

**SUBCHAPTER E. TEXAS WINDSTORM INSURANCE ASSOCIATION
DIVISION 3. LOSS FUNDING, INCLUDING CATASTROPHE RESERVE TRUST
FUND, FINANCING ARRANGEMENTS, AND PUBLIC SECURITIES
28 TAC §§5.4171 - 5.4173, 5.4181, 5.4182, 5.4184 - 5.4187, and 5.4189 - 5.4192**

1. INTRODUCTION. The Texas Department of Insurance adopts amendments to 28 TAC §§5.4171 - 5.4173, 5.4181, 5.4182, 5.4184 - 5.4187, and 5.4189 - 5.4192 to implement HB 3, 82nd Legislature, 1st Called Session, 2011. Sections 5.4171 - 5.4173, 5.4181, 5.4182, 5.4184 - 5.4187, and 5.4189 - 5.4192 are adopted with changes to the proposed text published in the February 14, 2014, issue of the *Texas Register* (39 TexReg 867).

2. REASONED JUSTIFICATION. The amendments are necessary to establish procedures for making and assessing premium surcharges under Insurance Code Chapter 2210, Subchapter M. Premium surcharges are required to repay class 2 public securities issued in the event of a catastrophe that results in losses that exceed the Texas Windstorm Insurance Association's premium, other revenue, available reserves, and amounts available in the catastrophe reserve trust fund (CRTF). In conjunction with this adoption, the department is also adopting the repeal of existing 28 TAC §5.4183 in a separate order, also published in this issue of the *Texas Register*. This rule adoption also relates to a separate rule adoption concerning loss funding, which is also published in this issue of the *Texas Register*. In that adoption, the department adds new 28 TAC

3302

§§5.4123 - 5.4128, 5.4135, 5.4136, 5.4148, and 5.4149, and amends 28 TAC §§5.4101, 5.4102, 5.4121, 5.4133, 5.4141 - 5.4147, and 5.4164 to implement HB 3.

The department accepted written comments on the loss funding and premium surcharge rule proposals from February 14, 2014, through March 10, 2014, and heard testimony at three public hearings in Beaumont, Austin, and Corpus Christi. During the comment period, the department received approximately 340 comments, both in writing and through oral comments at the public hearings.

In considering all of the comments and in adopting the rules, the department is constrained by two things: (1) the association's funding structure under existing law; and (2) the Legislature's statement in Insurance Code §2210.001 that, "the provision of adequate windstorm and hail insurance is necessary to the economic welfare of this state, and without that insurance, the orderly growth and development of this state would be severely impeded."

The association is the insurer of last resort for windstorm and hail insurance coverage in the catastrophe area along the coast. The association provides insurance coverage to those who are unable to obtain wind and hail insurance in the private market. The catastrophe area includes the 14 first tier coastal counties and parts of Harris County. The association's largest risk exposure is catastrophic losses from hurricanes.

In 2009, the Texas Legislature enacted HB 4409, 81st Legislature, Regular Session, which substantially changed how the association paid for losses that exceeded

3302

its premium, other revenue, and amounts available in the CRTF. HB 4409 amended Insurance Code Chapter 2210 to provide for three classes of public securities to pay for excess losses in the event of a catastrophe. In 2011, HB 3 amended the association's loss funding provisions again to authorize the association to request the issuance of class 1 public securities prior to a catastrophic event, and to permit the association to request the issuance of class 2 and class 3 public securities if the Texas Public Finance Authority (TPFA) is unable to issue all or any portion of the class 1 public securities. Class 1 public securities must be issued when losses in a catastrophe year exceed the association's premium, available revenue, and amounts in the CRTF. Class 1 public securities are to be paid with the association's net premium and other revenue. Losses not paid by class 1 public securities are to be paid by the proceeds of class 2 and class 3 public securities.

Insurance Code §2210.613 describes how the association must pay class 2 public securities. HB 4409 required that class 2 public securities be paid with member insurer assessments and a premium surcharge on coastal policyholders. Thirty percent of the cost of class 2 public securities was to be paid by member insurer assessments. Seventy percent of the cost of class 2 public securities was to be paid by premium surcharges assessed on all policyholders who resided or had operations in, or whose insured property was located in the catastrophe area. HB 3 amended Insurance Code §2210.613 so that 70 percent of the cost of class 2 public securities is to be paid by premium surcharges assessed on all policyholders of policies that cover insured

property located in the catastrophe area, including automobiles principally garaged in the catastrophe area. Member insurer assessments must still pay 30 percent of the cost of class 2 public securities. HB 3 also amended Insurance Code §2210.613 to specify the lines of insurance to which the premium surcharge applies. Before the enactment of HB 3, the premium surcharge in Insurance Code §2210.613 applied to “all property and casualty lines of insurance, other than federal flood insurance, workers’ compensation insurance, accident and health insurance, and medical malpractice insurance.” After HB 3, Insurance Code §2210.613 states that the premium surcharge applies to “all policies of insurance written under the following lines of insurance: fire and allied lines, farm and ranch owners, residential property insurance, private passenger automobile liability and physical damage insurance, and commercial automobile liability and physical damage insurance.”

If the comments are any indication, the adopted rules will displease many, and for different reasons. Coastal residents, businesses, and local governments expressed deep concern over premium surcharges. Some who have no connection to the association wondered why they might have to pay surcharges on their property and casualty insurance premiums to pay for the association’s losses. Many on the coast asked why the cost of windstorm insurance on the coast cannot be shared with the rest of the state. In addressing these comments, the department is constrained by the association’s funding structure under existing law.

3302

Since HB 4409 was enacted in 2009, Texas law has stated that if the association cannot pay claims using the premium its policyholders pay and other revenue, the association must issue public securities that are paid for, in part, by premium surcharges on coastal property and casualty insurance policies, including auto policies. The department adopted rules on premium surcharges consistent with HB 4409. The enactment of HB 3 made the department's rules implementing the premium surcharge required under Insurance Code §2210.613 obsolete. The adopted amendments conform the premium surcharge rules to the current §2210.613. Premium surcharges make up part of the association's funding structure, regardless of the department's rules. The department's rules are necessary to enable the association to effectively implement the funding structure it is given under statute to pay claims.

The insurance industry and other observers expressed concern that the loss funding rules are without statutory authority. Some industry members wrote of the costs they will incur in repaying premium surcharges to policyholders. In addressing these comments, the department is constrained by the need to implement Insurance Code §2210.6136 so that the association can pay claims, while still paying for its share of public securities under that statute. The adopted rules implement §2210.6136 so that the association can issue marketable public securities with which it can pay claims. Leaving the association unable to pay claims following a catastrophic event does not comport with the Legislature's intent that the Texas coast have adequate windstorm and hail insurance. The repayment requirements the industry objects to in comments about

3302

the rules comply with the Legislature's intent that the association, and not all coastal property and casualty insurance policyholders, pay for a specified portion of the public securities issued under §2210.6136.

Where possible, the department changed the proposed rules in response to comments to make them friendlier to consumers and less cumbersome for insurers. For example, the adopted rules require insurers to collect premium surcharges from policyholders in the manner that the insurer collects premium. This gives policyholders the same flexibility in paying premium surcharges that they have in paying premium. The adopted rules contain several changes in consideration of the characteristics of the surplus lines industry.

This order summarizes all of the comments the department received on the proposed rules. Although the department is constrained in the actions it may take to address the comments, the Legislature does not have the same limitations. The comments are presented here in the hope that the Legislature will consider them should it revisit the statutes the adopted rules implement.

In response to comments on the published proposal, the department has adopted changes to the proposed text of §§5.4184 - 5.4186, 5.4189, and 5.4190. The changes do not introduce new subject matter, create additional costs, or affect persons other than those previously on notice from the proposal.

The following explains adopted §§5.4171 - 5.4173, 5.4181, 5.4182, 5.4184-5.4187, and 5.4189-5.4192 in greater detail.

§5.4171. Premium Surcharge Requirement. This section concerns the premium surcharge that insurers must assess if the association issues class 2 public securities under Insurance Code §2210.613. The department amends this section to conform it to other adopted rule amendments and to changes HB 3 made to Insurance Code §2210.613. Subsection (a) is amended for agency style and to clarify that the premium surcharge applies to covered insured property including automobiles principally garaged in the catastrophe area. Subsection (b) is amended to specify the lines of insurance that are subject to the premium surcharge consistent with Insurance Code §2210.613.

§5.4172. Premium Surcharge Definitions. The department amends the definition of insured property to clarify that it includes motorcycles, recreational vehicles, and all other vehicles eligible for coverage under a private passenger automobile or commercial automobile policy. The department adds residential property insurance as a defined term for clarity, and removes the definitions for operations and premises consistent with HB 3.

§5.4173. Determination of the Surcharge Percentage. The department amends this section for agency style and to conform it to other adopted amendments. To conform the section to Insurance Code §2210.613, the department also amends the section to require that the premium surcharge date specified by the commissioner be at least 180 days after the commissioner approves issuance of class 2 public securities.

3302

§5.4181. Premiums to be Surcharged. The department amends this section to clarify that the premium surcharge applies to premium subject to surplus lines premium tax and premium subject to independently procured premium tax.

§5.4182. Method for Determining the Premium Surcharge. The department amends this section so that it applies to policies written in the lines of insurance specified in HB 3. The department also amends this section to allow insurers to determine the premium surcharge for certain composite-rated policies based on the insured address. For these policies, if the insured address is not within a designated catastrophe area, no premium surcharge applies to that policy.

§5.4184. Application of the Surcharges. The department amends this section to require the refund of premium surcharges to policyholders if a policy subject to a premium surcharge is canceled or a midterm or postexpiration change results in a premium decrease. The amended rule requires that insurers, with the exception of affiliated surplus lines insurers and surplus lines agents permitted to credit or refund surcharges on their behalf, credit or refund the excess surcharge within 20 days of the date of the transaction. Affiliated surplus lines insurers and surplus lines agents must credit or refund excess surcharges not later than the last day of the month following the month in which the corresponding transaction was effective. These changes are consistent with the fact that the surcharges may be refunded under Insurance Code §2210.613. The department also deletes references to §5.4183 (relating to Allocation

Method for Other Lines of Insurance), which is being repealed in a separate rule adoption.

§5.4185. Mandatory Premium Surcharge Collection. This section concerns how insurers collect premium surcharges. The department amends the section to require an insurer to collect the premium surcharge proportionately as it collects premiums from the policyholder. This means that if an insurer allows policyholders to pay premiums in installments, policyholders will pay the premium surcharges in the same way.

§5.4186. Remittance of Premium Surcharges. This section provides the procedures for how insurers are to remit the premium surcharges to the association. The department amends this section to conform it to the proposed amendments to §5.4143 (relating to Trust Funds for the Payment of Class 2 Public Securities) and §5.4185 (relating to Mandatory Premium Surcharge Collection).

§5.4187. Offsets. The department amends this section to make it consistent with the amendments to §5.4185 (relating to Mandatory Premium Surcharge Collection) that require insurers to refund premium surcharges to policyholders in certain cases and to conform the section to the proposed amendments to §5.4143 (relating to Trust Funds for the Payment of Class 2 Public Securities).

§5.4189. Notification Requirements. The department amends this section to make the premium surcharge notice that insurers must give policyholders consistent with the amendments to §5.4185 (relating to Mandatory Premium Surcharge Collection) that require insurers to refund premium surcharges to policyholders in certain cases. The

department also amends this section to provide a separate deadline by which affiliated surplus lines insurers and surplus lines agents must provide the notice.

§5.4190. Annual Premium Surcharge Report. This section concerns the annual premium surcharge report that insurers must submit to the association. The department amends this section based on changes to Insurance Code §2210.613 resulting from HB 3. The department also amends subsection (f) to conform the section to the amendments to §5.4143 (relating to Trust Funds for the Payment of Class 2 Public Securities).

§5.4191. Premium Surcharge Reconciliation Report. The department amends this section so that it applies to policies written in the lines of insurance specified in HB 3. The department also amends this section to make it consistent with the amendments to §5.4185 (relating to Mandatory Premium Surcharge Collection) that require insurers to refund premium surcharges to policyholders in certain cases.

