenewedData-2015-2019-101920.pdf.

26. Matthew Nuttle, *California Blocks Insurance Companies From Dropping Residents in Fire-Prone Areas*, ABC10 SACRAMENTO (last updated Dec. 5, 2019, 6:41 PM), https://www.abc10.com/article/news/politics/insurance-non-renewal-moratorium/103-40050393-6915-41c4-a6f0-0e525990cce7.

27. John Egan, *Many California ZIP Codes Get Protection From Home Insurance Non-Renewals*, FORBES ADVISOR (last updated Apr 4, 2024, 6:07 AM), https://www.forbes.com/advisor/homeowners-insurance/california-policy-non-renewals, *reprinted in* NASDAQ (Jan. 6, 2021, 2:32 PM),

During the COVID-19 pandemic, CDI instituted a rate freeze in auto insurance and accused the industry of profiteering.[28] In June 2020, California Insurance Commissioner Ricardo Lara took credit for ordering $1.03 billion in premium refunds, dividends, or credits for auto insurance policyholders, as well as "an additional $180 million in future rate increases that insurance companies reduced in response to the Commissioner's orders."[29]

In fact, most of the early rebates were voluntary, in line with similar voluntary rebates that insurers issued across the country.[30] CDI would not publish its methodology for mandatory rebates until March 2021, at which point it declared that rather than the 9% of premium that California auto insurers returned to policyholders from March through September 2020 they should have returned 17%.[31] In October 2021, the California Court of Appeal ruled in State Farm General Insurance Co. v. Lara that Prop 103 did not actually give the commissioner authority to order the retroactive rate refunds.[32]

CDI was also slow to lift its rate freeze even as the COVID-19 pandemic abated and many employers ended work-from-home policies. From May 2020 until October 2022 CDI did not approve a single auto insurance rate filing even though more than 75% of the state's auto insurers filed for an increase during that period.[33] In the meantime, the "motor vehicle repair"

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https://www.nasdaq.com/articles/many-california-zip-codes-get-protection-from-home-insurance-non-renewals-2021-01-06.

28. Press Release, Cal. Dep't of Ins., Commissioner Lara's Actions Lead to More Than $1.2 Billion in Premium Savings for California Drivers Due to COVID-19 Pandemic (June 25, 2020), https://www.insurance.ca.gov/0400-news/0100-press-releases/2020/release056-2020.cfm.

29. *Id.*

30. Ron Lieber, *Some Insurers Offer a Break for Drivers Stuck at Home*, THE N.Y. TIMES (Apr. 6, 2020), https://www.nytimes.com/2020/04/06/business/corona-virus-car-insurance.html.

31. Ricardo Lara, *Bulletin 2021-03*, CAL. DEP'T OF INS. (Mar. 11, 2021), https://www.insurance.ca.gov/0250-insurers/0300-insurers/0200-bulletins/bulletin-notices-commiss-opinion/upload/Bulletin-2021-03-Premium-Refunds-Credits-and-Reductions-in-Response-to-COVID-19-Pandemic.pdf; Press Release, Cal Dep't of Ins., Commissioner Lara Finds Auto Insurance Companies Overcharged Drivers as Accidents Plummeted During the Pandemic (Mar. 11, 2021), https://www.insurance.ca.gov/0400-news/0100-press-releases/2021/release030-2021.cfm#:~:text=After%20a%20systematic%20review%20of,due%20to%20the%20ongoing%20pandemic.

32. State Farm Gen. Ins. Co. v. Lara et al., 286 Cal. Rptr. 3d 146 (2021).

33. June Sham, *California Rate Filing Freeze Starts to Thaw*, BANKRATE (Dec. 1, 2022), https://www.bankrate.com/insurance/car/california-rate-filing-freeze-causes-unrest.

component of the Consumer Price Index (CPI) jumped by 19.5% between July 2022 and July 2023, far outstripping the 3.2% hike in overall CPI.[34]

With limited options on the pricing front, insurers have been forced to limit exposure in other ways. Since California is a "guaranteed issue" state for private-passenger auto insurance[35], auto insurers are attempting to limit the policies they take on by, for example, limiting advertising. Insurance rating agency A.M. Best Co. reported that auto insurers cut their advertising budgets by nearly 18% in the first half of 2022, compared with the same period in 2021.[36] In other cases, insurers have taken to asking for more premium upfront instead of allowing consumers to pay via monthly or other periodic installment plans.[37]

Meanwhile, as detailed more extensively in the sections below, the wildfire-driven homeowners insurance crisis that began before the COVID-19 pandemic has itself grown to epidemic levels, highlighted by State Farm General's 2023 decision to cease writing new business in the California market. The environmental news service ClimateWire observed:

> "Experts say State Farm's decision highlights a flaw in California policies that effectively blocks insurers from considering climate change in setting premiums and discourages them from seeking rate increases sufficient to cover the state's growing wildfire risk. In addition, the policies have created insurance premiums that are far too low and are forcing insurers to pull back their coverage in California to remain profitable."[38]

California's political leaders have also acknowledged the crisis. On September 21st, Governor Gavin Newsom issued an executive order noting

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34. Press Release, Bureau of Labor Statistics, Consumer Price Index – July 2023 (Aug. 10, 2023, 8:30 AM), https://www.bls.gov/news.release/archives/cpi_08102023.pdf.

35. CONSUMER WATCHDOG, *supra* note 10.

36. Anthony Bellano, *Where'd the Gecko Go? Auto Insurance Advertising Sees Dip*, BEST'S REV., Oct. 2022, at 80, https://www.ambest.com/multimedia/Bests_Review_October2022.pdf.

37. Ricardo Lara, *Bulletin 2022-10*, CAL. DEP'T OF INS. (Aug. 8, 2022), https://www.insurance.ca.gov/0250-insurers/0300-insurers/0200-bulletins/bulletin-notices-commiss-opinion/upload/Insurance-Commissioner-Ricardo-Lara-Bulletin-2022-10-Changes-to-Premium-Options-Without-the-Prior-Approval-of-the-Department-of-Insurance.pdf.

38. Thomas Frank, *Calif. Scared Off Its Biggest Insurer. More Could Follow*, E&E NEWS (May 31, 2023, 6:31 AM), https://www.eenews.net/articles/calif-scared-off-its-biggest-insurer-more-could-follow.

that insurance carriers representing 63% of the state's homeowners insurance market had in recent months announced plans to either cease or limit writing new policies.[39] He further announced that he was authorizing Insurance Commissioner Ricardo Lara to:

> "take prompt regulatory action to strengthen and stabilize California's marketplace for homeowners insurance and commercial property insurance, and to consider whether the recent sudden deterioration of the private insurance market presents facts that support emergency regulatory action."[40]

For his part, Lara announced an emergency response plan that included:

> "[T]ransition[ing] homeowners and businesses from the FAIR Plan back into the normal insurance market with commitments from insurance companies to cover all parts of California by writing no less than 85% of their statewide market share in high wildfire risk communities. . . .
>
> Giving FAIR Plan policyholders who comply with the new Safer from Wildfires regulation first priority for transition to the normal market, thus enhancing the state's overall wildfire safety efforts;
>
> Expediting the Department's introduction of new rules for the review of climate catastrophe models that recognize the benefits of wildfire safety and mitigation actions at the state, local, and parcel levels; . . .
>
> Holding public meetings exploring incorporating California-only reinsurance costs into rate filings;
>
> Improving rate filing procedures and timelines by enforcing the requirement for insurance companies to submit a complete rate filing, hiring additional Department staff to review rate applications and inform regulatory changes, and

39. Cal. Exec. Order No. N-13-23 (Sept. 21, 2023), https://www.gov.ca.gov/wp-content/uploads/2023/09/9.21.23-Homeowners-Insurance-EO.pdf.

40. *Id.*

> enacting intervenor reform to increase transparency and public participation in the process . . . ."[41]

A. Problems With Rate Regulation Under Prop 103

Prop 103 charges California's insurance commissioner with applying requirements articulated in the California Insurance Code and the California Code of Regulations to determine whether an insurer's requested rate change is "excessive, inadequate or unfairly discriminatory."[42] If the commissioner determines that a request is not "most actuarially sound," he or she can require a rate reduction or reject a rate filing completely.[43] Here, it should be noted that the "most actuarially sound" standard is unique to California,[44] and is not applied by other states that employ prior-approval regulatory systems for rate review.

The most obvious problem with rate regulation is that it restricts the availability of insurance. As the German economist Karl Henrik Borch put it in a landmark article on capital markets in insurance:

> "If premiums are low, the profitability of the insurance company will also be low, and investors may not be inclined to risk their capital as reserves for an insurance company. If the government imposes too low premiums, the whole system may break down, and high standard insurance may become impossible in a free economy."[45]

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41. Press Release, Cal. Dep't of Ins., Commissioner Lara Announces Sustainable Insurance Strategy to Improve State's Market Conditions for Consumers (Sept. 21, 2023), https://www.insurance.ca.gov/0400-news/0100-press-releases/2023/release051-2023.cfm.

42. CAL. INS. CODE §1861.137(b) (West 1990).

43. *Prior Approval Rate Filing Instructions*, CAL. DEP'T OF INS. (June 5, 2023), https://www.insurance.ca.gov/0250-insurers/0800-rate-filings/0200-prior-approval-factors/upload/PriorAppRateFilingInstr_Ed06-05-2023.pdf.

44. *See* AMERICAN ACADEMY OF ACTUARIES, ACTUARIAL SOUNDNESS, A PUBLIC POLICY SPECIAL REPORT (May 2012), https://www.actuary.org/sites/default/files/files/Actuarial_Soundness_Special_Report_5.10.12.pdf; THOMSON REUTERS, RATES AND RATING PLANS, 0110 SURVEYS 11 (Nov. 2023), https://1.next.westlaw.com/Document/I68a752d75b5411de9b8c850332338889/View/FullText.html?originationContext=documenttoc&transitionType=CategoryPageItem&contextData=(sc.Default).

45. Karl Borch, *Capital Markets and the Supervision of Insurance Companies*, 41 J. OF RISK & INS. 397, 403 (1974).

Insurers naturally respond to rate regulation by tightening their underwriting criteria, forcing some consumers to have to turn to the higher-priced residual market for coverage. In extreme cases, rate suppression can lead some insurers to exit the market altogether.

The empirical evidence of this effect is manifest. After California ordered mandatory 20% rate rollbacks following the passage of Prop 103 in 1988 (the effects of which were initially somewhat blunted by the courts) the number of insurers writing auto coverage in the state fell from 265 in 1988 to 208 in 1993.[46]

TABLE 1: Firms Selling Auto Insurance in California, 1988-1993

YEAR	ENTERED DURING	EXITED DURING	EXISTING AT YEAR-END	EXITING MARKET SHARE
1988	21	28	265	1.80%
1989	13	31	247	3.53%
1990	15	12	250	0.27%
1991	16	44	222	2.93%
1992	22	32	212	0.67%
1993	24	28	208	1.35%

SOURCE: *NAIC data, via Jaffe & Russell*[47]

More recently, Prop 103's deleterious effects on the availability of coverage have manifested most obviously in decisions by major homeowners insurers to exit the market. In 2019, following the deadliest wildfire season in California history,[48] the state's homeowners insurers responded by nonrenewing 235,250 policies, a 31% increase from the prior year.[49] In May 2023, California's largest writer of homeowners insurance, State Farm General,

46. DWIGHT M. JAFFEE & THOMAS RUSSELL, DEREGULATING PROPERTY-LIABILITY INSURANCE: RESTORING COMPETITION AND INCREASING MARKET EFFICIENCY 205 (J. David Cummins ed. 2002).

47. *Id.*

48. Tim Arango, Jose A. Del Real & Ivan Penn, *5 Lessons We Learned From the California Wildfires in 2019*, THE N.Y. TIMES (Nov. 4, 2019), https://www.nytimes.com/2019/11/04/us/fires-california.html.

49. Katherine Chiglinsky & Elaine Chen, *Many Californians Being Left Without Homeowners Insurance Due to Wildfire Risk*, INS. J. (Dec. 4, 2020), https://www.insurancejournal.com/news/west/2020/12/04/592788.htm.

announced it would halt the sale of new homeowners policies in the state.[50] Only a week later California's fourth-largest personal lines writer, Allstate, likewise announced it would cease writing new policies,[51] while Farmers, the second-largest writer, subsequently said it too would limit the writing of new policies.[52]

While Prop 103 calls for property and casualty insurers to earn a "fair profit" rate of return of 10%,[53] the industry has long reported that it finds it difficult to meet the California Department of Insurance's requirements to justify rate increases, even when such increases would allow premiums to better reflect true risk.[54] In fact, even after the state's extreme wildfires in 2017 and 2018, and despite trailing only Hawaii in median home prices,[55] Californians in 2020 paid an annual average of $1,241 in homeowners insurance premiums across all policy types—less than the national average of $1,311.[56]

As noted above, the homeowners insurance availability crisis has become particularly acute in the wake of devastating wildfires in 2017 and 2018. Under Prop 103, an insurer must justify its requested statewide premium for future wildfire losses based on its average annual wildfire losses over the last twenty years.[57] But as demonstrated in Figure I, review of the data from California's homeowners insurance market illustrates why such long-run averages are wholly inadequate to project future losses.

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50. Leslie Scism, *State Farm Halts Home-Insurance Sales in California*, WALL ST. J. (May 26, 2023, 7:45 PM), https://www.wsj.com/articles/state-farm-halts-home-insurance-sales-in-california-5748c771.

51. Ryan Mac, *Allstate Is No Longer Offering New Policies in California*, THE N.Y. TIMES (June 4, 2023), https://www.nytimes.com/2023/06/04/business/allstate-insurance-california.html.

52. Sam Dean, *Farmers, California's Second-Largest Insurer, Limits New Home Insurance Policies*, L.A. TIMES (July 11, 2023, 12:35 PM), https://www.latimes.com/business/story/2023-07-11/farmers-californias-second-largest-insurer-limits-new-home-insurance-policies.

53. JAFFEE & RUSSELL, *supra* note 46, at 197.

54. Rex Frazier, *California's Ban on Climate-Informed Models for Wildfire Insurance Premiums*, ECOLOGY L. Q. (Oct. 19, 2021), https://www.ecologylawquarterly.org/currents/californias-ban-on-climate-informed-models-for-wildfire-insurance-premiums.

55. *Median Home Price by State 2024*, WORLD POPULATION REV., https://worldpopulationreview.com/state-rankings/median-home-price-by-state.

56. Grace Gedye, *Four Things California Can Do as Home Insurers Retreat*, CALMATTERS (June 15, 2023), https://calmatters.org/economy/2023/06/california-home-insurance.

57. CAL. CODE REGS. tit. 10, § 2644.5 (2024).

FIGURE I: California Homeowners Estimated Industry Profits Since 1991

SOURCE: *Milliman*[58]

B. CATASTROPHE MODELS AND REINSURANCE

Insurers have access to tools like advanced wildfire catastrophe models that would allow them to project future wildfire losses in ways that consider both changing climactic factors and a given property's proximity to fuel load.[59] Such considerations are not currently permitted under California's Prop 103 system, but nor are they explicitly barred, as such models largely did not yet exist in 1988.[60] Indeed, the California Earthquake Authority uses catastrophe models to develop rates and mitigation discounts, determine the amount of claims-paying capacity the authority needs, and to estimate CEA losses after an event.[61] Moreover, California has begun taking steps toward permitting their use in certain limited contexts, including recent

58. Xu et al., *supra* note 24, at 1.

59. Robert Zolla & Melanie McFaul, *Wildfire Catastrophe Models and Their Use in California for Ratemaking*, MILLIMAN (July 21, 2023), https://www.milliman.com/en/insight/wildfire-catastrophe-models-california-ratemaking.

60. R.J. Lehmann, *How Do You Solve a Problem Like California?*, INS. J. (Sept. 23, 2022), https://www.insurancejournal.com/blogs/law-and-economics/2022/09/23/686531.htm.

61. Glenn Pomeroy, *Use of Catastrophe Models by California Earthquake Authority*, CAL. EARTHQUAKE AUTH., https://ains.assembly.ca.gov/sites/ains.assembly.ca.gov/files/CEA%20Use%20of%20Catastrophe%20Models%20-%20GP%20Statement.pdf.

regulations requiring insurers to disclose to consumers their "wildfire risk score."[62] In July 2023, Insurance Commissioner Ricardo Lara hosted a workshop on catastrophe modeling and insurance, noting in a public invitation that:

> "For the past 30 years, the use of actual historical catastrophe losses has been the method used for estimating catastrophe adjustments in the California rate-approval process. However, historical losses do not fully account for the growing risk caused by climate change or risk mitigation measures taken by communities or regionally, as a result of local, state, and federal investments. Catastrophe estimates based on historical losses only reflect losses after they occur. As a result of climate-intensified wildfire risk and continued development in the wildland urban interface areas, and recent increased efforts to mitigate wildfire risks, past experience may no longer reflect the current wildfire exposure for property owners and insurance companies."[63]

Prop 103 also prohibits insurers from using the cost of reinsurance as justification for rate filings.[64] After a long period of "soft" pricing from 2006 to 2016, reinsurance rates for North American property-catastrophe risk more than doubled from 2017 to 2023, including a 35% year-over-year hike in 2023 according to reinsurance broker Guy Carpenter.[65] When combined with prohibitions on the use of catastrophe models, this has essentially meant that California—a state that has long prided itself as being on the leading edge when it comes to its response to climate change—has effectively told insurers to ignore the science.[66]

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62. Press Release, Cal. Dep't of Ins., Commissioner Lara Announces New Regulations to Improve Wildfire Safety and Drive Down Cost of Insurance (Feb. 25, 2022), https://www.insurance.ca.gov/0400-news/0100-press-releases/2022/release019-2022.cfm.

63. *Invitation to Workshop Examining Catastrophe Modeling and Insurance*, CAL. DEP'T OF INS. (June 7, 2023), https://www.insurance.ca.gov/0250-insurers/0500-legal-info/0300-workshop-insurers/upload/California-Department-of-Insurance-Invitation-to-Workshop-Examining-Catastrophe-Modeling-and-Insurance.pdf.

64. CAL. INS. CODE § 623 (West 1935).

65. *Guy Carpenter U.S. Property Catastrophe Rate-On-Line Index*, ARTEMIS, https://www.artemis.bm/us-property-cat-rate-on-line-index (last visited Aug. 8, 2023).

66. R.J. Lehmann, *Even California Leaders Fail to Grasp Climate Change*, S.F. CHRON. (Jan. 10, 2018), https://medium.com/@sfchronicle/even-california-leaders-fail-to-grasp-climate-change-b960d7038fc7.

Thus, unsurprisingly, having been denied the ability to charge rates that reflect the future risk of wildfire, admitted-market insurers have pulled back from the most at-risk areas. Ironically, this has meant a migration of policies to surplus lines insurers and to the California Fair Access to Insurance Requirements (FAIR) Plan, both of which are allowed to use catastrophe models in setting their premiums.

From 2015 to 2021, the number of FAIR Plan policies increased by 89.7%, growing its share from 1.7% of the California homeowners insurance market to 3.0%.[67] With just $1.4 billion in aggregate loss retention and facing the prospect of claims-paying shortfalls in the event of another major wildfire, the FAIR Plan recently filed a request for an average 48.8% increase in its dwelling fire rates.[68]

C. An Inflexible System

Prop 103 is also remarkably inflexible, particularly given provisions that make it exceedingly difficult to amend by legislative enactment. Not only must any changes pass by a two-thirds vote in both chambers of the California Legislature, but they must also be found to "further the purposes" of the proposition.[69] As the 2nd District Court of Appeal wrote in the 1998 decision Proposition 103 Enforcement v. Quackenbush:

> "Any doubts should be resolved in favor of the initiative and referendum power, and amendments which may conflict with the subject matter of initiative measures must be accomplished by popular vote, as opposed to legislatively enacted ordinances, where the original initiative does not provide otherwise."[70]

With the bar to amendment set that high, it has proven to be functionally impossible for the law to respond to the enormous political,

67. Cal. Dep't of Ins., FACT SHEET: Insurance Policy Count Data 2015-2021 3 (2022), https://www.insurance.ca.gov/01-consumers/200-wrr/upload/CDI-Fact-Sheet-Residential-Insurance-Market-Policy-Count-Data-December-2022.pdf.

68. Jeff Lazerson, *FAIR Plan Seeks Nearly 50% Premium Hike from California Department of Insurance*, Orange County Register (May 19, 2023, 8:08 AM), https://www.ocregister.com/2023/05/19/fair-plan-seeks-nearly-50-premium-hike-from-california-department-of-insurance.

69. Consumer Watchdog, *supra* note 10.

70. Proposition 103 Enf't Project v. Charles Quackenbush, 76 Cal. Rptr. 2d 342, 349 (1998).

technological, and business practice changes that the insurance industry has undergone over the past thirty-five years.

In addition to the emergence of catastrophe models discussed above, another significant tool that insurers have taken increased advantage of in the years since 1988 is the use of credit-based insurance scores, particularly in auto insurance underwriting and rate making. Today, according to the Fair Isaac Corporation (FICO), 95% of auto insurers and 85% of homeowners insurers use credit-based insurance scores in states where it is legally permitted as an underwriting or risk classification factor.[71]

Notably, California is one of four states (along with Massachusetts, Hawaii, and Michigan) that does not permit their use,[72] because CDI has not adopted regulations acknowledging credit history as a rating factor with "a substantial relationship to the risk of loss." This is despite the Federal Trade Commission's (FTC) finding that, in the context of auto insurance, credit-based insurance scores "are predictive of the number of claims consumers file and the total cost of those claims."[73]

A similar disjunction between the inflexibility of Prop 103 and the emergence of new technologies can be seen in the development of "telematic" technologies that allow insurers to measure a range of factors directly relevant to auto insurance risk. These include not only the number of miles driven (a required rating factor under Prop 103)[74] but also how frequently the driver engages in sudden stops or rapid acceleration, as well as how often he or she drives after dark or in high-congestion situations.[75]

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71. *Credit-Based Insurance Scores*, NAIC (Jan. 31, 2024), https://content.naic.org/insurance-topics/credit-based-insurance-scores#:~:text=FICO%20estimates%20approximately%2095%25%20of,underwriting%20or%20risk%20classification%20factor..

