Demotech, Inc.

My name is Joseph Petrelli. I have been employed in the insurance industry since 1969, when I entered The College of Insurance on a work-study program. After graduation, I was employed by a regional insurer for four years, and then, a national insurer for two years. After many years as a consulting actuary, on September 9, 1985, Sharon Romano Petrelli and I co-founded Demotech, Inc., a financial analysis firm focused on the insurance industry. In 1989, we became the first insurer rating service to review and rate independent, regional and specialty insurers. In 1992, we became the first to review and rate Title underwriters. On July 11, 2022, Demotech secured registration with the US Securities and Exchange Commission Office of Credit Ratings as the tenth nationally recognized statistical rating organization. Our classification is Insurance Companies. We rate and follow 450 insurers operating in every state, writing virtually all lines of insurance.

As a credentialed actuary who has supervised or prepared thousands of rate, rule or form filings presented to virtually every state department of insurance, in addition to preparing approximately 1,600 statements of actuarial opinion as regards loss and loss adjustment expense reserves of insurers operating in multiple jurisdictions, I share my observations on the drivers of the availability and affordability crisis impacting way too many consumers.

The material damage lines of insurance; Homeowners, Farmowners, Automobile Physical Damage, are impacted by:

- inflationary costs on core materials; rugs, tar paper, windows, lumber, etc.
- inflationary costs on the salaries, benefits and training of skilled artisans
- shortage of skilled professionals to effect repairs
- cost of reinsurance, i.e., insurance for insurers, to facilitate sharing the cost of natural disasters, including flood, hurricane, wildfire, hail, tornado, or earthquake
- the efficacy and calibration of catastrophe modeling and their simulations.

Casualty lines of insurance are also impacted by claim frequency as well as claim inflation.

In addition to the traditional drivers of cost, research pioneered by Demotech in March, 2022, undertaken by Todd Kozikowski, a technologist with twenty-five years of data analytics, and artificial intelligence expertise, discovered opportunists were using the internet in an effort to secure contested claims against insurers and other targeted established brands across industries.

In response to this discovery, Demotech coined the term "tech-enabled claim instigation" as the confluence of litigation funding, litigation marketing, litigation platforms and search engine optimization by opportunists seeking to secure contested claims. Fortunately, the effort also lead to the development of responses that can be implemented by individual carriers in their effort to address the dilemma impacting the availability and affordability of insurance that distresses consumers. The recently discovered efforts of opportunists has been a significant contributor to the availability and affordability crises, particularly in catastrophe-prone jurisdictions.

Carriers are adversely impacted by tech-enabled claim instigation because the additional contested claims reduce profitability or exacerbate operating losses. Similarly, the solvency of smaller insurers might be threatened. Also, employment in the insurance industry may decline as insurers lay off employees or reduce commissions to producers in an effort to reduce expenses and mitigate

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operating losses. These expense reduction efforts are in addition to the rate increases and coverage restrictions that impact consumers.

Thousands of law firms and public adjusters are utilizing tech-enabled claim instigation. Specific examples provide a sense of the issue. In the southeast, one law firm targeting a small regional carrier utilizes 100+ key words to outrank the carrier for the carrier's own phone number, claims department number, and bill paying site. In a recent period, the firm's payment to Google for successful clicks was approximately $300,000 per month.

In Southern California, 19 law firms in 49 locations target insurers. These nineteen firms sped more than $11 million per year on online advertising. The analysis shows opportunists are securing hundreds of contested cases, which may not need to be contested. This increases the cost for insurers while leading to future increases in policyholders' premiums.

As hurricanes Ian and Idalia approached Florida, in 2022 and 2023 respectively, opportunists set up websites to enable insureds to report claims three to five days before the storms made landfall. As the Maui wild fires blazed opportunists were creating sites for policyholders to report claims – to the opportunists, not to their insurer.

To paraphrase Allen Kerr, Commissioner of Insurance, State of Arkansas, 2015-2020, Chairman of the National Association of Insurance Commissioners Industry Liaison Relations & Market Regulation and Consumers Affairs (D) Committee and the Market Analysis Working Group:

"the threat that ... has been unearthed has never been presented at the state or national level until now. Every carrier should understand … this discovery and move to respond at the earliest possible time."

I thank the Committee Chair, Vice Chair and Ranking Member as well as the Subcommittee Chair, Vice Chair and Ranking for their time. Having affirmed the traditional drivers of insurance costs while providing insights on the discovery of tech-enabled claim instigation and its insidious impact on the availability and affordability of insurance countrywide, particularly in catastrophe prone jurisdictions, I look forward to your questions.

Respectfully submitted,

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