**MEMORANDUM**

**To:** Members of the Committee on Financial Services

**From:** Committee Staff

**Date:** October 19, 2023

**Subject:** Housing and Insurance Subcommittee Hearing entitled, "Factors Influencing the High Cost of Insurance for Consumers"

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On Tuesday, October 24 at 2:00 p.m., in Room 2128 of the Rayburn House Office Building, the Subcommittee on Housing and Insurance will hold a hearing entitled, "Factors Influencing the High Cost of Insurance for Consumers." Testifying at the hearing will be:

- **Mr. Robert Gordon**, Senior Vice President, American Property and Casualty Insurance Association (APCIA)
- **Mr. Frank Nutter**, President, Reinsurance Association of America (RAA)
- **Ms. Grace Arnold**, Commissioner, Minnesota Department of Commerce, on behalf of the National Association of Insurance Commissioners (NAIC)
- **Mr. Joseph Petrelli**, President and Co-Founder, Demotech, Inc.
- **Mr. Baird Webel**, Specialist in Financial Economics, Congressional Research Service (CRS)
- **Dr. Carolyn Kousky**, Associate Vice President, Economics and Policy Analysis, Environmental Defense Fund

This hearing will focus on the status of our domestic insurance markets, particularly recent developments that have led to higher costs and lower availability for property and casualty insurance. Topics to be covered will include the overall high cost of insurance, current challenges in individual state markets, and the impact of federal and international regulatory developments. The Committee will explore these dynamics and their impact on consumers.

***Summary***

The U.S. domestic insurance industry is a vital component of our economy that provides financial protections for millions of American consumers and businesses. According to the Insurance Information Institute, the U.S. insurance industry generated $1.4 trillion in net premiums written and employed nearly 3 million people in 2021.[1] Property/casualty (P/C) lines of coverage such as

[1] Insurance Information Institute "Insurance Industry at a Glance," available at: https://www.iii.org/publications/a-firm-foundation-how-insurance-supports-the-economy/introduction/insurance-industry-at-a-glance.

homeowners, auto, and commercial insurance generated over half of those premiums, with auto accounting for the largest amount of direct premiums written.

However, in recent years many consumers have experienced a sharp increase in the cost of insurance products. Some consumers have also experienced a decrease in the availability of certain lines of coverage. The rising costs and reduced access to insurance represents a significant challenge for consumers and insurance providers alike. This so-called "hardening" of insurance markets, while typically cyclical, has led to some concerns that current market conditions might be prolonged or even reflect a fundamental shift in the factors that affect the cost of providing insurance to consumers. In response, certain jurisdictions have sought to address higher costs through strict price controls or new government mandates, only to see availability go down - thus exacerbating the negative impact on consumers. While insurance is, and should remain, a state regulated product, it is important that regulators encourage greater private sector insurance competition, deployment, and innovation to maintain well-functioning markets.

*State-Based Insurance Regulation Model*

For nearly 150 years, the states have regulated the business of insurance. Congress has periodically reviewed the effectiveness of state-based insurance regulation, and together with the states have worked to ensure greater regulatory uniformity within this system. In 1945, Congress passed the McCarran-Ferguson Act (15 U.S.C. 1011 et seq.), which confirmed the states' regulatory authority over insurance except where a federal law expressly provides otherwise.

Since enactment of the McCarran-Ferguson Act, insurance companies have been subject to comprehensive state regulation for both the products they sell and the financial solvency of their operations. In both instances, insurers are subject to intense scrutiny regarding their pricing, risk modeling, and use of historical and analytical information. Insurance is, and should be, a data-driven product that reflects the real-world risks and costs of providing access to financial protection against a peril in a marketplace.

While our state-based insurance model has long been successful, it is not immune from misguided policy choices. In addition to its prudential rules, in some places, regulators are attempting to add new requirements that are increasingly incompatible with how insurance companies operate in a solvent manner. For example, some jurisdictions are restricting the use of actual loss data or predictive modeling in setting premiums for certain types of perils. Instead of making insurance more consumer-accessible, concerns have been raised that these mandates will only further distort insurance markets leading to higher premiums and decreased product availability. The withdrawal of insurance companies has a pronounced impact on consumers and, in many cases, leaves them with very few affordable insurance options.[2]

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[2] Michael R. Blood, "California insurance market rattled by withdrawal of major companies," Associated Press, June 5, 2023, available at: https://apnews.com/article/california-wildfire-insurance-e31bef0ed7eeddcde096a5b8f2c1768f.