72. Deanna Dewberry, *Consumer Alert: Got a Bad Credit Score? You Pay Much More for Car Insurance in New York*, NEWS10NBC (last updated Apr. 27, 2023, 7:07 PM), https://www.whec.com/top-news/consumer-alert-got-a-bad-credit-score-you-pay-much-more-for-car-insurance-in-new-york.

73. FED. TRADE COMM'N, CREDIT-BASED INSURANCE SCORES: IMPACTS ON CONSUMERS OF AUTOMOBILE INSURANCE 3 (2007), https://www.ftc.gov/sites/default/files/documents/reports/credit-based-insurance-scores-impacts-consumers-automobile-insurance-report-congress-federal-trade/p044804facta_report_credit-based_insurance_scores.pdf.

74. Lyn Hunstad, Robert Bernstein & Jerry Turem, Executive Summary, *Impact Analysis of Weighting Auto Rating Factors to Comply with Proposition 103*, CAL. DEP'T OF INS. (Dec. 1994), https://www.insurance.ca.gov/0400-news/0200-studies-reports/0600-research-studies/auto-policy-studies/executive-summary.cfm.

75. Daniel Robinson, *What Is Telematics Insurance?*, MARKETWATCH GUIDES (Aug. 21, 2024), https://www.marketwatch.com/guides/insurance-services/telematics-insurance.

In July 2009, CDI adopted an amendment to the state insurance code that permitted the use of telematics devices to verify mileage for the purpose of advertised "pay per mile" rates.[76] But other regulations in the California code limit the ability to use telematics to offer "pay-how-you-drive" products that have become popular in other jurisdictions. For example, insurers are currently prohibited from collecting vehicle location information, which rules out rating on the basis of driving in congested areas.[77] Moreover, because the regulations do permit rating on the basis of the severity and frequency of accidents in the ZIP code where a vehicle is garaged,[78] identical drivers who spend equivalent time driving in congested areas may be charged different rates, with a suburban commuter earning a discount relative to an urban commuter.

Research by Jason E. Bordoff & Pascal J. Noel finds that generally low-mileage drivers cross-subsidize high-mileage drivers,[79] and that about 64% of Californians would save money if they switched to a per-mile plan.[80] The president of the California Black Chamber of Commerce has also argued that telematics offers a potential solution to problems of bias in underwriting, given evidence that drivers from predominantly African-American communities are quoted premiums that are 70% higher than similarly situated drivers in predominantly white communities.[81]

> "By voluntarily downloading an app to their smartphone, a driver agrees to allow an insurer to measure data about (and only about) their driving habits. This includes behaviors like hard braking and distracted driving. Based on that data an insurance company can assess how much of a risk the driver poses and offer fair insurance, free of bias and inflation, that the driver may choose to purchase."[82]

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76. CAL. CODE REGS. tit. 10, § 2632.5 (West 2024).

77. *Id.* § 2632.5(c)(2).F.5.B.

78. *Id.* § 2632.5(d)(15).

79. Jason E. Bordoff & Pascal J. Noel, *Pay-As-You-Drive Auto Insurance: A Simple Way to Reduce Driving-Related Harms and Increase Equity*, BROOKINGS INST. (July 25, 2008), https://www.brookings.edu/articles/pay-as-you-drive-auto-insurance-a-simple-way-to-reduce-driving-related-harms-and-increase-equity.

80. Jason E. Bordoff & Pascal J. Noel, *The Impact of Pay-As-You-Drive Auto Insurance in California*, BROOKINGS INST. (July 31, 2008), https://www.brookings.edu/articles/the-impact-of-pay-as-you-drive-auto-insurance-in-california.

81. Edwin Lombard III, *Telematics: A Tool to Curb Auto Insurance Discrimination*, CAPITOL WEEKLY (Feb. 18, 2020), https://capitolweekly.net/telematics-a-tool-to-curb-auto-insurance-discrimination.

82. *Id.*

III. PROP 103 RATE REVIEW IN PRACTICE

Dynamic aspects of insurance loss events and claim costs impose expenses on insurers if they cannot respond nimbly in matching rate to risk. Prop 103 and similar approaches to price regulation restrain insurers' ability to adjust to new information, thereby causing an increase in price, a decrease in availability, or both. Rate suppression occurs when regulators deny rate filings that request adequate and non-excessive rates. Examples of extreme rate suppression have rarely lasted very long. Insurers exit suppressed markets, leaving consumers with fewer choices and higher prices.

While the last section examined some of the high-level issues created by the Prop 103 system, in this section we draw from empirical data and recent legal precedent to demonstrate how the Prop 103 process, as applied by the CDI, has amplified these dislocations in ways that have proven extraordinarily counterproductive.

A. RATEMAKING AS MARKET-CONDUCT EXAMINATION

Filing for rates under Prop 103 is a complex and costly enterprise. The discretion that CDI maintains and the ever-present risk of intervention by third parties means that swift and predictable resolution is the exception, not the rule.

Further complicating ratemaking in California is the intrinsically political nature of the relationship between the insurance commissioner and its regulated entities. California's commissioner is one of eleven state insurance regulators in the United States to face direct election.[83] Thus, particularly in times of market strain or when policyholders are confronted with availability challenges or rate increases, the commissioner faces political incentives to pressure insurers to acquiesce to popular—if not market-based—demands. As a result, the ratemaking process can be misused as a proxy venue for larger ongoing disputes between the commissioner and insurers. Two recent cases highlight this phenomenon.

1. Rulemaking by ratemaking proceeding

State Farm General (SFG)—a California entity separate from the larger State Farm Mutual, which was established to cover non-automobile lines—sought a rate increase of 6.9% in 2015. Consumer Watchdog

83. *Insurance Commissioner (State Executive Office)*, BALLOTPEDIA, https://ballotpedia.org/Insurance_Commissioner_(state_executive_office) (last visited Aug. 16, 2023).

intervened, CDI rejected the proposed increase, and the matter went to a hearing before a CDI administrative-law judge. The department's hearing officer subsequently issued a far-reaching opinion, which was adopted by the commissioner, ordering SFG to retroactively reduce its rates and issue refunds. This sweeping order was based on a novel reading of Prop 103 that erased the difference between the balance sheets of a particular insurer and the larger group of which it is a part for purposes of ratemaking.

Faced with a foundational reinterpretation of insurance law created in the process of seeking a rate, SFG appealed to California courts, where it ultimately prevailed after a years-long protracted lawsuit and subsequent CDI appeal.[84]

While resolving open questions about a state's rate-making process is appropriate fodder for any department to undertake, the broader context in which then-Insurance Commissioner Dave Jones—who launched what would ultimately be a failed bid to be elected California's attorney general in 2018[85]—pursued the action against SFG speaks to a different motivation. Indeed, SFG had just, one year prior, sought and received a rate increase using the same formula subsequently rejected by CDI.[86] To wit, the basis of CDI's resistance was not the degree of the rate increase in question but was instead premised upon a broader question of law.

CDI has broad rulemaking authority and, when necessary, can seek legislative amendment to ensure that the laws governing ratemaking protect California consumers.[87] But the department also retains substantial leverage to secure acquiescence from insurers when it pursues novel ratemaking interpretations in the context of a particular rate application. This approach may be effective, but it frustrates well-established norms for creating rules of general applicability and deprives the industry as a whole of due process. Worse still, when it engages in facial abuses of its already broad discretion, the CDI undermines the Prop 103 ratemaking system's ability to prevent dislocation between price and risk.

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84. State Farm General Insurance Company v. Lara et al., 286 Cal. Rptr. 3d 124 (2021).

85. Jeff Daniels, *Becerra, Incumbent California Attorney General and Legal Thorn to Trump, to Face GOP Challenger Bailey in Fall General Election*, CNBC (last updated June 6, 2018, 7:46 PM), https://www.cnbc.com/2018/06/06/becerra-california-attorney-general-to-face-gop-rival-bailey-in-fall.html.

86. *SERFF Filing Access - California*, SERFF (last accessed Dec. 9, 2024) (Search by SERFF Tracking Number SFMA-129138676).

87. *Rulemaking Process*, CAL. DEP'T OF INS. (Aug. 2018), https://www.insurance.ca.gov/0250-insurers/0500-legal-info/0200-regulations/rule-making-process.cfm.

2. Corporate governance by ratemaking proceeding

The ratemaking process under Prop 103 is likewise susceptible to being used to direct the behavior of firms beyond the scope of ratemaking itself. Predictably, delays in ratemaking proceedings on account of nonprice factors trigger the same market-skewing dynamics and due-process issues discussed above. Intervenors like Consumer Watchdog have sought, for example, to prevent Allstate from receiving a mere 4% rate increase in its homeowners book on the basis of the firm's decision to limit its exposure to the California market more broadly.[88] In that case, the long-time intervenor alleged that ceasing to sell insurance—an underwriting determination—has an impact on rates and that as a result, the decision to cease offering coverage is itself a ratemaking action demanding review by the California Department of Insurance.[89]

To its credit, the department maintained that inactivity by a business does not constitute the use of an unapproved rate.[90] But Consumer Watchdog's broad reading of the acceptable scope of matters judicable in a ratemaking proceeding is no doubt borne directly of previous experiences in which insurers were made to acquiesce to demands related to business practices more broadly.

B. PROP 103'S DEAD LETTER DEEMER

Rate-approval delays have become a hallmark of the Prop 103 system, as well as the resulting asymmetry between rate and risk. But as originally presented to California voters, the law envisioned that rates would be deemed accepted if no action were taken by the CDI for 60 or 180 days.[91] Indeed, Prop 103 included this "deemer" provision because a reasonable speed-to-market for insurance products also protects consumers.

The law's deemer provision has been effectively rendered moot in practice because, as a matter of course, the CDI requests that firms waive the deemer.[92] If the deemer is not waived, the CDI has two options: approve the rate or issue a formal notice of hearing on the rate proposal. Because the CDI

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88. Harvey Rosenfield, *Allstate's $16M Homeowners Rate Hike Approved Despite Company Secretly Ending Sales of New Home Insurance in California*, CONSUMER WATCHDOG (June 13, 2023), https://consumerwatchdog.org/insurance/allstates-16m-homeowners-rate-hike-approved-despite-company-secretly-ending-sales-of-new-home-insurance-in-california.

89. *Id.*

90. *Id.*

91. CAL. INS. CODE §1861.05(d) (West 2024).

92. CAL. DEP'T OF INS, *supra* note 43.

is unable to complete timely review of filings within the deemer period, it always elects to move to a rate hearing.[93] In effect, CDI turns every rate filing without a deemer waiver into an "extraordinary circumstance."[94]

In practice, it has proven exceedingly challenging for petitioners to navigate the manner in which rate hearings—the nominal guarantors of due process—are conducted. The administrative law judges (ALJs) that oversee these proceedings are housed within the CDI.[95] The hearings themselves take a broad view of relevance that drives up the cost of participation. Upon ALJ resolution, the commissioner can accept, reject, or modify the ALJ's finding. There is little practical upside for an insurer to move to a hearing against the CDI.

Wawanesa General Insurance Company offers a case study of the differences between how Prop 103 was drafted and the way it is currently enforced. After initially waiving the law's deemer, Wawanesa reactivated the deemer in a 2021 private-passenger auto filing.[96] In so doing, Wawanesa elected to move to a hearing by the CDI. From start to finish, its December 2021 rate filing was not approved until March 2023—fifteen months after it was brought forward.[97] Ultimately, unable to get the rate it needed in a timely manner, Wawanesa's U.S. subsidiary was acquired by the Automobile Club of Southern California.[98]

Thus, in practice, insurers are faced with a starkly practical choice. One option is to waive their right to timely review of rates and hope that they gain approval in, on average, six months. The alternative is to move to a formal hearing and reconcile themselves with the fact that approval, if forthcoming, will take at least a year. The system of due process originally contemplated by Prop 103 simply bears no relationship with the system as it operates today.

Figure II shows the average number of days between submission and resolution of rate filings in each state (including the District of Columbia as a state, for these purposes). With a five-year average filing delay of 236 days for homeowners insurance and 226 days for auto insurance, California ranks fiftieth in each category, responding more slowly than all states except

93. *Id.*

94. CAL. INS. CODE §1861.05(d) (West 2024).

95. *Administrative Hearing Bureau*, CAL. DEP'T OF INS., https://www.insurance.ca.gov/0500-about-us/02-department/010-ahb/.

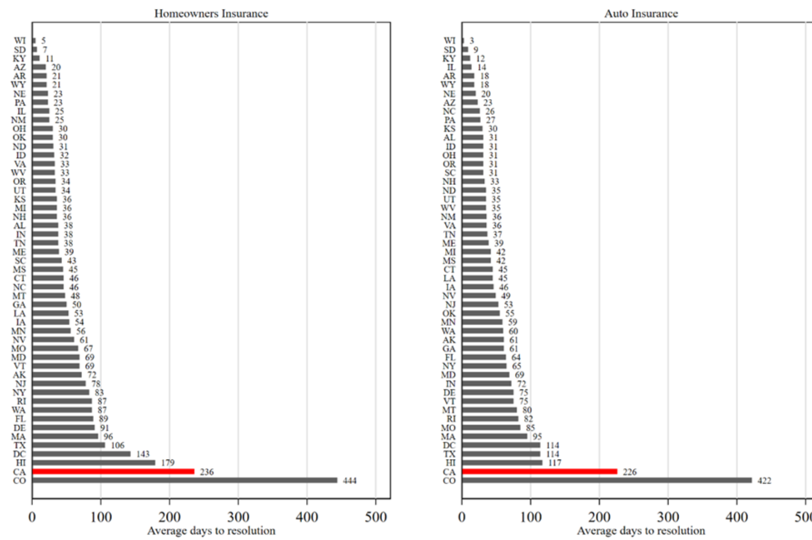
96. *SERFF Filing Access - California*, SERFF (last accessed Dec. 4, 2024) (Search by SERFF Tracking Number WAWA-133081408).

97. *Id.*

98. Press Release, Wawanesa Ins., Auto Club to Acquire the U.S. Subsidiary of Wawanesa Mutual (Aug. 1, 2023), https://www.wawanesa.com/canada/news/auto-club-acquires-wawanesa-general.

Colorado. Although the average delay is affected somewhat by extreme-outlier observations, California's rank is unchanged if we instead use the median delay.[99]

FIGURE II: Average Days to Resolution of Rate Filings by State, 2018-2022



SOURCE: *SERFF Rate Filing Data From S&P Capital*[100]

Another troubling aspect of California's sluggish regulatory system is that it appears to be getting slower over time. Obviously, California has been relatively slow to resolve rate filings since Prop 103 took effect.[101] In recent years, however, the average delay has increased, as wildfire losses and market conditions (e.g., inflation and the cost of capital) have increased the cost of providing insurance. Figure III shows the annual average number of days between filing and resolution of rate changes for homeowners insurance

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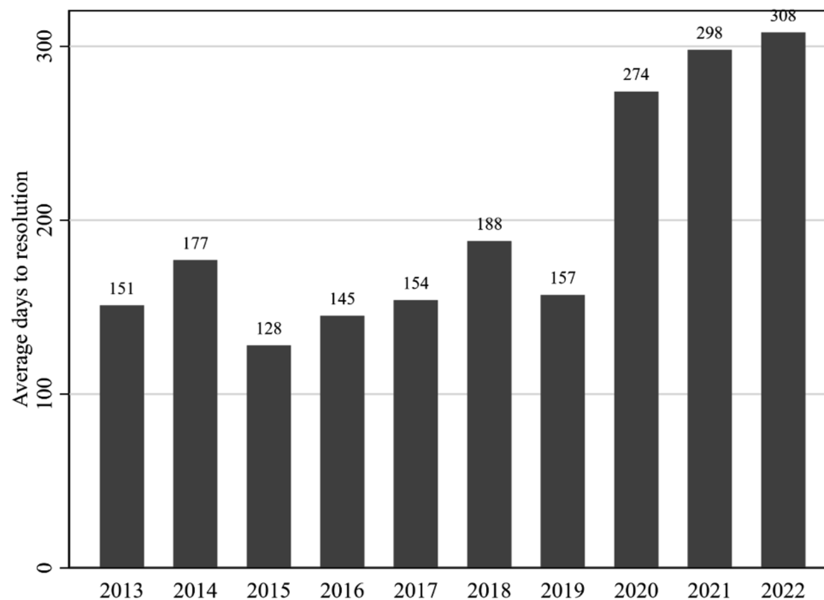
99. The median delay for homeowners rate filings in California is 198 days. For auto insurance rate filings, it is 185.5 days.

100. S&P CAPITAL IQ, SERFF RATE FILING DATA, AVERAGE DAYS TO RESOLUTION OF RATE FILINGS BY STATE (2018-2022).

101. *Id.*

in California.[102] The average delay from 2013 to 2019 was 157 days. For the last three years, the average delay has increased to 293 days.[103]

FIGURE III: California Homeowners Insurance Rate Filing Delays, 2013-2022



SOURCE: *SERFF Rate Filing Data From S&P Capital*[104]

C. THE INTERVENOR PROCESS

CDI's ability to review rate filings in a timely manner is further constrained by Prop 103's intervenor process. Intervenors are granted petitions to intervene, as a matter of right, on any rate filing. Personal-lines filings that request a rate increase of 6.9% or more (or 14.9% or more in commercial-lines filings) are subject to mandatory hearings, if requested, while the decision to grant hearings for those filings below 6.9% (or 14.9% for commercial lines) is at the commissioner's discretion.[105] Naturally, many personal lines

102. S&P CAPITAL IQ, SERFF RATE FILING DATA, CALIFORNIA HOMEOWNERS INSURANCE RATE FILING DELAYS (2013-2022).

103. *Id.*

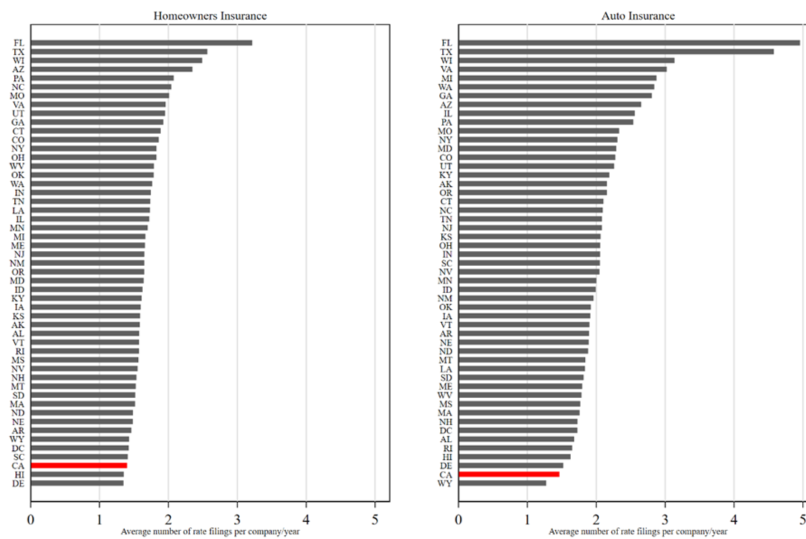
104. *Id.*

105. Brett Horoff, *How to Navigate the California Rate Filing Environment*, PERR KNIGHT, https://www.perrknight.com/2023/07/10/navigate-the-california-rate-filing-environment/ (last visited Nov. 29, 2024).

insurers opt to file below that threshold even if they actually require rate increases substantially in excess of 6.9%, simply to avoid dealing with intervenors (although many rate filings at or below 6.9% do also have intervenors).

The intervenor process has proven both costly and time-consuming. According to CDI data, since 2003, intervenors have been paid $23,267,698.72, or just over $1 million annually, for successfully challenging 178 filings.[106] While the process results in CDI receiving more filings to review than it otherwise would, the total number of filings it must review is significantly less than other jurisdictions (see Figure IV).[107]

FIGURE IV: Average Number of Rate Filings Per-Company by State, 2018-2022



SOURCE: *SERFF Rate Filing Data From S&P Capital*[108]

Intuitively, we can assume that states cannot change rates as frequently when rate filings take longer to resolve. Figure IV confirms this assumption, demonstrating the average number of rate filings made per-

106. *Informational Report on the CDI Intervenor Program*, CAL. DEP'T OF INS., https://www.insurance.ca.gov/01-consumers/150-other-prog/01-intervenor/report-on-intervenor-program.cfm (last accessed Aug. 15, 2023) (data obtained by gathering the total number of intervenor filings and total compensation awarded to intervenors from 2003–2023).

107. S&P CAPITAL IQ, SERFF RATE FILING DATA, AVERAGE NUMBER OF RATE FILINGS PER-COMPANY BY STATE (2018-2022).

108. *Id.*

company in each state for homeowners and automobile insurance from 2018 to 2022.[109] Over the last five years, California ranked forty-ninth in the number of homeowners insurance rates filed, and fiftieth in the number of auto insurance rates filed.[110]

D. Rate Suppression Under Prop 103

While a slow regulatory system limits the efficiency of insurance markets, a system that suppresses rates will also inhibit the deployment of capital, ultimately reducing the number of insurers who choose to participate.