§5.4192. Data Collection. This section concerns data that the department may collect from insurers to determine the applicable premium surcharge percentage. The department amends this section to conform it to other amendments relating to the lines of insurance specified in HB 3. The department also deletes references to §5.4183 (relating to Allocation Method for Other Lines of Insurance), which is being repealed in a separate rule adoption.

3302

The department makes changes to the proposed text as a result of comments. These changes do not affect persons not previously on notice, nor does it raise new issues.

As a result of comments, the department changed proposed §5.4184 to allow surplus lines agents to refund or credit excess surcharges on behalf of affiliated surplus lines insurers. Two new subsections make clear that affiliated surplus lines insurers are still responsible for implementing premium surcharges, and set the deadline by which the insurers and their agents must refund or credit excess surcharges to policyholders.

As a result of comments, the department changed proposed §5.4185(b) to require insurers to collect premium surcharges proportionately as they collect premium on the corresponding policy. The department has also removed §5.4185(c) from the adopted rule. Because the adopted rule requires that all insurers collect premium surcharges proportionately as they collect premium, rather than giving them a choice between two collection methods as the proposal did, there is no need to specify that insurers must apply the same method to all policyholders.

As a result of comments, the department changed proposed §5.4186 to remove a reference to the association establishing reporting requirements for surplus lines agents remitting premium surcharges on behalf of surplus lines insurers.

As a result of comments, the department changed proposed §5.4189 to permit affiliated surplus lines insurers to allow surplus lines agents to give policyholders the written notice required in the section. The department has also modified the proposed

3302

§5.4189 to add subsection (e), which states that the department may hold liable an affiliated surplus lines insurer that allows an agent to provide notice of premium surcharges on its behalf for the failure of its agent to comply with the section.

As a result of comments, the department changed proposed §5.4190 to conform it to adopted §5.4185. Because adopted §5.4185 requires that all insurers collect premium surcharges proportionately as they collect premium, rather than giving them a choice between two collection methods as the proposal did, there is no need for insurers to specify the collection method in the annual premium surcharge report.

The department has made other changes to text for clarity and consistency with agency style.

3. HOW THE SECTIONS WILL FUNCTION.

§5.4171. Premium Surcharge Requirement. This section specifies the premium surcharge that insurers must assess if the association issues class 2 public securities under Insurance Code §2210.613.

§5.4172. Premium Surcharge Definitions. This section provides definitions for the surcharge-related portions of the subchapter.

§5.4173. Determination of the Surcharge Percentage. This section specifies how the surcharge percentage is determined.

§5.4181. Premiums to be Surcharged. This section specifies how the surcharge percentage is applied.

3302

§5.4182. Method for Determining the Premium Surcharge. This section provides the method for determining the premium surcharge, and specifies to what types of policies the premium surcharge applies.

§5.4184. Application of the Surcharges. This section provides for the application of premium surcharges, including requirements relating to exceptions to surcharges, refunding, and midterm policy changes.

§5.4185. Mandatory Premium Surcharge Collection. This section concerns how insurers collect premium surcharges.

§5.4186. Remittance of Premium Surcharges. This section provides the procedures for how insurers are to remit the premium surcharges to the association.

§5.4187. Offsets. This section provides how insurers or agents may credit a premium surcharge on the next remission to the association.

§5.4189. Notification Requirements. This section specifies the premium surcharge notice that insurers must give policyholders.

§5.4190. Annual Premium Surcharge Report. This section concerns the annual premium surcharge report that insurers must submit to the association.

§5.4191. Premium Surcharge Reconciliation Report. This section specifies how an insurer must reply to a department request for a premium surcharge reconciliation report.

§5.4192. Data Collection. This section concerns data that the department may collect from insurers to determine the applicable premium surcharge percentage.

4. SUMMARY OF COMMENTS AND AGENCY RESPONSES.

Comments by Section

Comment on §5.4173(a)-(b): A commenter suggests removing the requirement that the association determine whether it can satisfy the estimated amount of class 2 public securities obligations and administrative expenses with available funds before it asks the commissioner to approve a premium surcharge under Insurance Code §2210.613. The commenter states that the requirement is inconsistent with §2210.613 and proposed §5.4184(e) (later clarified as §5.4127(e)) because those sections require that 30 percent of class 2 public securities be paid through member assessments and 70 percent through premium surcharges, as described in §2210.613(c).

Agency Response: The department declines to make changes based on the comment. Insurance Code §2210.609 governs the repayment of public security obligations under §§2210.612, 2210.613, 2210.6135, and 2210.6136. Section 2210.609(a) states, “If the association determines that it is unable to pay the public security obligations and public security administrative expenses, if any, with available funds, the association shall pay those expenses in accordance with Sections 2210.612, 2210.613, 2210.6135, and 2210.6136 as applicable.” The statute clearly provides that TWIA must exhaust its “available funds” before it pays public security obligations and administrative expenses from the sources described in those sections.

3302

Comment on §5.4173(c): Under proposed §5.4173(c), the policies subject to premium surcharges will be those in effect on a date specified by the commissioner. This date must be at least 180 days after the commissioner issues an order approving class 2 public securities. A commenter states that proposed §5.4173(c) should state that the policies subject to premium surcharges will be those in effect on or after 180 days after the date of the commissioner's order approving class 2 public securities *and* establishing the premium surcharges. The commenter states that, as written, proposed §5.4173(c) does not comply with Insurance Code §2210.613.

Agency Response: The department respectfully disagrees with the comment. Following the comment could create an absurd result in situations in which the commissioner approves class 2 public securities before a catastrophic event, which the association, under §5.4125(a)(2), may request. The issuance of class 2 public securities, the issuance of the commissioner's order establishing premium surcharges, and even the catastrophic event, could occur over 180 days after the commissioner's order approving the class 2 public securities. Under the commenter's suggestion, premium surcharges could apply to policies in effect before any of these events took place. This is not consistent with §2210.613.

Making premium surcharges apply to policies in effect on a date the commissioner specifies, which is at least 180 days after the date of the commissioner's order approving class 2 public securities, is consistent with §2210.613(b). The requirement that "[insurers] shall assess, as provided by this section, a premium

3302

surcharge to each policyholder of a policy that is in effect on or after the 180th day after the date the commissioner issues notice of the approval of the public securities,” is preceded by the phrase “on approval by the commissioner.” This gives the commissioner the ability to determine the effective date of the surcharges, as long as it is at least 180 days after the date of the order.

Comment on §5.4184: A commenter asks that affiliated surplus lines insurers be given 90 days to credit or refund excess surcharges if a midterm policy change decreases the premium, instead of the 20 days afforded insurers under §5.4184. The commenter also asks that surplus lines agents, who affiliated surplus lines insurers allow to credit or refund surcharges on their behalf, also be given 90 days to do so. In the alternative, the commenter asks that, for affiliated surplus lines insurers or surplus lines agents acting on their behalf, the deadline for crediting or refunding excess surcharges be extended to the last day of the second month following the month in which the transaction changing the policy occurred. The commenter states that when midterm changes occur in policies written by affiliated surplus lines insurers, the changes are usually related to individually rated and underwritten coverages, and the affiliated surplus lines insurer or surplus lines agent cannot rely on automation as admitted insurers normally can. The commenter notes that Insurance Code §542.055 and §542.057 give affiliated surplus lines insurers more time than admitted insurers to acknowledge receipt of a claim and to pay a claim, respectively.

3302

Agency Response: The department has modified the proposed §5.4184 in response to the comment. The department acknowledges that affiliated surplus lines insurers may find it practical to allow surplus lines agents to refund or credit excess surcharges on their behalf. The department also acknowledges that affiliated surplus lines insurers may require more time than admitted insurers to calculate a change in premium and then to calculate the amount of premium surcharge to refund or credit the policyholder. Accordingly, adopted §5.4184 permits affiliated surplus lines insurers to allow surplus lines agents to refund or credit excess surcharges, not only for premium changes resulting from midterm policy changes, but also from exposure or premium audits, retrospective rating adjustments, or other similar adjustments that occur after policy expiration.

Adopted §5.4184 also requires affiliated surplus lines insurers or surplus lines agents to credit or refund excess surcharges not later than the last day of the month following the month in which the corresponding transaction was effective. The department chose the adopted language because, as the commenter points out, it tracks the language used in §5.4186(b), which sets the deadline for remittance of premium surcharges. The department declines the commenter's request to give affiliated surplus lines insurers or surplus lines agents until the "last day of the *second* month following the month" in which the corresponding transaction occurred. Instead, the adopted language provides the same length of time as §5.4186(b), which sets the remittance deadline at "not later than the last day of the month following the month in

which the corresponding written premium transaction was effective.” The department expects that an identical formula for calculating deadlines for remittance, crediting and refunding, and giving notice under §5.4189(c) (see comment on §5.4189 below) will simplify these processes for affiliated surplus lines insurers and surplus lines agents.

The department has also modified the proposed §5.4184 to add subsection (h), which states that the department may hold liable an affiliated surplus lines insurer, that allows an agent to credit or refund excess surcharges on its behalf, for the failure of its agent to comply with the section. This is consistent with the similar provision in §5.4186(e) and consistent with the department’s intent that affiliated surplus lines insurers be responsible for implementing premium surcharges.

Comment on §5.4184: A commenter asks that §5.4184 be amended to relieve insurers of the requirement of refunding excess premium surcharges under that section if the amount to be refunded is less than a certain *de minimus* amount. The commenter suggests \$10, but states it is still seeking a more accurate estimate of the cost of issuing refunds. The commenter states that consumers will pay the costs of the refund process. The Legislature has supported the concept of waiving refunds of *de minimus* amounts in other situations. Insurance Code §651.158 and §651.162, concerning refunds of charges and unearned premiums in the context of premium financing agreements, waive an insured’s right to a refund of \$5 or less.

3302

Agency Response: The department appreciates the cost to insurers, and ultimately to consumers, imposed by the refund requirement, but declines to make the suggested change. What qualifies as a *de minimus* amount relative to different policies varies widely. While \$10 may be *de minimus* in the context of a commercial insurance policy with a premium in the tens of thousands of dollars, it would not be *de minimus* in the context of a 30-day auto policy.

Comment on §5.4185(b) and (c): A commenter states that §5.4185 should allow an insurer to collect a premium surcharge using the same billing method and frequency that it uses to collect a policyholder's premium. This commenter and a second commenter point out that under the proposed rule, a policyholder may have to pay a premium surcharge all at once, but pay the premium in installments. This may add to insurers' billing expenses and may confuse policyholders. Another commenter suggests that the proposed rule would place the insurer in an awkward situation with respect to the collection of the premium surcharge. The commenter states that the proposed rule would make paying the premium surcharge difficult for consumers.

Agency Response: The department agrees that under the proposed rule, a policyholder might have to pay a premium surcharge all at once, while paying the premium in installments, if that policyholder's insurer elected to collect surcharges on the effective date of the corresponding written premium transaction.

3302

The department has changed §5.4185(b) to require insurers to collect premium surcharges proportionately as they collect premium on the corresponding policy. This way policyholders who have chosen to pay premiums in installments will not be forced to pay premium surcharges all at once because their insurer has elected that collection method. Policyholders who pay premiums at the beginning of the policy term will pay premium surcharges the same way. The department hopes that requiring insurers to collect surcharges proportionately as they collect premium will reduce expenses for insurers and make payment simpler for policyholders.

The department has removed §5.4185(c) from the adopted rule. Because the adopted rule requires that all insurers collect premium surcharges proportionately as they collect premium, rather than giving them a choice between two collection methods as the proposal did, there is no need to specify that insurers must apply the same method to all policyholders. The department has also made a conforming change to adopted §5.4190 (relating to Annual Premium Surcharge Report). Because there is only one method, the reports need not specify the method used to collect premium surcharges.