*Impact of Inflation*

In addition to poor regulatory decision-making in certain places, persistent inflation has had a damaging impact on insurance markets across the country. This period of increased inflation has resulted in insurance companies experiencing higher claims payouts and operating costs, leading to more expensive premiums for the consumer. For example, as the cost of construction materials continues to increase, this leads to higher repair and replacement costs for damaged property. Supply chain disruptions also have strong effects on the costs of certain goods, such as vehicle parts, microchips, and other commodities. When the costs of these products rise, premiums must increase as insurance carriers seek to maintain profitable and remain competitive. According to a recent McKinsey estimate, in 2021, rising prices contributed to an approximately $30 billion increase in loss costs—the amount an insurer must pay to cover claims—over and above historical loss trends.[3]

*Reinsurance*

Reinsurance is a financial arrangement used by insurance companies to manage and mitigate their own risk. It involves one insurance company (the ceding company) transferring a portion of the insured risk it has underwritten to another insurance company (the reinsurer). This is done to spread the risk and limit potential financial losses that the ceding company might face if it were to pay out large and unexpected claims[4]. Overall, reinsurance helps maintain the financial stability and solvency of insurance companies and ensures that they can fulfill policyholders' claims during challenging circumstances like we see today.

Given that risks and associated costs have only increased over the past few years for insurance companies, higher reinsurance rates are contributing to the higher cost of premiums faced by customers. Reinsurance rates have increased over the past few years for a variety of reasons, including the COVID-19 pandemic, inflation, and the increased costs of natural disasters. According to a recent report from broker Gallagher Re, U.S. property catastrophe reinsurance rates rose by as much as 50 percent annually as measured by a key July 1 renewal date, with states such as California and Florida contributing significantly to these increases.[5] Most analysts predict reinsurance rates will most likely continue to rise across all business lines going into 2024, but at a slower pace than 2023. According to Fitch Ratings analyst Robert Mazzuoli: "Our current

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[3] Kia Javanmardian, Sebastian Kohls, Gavin McPhail, and Fritz Nauck, "Countering inflation: How US P&C insurers can build resilience," McKinsey & Company, August 25, 2022, available at: https://www.mckinsey.com/industries/financial-services/our-insights/countering-inflation-how-us-p-and-c-insurers-can-build-resilience.

[4] The National Association of Insurance Commissioners Center for Insurance Policy and Research, "Reinsurance," updated June 1, 2023, available at: https://content.naic.org/cipr-topics/reinsurance.

[5] Carolyn Cohn and Noor Zainab Hussain, "U.S. property catastrophe reinsurance rates rise up to 50% on July 1, report says," Reuters, July 3, 2023, available at: https://www.reuters.com/world/us/us-property-catastrophe-reinsurance-rates-rise-up-50-july-1-report-2023-07-03/.

expectation is the hard market environment will remain for 2024. We expect very incremental price increases…lower than the ones we have seen."[6]

*Commercial Insurance Challenges*

While the cost of consumer P/C insurance continues to increase, insurance costs have also climbed dramatically for commercial properties. According to Moody's, commercial real-estate insurance costs have risen 7.6 percent annually on average since 2017.[7] These increases represent a significant cost increase for developers and property owners and come at a particularly precarious time in the market given the increased costs of capital. Multifamily properties have been hit especially hard, leading to rising rents or prices that are then passed on to potential tenants or owners. These insurance increases are in many cases more damaging to property owners than rising interest rates and also exasperate housing affordability challenges.[8]

**Legislative Proposals**

- ***H.R. 5535, the Insurance Data Protection Act*** *(Rep. Fitzgerald)*

This bill would restrict the ability of the Federal Insurance Office (FIO) of the Department of the Treasury and other financial regulators from collecting data directly from insurance companies via subpoena, and ensure the confidentiality of any data collected from insurance companies.

- ***H.R. 2933, the Federal Insurance Office Elimination Act*** *(Rep. Cline)*

This bill would eliminate the Federal Insurance Office (FIO) within the Department of the Treasury. The bill would also remove the FIO director as a nonvoting member of the Financial Stability Oversight Council.

- ***H. Res. ___, expressing the continued support of Congress for the McCarran-Ferguson Act and its State-based regulatory system for the business of insurance*** *(Rep. Davidson)*

This Discussion Draft resolution would affirm Congress' support for the McCarran-Ferguson Act and its state-based regulatory system for the business of insurance as the law of the United States.

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[6] Carolyn Cohn, "Reinsurance rates to rise in 2024, soften in 2025, Fitch analyst says," Reuters, September 7, 2023, available at: https://www.reuters.com/business/reinsurance-rates-rise-2024-soften-2025-fitch-analyst-2023-09-07/#:~:text=Reinsurers%20%2D%20who%20insure%20insurers%20%2D%20have,natural%20catastrophes%2C%20boosting%20their%20profitability.

[7] Kevin Fagan, Natalie Ambrosio Preudhomme, and Caglar Demir, "Insurance Costs Trends Becoming a Headache for the CRE Market," Moody's Analytics, August 3, 2023, available at: https://cre.moodysanalytics.com/insights/cre-news/insurance-costs-trends-becoming-a-headache-for-the-cre-market/.

[8] Konrad Putzier, "Surging Insurance Costs Have Come for Office Landlords," The Wall Street Journal, September 26, 2023, available at: https://www.wsj.com/real-estate/commercial/commercial-real-estates-next-big-headache-spiraling-insurance-costs-604efe4d?mod=real-estate_feat2_commercial_pos1.