For example, if an insurer's rate analysis indicates that a 40% increase is required for rates to be adequate, and the regulator instead approves only a 15% increase, the effect of rate suppression is (40%–15%=) 25%. In this category, California again ranks fiftieth, approving rates that are, on average, 29% (homeowners) and 14% (auto) less than the actuarially indicated rate supported by the analysis in the filing.[111]

Figure V, which measures the difference between the actuarially indicated rate and the rate approved by regulators, demonstrates that California's regulatory system under Prop 103 is suppressive.[112] Although it is common for insurers to request rate changes below the indicated rates for strategic reasons, the measure would not differ consistently across states in the absence of suppressive rate regulation.

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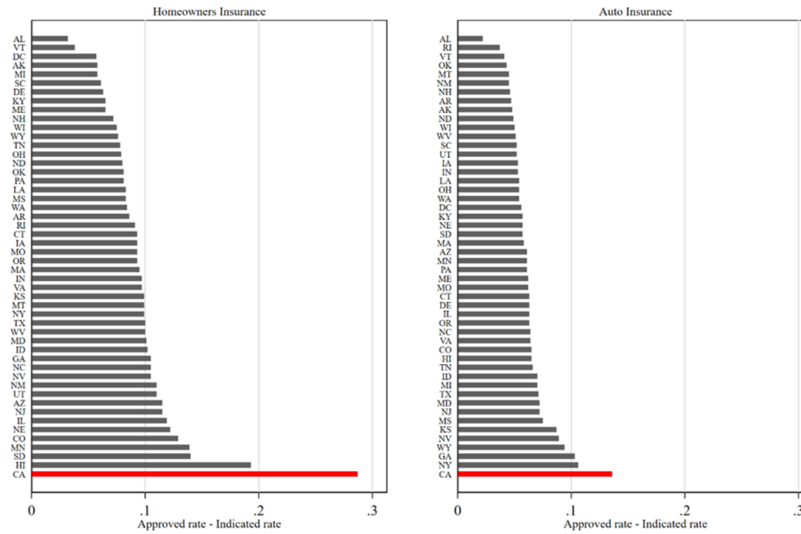
109. *Id.*

110. *Id.*

111. Data from Florida are not available for this measure; therefore, California ranks 50th out of 50 jurisdictions.

112. S&P Capital IQ, SERFF Rate Filing Data, Regulatory Rate Suppression by State (2018-2022).

FIGURE V: Regulatory Rate Suppression by State, 2018-2022



SOURCE: *SERFF Rate Filing Data From S&P Capital. Florida data are unavailable*.[113]

Similar to the growing chasm of filing delays observed in Figure III, Figure VI shows that rate suppression in California homeowners insurance has risen in response to the unprecedented wildfire losses incurred in 2017 and 2018. Although the level of rate suppression moderated somewhat in 2022, the average level of regulatory rate suppression for 2013 through 2018 was 18%, while the average for 2019 through 2022 was 30%.[114] Moreover, at 14.5% in 2022, California is more than one standard deviation (3.6%) above the mean (9.8%) and ranks forty-fifth among the fifty jurisdictions reporting data.[115]

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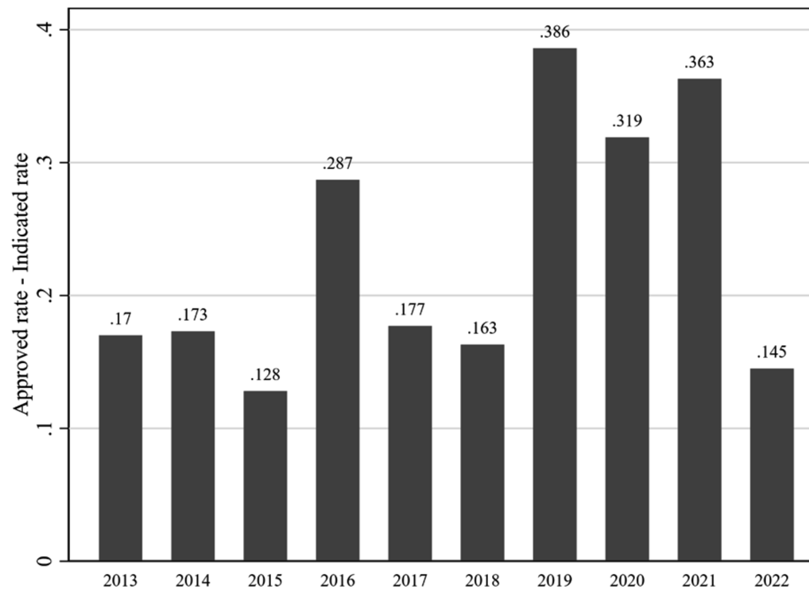
113. *Id.*

114. S&P CAPITAL IQ, SERFF RATE FILING DATA, RATE SUPPRESSION IN CALIFORNIA HOMEOWNERS INSURANCE (2013-2022).

115. *Id.*

FIGURE VI: Rate Suppression in California Homeowners Insurance, 2013-2022



SOURCE: *SERFF Rate Filing Data From S&P Capital*.[116]

In summary, the rate filing data clearly show that California's regulatory system under Prop 103 is expensive, slow, and currently causing unsustainable rate suppression, especially in the homeowners line.

IV. THE IMPACT OF PROP 103 ON OTHER STATES

Some of Prop 103's effects have arguably spilled over to other jurisdictions, either directly—via states adopting similar regulatory regimes—or indirectly. Recent research by Sangmin S. Oh, Ishita Sen, & Ana-Maria Tenekedjieva suggests that there is a significant indirect effect in the form of rate suppression in California and other "high-friction" states leading to cross-subsidies among policyholders of multi-state insurers and, ultimately, "distortions in risk sharing across states."[117]

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116. *Id.*

117. Sangmin S. Oh, Ishita Sen & Ana-Maria Tenekedjieva, *Pricing of Climate Risk Insurance: Regulation and Cross-Subsidies,* SSRN 3 (Jan. 15, 2021), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=3762235.

> "First, rates have not adequately adjusted in response to the growth in losses in states we classify as "high friction", i.e. states where regulation is most restrictive. Second, in low friction states rates increase both in response to local losses as well as to losses from high friction states. Importantly, these spillovers are asymmetric: they occur only from high to low friction states, consistent with insurers cross-subsidizing in response to rate regulation. Our results point to distortions in risk sharing across states, i.e. households in low friction states are in-part bearing the risks of households in high friction states."[118]

In other cases, the impact of Prop 103 has largely taken the form of political influence. As demonstrated in the previous section, states like Colorado, Maryland, and Hawaii have followed California's model of extended rate-review processes that significantly slow product approvals.

Among the first states to respond to Prop 103 with its own similar regulatory system was New Jersey, which in 1990 passed the Fair Automobile Insurance Reform Act. Under the terms of the law, effective April 1992, every admitted writer of automobile insurance in the state would be required to offer coverage for all eligible persons, with only a select group of motorists—including those convicted of driving under the influence or other automobile-related crimes, those whose licenses had been suspended, those convicted of insurance fraud, and those whose coverage had been canceled for nonpayment of premium—deemed ineligible.[119]

While the law nominally permitted insurers to earn an "adequate return on capital" of 13%, several companies would sue the state on grounds that the New Jersey Department of Banking and Insurance did not approve rate requests sufficient to meet that threshold.[120] In addition, the state assessed surcharges on insurers to close a $1.3 billion funding gap for the state's Joint Underwriting Authority.[121]

As in California, New Jersey saw the exit of twenty insurers from the state's auto insurance market in the decade after the Fair Automobile

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118. *Id.*

119. N.J. ADMIN. CODE § 11:3–33 app. A (2024).

120. *High Court Upholds N.J. Surcharges on Insurers*, A.M. BEST CO. (Mar. 19, 1996, 8:48 AM), https://news.ambest.com/newscontent.aspx?altsrc=108&refnum=16894.

121. Anthony Gnoffo Jr., *NJ, Insurers Near Deal to Close State Fund Gap*, J. COM. (May 31, 1994, 8:00 PM) https://www.joc.com/article/nj-insurers-near-deal-to-close-state-fund-gap-5420463.

Insurance Reform Act's passage.[122] When the state later liberalized its regulatory system with the passage of the Auto Insurance Reform Act in June 2003, the number of auto writers more than doubled from seventeen to thirty-nine, and thousands of previously uninsured drivers entered the system.[123]

A similar effect was seen in South Carolina, where a restrictive rating system in the 1990s had forced 43% of drivers into residual market policies undergirded by a state-run reinsurance facility.[124] After adopting a liberalized flex-band rating law in 1999, as in New Jersey, the number of insurers offering coverage in South Carolina doubled,[125] the residual market shrank (it is, today, only 0.016% of the market),[126] and overall rates actually fell.[127]

Even in Massachusetts, which retains a fairly restrictive rate-approval process, reforms passed in April 2008 to allow insurers to submit competitive rates (they were previously set by the commissioner for all carriers) had a notable impact.[128] Within two years of the reforms, rates had fallen by 12.7% and a dozen new carriers began offering coverage in the state.[129] Because it is still a very regulated state, Massachusetts still has a relatively large residual market. According to data from the Automobile Insurance Plan Service Office (AIPSO), in 2023, 4.38% of Massachusetts auto insurance customers had to resort to the residual market, the second-highest rate in the

122. Sharon L. Tennyson, Policy Brief, *Efficiency Consequences of Rate Regulation in Insurance Markets*, NETWORKS FIN. INST., Mar. 2007, at 16, https://papers.ssrn.com/sol3/papers.cfm?abstract_id=985578.

123. *Id.*

124. Martin F. Grace, Robert W. Klein & Richard W. Phillips, *Auto Insurance Reform: The South Carolina Story*, GA. STATE UNIV. CTR. FOR RISK MGMT. AND INS. RSCH. 2, 3 (2001), https://citeseerx.ist.psu.edu/document?repid=rep1&type=pdf&doi=bae61c3c10a95b535a11c83094abea0be16fa05a.

125. Tennyson, *supra* note 122.

126. *Ranking of States by Residual and Total Market Premium*, AUTO. INS. PLAN SERV. OFF. (2023), https://www.aipso.com/Industry-Data (Follow "Written Premiums" tab and select "Ranking of States by Residual and Total Market Premium" under "Annual Charts and Tables" to access raw data).

127. R.J. Lehmann, *Illinois Considers Slaughtering the Golden Goose of Competition*, INS. J. (Mar. 7, 2023), https://www.insurancejournal.com/blogs/law-and-economics/2023/03/07/710942.htm.

128. AUTOMOBILE INSURANCE: THE ROAD AHEAD, OFFICE OF ATTORNEY GENERAL MARTHA COAKLEY (2009), https://www.mass.gov/doc/autoinsuranceexecsummarypdf/download.

129. Jim Kinney, *Massachusetts Auto Insurance Deregulation Brought Variety, Lower Prices, National Association of Insurance Commissioners Says*, MASSLIVE (Jan. 18, 2012, 11:45 PM), https://www.masslive.com/business-news/2012/01/massachusetts_auto_insurance_deregulatio.html.

nation.[130] But before 2008, Massachusetts' residual-market share was routinely in the double digits.[131]

While those states that have opted to copy the California model have largely lived to regret it, others continue to explore the imposition of Prop 103-like regimes. Oregon lawmakers, for example, have repeatedly put forward legislation that would place the insurance industry under the state's Unlawful Trade Practices Act, granting customers the right to sue for damages beyond the face value of their policies and third parties to bring private rights of action against insurers with whom they have no contractual relationship.[132]

But perhaps the most notable recent proposal to shift to a Prop 103-like system is Illinois' H.B. 2203,[133] which would effectively transform the state from the most open and competitive insurance market in the country to one of the most restrictive. If approved, the legislation would require every insurer seeking to offer private passenger motor vehicle liability insurance in the state to file a complete rate application with the Department of Insurance, which once again would be empowered to approve or disapprove rates on a prior-approval basis.[134] The bill also would prohibit insurers from setting rates based on any "nondriving" factors, including credit history, occupation, education, and gender.[135]

As in California, the measure would also create a new system for public intervenors in the ratemaking process, stipulating that "any person may initiate or intervene in any proceeding permitted or established under the provisions and challenge any action of the Director under the provisions."[136]

Illinois is currently somewhat of an outlier in effectively having no formal rate-approval process at all. In 1971, the Illinois General Assembly neglected to extend legislation enacted a year earlier to create a "file-and-use"

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130. AUTO. INS. PLAN SERV. OFF., *supra* note 126.

131. *Residual Markets*, INSURANCE INFORMATION INSTITUTE (Dec. 2006), https://portal.ct.gov/-/media/cid/app12itt2006pdf.pdf#:~:text=market%20was%20North%20Carolina%2C%20at%2024%20percent%2C,premiums%20ends%20up%20in%20the%20residual%20market.

132. Nigel Jaquiss, *Oregon Lawmakers Will Try Again to Bring Insurers Under the State's Unlawful Trade Practices Act*, WILLAMETTE WEEK (Mar. 1, 2023, 6:45 AM), https://www.wweek.com/news/2023/03/01/oregon-lawmakers-will-try-again-to-bring-insurers-under-the-states-unlawful-trade-practices-act; Background Brief, *The Unlawful Trade Practices Act*, OREGON STATE LEGISLATURE 1, 3 (Feb. 2017), https://www.oregonlegislature.gov/lpro/Publications/BB2016TheUnlawfulTradePracticesAct.pdf.

133. Motor Vehicle Insurance Fairness Act, H.B. 2203, 103d Gen. Assemb. (Ill. 2023).

134. *Id.*

135. *Id.*

136. *Id.*

system, and the state has continued on without any insurance rating law for more than half a century.[137]

V. ESTIMATING THE COST OF PROP 103 IN CALIFORNIA AND OTHER STATES

For the last two decades, proponents of Prop 103 have asserted that the ballot measure saved Californians as much as $154 billion in auto insurance premiums from 1989 to 2015. Further, they claim that other states could have saved nearly $60 billion per-year over the same period by adopting insurance regulations similar to Prop 103.[138] As David Appel has noted, the analysis supporting these claims is flawed.[139] In the twenty years since industry critics began making this claim, however, no one has performed the correct analysis. Here, we perform an object analysis and draw dramatically different conclusions.

The analyses performed and cited by Prop 103's proponents assume that insurance premiums are a function of the prior year's premiums.[140] This approach is invalid because insurance premiums are instead a function of expected losses. For example, if a policy covering a $200,000 house has a lower premium than a policy covering a $500,000 house, that alone would not tell us whether the first policy is a better deal than the second. Equivalently, we

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137. Jon S. Hanson, *The Interplay of the Regimes of Antitrust, Competition, and State Insurance Regulation on the Business of Insurance*, 28 DRAKE L. REV. 767, 841 (1978–1979).

138. J. ROBERT HUNTER & DOUGLASS HELLER, AUTO INSURANCE REGULATION WHAT WORKS 2019: HOW STATES COULD SAVE CONSUMERS $60 BILLION A YEAR, CONSUMER FED'N OF AM. (Feb. 11, 2019), https://consumerfed.org/wp-content/uploads/2019/02/auto-insurance-regulation-what-works-2019.pdf.

139. DAVID APPEL, MILLIMAN INC., REVISITING THE LINGERING MYTHS ABOUT PROPOSITION 103: A FOLLOW-UP REPORT 11 (Sept. 2004), https://www.namic.org/wp-content/uploads/legacy/040921AppelFinalRpt.pdf; DAVID APPEL, MILLIMAN INC., ANALYSIS OF THE CONSUMER FEDERATION OF AMERICA REPORT "WHY NOT THE BEST" 2 (Dec. 2001), https://www.namic.org/pdf/01PolPaperAppelCFA.pdf; David Appel, *Comment on Chapter 5* in DWIGHT M. JAFFEE & THOMAS RUSSELL, DEREGULATING PROPERTY LIABILITY INSURANCE 238 (J. David Cummins ed., 2002).

140. JAFFEE & RUSSELL, *supra* note 46, at 195; J. ROBERT HUNTER, TOM FELTNER & DOUGLAS HELLER, CONSUMER FED'N OF AM., WHAT WORKS: A REVIEW OF AUTO INSURANCE RATE REGULATION IN AMERICA AND HOW BEST PRACTICES SAVE BILLIONS OF DOLLARS (Nov. 2013), http://consumerfed.org/wp-content/uploads/2010/08/whatworks-report_nov2013_hunter-feltner-heller.pdf; *see also* Hunter & Heller, *supra* note 138.

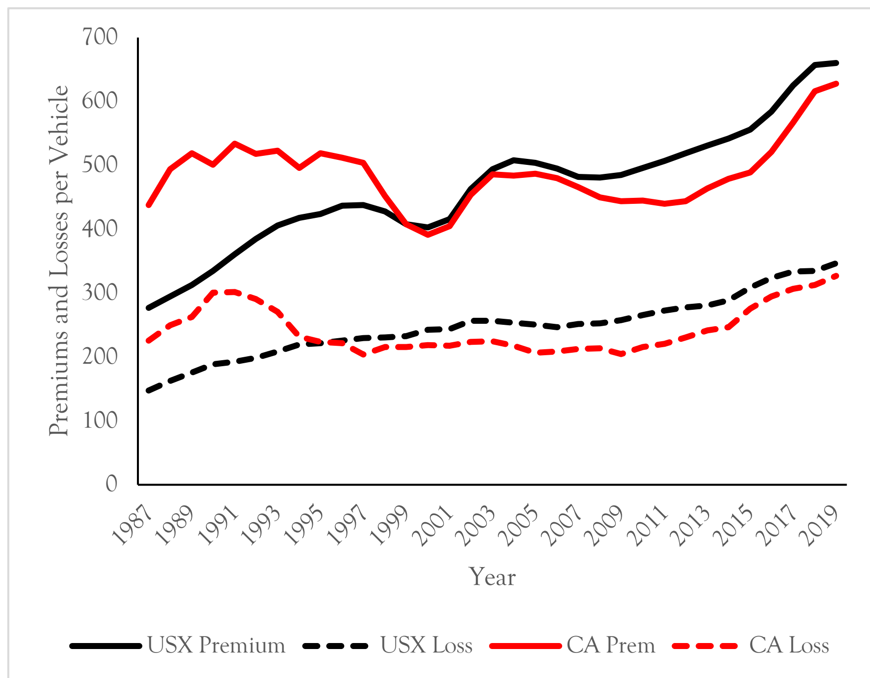
cannot tout the value of automobile insurance without comparing premiums to losses.

Figure VII shows that premiums in California and in other states (USX) largely follow losses.[141] Moreover, when insurance companies make rate filings asking state insurance departments to approve new rates, regulators evaluate them based on their similarity to past losses and loss trends. Therefore, a more appropriate method of creating a counterfactual comparing the results obtained under one state's regulatory approach to the insurance premiums that would be generated in other states is to apply the ratio of premiums to losses from one state to the losses of the other states, as in Equation 1:

$$\frac{Premium_{CA}}{Losses_{CA}} \times Losses_{USX} = USX\ Premium_{CA} \text{ Eq. (1)}$$

Where $USX\ Premium_{CA}$ is the estimate of USX premiums if we impose the effects of California's price controls on the rest of the country.

Figure VII: Premiums and Losses in California and the US, 1987-2019



141. FASTTRACK MONITORING SYSTEM, PREMIUMS AND LOSSES IN CALIFORNIA AND THE US (1987-2019).

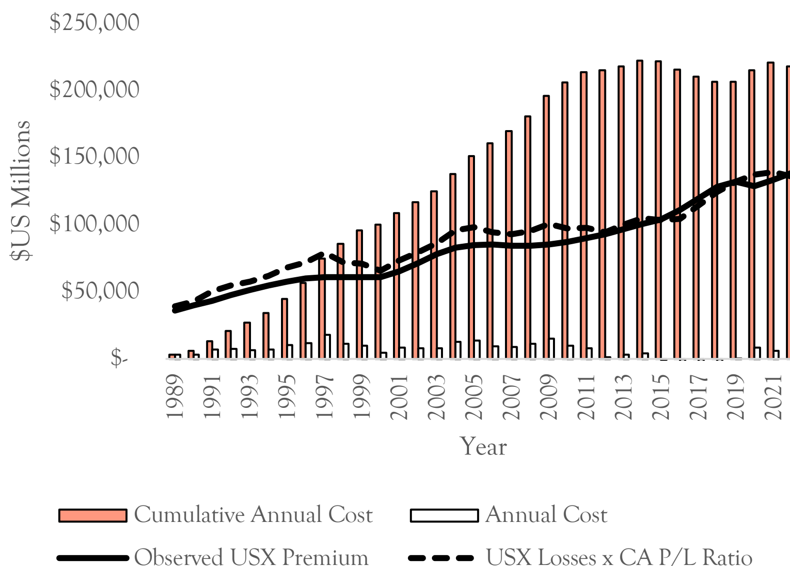
NOTES: *Premiums and losses are from liability coverage only. "USX" represents data from all states except for California. Data are from the FastTrack Monitoring System.*[142]

Figure VIII shows the results from solving Equation 1. In stark contrast to claims made by proponents of Prop 103, we find that if the rest of the country (USX) had passed Prop 103 in 1989, consumers would have paid more than $218 billion in additional auto insurance premiums. Likewise, results from solving Equation 2:

$$\frac{Premium_{USX}}{Losses_{USX}} \times Losses_{CA} = CA\ Premium_{USX} \quad \text{Eq. (2)}$$

Where $CA\ Premium_{USX}$ is the estimate of California premiums if we remove the effects of Prop 103 on California, indicate that Californians would have saved nearly $25 billion if they had not passed Prop 103. In light of these findings, regulators should be appropriately skeptical of claims that price controls reduce insurance premiums.