Comment on §5.4186(a) and (f): As proposed, §5.4186(f) gives TWIA the authority to establish reporting requirements for surplus lines agents remitting premium surcharges on behalf of affiliated surplus lines insurers. A commenter states that the department does not have statutory authority to authorize the association to impose reporting

3302

requirements on surplus lines agents. The commenter also complains that the existing language in §5.4186(a), which references “procedures established by the Association relating to premium surcharge remissions from surplus lines agents,” is without statutory authority.

The commenter disagrees with the estimates in the rule proposal’s cost note regarding the costs surplus lines agents would incur in programming their accounting and billing systems to comply with association-imposed requirements. Finally, the commenter disagrees with the cost note’s statement that a surplus lines agent can avoid any reporting requirement the association might establish by deciding not to remit premium surcharges on the surplus lines insurer’s behalf. The commenter states that market forces will leave surplus lines agents no choice but to collect and remit premium surcharges in the same way they collect and remit premium and premium taxes.

The commenter asks the department to remove references to the association’s authority to impose remitting and reporting requirements on surplus lines agents from the adopted rules. The commenter also asks the department to develop new rules for affiliated surplus lines insurers and surplus lines agents on premium surcharge collecting, remitting, and reporting that reflect “the complexity of the surplus lines insurance market and regulatory structure.”

Agency Response: The adopted rules do not give the association the authority to impose reporting requirements on surplus lines agents. The adopted §5.4186 contains no reference to association-imposed reporting requirements on surplus lines agents.

3302

The department declines to remove the sentence from §5.4186(a) that relates to surplus lines agents remitting premium surcharges to the association “in compliance with any procedures established by the Association relating to premium surcharge remissions from surplus lines agents.” This sentence is in the existing rule and the department proposed no substantive change to it. The association’s plan of operations gives its board general powers to make and change regulations for the management of the business affairs of the association and to perform “all other duties reasonably necessary to accomplish the purposes of the Act.” 28 TAC §5.4001(b)(2)(L)(i) and (x). It is important that the association be able to establish procedures for premium surcharge remissions from surplus lines agents because they are the only licensed agents the rules allow to remit premium surcharges. All other remissions would be from insurers. As the commenter points out, it is not uncommon for surplus lines agents to have contracts with as many as 50 affiliated surplus lines insurers. The association will need a uniform method by which each surplus lines agent identifies the insurer on whose behalf the agent is remitting a particular surcharge.

The department also declines to adopt new rules on premium surcharge collecting, remitting, and reporting exclusively for the surplus lines market. Although the surplus lines market differs from the admitted market, the association will need the same information from both markets to determine compliance with the premium surcharge rules. The need to ensure collection, remission, or deposit of the correct premium surcharge does not depend on whether a given policy is sold by an admitted

carrier. This is why, under the adopted rules, affiliated surplus lines insurers are still responsible for the annual premium surcharge reports in §5.4190, as they are under the existing rules. If the association needs to reconcile amounts reported by affiliated surplus lines insurers with amounts remitted or deposited by surplus lines agents, the department can use its authority under Insurance Code §38.001 to obtain information directly from surplus lines agents.

Comment on §5.4189: A commenter asks that affiliated surplus lines insurers be given 90 days to provide written notice to policyholders of a midterm change in the premium surcharge, instead of the 20 days afforded insurers under §5.4189. The commenter also asks that surplus lines agents, who affiliated surplus lines insurers allow to give notice on their behalf, also be given 90 days to do so. In the alternative, the commenter asks that, for affiliated surplus lines insurers or surplus lines agents acting on their behalf, the deadline for providing written notice be extended to the last day of the second month following the month in which the transaction changing the policy occurred. The commenter states that when midterm changes occur in policies written by affiliated surplus lines insurers, the changes are usually related to individually rated and underwritten coverages and the affiliated surplus lines insurer or surplus lines agent cannot rely on automation as admitted insurers normally can. The commenter notes that Insurance Code §542.055 and §542.057 give affiliated surplus lines insurers more

3302

time than admitted insurers to acknowledge receipt of a claim and to pay a claim, respectively.

Agency Response: The department has modified the proposed §5.4189 in response to the comment. The department acknowledges that affiliated surplus lines insurers may find it practical to allow surplus lines agents to provide written notice of premium surcharges on their behalf. The department also acknowledges that affiliated surplus lines insurers may require more time than admitted insurers to calculate a change in premium and then to calculate a change in the premium surcharge and notify the policyholder. Adopted §5.4189(d) permits affiliated surplus lines insurers to allow surplus lines agents to give policyholders the written notice required in the section. Adopted §5.4189(c)(3) also requires affiliated surplus lines insurers or surplus lines agents to provide the notice not later than the last day of the month following the month in which the corresponding transaction was effective. The department chose the adopted language because, as the commenter points out, it tracks the language used in §5.4186(b), which sets the deadline for remittance of premium surcharges. The department declines the commenter's request to give affiliated surplus lines insurers or surplus lines agents until the "last day of the *second* month following the month" in which the corresponding transaction occurred. Instead, the adopted language provides the same length of time as §5.4186(b), which sets the remittance deadline at "not later than the last day of the month following the month in which the corresponding written premium transaction was effective." The department expects that an identical formula

3302

for calculating deadlines for remittance, crediting and refunding, and giving notice under §5.4189(c) will simplify these processes for affiliated surplus lines insurers and surplus lines agents.

The department has also modified the proposed §5.4189 to add subsection (e), which states that the department may hold an affiliated surplus lines insurer that allows an agent to provide notice of premium surcharges on its behalf liable for the failure of its agent to comply with the section. This is consistent with the provision in §5.4186(e) and consistent with the department's intent that affiliated surplus lines insurers be responsible for implementing premium surcharges.

Comment on §5.4190(d) and (e) and §5.4192(c): A commenter acknowledges the department's and the association's need for data on policies and premium surcharges to ensure that the surcharges are correctly applied, but the commenter states that due to the characteristics of the surplus lines market, affiliated surplus lines insurers may not have all the data that they must provide under §5.4190 (relating to Annual Premium Surcharge Report) or under §5.4191 (relating to Premium Surcharge Reconciliation Report). Surplus lines agents may have some of the data and some data may not be obtainable for surplus lines policies under "current information collection and reporting systems." The commenter states that the cost of applying the requirements of §5.4190 to affiliated surplus lines insurers is prohibitive. According to the commenter, the

Surplus Lines Stamping Office of Texas is best suited to provide the data the rules require.

The commenter recommends that subsections (d) and (e) of §5.4190 be revisited, streamlined, and simplified to accommodate the special facts and circumstances of surplus lines insurance. The commenter also recommends that §5.4192 (relating to Data Collection), subsection (c) be revised to require the department to request the information required for annual premium surcharge reports under §5.4190 and premium surcharge reconciliation reports under §5.4191 from the stamping office, before requesting it from individual affiliated surplus lines insurers.

Agency Response: The department declines to revise §5.4190(d) and (e) and §5.4192(c). The requirements for §5.4190 have been in place since the rule became effective on February 3, 2011. Although the proposed §5.4190(e) contained a new requirement that insurers report the method they used to collect premium surcharges, that requirement is not in the adopted rule because adopted §5.4185(b) (relating to Mandatory Premium Surcharge Collection), provides for only one method of collecting premium surcharges. The only adopted changes to §5.4190 conform the section to the changes HB 3 made to Insurance Code §2210.613(c), regarding the lines of insurance subject to premium surcharges. Adopted §5.4190 does not add any new reporting requirements for insurers. It reduces the lines of insurance for which insurers must report.

The requirements for §5.4191 vary little from those in place since the rule's adoption in January 2011. The adopted §5.4191 differs from the previous version in that it requires information related to refunding premium surcharges and conforms to HB 3's changes regarding the lines of insurance subject to premium surcharges. The premium surcharge reconciliation reports described in §5.4191 are not required annually. Instead, the section puts insurers on notice that the department may request the information.

Section 5.4192(c) already provides that the department will, when possible and practical, obtain information necessary to determine the premium surcharge percentage from the Surplus Lines Stamping Office of Texas before requesting it from affiliated surplus lines insurers.

General Comments

Comment: A commenter appreciates that the proposed rules place responsibility for collecting premium surcharges and collecting and reporting surcharge data on affiliated surplus lines insurers, but is concerned that contracts between surplus lines agents and affiliated surplus lines insurers will shift the responsibility to the agents. The commenter suggests adding the following to an appropriate section of the rules, "An Affiliated Surplus Lines Insurer remains responsible for the performance of any duty of the Insurer under this division which is delegated to a surplus lines agent, except as otherwise provided by Chapter 981, Insurance Code, or this division."

3302

Agency Response: The department considers the suggested change unnecessary.

The comment itself alludes to §5.4171(a), which places responsibility for assessing premium surcharges on affiliated surplus lines insurers. Section 5.4186(e) states that the department may hold an affiliated surplus lines insurer liable for the failure of its agent to remit or timely remit premium surcharges. Nothing in the adopted rules states that agents may be held responsible.

Comment: One commenter states that there are still unanswered questions as to what lines of insurance the premium surcharges apply.

Agency Response: The department declines to revise proposed §5.4172 or §5.4184. Section 2210.613 states what lines of insurance the premium surcharge apply to and the types of policies affected. Section 5.4172 defines insured property. The application of the surcharges specified in §5.4184 implements Insurance Code §2210.613(c).

Comment: Many commenters state that the proposed rules are unnecessary. Several commenters suggest that the financial position of the association has improved significantly, and that the balance of the CRTF has increased. Other commenters state that premium surcharges are not necessary because there has not been a hurricane on the Texas gulf coast in four years, and no hurricane in Corpus Christi in more than 30 years. Other commenters suggest that the association has settled most of its Hurricane Ike-related claims and raised rates, and it is on a positive financial path.

3302

Agency Response: The department disagrees that the financial condition of the association eliminates the need for these adopted rule amendments. Existing Insurance Code Section 2210.613 already requires insurers to surcharge their coastal policyholders (and TWIA to assess its member insurers) if TWIA cannot pay its class 2 public security obligations and administrative expenses from available funds. This requirement exists even if the department does not adopt any amendments to its loss funding or premium surcharge rules. The rule amendments conform the department's premium surcharge and loss funding rules to current law, and provide an orderly process for the association to obtain public securities if it needs these funds to pay its policyholders' claims. While improvements in the association's financial condition reduces the possibility the association will have to rely on public securities to pay its policyholders' claims, it does not *eliminate* this possibility. For example, even if TWIA were to add \$200 million to the CRTF through a net gain in operations, TWIA would still need to obtain public securities if a 1-in-50 year event hit the Texas coast during the 2014 hurricane season, which would cause \$2.8 billion in insured property damage to TWIA's policyholders.

Comment: Several commenters suggest that the legislation, which the rules implement, is flawed and that the only authority that can address the legislation is the Texas Legislature.

3302

Agency Response: The rule amendments reflect the Legislature's intent to create a mechanism to allow for the issuance of public securities. The purpose of Insurance Code Chapter 2210 reflects the Legislature's findings that the provision of adequate windstorm and hail insurance is necessary to the economic welfare of this state, and that without that insurance, the orderly growth and development of this state would be severely impeded. When the department first proposed the rule amendments in 2012, the department received requests to postpone adopting the amendments until the 83rd Legislature had an opportunity to address TWIA's funding. As a result, the rules were withdrawn by operation of law on December 27, 2012. Because the 83rd Legislature did not address TWIA's funding, the department resumed its proposal of these rule amendments.

The 2014 hurricane season begins June 1. The potential harm in delaying TWIA's access to additional financial resources outweighs the benefits of further study on the potential economic impact of premium surcharges created by HB 4409 and amended by HB 3. The department will monitor TWIA and will keep the Legislature informed about the impact of implementing the use of public securities required by HB 4409 and HB 3, including the impact of any premium surcharges should they become necessary.

Comment: Many commenters suggest that the statute does not set a deadline for the department to adopt rules, and that there is no reason to adopt rules at this time. One

commenter asks why the rules are needed now, if the statute authorized rules several years ago. Several commenters suggest that the rules be withdrawn so that the 84th Legislature can address TWIA in 2015. These commenters say elected officials, not a regulatory agency, should propose and adopt legislation to meet the needs of the proposed rules. Another commenter states one option is for the department to do nothing. Another commenter states that the language of the statute that relates to the implementation of the rules is permissive and not mandatory.