Figure VIII: California P/L Ratio for USX Losses



142. *Id.*

NOTES: *Observed USX Premium is total private-passenger automobile premium written in the United States, excluding California. USX Losses x CA P/L Ratio is USX losses multiplied times California premiums/losses in each year. Annual Additional Premium is USX Losses x CA P/L Ratio minus Observed USX Premium. Cumulative Additional Premium sums Annual Additional Premium across years. Data are from NAIC Statements, 1989 through 2022.*[143]

VI. RECOMMENDED REFORMS

It is difficult, but not impossible, to amend Prop 103. Indeed, many reforms may be enacted by updating administrative interpretation alone. What follows is, first, a list of reforms that CDI could champion (some of which are included, in varying forms, in Commissioner Lara's emergency plan) to improve speed-to-market, procedural predictability, and rate accuracy. Second, is a list of structural reforms that would require legislative approval.

A. Interpretive Reforms

1. Fast-track noncontroversial filings

As discussed above, Prop 103 grants CDI discretion on whether to convene public hearings on rate changes of less than 7% for personal lines or 15% for commercial lines.[144] When the commissioner grants such hearings it adds expense, administrative burden, and delays to very modest changes in product offerings. Not only is this problematic as a matter of substance, but the data on delays in rate filing approvals demonstrate that CDI is routinely violating the explicit text of Prop 103 which requires that "a rate change application shall be deemed approved 180 days after the rate application is received by the commissioner" unless the commissioner either rejects the filing or there are "extraordinary circumstances."[145] CDI not only can, but must, act to uphold this provision of the law.

To do so, the CDI should entertain adopting a rate-approval "fast lane" premised on firms submitting filings that use actuarial judgments that embrace consumer-friendly assumptions. That is, if a filing is made on the basis of the least-inflationary or least-aggressive loss development assumptions, CDI should undertake a light touch review focused on rate sufficiency

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143. NAIC, California Premium Loss Ratio for US Losses (1989-2022).

144. Consumer Watchdog, *supra* note 10.

145. *Id.*

to expedite the approval process. This approach has the benefit of increasing both the predictability and speed of the ratemaking process.

2. Refocus rate proceedings

If CDI were to adopt a narrower reading of the universe of rate-related issues appropriate for adjudication in a ratemaking proceeding it would have the important benefit of limiting the universe of issues susceptible to controversy. In doing so, insurers and the department would be better able to focus on the resolution of rate applications in a timely manner that allows price to reflect risk. Relatedly, the department should continue to constrain intervenors from conflating rate-related and non-rate-related issues in the service of broader policy objectives.

3. Transparency

There is no single cause for California's substantial delay in approving rates, but it is clear that the state's unique intervenor system shapes both insurer and CDI behavior in ways that were not immediately cognizable when the law was adopted. One way to ensure that speed-to-market improves over the long term is to better understand the value that intervenors offer, and to ensure that intervenor engagement is both efficient and effective.

At the moment, CDI publishes quantitative data concerning intervenor compensation and rate differentiation in intervenor proceedings.[146] While this is helpful in conveying the scope of intervenor efforts, the data fails to capture the value actually provided by intervenors in the ratemaking process. The qualitative contribution made by intervenors is obscured by the fact that none of their filings appear publicly on SERFF. Not only is this an aberration relative to other proceedings before the CDI, but there could be significant value in getting greater transparency from the intervenor process given the delays and direct costs related to intervention.

For one, allowing the Legislature and the public to assess the substantive value of intervenor contributions would ensure not only substantial due-process protections for filing entities, but would also ensure that consumers are afforded a high level of representation in proceedings. For instance, such transparency would function as a guarantor that intervenor filings are not otherwise duplicative of CDI efforts. It would therefore allow the public to assess whether intervenors are diligent in their efforts on their behalf.

Therefore, CDI should consider requiring intervenors to have their filings reflected on SERFF. Doing so would cost virtually nothing and would

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146. *Informational Report on the CDI Intervenor Program*, CAL. DEP'T OF INS., https://www.insurance.ca.gov/01-consumers/150-other-prog/01-intervenor/report-on-intervenor-program.cfm (last visited Aug. 16, 2023).

benefit all parties. It should be noted that, as this paper was going to press, CDI had started to post intervenor filings (Petitions to Intervene and Petitions for Hearing) for public access.[147]

Beyond simply making intervenor contributions more transparent, CDI should exercise its discretion to reduce, and sometimes reject, fee submissions due to the lack of significant or substantial contribution. The department has long rubber-stamped fee requests, thereby creating incentives for unnecessary and costly delays in reviews and in actuarially justified rate increases.

4. Embracing catastrophe models

Another reform that may be possible to enact via regulatory action is allowing the use of wildfire catastrophe models to rate and underwrite risk on a prospective basis. As mentioned above, there is precedent for such interpretation as the FAIR Plan and the California Earthquake Authority already use catastrophe models for similar purposes.[148] The Legislature could contribute to this process by appropriating funds for a commission to formally review the output of wildfire models, much as the Florida Commission on Hurricane Loss Projection Methodology (FCHLPM) does for hurricane models.[149] A formal review process could also provide insurers with the certainty they would need to justify investing in refined pricing strategies without fear that regulators will later reject the underlying methodology.

B. LEGISLATIVE REFORMS

The following proposals would require one of the exceptional legislative processes outlined above. Under the most common, a bill would have to clear both chambers of the Legislature by a two-thirds majority, and courts would ultimately be called on to rule on any challenges (and there will be challenges) of whether the measure "furthers the purpose" of Prop 103.[150]

But there is another option. The Legislature could also, by simple majority vote, opt to pass a statute that becomes effective only when approved by the electorate. Past would-be reformers have largely eschewed this path,

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147. *Prop 103 Consumer Intervenor Process*, CAL. DEP'T OF INS., https://www.insurance.ca.gov/01-consumers/150-other-prog/01-intervenor/index.cfm.

148. Pomeroy, *supra* note 61.

149. *About the FCHLPM*, FLA. COMM'N ON HURRICANE LOSS PROJECTION METHODOLOGY, https://fchlpm.sbafla.com/about-the-fchlpm (last visited Aug. 9, 2023).

150. CONSUMER WATCHDOG, *supra* note 10.

considering the odds poor that the voting public would choose to make changes to Prop 103.

That may once have been obviously true, but as the California market continues to struggle, and as banks and property owners find it impossible to secure coverage at any price, it is difficult to say with certainty what voters would do. Prop 103 passed narrowly even against the backdrop of an insurance market crisis. As we find ourselves in yet another such crisis, anything may be possible.

1. Insurance Market Action Plan

One option to address availability concerns and shrink the bloated FAIR Plan would be for the Legislature to revive the Insurance Market Action Plan (IMAP) proposal that the Assembly passed by a 61-3 margin in June 2020.[151]

Similar to the "takeout" program used successfully to depopulate Florida's Citizens Property Insurance Corp., under IMAP, insurers that committed to write a significant number of properties in counties with large proportions of FAIR Plan policies would be allowed to submit rate requests that considered the output of catastrophe models and the market cost of reinsurance.[152] In addition, FAIR Plan assessments should be applied as a direct surcharge, not subject to CDI approval, to ensure that there is no unfair subsidization of the highest risks, as well as to guard against the burden of assessments contributing to the insolvency of private insurers.

IMAP filings would also receive expedited review by the insurance commissioner[153], which could alleviate the speed-to-market issues highlighted in Section III.

2. Telematics

There has also been some legislative interest in broadening the availability of telematics. In 2020, Assembly member Evan Low (D-Campbell) and then-Assembly member Autumn Burke (D-Marina Del Rey) co-authored an op-ed in which they called telematics "a sensible and fair approach" and encouraged CDI to continue to explore the issue with stakeholders.[154]

151. Assemb. B. 2167, Cal. Leg. Reg. Sess. (Cal. 2020).

152. *Id.*

153. *Id.*

154. Evan Low & Autumn Burke, *Modernize the Way We Price Auto Insurance – Telematics Is a Sensible Approach*, CALMATTERS (Aug. 19, 2020), https://calmatters.org/commentary/2020/08/modernize-the-way-we-price-auto-insurance-telematics-is-a-sensible-approach.

"Prop. 103 was passed in an age before cell phones, GPS Navigation and many other technological advancements. Its interpretation doesn't allow companies to rate customers on their driving behavior. Prop. 103 relies heavily on demographic factors, rather than basing your rate on how you drive."[155]

VII. CONCLUSION

As demonstrated in this paper, claims about Prop 103's savings to consumers[156] must be taken with an enormous grain of salt. Prop 103's suppression of property insurance rates in the private market has contributed to an availability crisis and the shunting of policyholders into the surplus-lines market and the California FAIR Plan, both of which will inevitably have to raise rates accordingly to be able to meet their obligations. This displacement into what are intended to be mechanisms of last resort also deprives consumers of the protections ordinarily offered in the admitted market.

155. *Id.*

156. Consumer Fed'n of Am., *supra* note 13.

FLORIDA'S HOMEOWNERS INSURANCE PROBLEMS

PETER MOLK[*]

ABSTRACT

Floridians have seen dramatically rising homeowners insurance premium increases over the past several years, with year-over-year increases of forty percent or more over multiple years. The problem grew so severe that the State legislature convened a special session in 2022 to address the problem, ultimately passing several efforts designed to moderate rates. This Article reviews the evidence of Florida's experience to interrogate why the State has suffered disparately high homeowners insurance premium increases. In light of this interrogation, I critically assess the prospects for the recent legislative efforts and other suggestions to address the underlying problems. Reform efforts predominantly address a perceived problem of excess litigation and insurance fraud, but I show how the available evidence suggests the bulk of recent rate increases may be due to other causes. Finding that recent legislative efforts offer only incomplete solutions as premiums continue to remain high, I provide additional possibilities for reform that target both potentially excessive litigation as well as other possible causes. Florida's successes and challenges with tackling increasing premiums is informative not just for Floridians, but also for other states that may have similar systems in place that may result in similar future premium increases unless preventative action is taken.

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TABLE OF CONTENTS

I. INTRODUCTION 42
II. POTENTIAL CAUSES OF RATE INCREASES 44
A. NATURAL HAZARD EXPOSURE 45
B. CONSTRUCTION COST INCREASES 48
C. EXCESSIVE LITIGATION AND INSURANCE FRAUD 51
III. RECENT REFORM EFFORTS 62
A. RECENT LEGISLATIVE CHANGES 62
B. NEWER PROPOSALS 68
1. Tax Cuts 68
2. Mortgage-Only Policies 69
3. Expand Government-Backed Insurance 71
4. State-Subsidized Home Hardening 75
IV. ADDITIONAL REFORM SUGGESTIONS 76
A. LEVERAGE CITIZENS'S INFLUENCE 76
B. DIRECTLY DETER FRAUD 78
C. REEVALUATE REFORM RESTRICTIONS OVER TIME 80
V. CONCLUSION 82

I. INTRODUCTION

Census estimates show that the year 2022 brought over 450,000 new residents to the state of Florida, over five times the rate of population increase as in the United States as a whole.[1] These new residents may have been unpleasantly surprised when the time came to insure their new homes; in addition to sunny weather, beaches, and theme parks, Florida features the highest average home insurance costs in America.[2] The average premium sits at $4,200, or triple the nation's average,[3] with reports of premiums commonly well into five digits.[4] Indeed, high premiums are reported to be driving many Floridians to relocate at rates almost double the national average.[5]

It was not always this way. High premiums are a recent phenomenon—by some reports increasing by 102% over just the prior three years.[6] Fingers were pointed at multiple likely targets. Some blame rising construction and labor costs.[7] Some blame Florida's unique exposure to natural hazard risk.[8] Most of the blame, however, fell on the perceived excessive litigation

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1. *See State-to-State Migration Flows*, U.S. CENSUS BUREAU, https://www.census.gov/data/tables/time-series/demo/geographic-mobility/state-to-state-migration.html (comparing 2022 figures to 2021) (last revised Oct. 7, 2024).

2. Giulia Carbonaro, *Florida Considers Socialist Model to Combat Soaring Insurance Costs*, NEWSWEEK, https://www.newsweek.com/florida-considers-socialist-model-insurance-costs-1858612 (last updated Jan. 9, 2024, 4:23 AM).

3. INS. INFO. INST., TRENDS AND INSIGHTS: ADDRESSING FLORIDA'S PROPERTY/CASUALTY INSURANCE CRISIS (2023), https://www.iii.org/sites/default/files/docs/pdf/triple-i_trends_and_insights_florida_pc_02152023.pdf. Other sources report even higher average rates for Florida of approximately $6,000 per year. Carbonaro, *supra* note 2.

4. *See, e.g.*, Greg Allen, *Feeling the Pinch of High Home Insurance Rates? It's Not Getting Better Anytime Soon*, NPR (Oct. 26, 2023, 5:01 AM), https://www.npr.org/2023/10/26/1208590263/florida-homeowners-insurance-soaring-expensive (reporting on a $20,000 premium).

5. Giulia Carbonaro, *Florida Homeowners Are Relocating in Droves over Insurance Crisis*, NEWSWEEK, https://www.newsweek.com/florida-homeowners-relocating-insurance-crisis-cost-1893248 (last updated Apr. 24, 2024, 10:24 AM).

6. Carbonaro, *supra* note 2.

7. Jeff Allen, *Rising Construction Costs Plague Insurance Rates*, SPECTRUM NEWS (Dec. 27, 2023, 8:45 PM) https://mynews13.com/fl/orlando/news/2023/12/28/home-insurance-costs.

8. Allen, *supra* note 4.

in Florida.[9] Although it is reported that Florida policies comprise only nine percent of nationwide homeowners insurance claims, they account for seventy-nine percent of homeowners insurance lawsuits.[10] Dealing with these claims, and the alleged fraud that spawned them, was seen as the major drain on insurance companies' coffers, forcing them to raise premiums in response.[11] To deal with these rising prices, Florida's legislature passed a total of five pieces of legislation from 2019 through 2023.[12]

While it will take some time for the full effect of these reforms to make their way through the insurance markets, reform advocates have already begun pointing to some signs of early success.[13] Any positive impacts have

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9. *See, e.g.*, Press Release, Ins. Info. Ins., Triple-I: Extreme Fraud and Litigation Causing Florida's Homeowners Insurance Market's Demise (June 23, 2022), https://www.iii.org/press-release/triple-i-extreme-fraud-and-litigation-causing-floridas-homeowners-insurance-markets-demise-062322 ("Floridians are seeing homeowners insurance become costlier and scarcer because for years the state has been the home of too much litigation and too many fraudulent roof replacement schemes."); Leslie Kaufman, *Florida's Home Insurance Industry May Be Worse than Anyone Realizes*, BLOOMBERG (Apr. 24, 2024, 7:00 AM), https://www.bloomberg.com/news/features/2024-04-24/home-insurance-with-lax-oversight-hides-florida-climate-risk?srnd=undefined (quote from the President of Demotech, which rates the solvency of Florida's insurers) ("The real problem with the state insurance market is consumer and contractor fraud."); *id.* (quoting Florida Commissioner of Office of Insurance Regulation Mike Yaworsky as stating that "pervasive and abusive insurance fraud" were the main causes of recent insurer failures); Danielle Prieur, *Nothing in Life Is Free: Roofing Scams Drive up Property Insurance Rates in Florida*, CENTRAL FLA. PUB. MEDIA (May 23, 2022, 2:30AM) https://www.cfpublic.org/2022-05-23/nothing-in-life-is-free-special-session-will-address-how-roofing-scams-are-driving-up-florida-property-insurance-rates (quote from Lisa Miller, founder of the government consulting and advocacy firm Lisa Miller and Associates) ("Widespread fraud including roofing scams and the resulting litigation are to blame [for recent homeowners insurance increases].").

10. State of Florida Executive Office of the Governor, Proclamation (Apr. 26, 2022), https://www.myfloridahouse.gov/FileStores/Web/HouseContent/Approved/Web%20Site/uploads/documents/proclamations/Governor%20Proclamation%202022%20SSD%20May%2023-27.pdf.

11. INSURANCE INFORMATION INSTITUTE, *supra* note 3.

12. MICHAEL YAWORSKY, FLA. OFF. OF INS. REGUL., PROPERTY INSURANCE STABILITY REPORT 22 (2024) https://www.floir.com/docs-sf/default-source/property-and-casualty/stability-unit-reports/july-2024-isu-report.pdf?sfvrsn=42a5a302_2.

13. *E.g.*, *id*. ("There are signs that the reforms are leading to modest rate reductions . . . .")

been fairly muted, however, generally taking the form of a slower pace of rate increases rather than any meaningful rate reductions.[14] The frustratingly slow pace of change has led to new suggestions for reducing rates using a variety of tools.[15] So far, most of these new suggestions have not been adopted, and the legislature seems finished for now with large-scale policy change.

I take advantage of this lull in regulatory efforts to provide a useful scholarly perspective on the issue. The goal is for this perspective to be useful both to those in Florida but also to those in other states, who may wish to avoid Florida's recent experience. Consequently, Part I surveys the arguments and evidence for the rapid recent increases in Florida homeowners insurance rates. The consensus has coalesced around excessive litigation and insurance fraud as the main drivers, but the complete picture is murkier than is traditionally summarized in the news or in legislative soundbites. Indeed, as I show in Part I, there is considerable doubt that these agreed-upon causes have been leading to the bulk of recent premium increases. Part II then assesses the efforts that have already been enacted and those that have recently been suggested. The ultimate success of these programs will depend on how significant litigation and insurance fraud have been contributing to premium hikes. Since available evidence suggests there are likely other, as-yet-unidentified causes that are material contributors to rate increases, it will be important to monitor ongoing developments and adapt regulatory efforts to the new challenges identified by, and caused by, existing efforts.[16] Nevertheless, even if the popularly identified causes of rate increases are the true causes, there are additional steps that could be taken to address them. Part III, therefore, provides original examples of those steps as well as actions that could target alternative causes for premium increases.

II. POTENTIAL CAUSES OF RATE INCREASES

14. *See, e.g.*, *id*. at 23 ("[A]ll [insurers] secured adequate reinsurance coverage, experiencing an average risk adjusted rate increase of around 27 percent, lower than the initially estimated 50 percent..").

15. William Rabb, *Florida Bill Would Require Option of Policies that Cover Only Unpaid Mortgage Amount*, INS. J. (Jan. 4, 2024), https://www.insurancejournal.com/news/southeast/2024/01/04/754264.htm.

16. *See generally* Peter Molk & Arden Rowell, *Reregulation and the Regulatory Timeline*, 101 IOWA L. REV. 1497, 1520–31 (discussing the potential benefits of learning from revealed experience with regulatory changes).

In this Part, I review the most commonly identified causes for Florida's high homeowners insurance premiums. As I show, some of the causes are more compelling than others, and each has questions about its relative significance. Unfortunately, if the causes of rate increases are unclear, so too are the recommended solutions—a theme I return to at the end of this Article.

A. NATURAL HAZARD EXPOSURE

The first cause that is often identified is Florida's comparatively unique exposure to natural hazards.[17] Because of its extensive coastline and lack of land elevation, Florida often experiences hurricane and tropical storm losses. These losses can be significant. Three of the top ten costliest global insured loss events since 1900 (numbers two, four, and nine) had major elements in Florida,[18] as did thirteen of the fifty most costly tropical cyclones to impact the U.S. since 1900.[19]

Compounding the problem is the fact that much of Florida's population lives along the exposed coasts. Seventy-six percent of the population lives in coastal counties, where destruction caused by hurricanes can be the most damaging.[20] Most of this population is concentrated in the southeast and the central west coasts, where hurricanes most often make landfall.[21] The

17. *See, e.g.*, Jedidajah Otte, *Florida Rocked by Home Insurance Crisis: 'I May Have to Sell Up and Move'*, THE GUARDIAN (July 15, 2023, 8:00 AM EDT), https://www.theguardian.com/us-news/2023/jul/15/florida-hurricane-insurance-crisis-climate; Cate Deventer & Shannon Martin, *Can Lawmakers Save the Collapsing Florida Home Insurance Market?*, BANKRATE (Sept. 19, 2023), https://www.bankrate.com/insurance/homeowners-insurance/florida-homeowners-insurance-crisis/.

18. *See* AON, CLIMATE AND CATASTROPHE INSIGHT 103 (2024), https://assets.aon.com/-/media/files/aon/reports/2024/climate-and-catastrophe-insights-report.pdf. The three were Hurricanes Ian, Irma, and Andrew. *Id.*

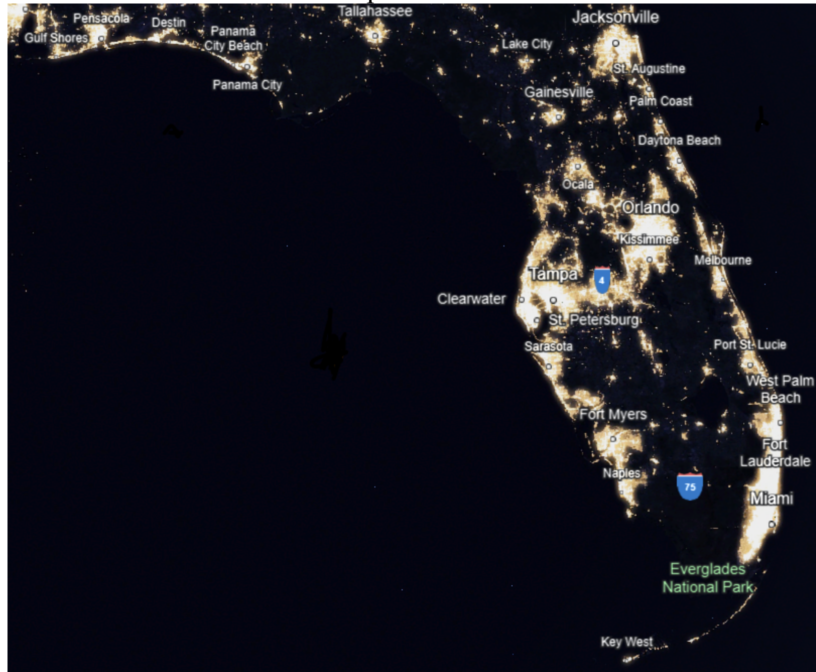
19. NOAA: NAT'L CTRS. FOR ENV'T INFO., COSTLIEST U.S. TROPICAL CYCLONES 2–5 (2024), https://www.ncei.noaa.gov/access/billions/dcmi.pdf. This list is the top disasters in terms of economic cost, which is not the same as the insured amount of that economic cost. *Id.*

20. St. Petersburg Coastal Mapping Program, *The Florida Coastal Mapping Program*, U.S. GEOLOGICAL SURV. (Mar. 30, 2018), https://www.usgs.gov/centers/spcmsc/science/florida-coastal-mapping-program.