Agency Response: The department disagrees that the rule amendments are not needed. The department first adopted premium surcharge and loss funding rules effective February 3, 2011, to implement HB 4409. Since that time, the Legislature enacted HB 3, which amended TWIA's funding provisions. The department previously proposed amendments to its loss funding rules in the June 22, 2012, issue of the *Texas Register*. The department postponed consideration of these proposed rule amendments to give the 83rd Legislature an opportunity to address TWIA's funding. As a result, the proposed rule amendments were withdrawn by operation of law on December 27, 2012. Because the 83rd Legislature did not address TWIA's funding, the department resumed its proposal of amendments to its loss funding and premium surcharge rules.

The 2014 hurricane season begins June 1. TWIA's financial condition and that of the CRTF has improved, but catastrophic weather events could harm TWIA's ability to fulfill its obligations to policyholders. Adopting these rules provides an orderly process

for TWIA to obtain public securities if it needs these funds to pay its policyholders' claims. Doing nothing could result in public securities that are not marketable, which would deprive TWIA of the resources it needs to pay its policyholders' claims. TWIA may simultaneously pursue other funding or risk reduction strategies including procuring a line of credit, assessments, reinsurance, catastrophe bonds, and depopulation. Adopting rules will help TWIA test the marketability of any public securities authorized by Insurance Code Chapter 2210. Also, the Legislature may benefit from studying whether implementation of Chapter 2210 is successful, and how well the public securities authorized by the chapter strengthen TWIA's claims-paying ability.

Comment: A commenter states that assessing premium surcharges at this time is not actuarially necessary, and therefore discriminatory. The commenter urges TDI and TWIA to order the approximately \$400 million in assessments, proposed but not approved by TWIA's board in September 2008, before considering premium surcharges.

The commenter recounts how, following Hurricane Ike, in September 2008, the TWIA board voted against assessing member insurance companies the full amount proposed under former Insurance Code §2210.058. The commenter states that since January 2009, TWIA policyholders have paid millions more in premiums than they would have had the board members representing TWIA-member insurance companies not voted against assessing the full amount proposed.

The commenter argues that imposing premium surcharges, before the possibility of assessing the insurance industry for Hurricane Ike losses has been exhausted, is discriminatory under Insurance Code §544.002. This section prohibits insurers from discriminating against individuals on the basis of, among other factors, geographic location. The commenter advises that Insurance Code §544.003 states that an insurer does not violate §544.002 if the insurer's action is based on sound underwriting or actuarial principles reasonably related to actual or anticipated loss experience. The commenter states that imposing premium surcharges is discriminatory because, until TWIA members are assessed for Hurricane Ike losses, premium surcharges are not based on sound actuarial principles.

Agency Response: Many commenters have urged the department to assess TWIA member insurers under former Insurance Code §2210.058. However, foregoing or delaying adoption of the amendments to the premium surcharge and loss funding rules while TWIA assesses member insurers is not an option for the department, for two reasons.

First, the department does not have and never has had the authority to assess TWIA member insurance companies. Former Insurance Code §2210.058, which provided for the assessment of TWIA members when, in a calendar year, losses and operating expenses exceeded premium and other revenue, did not contemplate department assessment of TWIA member companies. Under the version of §5.4001 in

3302

effect in 2008, the TWIA board must determine the necessity of an assessment and then order TWIA to make the assessment.

Second, existing Insurance Code statutes already require insurers to surcharge their coastal policyholders (and TWIA to assess its member insurers) if TWIA cannot pay its class 2 public security obligations and administrative expenses from available funds. This requirement exists even if the department does not adopt any amendments to its premium surcharge rules. See Insurance Code §§2210.609, 2210.613, and 2210.6136. Existing department rules provide for premium surcharges. The department adopted its current rules on loss funding and premium surcharges to implement HB 4409, 81st Legislature, 2009, which established TWIA's current funding structure. The question relevant to the adoption of the proposed amendments to the rules is not whether coastal policyholders will be subject to premium surcharges if the need arises, because current law already establishes this requirement. Instead, the question relevant to the adoption of the proposed rule amendments is whether the premium surcharges will be administered under the rules the department adopted in 2011 to implement HB 4409, or under amended rules that are consistent with current law. Note that some of the adopted amendments make the premium surcharge rules more consumer-friendly. As amended, §5.4184 requires insurers to refund premium surcharges when a midterm policy change or postexpiration policy change decreases the premium. This amendment reflects the fact that HB 3 removed the prohibition on making premium surcharges refundable.

3302

Even if it were in the department's power to assess TWIA member insurers under former Insurance Code §2210.058, the additional funds provided to TWIA through an assessment would not eliminate the need for the department's rules to be consistent with current law. Further, while an assessment of approximately \$400 million would result in an additional \$400 million in the CRTF, it would not eliminate the possibility that TPFA may need to issue class 2 public securities to help TWIA pay its policyholders' claims. Even if TWIA added \$400 million to the CRTF, TPFA may still need to issue class 2 public securities in order for TWIA to have sufficient funds to cover its policyholders' claims should a major hurricane hit the Texas coast. For example, a 1-in-50 year catastrophic event for TWIA would result in approximately \$2.8 billion in insured damage to TWIA's policyholders.

Finally, a discussion of unfair discrimination under Insurance Code §544.002, in the context of premium surcharges under Insurance Code §2210.613 or §2210.6136, is misplaced. Section 544.002 prohibits an insurer from, among other acts, charging an individual a rate that is different from the rate charged to other individuals for the same coverage because of the individual's geographic location. As the commenter points out, §544.003(b) provides an exception: an insurer does not unfairly discriminate if the different rate charged due to geographic location is actuarially justified. Premium surcharges are not insurance rates and cannot be judged based on standards that apply to insurance rates. Unlike insurance rates, premium surcharges are *not* designed to reflect the cost of insuring a particular risk. Instead, premium surcharges are

3302

designed to pay debt service and related expenses on public securities. See Insurance Code §2210.613(b).

Comment: Many commenters suggest that instead of adopting the proposed rules, TWIA should assess insurers for Hurricane Ike-related insurance claims. A commenter specifically asks why the department cannot require TWIA to assess insurers, if the department has oversight over TWIA. Several commenters suggest that assessments are a faster method to improve TWIA's reserves than the bond approval process. Several commenters suggest that the TWIA board, as currently structured, makes it unlikely that the board would vote to assess.

Agency Response: The department declines to withdraw the proposed rule amendments. The department disagrees that the possibility of assessing insurers eliminates the need to adopt these rule amendments. A decision to assess insurers is not mutually exclusive with a request to issue public securities. TPFA may still need to issue class 2 public securities in order for TWIA to have sufficient funds to cover its policyholders' claims should a major hurricane hit the Texas coast, even if TWIA were able to assess its member insurers for Hurricane Ike-related claims. The future financial circumstance of TWIA is unknowable, and the purpose of the rules is to conform the department's premium surcharge and loss funding rules to current law, and provide an orderly process for TWIA to obtain public securities if it needs these funds to pay its policyholders' claims.

3302

The current administrative oversight the department has over TWIA is limited.

The department does not directly manage TWIA and does not make operational decisions for TWIA. The board of directors of TWIA has the discretion to request an assessment under former Insurance Code §2210.058. Existing statute does not give the department or TWIA the authority to assess TWIA's member insurers to pay TWIA policyholders' claims resulting from future catastrophic events, except to pay for class 2 and class 3 public securities as provided in §§2210.613, 2210.6135, and 2210.6136.

The department acknowledges that the bond approval process may take time. The final adoption of rules prior to a windstorm event will allow TWIA and TPFA to study and review bond issuance-related issues before public securities are required. Delaying or withdrawing the rules would increase the solvency risk to TWIA and its policyholders.

The department does not have the power to change the structure of the association's board of directors. The composition of the board is specified in Insurance Code §2210.102. The board is composed of nine voting members and one nonvoting member, four of whom are representatives of the insurance industry. The statute establishes other requirements, including a minimum number of representatives that must live in first tier coastal counties. The primary objectives of the board are specified in Insurance Code §2210.107.

Comment: Several commenters requested a hearing in Cameron County.

Agency Response: The department declines to extend the rule comment period in order to hold a rule hearing in Cameron County. The department has held hearings in

3302

Austin, Beaumont, and Corpus Christi. The department received numerous written comments from interested parties at those hearings. Because TWIA may require additional resources if the 2014 hurricane season results in a need for TWIA to obtain funds through the issuance of public securities, delaying the rules to hold more hearings may be detrimental to TWIA and its policyholders. However, in response to the comment, the commissioner did hold a meeting in Cameron County on April 16, 2014, to allow the public and elected officials in attendance to voice concerns on TWIA and windstorm coverage, generally.

Comment: Several commenters state that the fiscal note in the proposed rules did not adequately address the true cost of the rules to state and local government. Several commenters suggest that the department was wrong to assert in the proposed rules that there will be no measureable effect on local employment or the local economy as a result of the proposal. One commenter requested that the department perform an analysis of the economic impact on the coastal counties before enacting the rule.

Agency Response: The adopted rule amendments do not create premium surcharges. The premium surcharges were created by the enactment of HB 4409. Any impact that possible premium surcharges may have on the coastal economy are a direct or indirect result of the statute and not the rule amendments. The department understands the economic concerns coastal residents and businesses have about the premium surcharges created by HB 4409, but declines to revise or withdraw its proposed rule

3302

amendments for this reason. The adopted rules do not impose any requirement on coastal policyholders that is not already required by statute, and the rules do not directly affect TWIA's rates. The department declines to perform additional economic analyses prior to adopting the proposed rule amendments. The potential harm in delaying TWIA's access to additional financial resources outweighs the benefits of further study on the potential economic impact of the law. The department will monitor TWIA and will keep the Legislature informed about the impact of implementing the use of public securities required under HB 4409 and HB 3, including the impact of any premium surcharges should they become necessary.

Comment: Several commenters suggest that the rules would create uncertainty over future rate or surcharge increases. One commenter states that there is no way to know how much the premium surcharges would be. The commenters ask if any actuarial calculations have been made to show what the impact of the rule will be on the 14 coastal counties. Another commenter states that the rules do not specify the amount or duration of the surcharge, and create uncertainty in the affected region. Another commenter suggests that the unknown nature of the surcharge is detrimental in bringing in new business and industry to the 14 coastal counties.

Agency Response: The proposed rule amendments implement the Legislature's intent in Insurance Code Chapter 2210. The department understands the concerns raised, but declines to revise or withdraw the proposed rule amendments. The calculation of

the premium surcharge depends on a number of factors that neither the department, TWIA, nor TPFA will know until, and if, the class 2 public securities are issued. These factors include the amount of class 2 public securities TWIA needs to pay its policyholders' claims, the term of the public securities, the interest rate on the public securities, and other bondholder requirements necessary to sell the public securities. Because of these factors, the surcharges cannot be known precisely until the class 2 public securities are issued.

Comment: Several commenters suggest that the surcharge would be poorly timed. The surcharges would occur after a hurricane damaged property, just as policyholders would be recovering from a storm. One commenter states that the premium surcharges would compound the financial burden faced by coastal residents. Another commenter states that postevent bonds are a crippling punishment for homeowners and business owners on the coast.

Agency Response: The department declines to withdraw the proposed rule amendments. Insurance Code §2210.613 states that the commissioner must make the surcharge effective on or after the 180th day after the date the commissioner issues notice of the approval of the public securities. Statute requires at least a six-month delay after the event, before the surcharges can be collected. The timing of the premium surcharge must be within the period set by statute. The department has very limited flexibility to delay the premium surcharge for class 2 public securities.