21. NOAA, *Total number of hurricane strikes by counties/parishes/boroughs, 1900-2010* (illustration) *in Tropical Cyclone Climatology*, NOAA: NAT'L HURRICANE CTR., https://www.nhc.noaa.gov/climo/ (last visited Sept. 29, 2024).

following image of Florida at night makes the point vividly, showing where most of the population tends to cluster.[22]

Figure 1
Florida's Population Distribution



Certainly, Florida's risk characteristics justify higher premium levels for policies that cover those risks. This might explain why Florida premiums are roughly three times higher than a low-risk state like Oregon, whose first two natural disaster risks identified by its Department of Emergency

22. This image was produced with the aid of Google Earth. Recreating Figure 1, GOOGLE EARTH, http://www.earth.google.com (Turn on "Earth at Night" feature, then find Florida on the map).

Management are "volcanoes" (Mount St. Helens, the most recent volcanic eruption to impact Oregon, last had a major eruption in 1980)[23] and "extreme heat."[24]

However, although the *levels* of homeowners insurance rates should be high, these risk characteristics do not explain why those levels would have *grown* by such significant amounts in each of the past recent years unless the State's perceived risk characteristics had also increased over each of those years. While climate science and catastrophe modeling are still evolving, it is unlikely that Florida's risk profile has changed enough, each of the last three or four years, to justify massive increases in premiums over those years. This point is particularly true since, because these policies are written on an annual basis, homeowners insurers are not exposed to the types of longer-term risk that are usually flagged by climate scientists. Moreover, premium increases have occurred fairly uniformly across insurers,[25] and while some may coordinate on common catastrophe modeling software, others (and their reinsurers) do not, which should lead to diversity in rate changes as different models predict different trends. That diversity has not been present.

Nevertheless, loss experience may have a transitory, short-term influence. Insurers sometimes respond to poor results in prior years by raising prices in future years to compensate.[26] Homeowners insurers in Florida suffered underwriting and net income losses from 2017 through 2023, with those

23. Laurel Demkovich, *Predicting Volcanic Eruptions 43 Years After the Mount St. Helens Blast*, WASH. STATE STANDARD (May 18, 2023, 1:00 AM), https://washingtonstatestandard.com/2023/05/18/predicting-volcano-blasts-43-years-after-the-mount-st-helens-eruption/.

24. *Hazards in Oregon*, OR. DEP'T OF EMER. MGMT., https://www.oregon.gov/oem/hazardsprep/pages/hazards-in-oregon.aspx (last visited Sept. 29, 2024).

25. *See, e.g.*, Matthew McClellan, *70% of Florida Homeowners See Rise in Insurance Costs or Changes in Coverage: Report*, FOX 13 TAMPA BAY (Apr. 19, 2024, 8:00 AM EDT), https://www.fox13news.com/news/70-of-florida-homeowners-see-rise-in-insurance-costs-or-changes-in-coverage-report (finding that even in 2024, Florida homeowners experience premium increases or coverage decreases at significantly higher rates than the national average).

26. *See, e.g.*, Jay Angoff, *Insurance Against Competition: How the McCarran-Ferguson Act Raises Prices and Profits in the Property-Casualty Insurance Industry*, 5 YALE J. ON REG. 397, 407 (1988). This is despite standard competition theory suggesting this should not occur. *See generally* Kyle D. Logue, *Toward a Tax-Based Explanation of the Liability Insurance Crisis*, 82 VA. L. REV. 895, 959 (1996) (analyzing the role of tax law on liability insurance increases in the mid-1980s).

losses particularly large in 2020, 2021, and 2022.[27] If insurers temporarily raise prices following loss periods, then their recent experience may provide a partial explanation. Still, it seems unlikely that natural hazard exposure justifies most of the continuing rate increases that have been put through,[28] particularly as 2019 and 2021 were comparatively low-damage years for insurers while premiums continued to increase.[29] Moreover, temporary market disruptions are not a compelling justification for the long-term regulatory changes that have been implemented. As a result, we should continue our search for an explanation.

B. CONSTRUCTION COST INCREASES

The next popularly identified candidate is construction and building costs. Homeowners insurance covers the cost to repair or rebuild a home.[30] Therefore, some have attributed at least a portion of Florida's premium increases to increasing construction costs in the State.[31]

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27. YAWORSKY, *supra* note 12, at 11–13.

28. Joey Solitro, *Two Home Insurers Eye Rate Hikes of More than 50% in Florida*, KIPLINGER, https://www.kiplinger.com/personal-finance/home-insurance/two-home-insurers-eye-rate-hikes-in-florida (reporting on fifty percent premium increases at Allstate and Amica) (last updated Feb. 16, 2024).

29. NAT'L CTRS. FOR ENV'T INFO., *Florida Summary*, NOAA., https://www.ncei.noaa.gov/access/billions/state-summary/FL (last visited May 9, 2024) (providing Florida disaster costs for 1981 through 2024).

30. Peter Molk, *Playing with Fire? Testing Moral Hazard in Homeowners Insurance Valued Policies*, 2018 UTAH L. REV. 347, 360 n.56.

31. *See, e.g.,* Allen*, supra* note 4 ("The cost of construction – up nearly 40% over the last five years – is also driving up premiums."); *How the Rising Cost of Construction Materials and Labor Is Affecting Home Insurance Rates,* DEL TORO INS. (Oct. 7, 2023), https://www.deltoroinsurance.com/learning_center/how-the-rising-cost-of-construction-materials-and-labor-is-affecting-home-insurance-rates/ ("The cost of construction materials and labor has been on an upward trajectory, especially in Florida."); Ryan Furtwangler, *Understanding the Rising Costs of Homeowners Insurance in Florida*, HBKS WEALTH ADVISORS (Oct. 30, 2023), https://hbkswealth.com/2023/10/understanding-the-rising-costs-of-homeowners-insurance-in-florida/ ("The high frequency of these [hurricane] events has led to increased construction costs as well as higher expenses associated with rebuilding and replacing damaged homes."); Steve Evans, *Florida Insurance Rates Unlikely to Fall, Reinsurance a Factor: KCC*, ARTEMIS (Oct. 11, 2023), https://www.artemis.bm/news/florida-insurance-rates-unlikely-to-fall-reinsurance-a-factor-kcc/ ("Recent material and labor shortages have caused double digit annual increases in the

As a matter of pure theory, this explanation has problems. Most homeowners insurance policies are written on a replacement cost basis, where the insurer agrees to pay the cost to replace a damaged home up to the policy limits.[32] If construction costs go up, then so too will replacement costs, seemingly driving up insurers' costs. However, since a policy's coverage amount is driven by replacement costs, higher replacement costs will also increase policy limits, with the net result that nominal premium *amounts* will increase to reflect higher value structures, but premium *rates*, or the cost to insure a constant dwelling value, should remain relatively constant.[33] Consequently, construction costs could explain observed premium increases that do not control for policy limit amounts, like the widely identified doubling of average

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cost of repairing or replacing a Florida home, and those increases have contributed significantly to the cost of homeowners insurance."); Christie Zizo, *You Want Florida Lawmakers to Lower Property Insurance Rates. Why That Likely Won't Happen*, CLICK ORLANDO, https://www.clickorlando.com/news/politics/2024/01/09/floridians-want-lawmakers-to-get-property-insurance-rates-down-why-that-likely-wont-happen-this-session/ (last updated Jan. 10, 2024, 10:44 AM) ("[Lisa Miller observed that i]f you have walked into a big box, hardware store and seeing the cost of a piece of plywood, it's up probably four or five times more than it was four or five years ago. So, it costs that much more to fix a home and that is reflected in our increase rates.").

32. *See, e.g.*, Molk, *supra* note 30 ("Homeowners insurance provides for either the amount the destroyed property was worth ('actual cash value'), or, more commonly, the amount needed to replace the destroyed property ('replacement cost')."); Daniel Schwarcz, *Reevaluating Standardized Insurance Policies*, 78 U. CHI. L. REV. 1263, 1317 n.196 (2011) ("Lenders do impose substantial requirements with respect to the financial strength of insurers.").

33. We might still expect some modest increases here to the extent insurers write policies whose limits exceed potential replacement costs. Because insurers in most states pay the lesser of policy limits or actual replacement costs in the event of a loss, higher replacement costs will impose higher expenses on insurers for policies whose limits exceed reasonable replacement costs even if the limits do not change. *See generally* Molk, *supra* note 32, at 388–91 (analyzing how other factors could also increase insurers' costs for this type of policy). However, most believe that policyholders generally buy too little insurance, rather than too much, making it unlikely this factor would drive Florida's dramatic recent rate increases.

insurance premiums over the past three years,[34] but they would have difficulty explaining the observed increases that do control.[35]

As a matter of empirical observation, this explanation also appears problematic. The organization Engineering News-Record ("ENR") publishes monthly construction cost estimates for various cities across the country.[36] Although it does not include any cities in Florida, it includes two in immediately neighboring states (Birmingham, Alabama and Atlanta, Georgia). Comparing construction cost changes in this southeast region to those in other parts of the country can shed light on whether Florida may have been experiencing dramatic, disparate relative changes. Of course, Florida is neither Birmingham nor Atlanta, but one would expect that rapid rises in Florida construction costs would have at least some spillover effects on these neighboring cities.

Figure 2 therefore compares changes in the building cost index for the southeast region (which I calculate as the simple average of changes in Birmingham and in Atlanta) to various other cities across the country.[37] The building cost index reports local changes in skilled labor rates, structural steel, cement, and lumber and is designed to give a sense of general construction costs, particularly for structures.[38] To facilitate comparisons across jurisdictions, I scale the building cost index values in each region relative to an anchor of January 2018.

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34. *See* Carbonaro, *supra* note 2 ("Insurance costs have grown by 102 percent in the past three years alone . . . .").

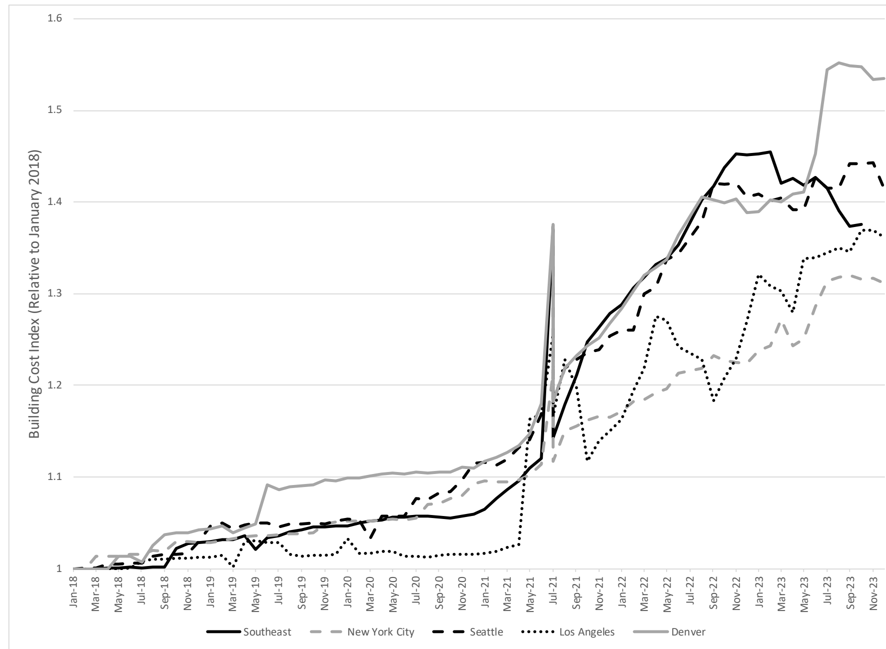
35. *See* YAWORSKY, *supra* note 12 (reporting on large increases in reinsurance rates on a risk-adjusted basis).

36. *Construction Economics*, ENR, https://www.enr.com/economics?oly_enc_id= (last visited Sept. 30, 2024).

37. ENR provides data for twenty US cities. *Id.* For presentation purposes, I show four, selected to represent broadly different regions of the country, in addition to the southeast. These four did not differ greatly from the other cities that I examined.

38. *Using ENR Indexes*, ENR, https://www.enr.com/economics/faq (last visited Sept. 30, 2024).

Figure 2
Construction Cost Increases
Southeast vs. Other Cities



As the Figure shows, the southeast has not suffered dramatically greater construction cost increases than other regions; indeed, it is largely in line with the other cities presented. Therefore, to the extent construction costs are driving premium increases in Florida, we should expect similar premium increases elsewhere. Florida's increases, however, remain an outlier. Therefore, I turn to consider the most widely identified contenders for Florida's premium increases: excessive litigation and, relatedly, insurance fraud.

C. EXCESSIVE LITIGATION AND INSURANCE FRAUD

The most commonly identified causes for Florida's premium increases are excessive litigation by policyholders (or, more commonly, those to whom policyholders have assigned their insurance benefits), and

policyholder-driven insurance fraud.[39] "Litigation," when used in this context, includes generally challenges that policyholders make against their insurers; of course, many of these will settle. Excessive litigation and insurance fraud are the causes mainly targeted by the State's recent legislative efforts.[40]

Excessive litigation and insurance fraud are thought to be particularly acute in Florida due to a problematic concatenation of legal and practical circumstances. I list the relevant factors here, developing each in more detail in the paragraphs that immediately follow. First, the State had a one-way fee shifting statute that required courts to award reasonable attorneys fees and costs to policyholders that prevailed in any coverage litigation against their insurer, including when the case is settled.[41] Next, the State's Supreme Court had held that contingency fee multipliers should not be limited to cases with "rare" and "exceptional" circumstances but instead could be awarded in more ordinary cases, if otherwise justified by the case's particular circumstances.[42] The contingency fee multiplier allowed trial courts to inflate lawyers' hourly rate by up to 250% to incorporate whether the case, at the outset, was likely to succeed and whether additional compensation would be needed to attract competent attorneys to the case.[43] These multipliers could apply whether the case was settled or went to verdict.[44] Third, Florida policyholders widely assigned benefits due to them under their homeowners insurance policies to contractors performing work on their houses.[45] Finally, homeowners in Florida generally had three years after damage occurred within to file a claim.[46]

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39. *See, e.g.*, Press Release, Ins. Info. Inst., *supra* note 9 and accompanying text.

40. State of Florida Executive Office of the Governor, Proclamation (Apr. 26, 2022), https://www.myfloridahouse.gov/FileStores/Web/HouseContent/Approved/Web%20Site/uploads/documents/proclamations/Governor%20Proclamation%202022%20SSD%20May%2023-27.pdf. The State also took smaller action to address its high premiums due to natural hazard exposure by requisitioning money to fund state-backed hurricane reinsurance, which should have a moderating influence on those rates. S.B. 2-A, 2022 Leg, Spec. Sess. (Fla. 2022).

41. Fla. Stat. § 627.428 (repealed 2023).

42. Joyce v. Federated Nat'l Ins. Co., 228 So. 3d 1122, 1123 (Fla. 2017).

43. *Id.* at 1125 (quoting Standard Guaranty Ins. Co. v. Quanstrom, 555 So. 2d 828, 834 (1990)).

44. *Id.* (discussing contingency fee multipliers in the context of a settled case).

45. *Assignment of Benefits*, FLA. OFF. OF INS. REGUL., https://floir.com/consumers/assignment-of-benefits-resources (last visited Sept. 28, 2024).

46. Ed Leefeldt, *Why Is Homeowners Insurance in Florida Such a Disaster?*, FORBES (Aug. 28, 2023), https://www.forbes.com/advisor/homeowners-insurance/why-is-homeowners-insurance-in-florida-such-a-disaster, *reprinted in*

This confluence of factors is seen as setting a framework for excessive challenging of insurers' claims handling and for insurance fraud. One-way fee shifting has the effect of encouraging litigation relative to the default rule of each party bearing its own costs – with fee shifting, plaintiffs bear their own costs only if they lose but not if they win or settle.[47] One-way fee shifting therefore should be expected to result in more suits filed against insurers, particularly at the margin where the prospect of bearing one's own fees shifts a case from an expected financial winner into a financial loser. If we suppose that low merit suits disproportionately fall into these marginal cases, then one-way fee shifting will disproportionately encourage those undesirable cases.

Contingency fee multipliers will also encourage similar cases. Like one-way fee shifting, contingency fee multipliers increase the expected returns to plaintiffs—in the worst case, no multiplier is applied and recovery is unchanged, and in the best case, recovery is increased significantly.[48] Like one-way fee shifting, multipliers will therefore disproportionately encourage cases that otherwise would be financial losers which, thanks to the potential for a multiplier, become winners.

Assigning benefits can encourage litigation as well, but for different reasons. An assignment of benefits to construction contractors allows them to pursue policyholders' claims against their insurance companies and get paid directly by insurers, rather than having policyholders first pay their contractors and then seek reimbursement from their insurers. Assignment of benefits provisions are common features of health insurance, where many readers may have encountered them during medical visits; policyholders often need not pay projected costs for the visits upfront and seek reimbursement from their insurers, but instead can allow their providers to be paid directly by their insurers. Assigning benefits changes who will be in charge of litigation against an insurer if a claim is brought, but not the potential claims that can be brought.

FLORIDIANS LAWSUIT REFORM (July 23, 2020), https://www.fltortreform.com/news/why-is-homeowners-insurance-in-florida-such-a-disaster/.

47. Harold J. Krent, *Explaining One-Way Fee Shifting*, 79 VA. L. REV. 2039, 2048–54 (1993).

48. *Joyce*, 228 So. 3d at 1125 (quoting Standard Guaranty Ins. Co. v. Quanstrom, 555 So. 2d 828, 834 (1990)) ("If the trial court determines that success was more likely than not at the outset, it may apply a multiplier of 1 to 1.5[.]").

Still, the identity of the plaintiff can matter. Contractors have no ongoing positive relationships with the policyholders' insurance companies and therefore lack the reputational constraints that may keep policyholders from bringing questionable claims in an effort to preserve a longer-term relationship.[49] Moreover, unlike policyholders who may have never experienced a loss, contractors are more likely to have interacted with insurance companies before, to be experienced with the litigation system, and to have contacts with plaintiff attorneys to bring a suit. They will, therefore, be more savvy plaintiffs who would be able to navigate the legal system at lower cost.

Assignment of benefits provisions can increase claim challenges against insurers for another reason. Assigning benefits to contractors solves potential liquidity issues that policyholders might otherwise have if they must pay for repairs upfront and then get reimbursed by insurers later. This liquidity means that policyholders should feel less pressure to accept insurers' early claims settlement offers as an alternative liquidity source.

Widespread assignment of benefits serves some of the same purposes as one-way fee shifting and damage multipliers, all of which are designed to incentivize suits that might not otherwise be brought.[50] Having suits end up in the hands of comparatively sophisticated litigants through claims assignments should increase the frequency with which claims challenges will be filed.

Finally, having three years to file a claim after a loss also encourages litigation. Mathematically, granting more time to discover problems after a loss event can only increase the number of claims that will be made.[51] Also, filing a claim long after a loss occurs can raise evidentiary issues that make it

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49. Reputation can be a powerful constraint in a wide variety of situations. Peter Molk, *Where Nonprofits Incorporate and Why It Matters*, 108 IOWA L. REV. 1781, 1820 (2023). This may be particularly important in homeowners insurance, which is sometimes described as a "use it and lose it" product where policyholders are dropped from coverage after making the claim. RUTGERS CTR. FOR RISK & RESP. & UNITED POLICYHOLDERS, ESSENTIAL PROTECTIONS FOR POLICYHOLDERS 24 (2019), https://epp.law.rutgers.edu/epp/wp-content/uploads/sites/16/2016/10/EPP-full-2019_0.pdf.

50. To be sure, assignment of benefit provisions serve other pro-policyholder purposes as well, like allowing them to start repairs faster, that might make them desirable. I return to this point *infra* Section III.C.

51. However, one would expect this increase to taper off after a relatively short period of time within which the obvious and most of the latent losses will be discovered.

difficult for an insurance company to contest coverage.[52] Although the policyholder generally bears the burden of showing that coverage is triggered, doing so is fairly easy for an all risks policy like a standard homeowners insurance policy—the policyholder simply shows that the dwelling has experienced a loss.[53] The insurer then bears the burden of showing that an exclusion applies, such as that the damage was due to an excluded cause like flooding or that it occurred during a year covered by another insurance company. Meeting this burden grows increasingly difficult when events are alleged to have occurred years in the past—proving that previously-hidden damage was due to flooding, or that it happened four or two years ago but not three, can present insurmountable proof problems.