Comment: Many commenters state that the premium surcharges are unfair to the residents of the 14 coastal counties. Several commenters suggest that the people of the 14 tier one counties are being treated differently than the people in the other 240 counties in Texas. One commenter suggests that the proposed rules effectively “redline” the 14 tier one counties. The commenter states that the premium surcharges would be predatory and discriminatory in an area that already pays more to insure their property than the rest of the state. One commenter states that the premium surcharges on the 14 tier one counties constitutes discrimination based on geographic location. Another commenter states that because assessments may be available, the premium surcharge is not actuarially necessary and, therefore, discriminatory. One commenter suggests that the exclusion of most of Harris County illustrates how corrupt the current windstorm system is.

Several commenters suggest that the proposed rules may be discriminatory on racial grounds. The commenters suggest that the effect of the proposed rules would be harshest toward minorities and others who live and work along the Texas coast. One commenter states that they believe that the premium surcharges are contrary to the principles of the United States Constitution and the Texas Constitution. Another commenter states that the proposed rules are discriminatory under Texas Insurance Code Chapters 544 and 560.

3302

Agency Response: The department understands the concerns but declines to revise or withdraw the proposed rule amendments. The adopted rule amendments conform the department's premium surcharge and loss funding rules to current law, and they provide an orderly process for TWIA to obtain public securities if it needs these funds to pay its policyholders' claims. The adopted rule amendments do not impose any requirement on coastal policyholders that is not already required by the statute, and the amendments do not directly affect TWIA's rates.

A discussion of unfair discrimination under Insurance Code §544.002, in the context of premium surcharges under Insurance Code §§2210.613 or 2210.6136, is misplaced. Section 544.002 prohibits an insurer from, among other acts, charging an individual a rate that is different from the rate charged to other individuals for the same coverage because of the individual's geographic location. As another commenter points out, §544.003(b) provides an exception: an insurer does not unfairly discriminate if the different rate charged due to geographic location is actuarially justified. But premium surcharges are not rates and cannot be judged by whether they are actuarially justified. Premium surcharges are, unlike rates, *not* designed to reflect the cost of insuring a particular risk; premium surcharges are designed to pay debt service and related expenses on public securities. See Insurance Code §2210.613(b).

Comment: One commenter states that the surcharge contradicts the legislative intent to not have rates go up by more than 5 percent per year. Section 32 of HB 4409,

3302

codified as §2210.351, states that TWIA may use a filed rate without prior approval if it does not exceed 105 percent of the existing rate. Section 33 of the bill has a similar limitation for the required annual manual rate filings. The commenter suggests that by imposing the premium surcharges the rates would exceed the 5 percent rate increase.

Agency Response: The department declines to revise or withdraw the proposed rule amendments. The premium surcharges required under Insurance Code §2210.613 are distinct from TWIA's rates. TWIA's premium rates are designed to cover TWIA's cost to insure a particular risk. Unlike TWIA's rates, the premium surcharges are designed to pay debt service and related expenses on public securities. In addition, Insurance Code §2210.613 requires that the commissioner set the surcharge in an amount sufficient to pay, for the duration of the public securities, 70 percent of all debt service not already covered by TWIA's available funds.

Comment: Many commenters suggest that the proposed rules are illogical in their application. One commenter states that those with second homes on the coast may benefit, while coastal residents may have to pay for premium surcharges. A commenter also asks how commercial fleet vehicles or rental car companies will be impacted. Several commenters suggest those businesses may relocate to areas outside the premium surcharge area.

Agency Response: The department understands the concerns but declines to revise or withdraw the rule amendments. The statute provides that the premium surcharges

3302

would apply to policies insuring second homes that are located in the catastrophe area but that may be owned by non-coastal residents. Premium surcharges would also apply to policies covering automobiles principally garaged in the catastrophe area. The adopted rules conform the department's premium surcharge and loss funding rules to current law, and provide an orderly process for TWIA to obtain public securities if it needs these funds to pay its policyholders' claims. Insurance Code §2210.613, as created by HB 4409 and amended by HB 3, states that the premium surcharges "... shall be assessed on *all* policyholders of policies that cover insured property that is *located in a catastrophe area, including automobiles principally garaged in a catastrophe area.*" (emphasis added). The adopted rules do not impose any requirement on coastal policyholders that is not already required by the statute, and the rules do not directly affect TWIA's rates. The department will monitor complaints and insurer compliance, and it will keep the Legislature informed about the impact of implementing the use of public securities required by HB 4409 and HB 3, including the impact of any premium surcharges should they become necessary.

Comment: Many commenters suggest that premium surcharges on automobile insurance are not fair. Several commenters suggest that automobile coverage is not logically related to TWIA. One commenter states that connecting premium surcharges for TWIA to automobiles creates a bad precedent. Another commenter states the automobile insurance premium surcharge is illogical since coastal residents would be

evacuating their personal automobiles away from a storm. Another commenter states that TWIA does not pay for automobile claims, and suggests that it is inappropriate to assess windstorm related claims to automobile policies. One commenter suggests that the premium surcharges are a transparent ploy to make money for rich insurance companies.

Agency Response: The department understands the concerns but declines to revise or withdraw the rule amendments. The adopted rule amendments conform the department's premium surcharge and loss funding rules to changes made by HB 3, and provide an orderly process for TWIA to obtain public securities if it needs these funds to pay its policyholders' claims. HB 3 amended Insurance Code §2210.613 to provide that the premium surcharges "... shall be assessed on *all* policyholders of policies that cover insured property that is located in a catastrophe area, *including automobiles principally garaged in a catastrophe area.*" (emphasis added). The adopted amendments do not impose requirements on coastal policyholders that are not already required by the statute and the amendments do not directly affect TWIA's rates. The premium surcharges are not designed to reflect the cost of insuring a particular risk. Instead, the premium surcharges are designed to pay debt service and related expenses on public securities. The department will monitor complaints and insurer compliance, and it will keep the Legislature informed about the impact of implementing the use of public securities required by HB 4409 and HB 3, including the impact of any premium surcharges should they become necessary.

3302

Comment: One commenter suggests that the detrimental impact of the proposed rules would have negative geopolitical implications. The commenter explains that Texas coastal exports of natural gas can help western Europe reduce its reliance on Russian natural gas. The commenter states that the premium surcharges would cripple the ability for coastal industry to expand the supply and export of liquid natural gas.

Agency Response: The department understands the concerns but declines to revise or withdraw the proposed rule amendments. Existing Insurance Code §2210.613 already requires insurers to surcharge their coastal policyholders (and TWIA to assess its member insurers) if TWIA cannot pay its class 2 public security obligations and administrative expenses from available funds. This requirement exists even if the department does not adopt any amendments to its loss funding or premium surcharge rules. The adopted rule amendments conform the department's premium surcharge and loss funding rules to changes made by HB 3, and provide an orderly process for TWIA to obtain public securities if it needs these funds to pay its policyholders' claims. The department will monitor complaints and insurer compliance, and it will keep the Legislature informed about the impact of implementing the use of public securities required by HB 4409 and HB 3, including the impact of any premium surcharges should they become necessary.

Comment: Many commenters state that the coastal economy will be adversely impacted. Several commenters suggest that the rules will have an adverse economic

3302

impact on the state as a whole. Many commenters suggest that the proposed rules will increase the cost of doing business in Texas. Many commenters explain how important and critical the economic contribution of the coast is to Texas, stating that the coast is home to key industries, it facilitates trade, and it provides goods and energy necessary for commerce.

Many commenters express concern over the impact of the rules on the state's workforce. Several commenters suggest that the premium surcharges will drive away workers. One commenter states that the rule would cut off business from its most important resource: people. Several commenters suggest that industrial development in the coastal region depends on workers who must pay for TWIA insurance. If workers leave the coastal area, the remaining workforce would be insufficient to support industry. Several commenters suggest that the high cost of insurance negatively impacts the real estate market. One commenter states that home buyers already experience sticker shock for insurance costs. Several commenters suggest that coastal communities will be at a disadvantage when competing against noncoastal communities. Other commenters suggest that coastal communities in other states may compete for and attract business away from the area, and that the proposed rules may place Texas coastal communities at a disadvantage. Another commenter suggests the uncertainty of the additional costs is a negative impact for economic competition. Another commenter suggests that it will be difficult to explain to relocating persons that property in addition to their home may face premium surcharges. Another commenter

states that in commercial real estate, increased costs are difficult to incorporate due to the long lease terms.

Several commenters state that they live on a fixed income and cannot afford increased insurance costs. Many commenters suggest that insurance costs in coastal communities are already too high. Several commenters state that the 14 tier one coastal counties are some of the nation's poorest, and they are home to people who can least afford to pay premium surcharges.

Agency Response: The department understands the concerns but declines to revise or withdraw the proposed rule amendments. Existing Insurance Code §2210.613 already requires insurers to surcharge their coastal policyholders (and TWIA to assess its member insurers) if TWIA cannot pay its class 2 public security obligations and administrative expenses from available funds. This requirement exists even if the department does not adopt any amendments to its loss funding or premium surcharge rules. The adopted rule amendments conform the department's premium surcharge and loss funding rules to changes made by HB 3, and provide an orderly process for TWIA to obtain public securities if it needs these funds to pay its policyholders' claims. The rules do not impose any requirement on coastal policyholders that is not already required by the statute, and the rules do not directly affect TWIA's rates. The department will monitor complaints and insurer compliance, and it will keep the Legislature informed about the impact of implementing the use of public securities

3302

required by HB 4409 and HB 3, including the impact of any premium surcharges should they become necessary.

The purpose of Insurance Code Chapter 2210 reflects the Legislature's findings that the provision of adequate windstorm and hail insurance is necessary to the economic welfare of this state, and without that insurance the orderly growth and development of this state would be severely impeded. Insurance Code Chapter 2210 provides a method to obtain adequate windstorm and hail insurance. Subchapter B-1 of Chapter 2210 provides that TWIA must pay its policyholders' claims in part through the issuance of class 1, class 2, and class 3 public securities. Subchapter M of Chapter 2210 provides that if TWIA cannot pay its class 2 public security obligations and administrative expenses from available funds, then 70 percent of those obligations must be paid through coastal premium surcharges and the remaining 30 percent paid through assessments to TWIA's insurer members.

Comment: Several commenters suggest that the premium surcharges will harm local governments. Several commenters suggest that the proposed rules will make it more difficult for local governments to fund services. One commenter states that the proposed rules would kill any reason to build or keep property in the 14 tier one counties. Another commenter states that economic diversity is required for a community to exist. One commenter gave the example of the increasing costs of premium depreciating the value of a home from \$200,000 to \$150,000. Another

commenter states that municipalities may be negatively impacted twice: first by the extra premiums, and then by the reduced ad valorem tax base. The net result is that tax revenues would decline, jeopardizing communities' ability to provide transportation, safety, emergency response, and public water infrastructure.

Agency Response: The department understands the concerns but declines to revise or withdraw the proposed rules. Existing Insurance Code §2210.613 already requires insurers to surcharge their coastal policyholders (and TWIA to assess its member insurers) if TWIA cannot pay its class 2 public security obligations and administrative expenses from available funds. This requirement exists even if the department does not adopt any amendments to its loss funding or premium surcharge rules. The adopted rule amendments conform the department's premium surcharge and loss funding rules to changes made by HB 3, and provide an orderly process for TWIA to obtain public securities if it needs these funds to pay its policyholders' claims. The adopted rules do not impose any requirement on coastal policyholders that is not already required by the statute, and the rules do not directly affect TWIA's rates. The department will keep the Legislature informed about the impact of implementing the use of public securities required by HB 4409 and HB 3, including the impact of any premium surcharges should they become necessary.

Comment: Many commenters suggest that coastal residents already pay high insurance premiums. One commenter states that not only have windstorm insurance

costs increased in many areas, but flood insurance premiums have increased. Many commenters suggest that the high and rising costs of insurance may force them to relocate.

Agency Response: The department understands the concerns but declines to revise or withdraw the proposed rule amendments. Existing Insurance Code §2210.613 already requires insurers to surcharge their coastal policyholders (and TWIA to assess its member insurers) if TWIA cannot pay its class 2 public security obligations and administrative expenses from available funds. This requirement exists even if the department does not adopt any amendments to its loss funding or premium surcharge rules. The adopted rule amendments conforms the department's premium surcharges and loss funding rules to changes made by HB 3, and provide an orderly process for TWIA to obtain public securities if it needs these funds to pay its policyholders' claims. The adopted rules do not impose any requirement on coastal policyholders that is not already required by the statute, and the rules do not directly affect TWIA's rates. The department will keep the Legislature informed about the impact of implementing the use of public securities required by HB 4409 and HB 3, including the impact of any premium surcharges should they become necessary.

Comment: Several commenters suggest that premium surcharges on automobile insurance may increase the number of uninsured motorists on Texas roads.

3302

Commenters state that the additional cost of insurance will cause motorists to drop their insurance because they may be unable to afford the premiums.

Agency Response: The department understands the concerns but declines to revise or withdraw the proposed rule amendments. Insurance Code §2210.613, as created by HB 4409 and amended by HB 3, states that the premium surcharges “ ... shall be assessed on all policyholders of policies that cover insured property that is located in a catastrophe area, *including automobiles principally garaged in a catastrophe area.*” (emphasis added). The adopted rule amendments conform the department’s premium surcharge and loss funding rules to changes made by HB 3, and provide an orderly process for TWIA to obtain public securities if it needs these funds to pay its policyholders’ claims. The adopted rules do not impose any requirement on coastal policyholders that is not already required by the statute, and the rules do not directly affect TWIA’s rates. The department will keep the Legislature informed about the impact of implementing the use of public securities required by HB 4409 and HB 3, including the impact of any premium surcharges should they become necessary.

Comment: Several commenters suggest that the expiration of WPI-8 certificates will harm coastal residents. One commenter expressed frustration with their problems in getting a WPI-8 certificate, and the process for engineering oversight. Several commenters state that the lack of grandfathering provisions or full disclosures negatively impacts persons affected by storms.

Agency Response: The department understands the concerns but declines to revise or withdraw the proposed rule amendments. The adopted rule amendments conform the department's premium surcharge and loss funding rules to changes made by HB 3, and provide an orderly process for TWIA to obtain public securities if it needs these funds to pay its policyholders' claims. The rule amendments do not address WPI-8 certificates or provisions related to grandfathering WPI-8 certificates.

Comment: Several commenters suggest that the potential for premium surcharges is unfair because TWIA's problems are the result of mismanagement by TWIA. One commenter suggests that the premium surcharges, including surcharges on automobile policies, are intended to shore up the state-run financial mismanagement of TWIA. Another commenter suggests that it should not be coastal residents who have to pay for the mismanagement of TWIA.

Agency Response: The department understands concerns relating to TWIA management, but declines to revise or withdraw the proposed rule amendments. The adopted rule amendments conform the department's premium surcharge and loss funding rules to changes made by HB 3 and provide an orderly process for TWIA to obtain public securities should they be needed. The need to conform the department's rules to existing statute and to provide an orderly process for TWIA to obtain funds should they become necessary exists regardless of TWIA's financial condition. Delay or

3302

withdrawal of the proposed rules could harm TWIA's policyholders. The department will monitor complaints and insurer compliance.

Comment: Several commenters suggest that coastal windstorm coverage should be available through other insurers. One commenter states that the department can get insurance companies to return to selling windstorm coverage.

Agency Response: The department understands concerns relating to competition in the property market along the coast, but declines to revise or withdraw the proposed rule amendments. Implementing statutes designed to ensure funding for TWIA's policyholders is a separate issue from that of the availability of private market insurance along the coast. The adopted rule amendments conform the department's premium surcharge and loss funding rules to changes made by HB 3, and provide an orderly process for TWIA to obtain public securities if it needs these funds to pay its policyholders' claims. The rules do not impose any requirement on coastal policyholders that is not already required by the statute, and the rules do not directly affect insurance market competition. The department will keep the Legislature informed about the impact of implementing the use of public securities required by HB 4409 and HB 3, including the impact of any premium surcharges should they become necessary.

Comment: Many commenters suggest that the department needs to explore alternate funding sources to spread the cost and risk of a catastrophic event across the state.

One commenter states that the department should study what other states have done to address coastal windstorm coverage. Many commenters state that residents across Texas should contribute to the cost of windstorm insurance on the coast. Commenters suggest that the purpose of insurance is to pool risks.

Agency Response: The department understands the concerns but declines to revise or withdraw the proposed rule amendments. The adopted rule amendments conform the department's premium surcharge and loss funding rules to changes made by HB 3, and provide an orderly process for TWIA to obtain public securities if it needs these funds to pay its policyholders' claims. The Insurance Code does not authorize the department to require insurers to surcharge statewide policyholders. Insurance Code §2210.613, as created by HB 4409 and amended by HB 3, requires that the premium surcharges "... be assessed on all policyholders of policies that cover insured property that *is located in a catastrophe area*, including automobiles principally garaged *in a catastrophe area*." (emphasis added). The department will keep the Legislature informed about the impact of implementing the use of public securities required by HB 4409 and HB 3, including the impact of any premium surcharges should they become necessary.

Comment: Many commenters suggest that coastal residents are subsidizing other parts of the state. Several commenters suggest that recent property losses from wildfires, tornados, hailstorms, and severe freezes have been paid for by coastal

3302

policyholder premiums. Several commenters suggest that the insurance risks for coastal property is not different than the risks faced in other parts of the state.

Agency Response: The department understands the concerns but declines to revise or withdraw the rules. The adopted rule amendments conform the department's premium surcharge and loss funding rules to changes made by HB 3. The Insurance Code does not authorize the department to require insurers to surcharge statewide policyholders. Insurance Code §2210.613, as created by HB 4409 and amended by HB 3, requires that the premium surcharges "... be assessed on all policyholders of policies that cover insured property that *is located in a catastrophe area*, including automobiles principally garaged *in a catastrophe area*." (emphasis added). The department will keep the Legislature informed about the impact of implementing the use of public securities required by HB 4409 and HB 3, including the impact of any premium surcharges should they become necessary.

Comment: Many commenters suggest alternative funding methods. One commenter states that the easiest way to do that is to ask the insurance companies to purchase the bonds in the event of a storm. Several commenters suggest that residents in all of the United States should contribute to the costs of insuring risks anywhere in the United States. Another commenter suggests a similar federal mechanism involving other states that share coastal windstorm risks. Another commenter suggests that the funding for the public securities should come from the insurance premium taxes that are

3302

based on the admitted and nonadmitted carriers operating in Texas. One commenter suggests that insurance companies should be asked to fund the cost of reinsurance and let them spread those costs throughout the state. Another commenter suggests that funding should come from forcing all home and building owners to pay a prorated premium rate that is based on the value of the homes or buildings. One commenter suggests that if TWIA needs more money, it ought to raise the rates of current TWIA policyholders. Another commenter suggests an additional hotel tax on visitors to the coastal areas.

Many commenters suggest other methods to insure the coast or to mitigate the need for TWIA. Many commenters state that the premium surcharge should apply statewide. One commenter states that the solution to the TWIA problem is the removal of all new homes and homes built to code from the TWIA pool. Another commenter states that if the Uniform Building Codes were enforced across the state, property damage would be mitigated. Several commenters state that the department should require insurance companies to write insurance in all of Texas. One commenter suggested that all property and casualty insurance companies that do business in Texas offer windstorm coverage statewide, at a rate not to exceed 1 percent of the insured value of the property. One commenter suggests that tort reform would be helpful. Another suggests a consumer and user tax on products specifically earmarked for the windstorm fund. One commenter suggests that the department look to federal flood insurance for a viable funding method. Another commenter suggests that the

3302

department require better underwriting rules, adequate rates, liability limits, other funding strategies, and encourage the private insurance market. Another commenter suggests encouraging underwriting flexibility to encourage insurance companies to write coverage on the coast. One commenter suggests that TWIA policies should only cover named storms. One commenter states that the premium surcharge should be 3 percent on the coast and 1 percent everywhere else. One commenter suggests that rates should vary by wind maps and that the department should conduct further study to produce wind maps that provide a reasonable measure of the degree of risk across Texas. Another commenter states that all beach property and property within two miles of the beach should pay the premium surcharge. Another commenter suggests expanding the list of counties to any county where the wind speed maps show that wind may exceed 90 miles an hour. The commenter states that expanding the coastal zone would include 50 more counties than the 14 specified tier one counties. One commenter suggests that TWIA coverage should be more like flood insurance, and premium should be 100 percent earned when written. Then the only way a policy can be canceled is if the homeowner sells their property.

Several commenters suggest funding solutions relating to imposing a tax or surcharge on goods that are produced or transported from the coast to other areas of the state. Another commenter suggests that the state should cover any shortcomings in the association's ability to pay claims. Several commenters suggest that the state's rainy day funds be available for windstorm costs.

3302

Agency Response: The department declines to revise or withdraw the proposed rule amendments. The adopted rule amendments conform the department's premium surcharge and loss funding rules to changes made by HB 3, and provide an orderly process for TWIA to obtain public securities if it needs these funds to pay its policyholders' claims. The statute prescribes the method for financing public securities. The department will keep the Legislature informed about the impact of implementing the use of public securities required by HB 4409 and HB 3, including the impact of any premium surcharges should they become necessary. The authority of the department is limited to the statutory methods that the Legislature has created. The department will continue to do what it can to encourage authorized insurers to write insurance on a voluntary basis and to minimize the use of TWIA as a means to obtain insurance, as required by Insurance Code §2210.009. During the next legislative session, the department will serve as a resource for the Legislature, should the Legislature address TWIA's funding structure.

Comment: One commenter suggests that residents on the coast should not have two different deductibles, and that the standard TWIA policy should cover all hazards the same way.

Agency Response: The department understands the concerns but declines to revise or withdraw the proposed rule amendments. The rule amendments conform the department's premium surcharge and loss funding rules to changes made by HB 3, and

3302

provide an orderly process for TWIA to obtain public securities if it needs these funds to pay its policyholders' claims. The authority of the department is limited to the regulatory authority specified in Chapter 2210, TWIA's governing statute. The type of coverage that TWIA may provide is prescribed by Chapter 2210. The adopted rules do not address the type of coverage that TWIA may provide or the contractual language in a TWIA policy.

Comment: Several commenters suggest TWIA should depopulate and cover less property in order to remove some of the risk. One commenter suggests that the statutory language imposes a requirement on the department to develop incentives. The commenter states that the department should push incentives even if insurance companies do not like the incentives. Another commenter suggests that TWIA is not interested in depopulation.

Agency Response: The department agrees that reducing TWIA's risk, including TWIA depopulation strategies, should be pursued. However, the department declines to revise or withdraw the proposed rule amendments. The adopted rule amendments conform the department's premium surcharge and loss funding rules to changes made by HB 3, and provide an orderly process for TWIA to obtain public securities if it needs these funds to pay its policyholders' claims. The department is continuing its administrative oversight of TWIA. The department will continue to do what it can to encourage authorized insurers to write insurance on a voluntary basis and to minimize

3302

TITLE 28. INSURANCE
Part I. Texas Department of Insurance
Chapter 5. Property and Casualty

Adopted Sections
Page 61 of 87

the use of TWIA as a means to obtain insurance, as required by Insurance Code §2210.009.

Comment: One commenter states that the department should look into dissolving TWIA. The commenter states that TWIA should not be allowed to continue making mistakes that cost taxpayers and citizens.

Agency Response: The department understands the concerns but declines to revise or withdraw the rule amendments. The department does not have authority to change TWIA's statutory structure, which the Legislature enacted. The department is continuing its administrative oversight of TWIA.

Comment: Several commenters suggest that they support the proposed rules in general. Supportive commenters also offer similar constructive comments to those suggested by commenters not in support of the rules.

Agency Response: The department appreciates the supportive comments.

5. NAMES OF THOSE COMMENTING FOR AND AGAINST THE PROPOSAL.

For: Two individuals.

For with changes: American Insurance Association, Association of Fire and Casualty Companies of Texas, Bank of America Merrill Lynch, Insurance Council of

3302

TITLE 28. INSURANCE
Part I. Texas Department of Insurance
Chapter 5. Property and Casualty

Adopted Sections
Page 62 of 87

Texas, JP Morgan Chase, Texas Public Finance Authority, Texas Surplus Lines Association.