Combined, these dynamics can increase the incidence of homeowners insurance claims. Prevailing laws and practice facilitated those claims moving to sophisticated plaintiffs' hands, and made it difficult for insurance companies to contest them. At the extreme, these attributes also can make insurance fraud particularly attractive. A commonly alleged fraud involves roofing contractors who visit neighborhoods after a storm, promising policyholders free roofs even if those roofs were undamaged in exchange for an assignment of benefits against the policyholders' insurance companies.[54] Roofs are

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52. *See* TASHA CARTER, FLA. DEP'T OF FIN. SERVS., FLORIDA'S INSURANCE CONSUMER ADVOCATE POLICYHOLDER LITIGATION CLAIMS SURVEY DATA (2020), https://s3.documentcloud.org/documents/24041912/policyholder-litigation-claims-survey-results96.pdf (finding many more claims are filed within two weeks of a loss than more than one year after a loss).

53. Claiming a loss for named peril coverage, like the personal property within the dwelling, is more difficult, since the policyholder needs to show damage was due to an enumerated peril. The difference between these two burdens was made vividly clear during the widespread Hurricane Katrina litigation about both dwelling and personal property damage. *See, e.g.*, Broussard v. State Farm Fire & Cas. Co., 523 F.3d 618, 625–27 (5th Cir. 2008) (discussing the impact of differing burdens of proof for dwelling and for personal property damage).

54. Kevin Accettulla, *Tampa-Area Roofers Accused of Faking Damage, Inflating Insurance Claims, CFO Says*, WFLA NEWS, https://www.wfla.com/news/hillsborough-county/tampa-area-roofers-accused-of-faking-damage-inflating-insurance-claims-cfo-says/ (last updated Dec. 1, 2023, 4:34 PM); Jon Schuppe, *Florida Lawmakers Scramble to Fix a Property Insurance Crisis before Hurricane Season*, NBC NEWS (May 21, 2022, 4:30 AM) https://www.nbcnews.com/news/us-news/roofing-scams-florida-property-insurance-hurricane-rcna29649. In this way, we might think of these contractor-led activities as a type of undesirable third party moral hazard generated from homeowners insurance. Gideon Parchomovsky & Peter Siegelman,

expensive to replace, and insurance companies in Florida have a history of dropping policyholders whose roofs were more than fifteen years old regardless of their condition,[55] so contractors promises may be particularly appealing to insured homeowners. The contractor then manufactures a claim for loss and files it with the homeowner's insurer, threatening to sue if the claim is not paid.[56] From the insurer's perspective, it can be cheaper to pay these claims rather than contest them and risk paying a plaintiff's attorney fees, potentially increased by a multiplier, if the case later settles or judgment is rendered for the plaintiff. As news of this scheme proliferates, so too does the incidence of fraud.

In addition to anecdotal cases about insurance fraud, insurance reform advocates point to studies showing that Florida has an outsized portion of insurance litigation. The Florida Office of Insurance Regulation found that in 2016, Florida constituted under eight percent of all nationwide *claims* against homeowners insurers but almost sixty-five percent of all *suits* against homeowners insurers, showing that homeowners insurers in Florida were far more likely to be sued per claim than the nationwide average.[57] By 2024, Florida comprised fifteen percent of nationwide claims and seventy-one percent of suits.[58] Moreover, the Office found that processing litigated claims costs insurers more than five times the amount of non-litigated claims (excluding any compensation that is ultimately paid),[59] and insurers' defense costs and containment expenses have grown each year since 2015.[60] High litigation rates impose high costs on insurers, who increasingly respond by passing those

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Third Party Moral Hazard and the Problem of Insurance Externalities, 51 J. LEGAL STUD. 93 (2022) (developing this concept in-depth).

55. This practice was so prevalent that the Florida legislature took steps to address it in 2022, prohibiting insurers from denying coverage when a roof is less than fifteen years old or has at least five more years of useful life remaining. S.B. 2-D, 2022 Leg., Spec. Sess. (Fla. 2022).

56. Accettulla, *supra* note 54.

57. YAWORSKY, *supra* note 12, at 4.

58. *Id.*

59. FLA. OFF. OF INS. REGUL., OIR RESIDENTIAL PROPERTY CLAIMS AND LITIGATION REPORT (2024), https://www.floir.com/docs-sf/default-source/property-and-casualty/other-property-casualty-reports/january-2024-pclr.pdf; YAWORSKY, *supra* note 12, at 11–12.

60. Letter from David Altmaier, Ins. Comm'r, Fla. Off. of Ins. Regul., to Blaise Ingoglia, Chair, Fla. S. Com. Comm. (Feb. 24, 2021) (on file with author) ; YAWORSKY, *supra* note 12, at 4.

costs along to policyholders in the form of higher premiums, allegedly causing the dramatic recent rate increases.[61]

Excessive litigation and insurance fraud have emerged as the consensus explanation for Florida's increasing premiums, and they are the main targets of recent legislative reform efforts. Before turning to how the legislature addressed these concerns, I first consider some potential problems with relying on these factors as the principal drivers behind recent insurance premium increases. Although they offer an intuitive explanation, there are some issues with the story, and if policymakers ignore other potential causes, then they may be disappointed if premiums do not ultimately decrease appreciably.

Among those who have raised questions about the consensus story is Birny Birnbaum, the executive director at the Center for Economic Justice, an organization advocating for low-income and minority interests on economic justice issues.[62] Birnbaum examined publicly available insurer data used by Florida's Office of Insurance Regulation and concluded that high litigation rates are driven by only a handful of insurers and that most have relatively low rates of litigation compared to the number of cases closed without payment.[63] These facts would suggest that "excessive" litigation may instead be justifiable litigation driven by select insurers' claims practices, and that they could not explain why premiums have increased across the industry as a whole. If excessive litigation were the sole cause, then all insurers should be suffering from it.

Additionally, Ken Klein, a law professor at California Western School of Law, noted that despite enacting several rounds of legislation designed to curb excessive homeowners insurance litigation over multiple years, litigation rates have not trended down during that time.[64] This fact suggests that litigation is driven by factors other than the ones discussed above that

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61. Press Release, Ins. Info. Inst., *supra* note 9. ("Floridians are seeing homeowners insurance become costlier and scarcer because for years the state has been the home of too much litigation and too many fraudulent roof-replacement schemes.").

62. *Who We Are*, CENTER FOR ECON. JUST., http://www.cej-online.org/whoweare.php (last visited Aug. 24, 2024).

63. BIRNY BIRNBAUM, REVIEW OF NAIC MARKET CONDUCT ANALYSIS STATEMENT DATA IN APRIL 2, 2021 LETTER FROM FLOIR TO CHAIRMAN INGOGLIA 7 (2021) (on file with author).

64. Kenneth S. Klein, *Looking for a Lawsuit Crisis in 20 Charts*, 44 REV. LITIG. *passim* (forthcoming 2025).

encourage low-merit litigation.[65] Relatedly, the Tampa Bay Times ran a comprehensive story noting the lack of evidence linking existing high insurance litigation rates to high premiums.[66] Additionally, the American Policyholder Association, an organization dedicated to assisting policyholders in property insurance loss adjustment proceedings, found that Florida policyholders file general *complaints* against their homeowners insurers at higher-than-average rates, suggesting their high *litigation* rates may be caused by rightfully aggrieved policyholders rather than by fraud.[67]

Moreover, an analysis of publicly available data on premium rates from the National Association of Insurance Commissioners (the "NAIC") tentatively suggests that other factors may be relevant causes of recent premium increases. The NAIC annually publishes statewide average premiums for different property insurance policy types at eleven different exposure ranges.[68] Figure 3 shows percentage changes in average premiums over the prior year, through 2021 (the last year of available data) for a standard HO-3 homeowners policy with limits of $200,000 to $299,999 (which is in the midrange of available exposures), charting rates in Florida compared to Connecticut and the entire country.[69] Consistent with popular experience, the data show a

65. *See, e.g.*, *id.* (manuscript at 31) ("[T]he data on litigation outcomes neither describes a litigation crisis nor compellingly makes a case for an emergent need for reform.").

66. Lawrence Mower, *Florida Leaders Blame Insurance Crisis on Lawsuits, but Evidence is Thin*, TAMPA BAY TIMES, https://www.tampabay.com/news/florida-politics/2023/10/19/florida-leaders-blame-insurance-crisis-lawsuits-evidence-is-thin/ (last updated Oct. 20, 2023) (quote from Florida Sen. Jason Pizzo) ("We've been getting more information from our federal government on UFOs in the past year than we have on insurance data from the state of Florida[.]").

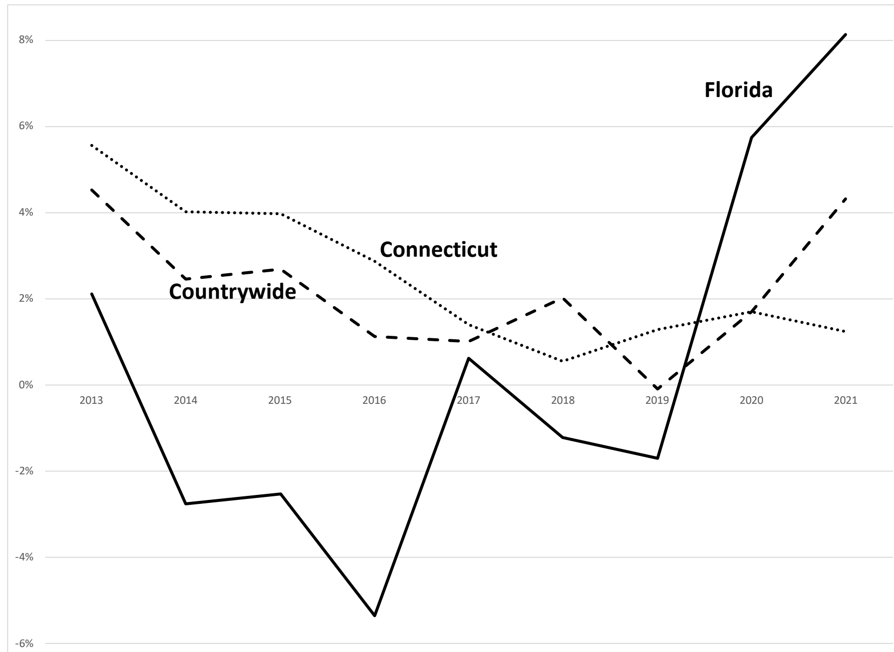
67. AM. POLICYHOLDER ASS'N, JUSTIFIABLE GRIEVANCES 2–4 (2023), https://www.propertyinsurancecoveragelaw.com/wp-content/uploads/2023/11/FILE_8830.pdf (finding that Florida homeowners insurers constitute eight percent countrywide premiums but fifty-six to sixty-one percent of closed, confirmed complaints against insurers).

68. *See, e.g.*, NAIC, DWELLING FIRE, HOMEOWNERS OWNER-OCCUPIED, AND HOMEOWNERS TENANT AND CONDOMINIUM/COOPERATIVE UNIT OWNER'S INSURANCE REPORT: DATA FOR 2021, at 28, 42, 48, 133, 140, 143 (2023), https://naic.soutronglobal.net/Portal/Public/en-GB/DownloadImageFile.ashx?objectId=10478&ownerType=0&ownerId=2006.

69. *See* Center for Insurance Policy and Research, *Dwelling Fire, Homeowners, Owner-Occupied, and Homeowners Tenant and Condominium/Cooperative Unit Owner's Insurance Report*, NAIC, https://naic.soutronglobal.net/Portal/Public/en-GB/RecordView/Index/2006 (last visited Dec. 5, 2025) (providing the 2013 to 2021

marked upward trend in homeowners insurance rates beginning in 2020, although still a somewhat modest trend.

Figure 3
Annual Percentage Change in Premium Levels
HO-3 Policy, $200,000-$299,999 Limits



At the same time, the NAIC report also includes data for other homeowners policy types that should be differentially impacted by the factors conventionally assumed to be causing excessive litigation and insurance fraud and therefore contributing to rising homeowners insurance rates.[70] In particular, the NAIC report provides average premiums for standard HO-6

reports, which feature the data necessary to recreate the calculations used to make Figure 3).

70. *Id.*

condominium policies within different coverage bands.[71] These policies have some coverage similarities with homeowners insurance, including covering personal property, personal liability, and loss of use.[72] However, unlike homeowners insurance, standard condominium insurance policies cover dwelling damage only from the drywall inward—the structure itself, including the roof, will be covered by the condominium association's master policy, and not the policyholder's HO-6 policy.[73]

Condominium insurance policies should therefore be affected by some of the same loss factors as homeowners insurance, like natural hazard exposure, which can cause covered losses to condominium interiors and personal property in the same way as to homes, or owners' legal liability risk, which is covered similarly under both policy types. On the other hand, factors that mostly result in losses to the structure's exterior will disproportionately impact homeowners insurance rates, because those losses are covered under homeowners policies but not condominium ones.

Most of the factors seen as contributing to excessive litigation and insurance fraud would seem to fall into this latter category of impacting homeowners, but not condominium, policies. Since condominium insurance policies do not cover roof damage, the prevalence of costly roof repairs, assigning benefits to contractors, and roofing frauds should have little influence on condominium insurance rates. Indeed, the most relevant factor should be the contingency fee multiplier, which the State Supreme Court cemented in 2017. To the extent excessive litigation and insurance fraud are driving up homeowners insurance premiums, we should expect average Florida HO-3 homeowners policy rates for a constant level of coverage to increase faster than average HO-6 condominium policy rates for a constant level of coverage.

To see if this is the case, Figure 4 plots the differential premium changes between HO-3 and HO-6 policies for Florida, Connecticut, and the countrywide average. To calculate the differential, I subtract the annual percentage changes in average HO-6 policies at the coverage limit range of $38,000 to $44,000, the midrange coverage band for HO-6 policies, from the annual percentage changes in average HO-3 policies of $200,000 to $299,999 policies.[74] Positive numbers show the extent to which homeowners premiums

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71. *E.g.*, *id.*

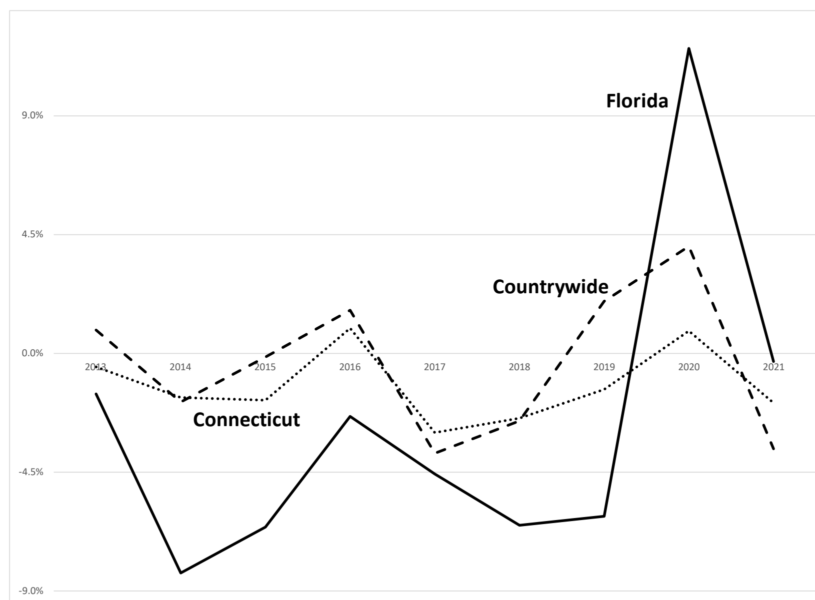
72. *E.g.*, *What Is Condo Insurance?*, PROGRESSIVE, https://www.progressive.com/answers/condo-101/ (last visited Apr. 25, 2024) (describing what is covered in Progressive's condominium insurance policy).

73. *Id.*

74. *See supra* note 68 (providing the data used to create Figure 4).

are growing at a faster rate for a constant coverage amount than condominium owner premiums; negative numbers occur when condominium owner premiums increase faster than homeowners premiums.

Figure 4
Difference in Annual Percentage Changes in Premium Levels
HO-3 Policy and HO-6 Policy



Surprisingly given the popular narrative, the Figure shows greater percentage increases in Florida condominium owner policies than in homeowners policies in recent years. The major exception is 2020, in which homeowners policies increased by a meaningful eleven percentage points over the rate of increase in condominium policies. However, an explanation focused on excessive litigation and insurance fraud would be expected to show large relative increases beginning at least around 2017, when the legal landscape began to shift towards encouraging litigation and fraud with more routine awards of contingency fee multipliers.[75] This is not what the Figure shows; in

75. *See* Joyce v. Federated Nat'l Ins. Co., 228 So. 3d 1122, 1135 (Fla. 2017). (affirming the use of contingency fee multipliers in Florida). The law regarding assignment of benefits and the period in which claims for losses had to be filed remained

fact, it suggests Florida has followed a similar trajectory to that of the rest of the country.

At the same time, the Figure does not show that homeowners insurance premiums have not suffered dramatic increases; instead, it shows that homeowners and condominium owners premiums have mostly increased and decreased in tandem. Thus, the Figure suggests caution before concluding that the observed increases in Florida are mostly due to excess litigation and insurance fraud, rather than other factors that would tend to move homeowners and condominium owners' policy rates together.

There are reasons to be cautious when interpreting the NAIC data. Among others, only average statewide figures are provided, and perhaps excessive litigation and fraud are confined to particular locations obscured by statewide averages; the underlying data are not available to assess the reliability of the averages; the data include multiple limit levels for each policy type and some of them might show different trends than the one presented here;[76] and the data run through 2021 and therefore would not capture any dramatic changes since then.

Still, the available data cautions against pointing to excessive litigation and insurance fraud as the main drivers of recent premium increases. Nevertheless, the Florida legislature targeted almost exclusively these factors in its recent efforts to correct for increasing premiums. The next Part turns to a consideration of those efforts and others that have since arisen as premiums remained high.

III. RECENT REFORM EFFORTS

Florida's substantive legislative response to increasing homeowners insurance premiums began in 2019 and continued through 2023. However, premiums have still not begun to decrease, generating new, yet-to-be-enacted proposals. In this Part, I review the major legislative efforts from 2019 through 2022 and then turn to the proposals that have been offered since then.

A. RECENT LEGISLATIVE CHANGES

steady until reform began at the end of this period, meaning those other relevant background factors for excessive litigation and insurance fraud were otherwise constant. *See infra* Section II.A.

76. That said, I examined two exposure levels for each policy type and did not find a meaningfully different trend emerge when doing so.

The legislative response to rising homeowners insurance premiums began in 2019 with House Bill ("HB") 7065.[77] The Bill targeted perceived abuse from assignment of benefits to contractors and other third parties, a practice that had increasingly become a subject of litigation since 2006.[78] The Bill amended Florida's statutes to require the assignee of benefits (typically the contractor) to notify the insurer promptly after an assignment has occurred.[79] It also sought to decrease the attractiveness of bringing these, and other cases, by limiting recovery of attorney's fees in cases where obtained judgments did not exceed 150% of the amount of a pre-suit settlement offer made by the insurer.[80] The Bill also allowed insurers to sell policies that contractually eliminated policyholders' ability to assign insurance benefits after a loss, as long as those policies' premiums were discounted relative to other policies.[81]

Surprisingly, the legislation had little effect on overall litigation rates, with disputes against insurers still growing by roughly thirty percent over the next two years.[82] Litigation over disputes involving assignment of benefit clauses dropped by half, however, suggesting that the focus of litigation had shifted to other areas.[83]

As homeowners insurance premiums continued to rise, Florida responded in 2021 with Senate Bill ("SB") 76. The law had two main areas of focus. The first was to reduce the time after a loss in which homeowners could file initial claims from three years to two.[84] The second was to prohibit contractors from encouraging homeowners to make claims against their insurers

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77. YAWORSKY, *supra* note 12, at 6.

78. *Assignment of Benefits*, FL. OFF. OF INS. REGUL., https://floir.com/consumers/assignment-of-benefits-resources (last visited Aug. 29, 2024) (claiming an increase of seventy times during this period).

79. H.B. 7065, 2019 Leg., Reg. Sess. (Fla. 2019).

80. FLA. STAT. ANN. § 627.7152 (West 2019) (amended 2022).

81. FLA. STAT. ANN. § 627.7153 (West 2019). At the time, some Florida courts had already held that policies with some restrictions on assignment of benefits were enforceable. *E.g.*, Restoration 1 of Port St. Lucie v. Ark Royal Ins. Co., 255 So. 3d 344, 348 (Fla. Dist. Ct. App. 2018). The statutory change allowed insurers to eliminate the practice altogether. § 627.7153.

82. YAWORSKY, *supra* note 12, at 5.

83. *Id.* at 6.

84. S.B. 76, 2021 Leg., Reg. Sess. § 10 (Fla. 2021) (amending Florida Statutes section 627.70132).

for roof damage, with violations subject to license discipline and a $10,000 fine per violation.[85] Litigation rates declined immediately after the legislation by roughly half.[86] Unfortunately, premiums did not do the same.[87]

Consequently, Florida's legislature again took action in 2022 and 2023. Litigation rates continued to drop during this time, but premiums were increasing dramatically. First, in June 2022, the State enacted SB 2-D, which established a $2 billion reinsurance layer available to homeowners insurers at no cost, and a $150 million fund to subsidize hardening of certain high-risk, low-valued homes against hurricane losses.[88] Each of these actions could have the effect of indirectly reducing premiums by decreasing insurers' overall expected coverage cost: the first by reducing primary insurers' reinsurance costs, and the second by decreasing the riskiness of insured homes. Neither targeted excessive litigation or insurance fraud. They are, however, the most meaningful attempts by the State to target alternative causes of increasing insurance premiums, and I return to them as potential solutions in Part III.

Later in December, Florida passed SB 2-A, which had broad impacts on the homeowners insurance market. SB 2-A provided an additional subsidized layer of reinsurance beyond SB 2-D's layer to homeowners insurers. This layer did not target the perceived excessive litigation and insurance fraud problems,[89] but other provisions of SB 2-A did. The bill also reduced the time period in which policyholders could first file a claim after a loss from two years (which had been reduced from three years only a year before) down to one year.[90] It also eliminated one-way fee shifting for residential or commercial property insurance policy litigation,[91] and it eliminated the ability for an assignment of rights after a loss for property insurance policies.[92] Then, in March 2023, Florida enacted HB 837, which eliminated any presumption of contingency fee multipliers, reserving them only for "rare and exceptional

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85. *Id.* § 1 (enacting Florida Statutes section 489.147).

86. YAWORSKY, *supra* note 12, at 5.

87. *Id.* at 15.

88. S.B 2-D, 2022 Leg., Spec. Sess. D §§ 1, 4 (Fla. 2022) (creating Florida Statutes section 215.5551(3)).

89. S.B. 2-A, 2022 Leg., Spec. Sess. A § 1 (Fla. 2022) (creating Florida Statutes section 215.5552).

90. *Id.* § 16 (amending Florida Statutes section 627.70132).

91. *Id.* § 6 (amending Florida Statutes section 626.9373).

92. *Id.* § 21 (amending Florida Statutes section § 627.7152(13)).

circumstance[s] with evidence that competent counsel could not otherwise be retained."[93]

Collectively, these efforts should have dramatically reduced the amount of excessive litigation and insurance fraud connected to homeowners insurance. The legislation, on a prospective basis, eliminates the financial incentives to bring much of the potential low-merit litigation against insurers. This effect should be particularly noticeable to the extent that litigation is driven by contractors (who now can no longer bring litigation because of the ban on assignment of benefit provisions) or by the potential to recover generous payouts (which are less attractive now that one-way fee shifting is eliminated and contingency fee multipliers are rare). We might also expect these reforms to have an early impact on suits being filed for new damage, given the decrease in litigation rates that happened immediately after HB 7065 allowed insurers to begin restricting assignment of benefit provisions and limited one-way fee shifting.[94] At the same time, because the changes applied on a prospective basis, and because policyholders previously had up to two years post-loss to file a claim, it could take a full two to three years, or up to the end of 2025, for the entire effect of changes to be felt, given that residential policies operate on twelve-month renewal cycles.[95]

This means that, by mid 2024, at the time of writing this Article, we should be seeing the bulk of the significant impacts from the reform efforts, with the remainder trickling in over the following eighteen months. Some modest positive signs have already begun to emerge. The Florida Office of Insurance Regulation has claimed "emerging signals that the reforms signed into law are having a positive impact on Florida's property insurance market."[96] These emerging signals consist of several new regional homeowners insurance companies beginning operations in Florida, increased willingness among private insurers to assume policies from the state-backed Citizens

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93. H.B. 837, 2023 Leg., Reg. Sess. § 1 (Fla. 2023) (amending Florida Statutes section 57.104).

94. *See supra* p. 21 ("Litigation over disputes involving assignment of benefit clauses dropped by half, however, suggesting that the focus of litigation had shifted to other areas.").

95. In the extreme case, someone who takes out a new policy right before legislative changes are adopted could recover under the former regime three years later, if damage occurs right at the end of the policy year and the policyholder waits the full two years to file a claim for it.

96. YAWORSKY, *supra* note 12, at 22.

homeowners insurance plan, and anecdotal evidence of some premium decreases for certain high-risk plans covered by Citizens.[97]

However, premiums have still not decreased appreciably.[98] Instead, successes are now generally counted when premiums experience minimal declines or, more commonly, are increasing but at a decreased pace. Lower rate increases are of course better than higher rate increases, but they are not as good as meaningful rate *decreases*, which might be expected if the principal cause of prior increases was due to the now-eliminated causes of costly litigation and fraud. In competitive markets, rates are set based on the expected costs of covering the underlying property, including any potential litigation costs.[99] If litigation expense and insurance fraud were the main drivers for a more-than-doubling in insurance premiums, then a material decrease in those factors' influence should have a similar material decrease in insurance premiums. While it would be unrealistic to presume premiums would return to the pre-run up levels, since other underlying factors have also surely increased over that time,[100] it would not seemingly be unrealistic to presume that some significant decreases in premiums should result from the reform.

Nevertheless, reform advocates now seem to be hoping that legislation will produce, at best, only modest rate decreases, and, more likely, just reductions in rate increases. For instance, the Florida Office of Insurance Regulation noted the favorable development that, despite concerns from insurers

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97. *Id.* at 22–23.

98. *See supra* Figure 3 (showing that premiums have not decreased in Florida in recent years).

99. *See, e.g.*, Daniel Schwarcz, *Ending Public Utility Style Rate Regulation in Insurance*, 35 YALE J. ON REG. 941, 956 (2018) ("[P]roperly priced insurance . . . reflect[s] the actual risk associated with property."); Omri Ben-Shahar & Kyle D. Logue, *Outsourcing Regulation: How Insurance Reduces Moral Hazard*, 111 MICH. L. REV. 197, 206 (2012) ("When underwriting individual policies (as opposed to group policies), insurers can refine their premiums through the practice of 'feature rating,' in which they examine the insured's individual risk characteristics and adjust premiums accordingly.").

100. In addition to the factors discussed *supra* Sections I.A. and I.B., general inflationary pressure will push up premiums each year, for both a constant amount of coverage (as insurers' fixed costs rise) and for coverage amounts that adjust for replacement costs (as replacement costs, coverage amounts, and premiums increase over time). Inflation alone would contribute a twenty-four percent increase in general costs from January 2019 through March 2024. Calculating CPI from Jan. 2019 to Mar. 2024, BUREAU OF LAB. STATS., https://data.bls.gov/cgi-bin/cpicalc.pl (enter a $1 amount, then enter the starting date of January, 2019 and end date of March, 2024, and then calculate).

over low reinsurance capacity at high prices, "all companies secured adequate reinsurance coverage, experiencing an average risk adjusted rate increase of around 27 percent, lower than the initially estimated 50 percent."[101] This trend implies lower rate increases, rather than actual rate decreases. Other prominent commentators have expressed similar sentiments.[102]

It is doubtlessly true that the full effect of reform efforts has yet to materialize. Litigation takes time, and we have not yet approached the point at which legislative efforts would fully influence current homeowners insurance policies and the suits filed to enforce those policies. Once existing litigation related to earlier policies clears through the judicial system, then the full impact of the legislative changes can be assessed.[103]

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101. YAWORSKY, *supra* note 12, at 23. The Florida Office of Insurance Regulation also recently touted the news that ten insurers filed no annual rate increases, while eight filed for rate decreases. FLA. OFF. OF INS., FLORIDA PROPERTY INSURANCE MARKET UPDATE (2024), https://floir.com/docs-sf/property-casualty-libraries/property-insurance-market-overview/insurance-update-may-2024.pdf?sfvrsn=1f0259bb_2. However, the NAIC reports there are at least 101 insurers in Florida in 2022; consequently, if all insurers have filed rates for 2024, apparently eighty percent of insurers are filing for rate increases. *Market Conduct Annual Statement Scorecard*, NAIC, https://content.naic.org/mcas_data_dashboard.htm (last visited Oct. 1, 2024).

102. *See, e.g.*, Zizo, *supra* note 31 (quote from Lisa Miller) ("I don't think rates are gonna go down dramatically . . . . We can't change the weather. We can't change inflation. Litigation is what litigation is, but we can try to do our best to stem some of these rate increases."); INSURANCE INFORMATION INSTITUTE, *supra* note 3 (quote from Mark Friedlander) ("The first goal of this legislation is to moderate rate increases. . . . If Florida could get into the high single digits, similar to the national average increase of 9 percent in 2022, that would be a big win in our eyes.").

103. *See generally* Caden DeLisa, *Despite Persisting Challenges, Florida's Property Insurance Market Shows Improvement Amid Reforms*, THE CAPITOLIST (Apr. 25, 2024), https://thecapitolist.com/despite-persisting-challenges-floridas-property-insurance-market-shows-improvement-amid-reforms/ (quote from Florida's Chief Financial Officer Jimmy Patronis) ("When those [legislative] changes [were] made, we needed 12 to 18 months for their corrections to take effect."); Céline McArthur, *What Are Florida Lawmakers Doing to Lower Your Property Insurance Rates? WINK Investigative Reporter Goes to Tallahassee to Find Out*, WINK (Feb. 7, 2024), https://winknews.com/2024/02/07/what-are-florida-lawmakers-doing-to-lower-your-property-insurance-rates-wink-investigative-reporter-goes-to-tallahassee-to-find-out/ (quoting Senator Jim Boyd, chairman of the Banking and Insurance Committee, as offering the same timeline).

Still, when the main accepted driver of recent rate increases is reversed, one should expect that so too would the course of premiums. Continued rate increases, even modest ones, could be justified if insurers' overall expected costs continued to rise. Why then are rates still rising? Cost increases could be occurring if other factors are still increasing insurers' exposures at a faster pace than litigation reform is shrinking them, but there has been little discussion of what those factors might be. I return to considering some of these factors in Part III. Before doing so, I highlight some other recent policy proposals that respond to the failure of premiums to decline even as excessive litigation and fraud are presumably retreating.

B. NEWER PROPOSALS

Recent proposals, like the dramatic legislative reform of 2021 through 2023, carry the same goal of reducing homeowners insurance premiums, although they suggest different avenues for accomplishing that goal. Some propose changes directly targeting high rates. Others have the potential to alter fundamentally the existing homeowners insurance market. None, however, likely offers the type of long-lasting meaningful positive effects that their advocates desire.

1. Tax Cuts

Most modestly, Florida's legislature is currently considering a tax cut on homeowners insurance premiums comprised of a reduction in assessments for the State's insurance solvency guarantee fund and a reduction in State premium taxes levied on homeowners insurance.[104] Collectively, these tax cuts would save homeowners up to 3.5% of their premiums for each year the cuts are in effect.[105] Setting aside whether these tax cuts would be financially sustainable over the long term, they do not affect any underlying fundamentals contributing to recent premium increases. Consequently, they should be expected to have, at best, a marginal effect on premiums, with "those

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104. Gray Rohrer, *Gov. DeSantis' Insurance Cut Back on Track as House Adds to Tax Package*, FLA. POL. (Feb. 20, 2024), https://floridapolitics.com/archives/660415-gov-desantis-insurance-cut-back-on-track-as-house-adds-to-tax-package/.

105. *Id.*

reductions . . . certain to be less than annual increases already facing most Florida homeowners and businesses."[106]

2. Mortgage-Only Policies

More aggressively, State Representatives Alina Garcia and Mike Redondo introduced a bill that would require insurers to offer mortgage-only policies that insure only the dwelling's unpaid principal on an outstanding mortgage.[107] Although policyholders could still buy traditional policies with coverage limits up to a home's total replacement cost, the bill would allow them to choose these alternative policies with lower coverage limits equal to a mortgage's outstanding principal. Lower coverage limits should also result in lower premiums.

Although this legislation may nominally reduce premiums, it is problematic for several other reasons. First, any reduction in premiums is likely to be more modest than hoped. Insurers' cost of adding an incremental dollar to a house's coverage limits declines as those limits increase. Low coverage limits cap an insurer's exposure only for relatively rare total or close-to-total losses; more commonplace smaller, partial losses will trigger similar payouts for both mortgage-only and total replacement cost policies as long as the outstanding mortgage balance exceeds the loss. An insurer covering a $300,000 home with a $200,000 mortgage, for example, will face identical expected losses for a roof replacement under either a mortgage-only policy with a $200,000 limit or a replacement cost policy with a $300,000 limit; only that subset of overall losses that will cause more than $200,000 in expected losses will result in differing premiums. This declining marginal cost of coverage justifies why standard homeowners insurance policies require a home to be insured for at least eighty percent of its replacement cost for replacement coverage to apply.[108] This math is reinforced when one considers that the decrease

106. John Kennedy, *As DeSantis Grip on Lawmakers Loosens, Florida Senate Comes to Rescue on Insurance Tax Cut*, TALLAHASSEE DEMOCRAT, https://www.tallahassee.com/story/news/politics/2024/02/19/florida-senate-comes-to-gov-desantis-rescue-insurance-tax-cut-2024-legislative-session/72662158007/ (last updated Feb. 20, 2024, 4:25 PM) (quoting comments by Mark Friedlander).

107. H.B. 809, 2024 Leg., Reg. Sess. (Fla. 2023).

108. *See, e.g.*, *Homeowners 3 – Special Form*, INS. SERVS. OFF., INC. (1999), https://www.iii.org/sites/default/files/docs/pdf/HO3_sample.pdf (providing an example a standard homeowners insurance policy, which has this eighty-percent-insured requirement in Section I.C.2).

in dwelling coverage would not flow through to personal property or to liability coverage, which under the proposed legislation would continue to be set by existing approaches.[109] So, cutting coverage limits in half should reduce premiums by significantly less than half.

Second, mortgage-only policies make it easier for policyholders to opt out of insurance coverage for their home equity, raising adverse selection concerns.[110] If mortgage holders can now self-insure their home equity, then we would expect policyholders with below-market risk levels to exit standard homeowners insurance markets, increasing risk levels of the remaining pool. As those risk levels rise, so too will premiums. Perversely, mortgage-only policies may therefore result in premium increases for policyholders with traditional policies, encouraging more of them to exit.

Exit from traditional insurance policies also raises public policy concerns. Mortgage-only insurance policies mean that policyholders would self-insure the equity in their home, which is most commonly their largest asset.[111] Individual policyholders are in a poor position to bear the risk of losing this asset, as a mortgage-only policy would require, and standard economic theory suggests, that transferring this risk to insurance companies at actuarially-fair prices could make all parties better off.[112] The worry with mortgage-only policies is that policyholders who self-insure their home equity are doing so either because they do not appreciate the severity of this risk or because they are anticipating a government bailout in the event of a loss. The first situation is undesirable; and for the second, if externalizing risks to a government

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109. *See, e.g.*, Brooklee Han, *New Bill in Florida Looks to Help Cut Homeowner's Insurance Premium Costs*, HOUSINGWIRE (Jan. 4, 2024, 11:26 AM), https://www.housingwire.com/articles/new-bill-in-florida-looks-to-help-cut-home-owners-insurance-premium-costs/ ("[T]his type of policy would not cover the contents of the home.").

110. For additional discussion on when adverse selection concerns will be acute and when they will not, see Peter Siegelman, *Adverse Selection in Insurance Markets: An Exaggerated Threat*, 113 YALE L.J. 1223 (2004).

111. Jamie Hopkins, *Study Uncovers Opportunities for Using Housing Wealth in Retirement*, FORBES (Mar. 28, 2024, 8:56 AM), https://www.forbes.com/sites/jamiehopkins/2024/03/28/study-uncovers-opportunities-for-using-housing-wealth-in-retirement/.

112. Peter Molk, *Private Versus Public Insurance for Natural Hazards: Individual Behavior's Role in Loss Mitigation*, *in* RISK ANALYSIS OF NATURAL HAZARDS 265, *passim* (Paolo Gardoni et al. eds., 2015); Peter Molk, *Barriers to Insurance Innovation*, YALE J. ON REG. (forthcoming 2025) (manuscript 3–7), https://www.yalelawjournal.org/pdf/237_yy2gwsnp.pdf.

backer were the goal, then it could be better achieved by having the government directly provide insurance to all rather than to the select group that gambled on an implicit backstop.[113] Indeed, some policymakers have proposed precisely this plan, which I discuss next.

3. Expand Government-Backed Insurance

Two plans have been suggested to shift Florida's hurricane risk to public entities. The first plan would externalize it to all Florida residents, by having the State-run Citizens insurance company provide hurricane coverage;[114] coverage for other risks would remain in the hands of private insurers. The second plan would externalize it to the entire country, by having the federal government issue debt to cover particularly damaging storms. I discuss each in turn.

The proposed plan to expand Citizens has been compared to the National Flood Insurance Program, in which the federal government backstops insurance policies that cover losses from flood risks while private insurers cover losses from other sources.[115] The National Flood Insurance Program is an apt comparison that highlights some of the potential benefits and problems with expanding Citizens to all Florida homeowners. The main economic benefit of this plan would be that it could save the costs associated with having to maintain large reserves to cover unlikely catastrophic losses.[116] Private

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113. *See generally* Peter Molk, *The Government's Role in Climate Change Insurance*, 43 B.C. ENV'T AFFS. L. REV. 411, 416–23 (2016) (discussing the relative benefits and costs of government-provided versus private insurance).

114. H.B. 1213, 2024 Leg., Reg. Sess. (Fla. 2024). *See generally* Lawrence Mower, *Florida Lawmakers Pitch Radical Idea to Solve Property Insurance Crisis*, TAMPA BAY TIMES (Feb. 6, 2024), https://www.tampabay.com/news/florida-politics/2024/02/06/florida-property-home-insurance-crisis-hurricane-premiums-ian-citizens/ (summarizing the bill's contents).

115. *See* Mower, *supra* note 114 ("Instead of Floridians paying hurricane premiums to private, for-profit insurers, they could be covered by the state-run Citizens Property Insurance, and probably for cheaper. Citizens would collect the money, much like the National Flood Insurance Program. . . .").

116. Advocates also highlight the benefit of foregoing the profits and executive compensation payments associated with for-profit insurers. *Id.* However, these benefits come with the potential for the offsetting costs of increased administrative expenses and inefficiencies associated with removing profit-generating competitive effects. *See generally* HENRY HANSMANN, THE OWNERSHIP OF ENTERPRISE 35–49 (1996) (discussing the costs and benefits of various ownership methods); Peter Molk,

insurers' costs of maintaining reserves for these events can be sizable, as the money set aside cannot be put towards other profitable ventures, and the tax treatment of these reserves is not always favorable.[117] State and federal governments, however, have the capacity to levy taxes and a greater capacity to borrow funds than private insurers, allowing them to offer similar solvency commitments with lower standing reserves and, therefore, lower financial costs.[118] It should be noted, however, that government-backed programs are often criticized when they attempt to leverage this advantage by maintaining slim excess reserves,[119] raising questions about whether this advantage could actually be achieved in practice.

Moreover, historically government-sponsored insurance programs, including those in Florida,[120] have had difficulty charging anything close to actuarially fair premiums, instead undercharging high risks and overcharging low ones. In addition to fairness concerns raised by this type of model, this type of pricing sends distortionary market signals, subsidizing high-risk activities and discouraging low ones.[121] This result is precisely the opposite of what policymakers should prefer.[122]

The Puzzling Lack of Cooperatives, 88 TUL. L. REV. 899, 905–10 (2014) (considering several different ownership methods).

117. Logue, *supra* note 26, at 913–18.

118. Molk, *supra* note 113, at 417.

119. *See, e.g.*, Ryan Smith, *DeSantis: Florida Insurer of Last Resort Is "Not Solvent"*, INS. BUS. (Feb. 29, 2024), https://www.insurancebusinessmag.com/us/news/catastrophe/desantis-florida-insurer-of-last-resort-is-not-solvent-479270.aspx (Governor Ron DeSantis criticizing Citizens); Mary Williams Walsh, *A Broke, and Broken, Flood Insurance Program*, N.Y. TIMES (Nov. 4, 2017), https://www.nytimes.com/2017/11/04/business/a-broke-and-broken-flood-insurance-program.html ("[T]he [National Flood Insurance P]rogram was supposed to take the burden off taxpayers but has not . . . ."); Cary Barbor & Amanda Wittamore, *Roach and Cassel Visit FGCU to Talk Insurance, Bipartisanship*, WGCU, https://news.wgcu.org/section/public-affairs/2024-04-04/roach-cassel-visit-fgcu-to-talk-insurance-bipartisanship (Apr. 4, 2024, 4:53 PM) (Mark Friedlander) ("[T]he bill is a bad idea . . . . Citizens has extreme risk exposure, to the point where a major hurricane could deplete its reserves and trigger what is commonly called the hurricane tax, which is a surcharge that could be applied not only to all Citizens customers' premium bills, but all other policyholders in the state of Florida.").

120. Omri Ben-Shahar & Kyle D. Logue, *The Perverse Effects of Subsidized Weather Insurance*, 68 STAN. L. REV. 571, 597–609 (2016); Walsh, *supra* note 119.

121. Ben-Shahar & Logue, *supra* note 120 at 611–16.

122. Molk, *supra* note 113, at 416–23.

There is no inherent requirement that every public insurance plan must follow this distortionary pricing path. Yet, even if a Citizens-for-all model were able to defy the experience of other government-run programs, an undeniably negative feature of this plan is that it would generate new points of friction in the insurance claims settlement process, just as occurs with the National Flood Insurance Program. Homeowners insurance dwelling coverage is "all risk" coverage, meaning that damage from any non-excluded risk will be covered by insurers. Since hurricanes are a non-excluded risk, insurers do not care much about whether a loss is classified as due to a hurricane rather than a hurricane's non-excluded associated non-flood effects, like wind, or whether a storm system is classified as a hurricane versus a tropical storm. Currently, the difference matters only for triggering a policy's hurricane deductible, which might be higher than the standard deductible, but which will still be relatively modest in the scheme of overall hurricane losses.[123] However, if hurricane losses are covered by Citizens while other losses are covered by private insurers, then both the State and private insurers will care deeply about whether losses are attributed to hurricanes or something else, since that determination decides which entity will bear financial losses. In the meantime, policyholders may go without insurance payouts to deal with financial losses at precisely the time those payments would be most useful, while insurance companies work through these disputes in the background. Hurricane Katrina highlighted just how problematic these delays can be, as legal disputes dragged on for years over whether losses were due to hurricane winds, which would be covered by private insurers, or the flooding associated with those winds, which would be covered by the federal government.[124] These issues were still being decided sixteen years after the damage occurred.[125]

123. *What Are Named Storm Deductibles?,* NAT'L ASS'N OF INS. COMM'RS (June 3, 2024), https://content.naic.org/article/consumer-insight-what-are-named-storm-deductibles ("Deductibles for named storms] can range from 1% to 10% of the value of the insured home . . . [and] can also be a fixed dollar amount.").