Against: One U.S. congressman; three state senators; 11 state representatives; five mayors; four county commissioners; one city secretary; 13 city councilpersons; three county judges; Associated General Contractors of Southeast Texas; Beaumont Board of Realtors; Beaumont Chamber of Commerce; Braselton Homes; Brownsville Chamber of Commerce; Builders Association of Corpus Christi; Catholic Charities of Southeast Texas; Coastal Windstorm Task Force; Corpus Christi Association of Realtors; Corpus Christi Chamber of Commerce; Del Mar College; Hamilton Real Estate; Island Retreat Condominiums; League of United Latin American Citizens of Corpus Christi; Mr. Sidings, Windows, and Sunrooms; Padre Island Chamber of Commerce; Padre Isles Property Owners Association; Port Aransas Chamber of Commerce and Tourist Bureau; Port of Corpus Christi Authority; Port Royal Ocean Resort; Regional Economic Development Initiative; Salter Insurance Agency; South Padre Island Chamber of Commerce; Southeast Texas Plan Managers Forum; Terry Cauthen Insurance; Texas Association of Realtors; Texas Watch; Thurmen-Fonden Glass; TPCO America Corporation; and 238 individuals.

6. STATUTORY AUTHORITY. The amendments are adopted under Insurance Code §§36.001, 2210.008, 2210.071, 2210.073, 2210.609, 2210.611, 2210.613, and 2210.6136. Section 2210.008(b) authorizes the commissioner to adopt reasonable and

3302

necessary rules in the manner prescribed by Insurance Code Chapter 36, Subchapter

A.

Section 36.001 provides that the commissioner may adopt any rules necessary and appropriate to implement the powers and duties of the Texas Department of Insurance under the Insurance Code and other laws of the state.

Section 2210.071 provides that if an occurrence or series of occurrences in a catastrophe area results in insured losses and operating expenses of the association in excess of premium and other revenue of the association, the excess losses and operating expenses must be paid as provided in Insurance Code Chapter 2210, Subchapter B-1, which includes the issuance of public securities. Section 2210.073 authorizes the association to use the proceeds of class 2 public securities issued after an occurrence or series of occurrences to pay for losses not paid under §2210.072, and establishes that class 2 public securities must be repaid in the manner prescribed by Insurance Code Chapter 2210, Subchapter M.

Section 2210.609 provides that the association must repay all public security obligations from available funds, and if those funds are insufficient, then from revenue collected under Insurance Code §§2210.612, 2210.613, 2210.6135, and 2210.6136. Section 2210.611 establishes that for class 2 public securities, the association may use premium surcharge revenue and member assessment revenue collected under Insurance Code §2210.613 in any calendar year that exceeds the amount of the class 2 security obligations and public security administrative expenses payable in that

3302

calendar year, and the interest earned on those funds to: (i) pay the applicable public security obligations payable in the subsequent year; (ii) redeem or purchase outstanding public securities; or (iii) make a deposit in the CRTF.

Section 2210.613 provides that the association must collect premium surcharges and member assessments to pay class 2 public securities issued under §2210.073. Section 2210.613(c) establishes the lines of insurance to which the premium surcharge applies. Section 2210.6136 provides that the commissioner may order the issuance of class 2 public securities if all or any part of the class 1 public securities cannot be issued. Section 2210.6136 further provides that the commissioner shall order the association to repay the premium surcharges and member assessments used to pay the cost of a portion of the class 2 public securities issued under this section.

7. TEXT.

§5.4171. Premium Surcharge Requirement.

(a) Following a catastrophic event, insurers may be required to assess a premium surcharge under Insurance Code §2210.613(b) and (c) on all policyholders of policies that cover insured property that is located in a catastrophe area, including automobiles principally garaged in the catastrophe area. This requirement applies to property and casualty insurers, the association, the Texas FAIR Plan Association, Texas Automobile Insurance Plan Association (TAIPA) policies, affiliated surplus lines

insurers, and includes property and casualty policies independently procured from affiliated insurers.

(b) This section and §§5.4172, 5.4173, 5.4181, 5.4182, and 5.4184 - 5.4192 of this division (relating to Premium Surcharge Definitions, Determination of the Surcharge Percentage, Premiums to be Surcharged, Method for Determining the Premium Surcharge, Application of the Surcharges, Mandatory Premium Surcharge Collection, Remittance of Premium Surcharges, Offsets, Surcharges Not Subject to Commissions or Premium Taxes, Notification Requirements, Annual Premium Surcharge Report, Premium Surcharge Reconciliation Report, and Data Collection, respectively) only apply to policies written for the following types of insurance: commercial fire; commercial allied lines; farm and ranch owners; residential property insurance; commercial multiple peril (nonliability portion); private passenger automobile no fault (personal injury protection (PIP)); other private passenger automobile liability; private passenger automobile physical damage; commercial automobile no fault (PIP); other commercial automobile liability; and commercial automobile physical damage.

(c) This section and §§5.4172, 5.4173, 5.4181, 5.4182, and 5.4184 - 5.4192 of this division do not apply to:

(1) a farm mutual insurance company operating under Insurance Code Chapter 911;

3302

(2) a nonaffiliated county mutual fire insurance company described by Insurance Code §912.310 that is writing exclusively industrial fire insurance policies as described by Insurance Code §912.310(a)(2);

(3) a mutual insurance company or a statewide mutual assessment company engaged in business under Chapter 12 or 13, Title 78, Revised Statutes, respectively, before those chapters' repeal by §18, Chapter 40, Acts of the 41st Legislature, First Called Session, 1929, as amended by Section 1, Chapter 60, General Laws, Acts of the 41st Legislature, Second Called Session, 1929, that retains the rights and privileges under the repealed law to the extent provided by those sections; and

(4) premium and policies issued by an affiliated surplus lines insurer that a federal agency or court of competent jurisdiction determines to be exempt from a premium surcharge under Insurance Code Chapter 2210.

(d) For all lines of insurance subject to this division, this section and §§5.4172, 5.4173, 5.4181, 5.4182, and 5.4184 - 5.4192 of this division are effective June 1, 2011.

§5.4172. Premium Surcharge Definitions. The following words and terms when used in §§5.4171, 5.4173, 5.4181, 5.4182, and 5.4184 - 5.4192 of this division (relating to Premium Surcharge Requirement, Determination of the Surcharge Percentage, Premiums to be Surcharged, Method for Determining the Premium Surcharge, Application of the Surcharges, Mandatory Premium Surcharge Collection, Remittance of Premium Surcharges, Offsets, Surcharges not Subject to Commissions or Premium

3302

Taxes, Notification Requirements, Annual Premium Surcharge Report, Premium Surcharge Reconciliation Report, and Data Collection, respectively) will have the following meanings unless the context clearly indicates otherwise:

(1) **Affiliated insurer**--An insurer that is an affiliate, as described by Insurance Code §823.003, of an insurer authorized to engage in the business of property or casualty insurance in the State of Texas. Affiliated insurer includes an insurer not authorized to engage in the business of property or casualty insurance in the State of Texas.

(2) **Affiliated surplus lines insurer**--An eligible surplus lines insurer that is an affiliate, as described by Insurance Code §823.003, of an insurer authorized to engage in the business of property or casualty insurance in the State of Texas.

(3) **Exposure**--The basic unit of risk that is used by an insurer to determine the insured's premium.

(4) **Insured property**--Real property, or tangible or intangible personal property including automobiles, covered under an insurance policy issued by an insurer. Insured property includes motorcycles, recreational vehicles, and all other vehicles eligible for coverage under a private passenger automobile or commercial automobile policy.

(5) **Insurer**--Each property and casualty insurer authorized to engage in the business of property or casualty insurance in the State of Texas and an affiliate of the insurer, as described by Insurance Code §823.003, including an affiliate that is not

3302

authorized to engage in the business of property or casualty insurance in the State of Texas, the association, and the FAIR Plan. The term specifically includes a county mutual insurance company, a Lloyd's plan, and a reciprocal or interinsurance exchange.

(6) Premium surcharge percentage--The percentage amount determined by the commissioner under §5.4173 of this division.

(7) Residential property insurance--Insurance against loss to real or tangible personal property at a fixed location, including through a homeowners insurance policy, a tenants insurance policy, a condominium owners insurance policy, or a residential fire and allied lines insurance policy.

§5.4173. Determination of the Surcharge Percentage.

(a) The association must review information provided by TPFA concerning the amount of the class 2 public security obligations and estimated amount of the class 2 public security administrative expenses, including any required contractual coverage amount, to determine whether the association has sufficient available funds to pay the public security obligations and public security administrative expenses, if any, including any contractual coverage amount, or whether a premium surcharge under Insurance Code §2210.613 is required. The association may consider all of the association's outstanding obligations and sources of funds to pay those obligations.

(b) If the association determines that it is unable to satisfy the estimated amount of class 2 public security obligations and administrative expenses with available funds,

3302

the association must submit a written request to the commissioner to approve a premium surcharge on policyholders with insured property in the catastrophe area as authorized under Insurance Code §2210.613. The association's request must specify:

(1) the total amount of the class 2 public security obligations and estimated amount of the class 2 public security administrative expenses, including any required contractual coverage amount, provided in the TPFA notice;

(2) the amount to be collected from insurers through a member assessment, which may not exceed 30 percent of the amount specified in the TPFA notice;

(3) the amount to be collected from catastrophe area policyholders through premium surcharges, which may not exceed 70 percent of the amount specified in the TPFA notice; and

(4) the date on which the premium surcharge is to commence and the date the premium surcharge for the noticed amount is to end.

(c) On approval by the commissioner, each insurer must assess a premium surcharge in a percentage amount set by the commissioner to the insurer's policyholders. The premium surcharge percentage must be applied to the premium attributable to insured property located in the catastrophe area on policies that become effective, or on multiyear policies that become effective or have an anniversary date, during the premium surcharge period when the premium surcharge percentage will be in effect, as specified in §§5.4181, 5.4182, and 5.4184 - 5.4188 of this division (relating

3302

to Premiums to be Surcharged, Method for Determining the Premium Surcharge, Application of the Surcharges, Mandatory Premium Surcharge Collection, Remittance of Premium Surcharges, Offsets, and Surcharges not Subject to Commissions or Premium Taxes, respectively). The premium surcharge date specified by the commissioner must be at least 180 days after the date the commissioner issues notice of approval of the public securities.

(d) This section is part of the association's plan of operation and will control over any conflicting provision in §5.4001 of this subchapter (relating to Plan of Operation).

§5.4181. Premiums to be Surcharged.

(a) The premium surcharge percentage must be applied to:

(1) amounts reported as premium for the purposes of reporting under the Annual Statement, Exhibit of Premiums and Losses (Statutory Page 14), Texas;

(2) if not reported as described in paragraph (1) of this subsection, those additional amounts collected by insurers that are subject to premium taxation by the comptroller, including policy fees not reported as premium; and

(3) premium subject to surplus lines premium tax, and premium subject to independently procured premium tax.

(b) Premium surcharges do not apply to fees that are neither reported as premium in the Annual Statement, Exhibit of Premiums and Losses (Statutory Page 14), Texas, nor subject to premium taxation by the comptroller.

§5.4182. Method for Determining the Premium Surcharge.

(a) The methods addressed in this section will apply to all:

(1) policies written and reported under the following annual statement lines of business: fire; allied lines; farm and ranch owners; homeowners; commercial multiple peril (nonliability portion); private passenger auto no fault (personal injury protection (PIP)), other private passenger auto liability, and private passenger auto physical damage; and commercial auto no fault (PIP), other commercial auto liability, and commercial auto physical damage; and

(2) personal and commercial risks assigned by TAIPA under Insurance Code Chapter 2151.

(b) The premium surcharge will be determined by applying the premium surcharge percentage to the policy premium determined in §5.4181 of this division (relating to Premiums to be Surcharged), attributable to insured property located in the catastrophe area.