124. *See, e.g.*, ROBERT P. HARTWIG & CLAIRE WILKINSON, INS. INFO. INST., HURRICANE KATRINA: THE FIVE YEAR ANNIVERSARY 5, https://www.iii.org/sites/default/files/1007Katrina5Anniversary.pdf ("Whether damage was caused by wind or water became a key focus of the post-Katrina litigation.").

125. *See, e.g.*, Anita Lee, *State Farm Will Pay Feds $100 Million over Hurricane Katrina Insurance Claims*, NOLA (Aug. 25, 2022), https://www.nola.com/news/courts/state-farm-will-pay-feds-100-million-over-hurricane-katrina-insurance-claims/article_dda1d866-24ce-11ed-9eae-db37f9eda4ab.html ("State Farm Fire and Casualty Co. has agreed to pay the federal

Further fractionating coverage across private insurers, the federal government, and the state of Florida promises to bring additional disputes like these. Therefore, unless expanding Citizens promises potential benefits that outweigh these costs (and any other costs like more government-induced cross-subsidization or inefficiencies), other reform efforts should likely be a priority.

The second proposed plan, instead of externalizing risks just across Florida, would externalize risks to the federal government—and therefore across America. This plan, advocated by Florida Congressman Jared Moskowitz, would have the U.S. Treasury issue debt to cover particularly damaging storms,[126] effectively turning the Treasury into a reinsurance company that provides the top layer of reinsurance coverage to private insurers. Like the Florida-specific plan, this alternative offers the benefit of maintaining lower reserves, which reduces premiums by the costs of maintaining higher reserves.[127] Unlike the Florida-specific plan, this plan does not divide up coverage questions across different entities, so it should not result in additional coverage disputes.

However, expanding government-backed insurance—either within the state of Florida or across the country—does not directly address underlying issues that have led to recent cost increases. Instead, they target (at best) indirect effects arising from those issues[128] and may shift costs from high-risk homeowners to others, which sends inappropriate loss-prevention signals to

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government $100 million . . . settling a lawsuit that two whistleblowers filed against the company more than 16 years ago.").

126. *Moskowitz Reintroduces Bill to Reduce Cost of Homeowners Insurance*, JARED MOSKOWTIZ: U.S. HOUSE OF REPRESENTATIVES (May 18, 2023), https://moskowitz.house.gov/posts/natural-disaster-risk-reinsurance-program-act-of-2023; Ron Hurtibise, *South Florida Proposes Lowering Insurance Costs 25%*, GOVERNING (Mar. 15, 2024), https://www.governing.com/finance/south-florida-proposes-lowering-insurance-costs-25.

127. The Bill's advocates argue that the plan would reduce premiums by twenty-five percent, but those reductions overstate the economic benefits of the plan, because much of the reduction is achieved simply by shifting costs to the Treasury in the event of high-loss years. Hurtibise, *supra* note 126. How to allocate losses is an important issue, but simply shifting one dollar of loss away from policyholders should not count as a pure one-dollar benefit.

128. To the extent cost increases are attributable to increased natural hazard exposure which increases insurers' reserves, and the cost of holding those reserves has an attenuated effect on recent cost increases.

homeowners. This series of proposals should therefore not be expected to have a long-term, lasting impact on reducing insurers' costs.

4. State-Subsidized Home Hardening

The final proposal I consider here is one that subsidizes home improvements to resist hurricane damage. Originally passed in 2006 and updated as part of 2022's legislative efforts,[129] the program provides free home inspections to identify potential home improvements to increase hurricane resilience, and it provides state matching funds equal to 200% of homeowner investments into hurricane resistance improvements.[130] To be eligible, homeowners must own relatively older, lower-value homes in higher-risk areas.[131]

Bills in 2024 have proposed expanding this program along several dimensions. In addition to providing more money to the program, proposals would open eligibility to condominiums and provide reimbursements for a broader range of contractors, while prioritizing eligibility for older and less wealthy homeowners.[132]

Home hardening programs are the principal policy response aimed at causes of high premiums other than excessive litigation and insurance fraud. They therefore provide a valuable alternative to most of the recent legislative attention, particularly given homeowners premiums' stubborn refusal to decrease meaningfully in the wake of those legislative efforts. By enhancing homes' loss resistances, home hardening brings the promise of reducing premiums directly by decreasing insurers' expected losses.

However, this program is also not immune from criticism. Because only the highest-risk geographic areas in Florida are eligible, but all taxpayers fund the improvements, the program effectively cross-subsidizes participating policyholders in high-risk areas, bringing the same fairness and efficiency

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129. C.A. Bridges, *My Safe Florida Home Bill Adds $100 Million in Funding, Prioritizes Low-Income Homeowners*, TALLAHASSEE DEMOCRAT, https://www.tallahassee.com/story/news/politics/2024/02/20/my-florida-safe-home-new-funding-applications-when/72668278007/ (last updated Mar. 8, 2024, 8:18 AM).

130. *My Safe Florida Home*, FLA. DEP'T OF FIN. SERVS., https://mysafeflhome.com/ (last visited Aug. 29, 2024).

131. *Id.*

132. Bridges, *supra* note 129.

concerns raised earlier in the context of government-backed insurance.[133] Additionally, although the program is heavily subsidized, policyholders must still pay one-third of the costs associated with home hardening.[134] Since these costs regularly run in the thousands of dollars, those numbers may be simply too high for some policyholders to afford, even when heavily subsidized, making uptake lower than would be optimal and keeping the lowest-income homeowners from making desirable improvements.

IV. ADDITIONAL REFORM SUGGESTIONS

Policymakers have devoted an impressive amount of attention to addressing Florida's high homeowners insurance premiums. Although existing efforts hopefully have addressed at least the excessive litigation and insurance fraud problems, more can still be done. Consequently, I close by offering two concrete suggestions to further enhance any positive effects on premium reversals, and one related concrete suggestion on regulatory best practices.

A. LEVERAGE CITIZENS'S INFLUENCE

State-subsidized home hardening has the potential to reduce, directly, homeowners' risk levels and therefore their premiums. Two main problems with the existing approach are that policyholders must still front a significant percentage of the improvement costs, and that the costs of the state subsidy are borne by all residents of the State. Both these factors could be addressed, particularly for those policyholders in the state-backed Citizens program.

Citizens serves as the insurer of last resort for Florida homeowners, emerging as the choice when there are either no private insurer options or no private insurer options at affordable prices.[135] Although the State has engaged in concerted efforts to reduce the number of policyholders within the program,

133. *See supra* pp. 26–27 ("The worry with mortgage-only policies is that policyholders that self-insure their home equity are doing so either because they do not appreciate the severity of this risk or because they are anticipating a government bailout in the event of a loss. The first situation is undesirable; and for the second, if externalizing risks to a government backer were the goal, then it could be better achieved by having the government directly provide insurance to all rather than to the select group that gambled on an implicit backstop.").

134. *My Safe Florida Home*, *supra* note 130.

135. *Programs*, CITIZENS PROP. INS. CORP. OF FLA., https://www.citizensfla.com/programs (last visited Oct. 2, 2024).

many remain customers for multiple years as they lack the practical ability to obtain private insurance.[136] For those homeowners who are expected to remain with Citizens for multiple years, the State could offer to cover 100% of cost-effective home hardening costs in exchange for capturing some, most, or all of the premium reductions due to the associated reduction in risk over a period of time. If a more aggressive approach is needed to induce greater policyholder uptake, Citizens could even require those improvements to be made as a condition of coverage, a requirement that could have considerable force given Citizens's position as policyholders' insurer of last resort.

This suggestion solves one of the recurring problems in private homeowners insurance contracts. Because those contracts are written for terms of only one year, it is rarely in insurers' interests to invest in offering policyholders loss mitigation advice or incentives that provide long-term benefits, since the cost of those programs will be borne by the single investing insurer but the benefits accrue to all future insurers who cover the risk.[137] Since Citizens offers what will be effectively multiyear policies, the math more often may work out so that improvements will end up being cost-effective over the time a policyholder remains at the company, meaning Citizens will be in a better financial position even if it pays for all of the home improvement costs, since it can capture some of the benefits of the reduced loss exposure. Citizens's incentive to offer these improvements arguably becomes even stronger still, since as a State-owned enterprise it lacks the same strong profit motivation of most private insurers and therefore may be more interested in providing benefits to its policyholder-constituents.[138]

Moreover, the same logic could apply more broadly beyond home improvement projects for Citizens policyholders. The State could consider making the same offer to homeowners of private insurers, paying for home improvements in exchange for a share of associated premium reductions for

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136. *See generally Policies in Force*, CITIZENS PROP. INS. CORP. OF FLA., https://www.citizensfla.com/policies-in-force (last visited May 9, 2024) (identifying the number of participating policyholders at the end of each month).

137. *See generally* HOWARD C. KUNREUTHER, MARK V. PAULY & STACEY MCMORROW, INSURANCE AND BEHAVIORAL ECONOMICS: IMPROVING DECISIONS IN THE MOST MISUNDERSTOOD INDUSTRY 236–38 (2012) (examining the related problem of insufficient incentives for policyholders to adopt loss mitigation programs because of short-term policies).

138. For discussion of how ownership structure can influence an insurer's operations, see Peter Molk, *The Ownership of Health Insurers*, 2016 U. ILL. L. REV. 873.

a period of time.[139] Since homeowners insurers file rate forms with the State detailing premium reductions associated with different rating factors, tracking these premiums would be surprisingly easy, even if policyholders change insurers over time.[140] Or the State could consider undertaking municipal improvement projects that impact broad ranges of homes' loss resistance, paying for those projects by capturing a portion of the premium savings accruing to Citizens-issued policies. These bigger projects can be much more impactful than the type of improvements that individual homeowners can undertake.

B. DIRECTLY DETER FRAUD

The next suggestion is to directly deter insurance fraud directly. While reform advocates did an admirable job of convincing policymakers about the role of excessive litigation and insurance fraud in recent premium increases, the legislative response was mainly to take away the financial rewards for fraud, rather than directly dissuade fraud.

Left out of the discussion about excessive litigation and insurance fraud was a consideration of why these problems arose in Florida in the first place. Recall that the groundwork for these problems arose from one-way fee shifting statutes, widespread assignment of benefits to contractors, contingent fee multipliers, and a three-year post-loss period in which to file claims.[141] This same groundwork, however, also exists in other states, yet those states do not seem to suffer from the dramatic premium increases, excessive litigation, or insurance fraud experienced in Florida. Most states provide one-way fee shifting in insurance disputes.[142] Insurance policy claims also can be freely

139. In fact, there is no requirement that this logic be limited to the State. Presumably private insurers also could subsidize hardening efforts in exchange for a share of future premium discounts for a number of years, with a transferable right to collect this share if the policyholder switches private carriers before the collection period expires.

140. Policyholders receive a copy of these rate discounts as well. *Notice of Premium Discounts for Hurricane Loss Mitigation*, FLA. OFF. OF INS. REGUL. (2010), https://floir.com/docs-sf/default-source/property-and-casualty/oir-b1-1655.pdf.

141. *See supra* pp. 11–14 (discussing these phenomena in detail).

142. *See, e.g.*, Jeffrey C. Bright, *Unilateral Attorney's Fees Clauses: A Proposal to Shift to the Golden Rule*, 61 DRAKE L. REV. 85, 119, 119 n.167 (2012) ("Thirty-one states do not protect weaker parties from one-sided attorney's fees clauses. Such states may provide unique statutes regarding fee-shifting . . . . Several states provide specific statues for vexatious or frivolous litigation as well as statutes for insurance contracts.").

assigned in most states; indeed, courts (including, at one time, Florida's) have even prohibited insurers from restricting post-loss assignment of benefits.[143] Other courts award damages multipliers like Florida's contingency fee multiplier in a variety of situations.[144] Florida's original three-year period after a loss in which to file a claim seems more unusual, but not unique.[145] Nevertheless, other states do not seem to have the same problematic experience as Florida.[146]

Additionally, these background factors that were seen as facilitating excessive litigation and insurance fraud even existed in Florida for years without rampant premium increases. The only meaningful expansion was in 2017, when the State's Supreme Court reaffirmed that the long-extant contingency fee multiplier should not be limited to rare and exceptional cases but rather should apply, among other times, to "discourage insurance companies from contesting valid claims, and to reimburse insureds for their attorney's fees incurred when they must enforce in court their contract with the insurance company."[147] Yet despite these factors existing for years in Florida, litigation did not remain a problem, and premiums did not begin to increase, until 2020.[148]

Assuming increased litigation and fraud were at least a partial driver of recent insurance premium increases, these facts suggest an interesting sociological phenomenon was at play, isolated to the State of Florida. For

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143. *See, e.g.*, Mark Broom, Note, *Assignments of Benefits in the Homeowner's Insurance Market: Why Florida's Rates are Skyrocketing, and How to Control the Spiral*, 38 REV. LITIG. 151, 152 (2018) ("[T]he Florida Supreme Court held over on hundred years ago that anti-assignment provisions in insurance policies do not apply to post-loss assignment.").

144. *See, e.g.*, John P. Dacey, *Focus*, L.A. DAILY J., Aug. 7, 2007, at 7 (discussing multipliers in California).

145. *See, e.g.*, *How Long Do I Have to File an Insurance Claim for Damage to My Home or Business?*, VOSS LAW FIRM, https://www.vosslawfirm.com/library/time-limits-for-filing-a-property-damage-claim.cfm (last visited Aug. 30, 2024) ("Typically, homeowners have one year to file a claim, but this can vary significantly. In some states, you may have two years—or even up to six years—to file a claim.").

146. *See supra* Part I ("Florida features the highest average home insurance costs in America.").

147. Joyce v. Federated Nat'l Ins. Co., 228 So. 3d 1122, 1132 (Fla. 2017) (quoting Bell v. U.S.B. Acquisition Co., 734 So. 2d 403, 410 n.10 (1999)).

148. *See supra* Figure 4.

whatever reason, although the conditions for litigation and fraud were favorable for many years, participants did not begin taking advantage until relatively recently. Perhaps after the practice began to catch on, norms and other factors that would prevent the practice became less of a deterrent as the practice became more socially acceptable, driving increasingly high litigation rates and fraud. Fortunately for other states with the same conditions, the practice has not yet seemed to have spilled over to other jurisdictions. While the story of what finally caused participants to embrace opportunistic behavior—and why similar states have not suffered the same experience—is deserving of more study, for now, it suffices to note that incentives for litigation and fraud, and actual litigation and fraud, need not go hand-in-hand, as years of experience in Florida show.

Existing legislative efforts attempted to remove most of the conditions for excessive litigation and fraud. However, an alternative approach would be to focus on deterring fraud directly, rather than just the incentives that make those practices rewarding. Florida has a Bureau of Insurance Fraud tasked with investigating, among other areas, homeowners insurance fraud.[149] If premium increases were driven by increasing costs from insurance fraud, then some well-publicized prosecutions against those fraudsters could go a long way in deterring the practice. It may be that the proof problems in those cases would be difficult to overcome, but if a clear message were sent that suspected fraud would not be tolerated, then there could be meaningful success in deterring the practice. And, since fraud is seen by many as the major driver of excessive litigation, directly discouraging that underlying cause of high litigation rates could flow through to reducing low merit litigation.

Directly targeting fraud has other benefits too, making it a potentially superior choice when dealing with high litigation and fraud rates. Removing incentives for excessive litigation, as recent reform efforts have done, has undesirable spillover effects, since it deters *all* litigation against insurance companies, not simply the low-merit type. To the extent that litigation is socially valuable, such as when it corrects for undesirable insurer practices or generates useful judicial interpretations of standard-form contract language, this is a bad policy outcome. Consequently, as I develop next, lawmakers should periodically reevaluate the necessity of continuing restrictions that reduce all litigation, both undesirable and desirable.

C. Reevaluate Reform Restrictions Over Time

149. *Bureau of Insurance Fraud*, MY FLA. CFO, https://www.myfloridacfo.com/division/difs/insurance-fraud (last visited Aug. 24, 2024).

Florida's legislative reform dramatically changes the landscape for suing insurance companies. Plaintiffs can no longer assign their benefits to more sophisticated parties to pursue claims on their behalf, and winning plaintiffs' fees will no longer be covered or increased by relevant contingency fee multipliers. While these changes may have the desirable effect of deterring low-merit litigation, they may also have the undesirable effect of deterring high-merit litigation. Claims against insurance companies for wrongfully denied claims often cannot be brought as class actions, because questions of fact in these cases are individualized to each potential class member, even when the claims stem from a common loss cause or claims management practice.[150] In many cases, then, individual policyholders will not have enough at stake to justify suing their insurer, even if the claim has merit.

Florida's pre-reform litigation landscape helped to correct for this problem. Private suits can act as a substitute for costly regulatory oversight across contexts, including in insurance regulation.[151] With those financial incentives removed, the worry is that insurers will be under-deterred from engaging in opportunistic conduct, like denying payouts for plausibly covered claims. In the absence of private litigation, more oversight by other actors could fill some of the vacant space. State regulators would therefore be well served to pay particularly close attention to insurers' claims management practices to make sure this type of conduct does not occur. Indeed, at the urging of Florida's insurance commissioner, part of Florida's recent reforms

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150. *See, e.g.*, Robert S. Gianelli, *Certifying the Insurance Class-Action Case*, ADVOCATE (Nov. 2011), https://www.gmlawyers.com/wp-content/documents/Gianelli-Certifying-the-insurance-class-action-case.pdf ("This leaves the issue of commonality as the central battlefield on certification."); Basurco v. 21st Century Cas. Co., 133 Cal. Rptr. 2d 367, 369 (Cal. Ct. App. 2003) ("The trial court denied plaintiff's class certification motion, finding that common questions of law and fact did not predominate over individual issues and that a class action would not be superior to individual lawsuits. We agree with the reasons given by the trial court and affirm.").

151. *See, e.g.*, Peter Molk & Frank Partnoy, *The Long-Term Effects of Short Selling and Negative Activism*, 2022 U. ILL. L. REV. 1, 30–41 (studying the private attorney general role played by private plaintiffs in securities litigation); Stephen J. Choi, Jessica M. Erickson, & A.C. Pritchard, *Paying for Performance? Attorneys' Fees in Securities Fraud Class Actions*, (Univ. of Mich. L. Sch., L. & Econs. Working Papers, Paper No. 273, 2024), https://papers.ssrn.com/sol3/papers.cfm?abstract_id=4707763 (studying the role of plaintiffs' lawyers in the same context).

included a provision increasing penalties levied against insurers that mishandle claims,[152] a sensible, proactive way to address potential problems from removing the threat of policyholder litigation.

This regulator attention may be particularly warranted given signs suggesting that a handful of insurers generate a disproportionate number of suits from policyholders, even during the pre-reform period. Most Florida insurers experience few lawsuits relative to their overall book of business, at levels comparable to insurers in other states.[153] Some insurers attract policyholder complaints at rates far higher than others.[154] Disparate complaint rates could be consistent with some insurers concentrating business in more fraud-prone areas of the State, in which case fewer policyholder suits are less troubling. However, they could also be consistent with some insurers treating their policyholders unfavorably, in which case fewer policyholder litigation-induced checks against those companies could be troubling.

In addition to careful attention from regulators, then, it may also be fruitful for policymakers and regulators to evaluate periodically whether litigation incentive restrictions could be relaxed. If social norms or regulatory crackdowns shift the landscape so that fraud would not occur even if pre-reform incentives were introduced—as apparently used to be the case for many years in Florida—then policymakers should think about reinstating some of the pre-reform structure so that, at a minimum, meritorious policyholder suits are not discouraged. It may be that reinstating all or any of these incentives never becomes a good idea. However, as long as they remain absent, the threat of insurer opportunism is higher, and so too will be the costs regulators must incur from their increased monitoring to compensate.

V. CONCLUSION

Recent legislative efforts have significantly changed the incentives for policyholders to bring meritless claims and litigation and to engage in insurance fraud—traditionally seen as the principal drivers behind Florida's dramatic increases in homeowners insurance premiums. However, some signs show that additional factors may be at play, especially as premiums continue to remain stubbornly high, and these factors remain largely unaddressed by

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152. S.B. 7052, 2023 Leg., Spec. Sess. (Fla. 2023) (among other things, increasing by 500% the maximum penalties that can be applied to insurers' claims practices).

153. BIRNBAUM, *supra* note 63, at 6.

154. AMERICAN POLICYHOLDER ASSOCIATION, *supra* note 67, at 9.

policymakers. Consideration of the additional reform suggestions in this Article, including leveraging the influence of the State's insurer of last resort and of directly deterring problematic conduct like insurance fraud, may help Florida policymakers if those high premiums persist. Moreover, because legislative reforms deter *all* policyholder litigation, including meritorious claims, it is beneficial to examine critically the efficacy of reform efforts over time and to consider relaxing them when possible. Regulators in other states with similar incentive structures should find the Florida experience helpful, should they eventually experience rising premiums of their own.