(c) In cases where the policy is composite rated and the premium attributable to insured property located in the catastrophe area cannot be reasonably determined, the insurer must determine the premium surcharge based on the insured address. If the insured address is within a designated catastrophe area, then the insurer must determine the premium surcharge by applying the premium surcharge percentage to the

full policy premium determined in §5.4181 of this division. If the insured address is not within a designated catastrophe area, then no premium surcharge applies to the policy.

§5.4184. Application of the Surcharges.

(a) When assessed under Insurance Code §2210.613, the premium surcharges must apply to all policies with insured property in the catastrophe area that are issued or renewed with effective dates in the assessment period specified in the commissioner's order, with two exceptions:

(1) insurers must not surcharge policies, and are not responsible for collecting premium surcharges on policies, that did not go into effect or were canceled as of the inception date of the policy; and

(2) for multiyear policies, the premium surcharge in effect on the effective date of the policy, or the anniversary date of the policy, must be applied to the 12-month premium for the applicable policy period.

(b) Premium surcharges are refundable under Insurance Code §2210.613.

(1) If the policy is canceled, an amount of the surcharge that is proportionate to the return premium must be refunded to the policyholder; however,

(2) instead of a refund of the premium surcharge, the insurer may credit the return premium surcharge against amounts due the insurer but unpaid by the policyholder; and

(3) an additional surcharge will not apply to a policy that was canceled after the effective date of the policy, and is later reinstated, if the premium surcharge was paid in full. If the policyholder did not pay the premium surcharge in full, the policyholder must pay the premium surcharge that is due but unpaid before the insurer may reinstate the policy. For purposes of this section a policy is reinstated if it covers the same period as the original policy without a lapse in coverage, except as provided in Insurance Code §551.106.

(c) If a midterm policy change increases the premium on the policy, the policyholder must pay an additional surcharge for the increased premium attributable to insured property located in the catastrophe area, which will be determined by applying the applicable premium surcharge percentage to that portion of the additional premium attributable to insured property located in the catastrophe area.

(d) If a midterm policy change decreases the premium, the policyholder is due a refund of the surcharge for the decreased premium attributable to insured property located in the catastrophe area, which must be determined by applying the applicable premium surcharge percentage to that portion of the return premium attributable to insured property located in the catastrophe area. The insurer must credit or refund the excess surcharge to the policyholder within 20 days of the date of the transaction, except as provided by subsection (g) of this subsection. The insurer, or surplus lines agent allowed by an affiliated surplus lines insurer to credit or refund excess

3302

surcharges, may credit any refund paid or credited to the policyholder to the association through the offset process described in §5.4187 of this division (relating to Offsets).

(e) Surcharges or refunds must apply to all premium changes resulting from exposure or premium audits, retrospective rating adjustments, or other similar adjustments that occur after policy expiration. On inception of the policy, the premium surcharge must be collected on the deposit premium paid. If, after exposure or premium audit, retrospective rating adjustment, or similar adjustment after policy expiration, an additional premium is required, an additional surcharge must be paid. If, after exposure or premium audit, retrospective rating adjustment, or other similar adjustment after policy expiration, the deposit premium exceeds the actual premium, the excess surcharge must be refunded to the policyholder, and the insurer, or surplus lines agent allowed by an affiliated surplus lines insurer to credit or refund excess surcharges, may credit any refund paid to the association through the offset process described in §5.4187 of this division. Additional surcharges and refunds must be determined by applying the premium surcharge percentage in effect on the inception date of the policy, or the anniversary date of the policy in the case of multiyear policies, to the additional premium (or return premium) attributable to insured property located in the catastrophe area.

(f) Even if a surcharge was in effect on the inception date of the policy, or the anniversary date in the case of multiyear policies, no additional premium surcharges or refunds will apply to premium changes resulting from exposure or premium audits,

retrospective rating adjustments, or other similar adjustments that occur when there is no premium surcharge in effect.

(g) An affiliated surplus lines insurer may allow a surplus lines agent to credit or refund premium surcharges on its behalf. An affiliated surplus lines insurer, or surplus lines agent allowed to credit or refund premium surcharges on its behalf, must credit or refund the excess surcharge to the policyholder under subsections (d) and (e) of this section not later than the last day of the month following the month in which the corresponding transaction was effective.

(h) An affiliated surplus lines insurer that allows an agent to credit or refund premium surcharges on its behalf under subsection (g) of this section may be held liable by the department for the failure of its agent to comply with this section.

§5.4185. Mandatory Premium Surcharge Collection.

(a) Except as provided in §5.4127(h) of this division (relating to Payment of Class 2 Public Securities Issued Under §5.4126 and Repayment of Premium Surcharges and Member Assessments), insurers may not pay the surcharges instead of surcharging their policyholders. However, an insurer may remit a surcharge prior to collecting the surcharge from its policyholder.

(b) Insurers must collect the premium surcharges proportionately as the insurer collects the premium.

(c) Under Insurance Code §2210.613(d), the failure of a policyholder to pay the premium surcharge constitutes failure to pay premium for the purposes of policy cancellation.

§5.4186. Remittance of Premium Surcharges.

(a) Except as provided in §5.4143 of this division (relating to Trust Funds for the Payment of Class 2 Public Securities), insurers must remit to the association the aggregate amount of surcharges as provided by this section. An affiliated surplus lines insurer may allow a surplus lines agent to remit premium surcharges to the association on its behalf in compliance with any procedures established by the association relating to premium surcharge remissions from surplus lines agents.

(b) Insurers, or surplus lines agents allowed by affiliated surplus lines insurers to remit surcharges under subsection (a) of this section, must remit all surcharges not later than the last day of the month following the month in which the corresponding written premium transaction was effective.

(c) Insurers and agents may not allow or require policyholders to make separate payments for the surcharge amounts that are payable to the association or the premium surcharge trust fund.

(d) Subsection (b) of this section applies to all insurers regardless of whether the policyholder paid the premium surcharge through an agent of the insurer or the policyholder paid the premium surcharge directly to the insurer.

(e) An affiliated surplus lines insurer that allows an agent to remit premium surcharges to the association under subsection (a) of this section may be held liable by the department for the failure of its agent to remit the premium surcharges or timely remit the premium surcharges, under subsection (b) of this section.

§5.4187. Offsets.

(a) An insurer may credit a premium surcharge amount on its next remission to the association if the insurer has already remitted the amount to the association for:

(1) the portion of the surcharge the insurer was not able to collect from the policyholder, if the policy was canceled or expired;

(2) the portion of the surcharge remitted to the association, or deposited directly in the premium surcharge trust fund, that was later refunded to the policyholder as a result of a midterm cancellation or midterm policy change, as described in §5.4184 of this division (relating to Application of the Surcharges); or

(3) the portion of a surcharge remitted to the association, or deposited directly in the premium surcharge trust fund, in excess of a deposit premium as described in §5.4184 of this division.

(b) An agent may not offset payment of a premium surcharge to the insurer for any reason. However, a surplus lines agent allowed by an affiliated surplus lines insurer to remit surcharges to the association on its behalf under §5.4186(a) of this

division (relating to Remittance of Premium Surcharges), may offset as provided in this section.

§5.4189. Notification Requirements.

(a) Insurers must provide written notice to policyholders receiving a premium surcharge that their policy contains a surcharge. The notice must read: "Texas Insurance Code Sections 2210.073 and 2210.613 require a premium surcharge be added to certain property and casualty insurance policies providing coverage in the catastrophe area to pay the debt service on public securities issued to pay Texas Windstorm Insurance Association claims resulting from a catastrophic event. A premium surcharge {in the amount of \$_____} has been added to your premium. Should your policy be canceled by you or the insurer prior to its expiration date, a proportionate amount of the premium surcharge will be refunded to you. Failure to pay the surcharge is grounds for cancellation of your policy."

(b) Insurers must provide written notice to policyholders of the dollar amount of the premium surcharge.

(c) Except as provided in subsection (d) of this section, notices required under subsections (a) and (b) of this section must:

(1) be provided at the time the policy is issued, in the case of new business;

(2) be provided with the renewal notice, in the case of renewal business;

(3) be provided within 20 days of the date of the transaction for any midterm change in the premium surcharge; and

(4) use at least 12-point font and either be contained on a separate page or shown in a conspicuous location on the declarations page.

(d) An affiliated surplus lines insurer, or surplus lines agent allowed to provide notices on its behalf, must provide the notice required under subsection (c)(3) of this section to the policyholder not later than the last day of the month following the month in which the transaction for any midterm change in the premium surcharge became effective.

(e) An affiliated surplus lines insurer that allows an agent to provide notices required under this section may be held liable by the department for the failure of its agent to comply with this section.

§5.4190. Annual Premium Surcharge Report.

(a) This section applies to an insurer that, during the calendar year, wrote any of the following types of insurance: commercial fire; commercial allied lines; farm and ranch owners; residential property insurance; commercial multiple peril (nonliability portion); private passenger automobile no fault (personal injury protection (PIP)); other private passenger automobile liability; private passenger automobile physical damage; commercial automobile no fault (PIP); other commercial automobile liability; or commercial automobile physical damage.

3302

(b) No later than 90 days following the end of a calendar year in which a premium surcharge was in effect, each insurer must provide the association with an annual premium surcharge report for the calendar year unless premium surcharges were in effect for less than 45 days within the calendar year.

(c) Annual premium surcharge reports must provide information for each insurance company writing property or casualty insurance in the State of Texas, including affiliated surplus lines insurers, and affiliated insurers not authorized to engage in the business of insurance that issued independently procured insurance policies covering insured property in the State of Texas.

(d) Annual premium surcharge reports must provide information for the following annual statement lines of business: fire; allied lines; farmowners multiple peril; homeowners multiple peril; commercial multiple peril (nonliability portion); private passenger automobile no fault (PIP); other private passenger automobile liability; private passenger automobile physical damage; commercial automobile no fault (PIP); other commercial automobile liability; or commercial automobile physical damage for which the insurer reported premium for the applicable calendar year.

(e) Annual premium surcharge reports must provide the following information:

- (1) the name and contact information of the individual responsible for submitting the report;
- (2) the five-digit NAIC number of the insurance company;
- (3) the name of the insurance company;

3302

(4) for policies with effective dates, or multiyear policies with anniversary dates, within the calendar year, separately for each surcharge period in effect during the calendar year, and within each surcharge period in effect during the calendar year for all applicable lines of business:

(A) for all policies subject to a premium surcharge:

(i) the total written premium attributable to insured property located in the catastrophe area; and

(ii) the total written premium attributable to insured property located outside the catastrophe area; and

(B) the total written premium for policies not subject to a premium surcharge because the policyholder had no insured property located in the catastrophe area;

(5) for policies effective in portions of the calendar year when no surcharge period was in effect, or in the case of multiyear policies with an anniversary date in portions of the calendar year when no surcharge was in effect, the total written premium;

(6) the total amount of premium surcharges collected during the applicable calendar year; and

(7) the total amount of premium surcharges remitted to the association during the applicable calendar year.

(f) The association must:

3302

(1) review the reports submitted under this section as necessary to determine:

(A) the consistency of premium surcharges actually remitted to the association or deposited directly into the premium surcharge trust fund, with premium surcharges shown in the reports as collected and the premium surcharges shown in the reports as remitted to the association or deposited directly into the premium surcharge trust fund; and

(B) the consistency of premiums shown in the reports as attributable to the catastrophe area with premium surcharges shown in the reports as collected by the insurer, given the requirements regarding the determination of premium surcharges in this division;

(2) inform the department of any insurer the association believes may not be in compliance with the rules established under this division; and

(3) before July 1 on each year reports are required to be submitted to the association, provide an aggregate summary of the reports to the department.

§5.4191. Premium Surcharge Reconciliation Report.

(a) This section applies to an insurer that, during an applicable calendar year, wrote any or all of the following types of insurance: commercial fire; commercial allied lines; farm and ranch owners; residential property insurance; commercial multiple peril (nonliability portion); private passenger automobile no fault (personal injury protection

3302

(PIP)); other private passenger automobile liability; private passenger automobile physical damage; commercial automobile no fault (PIP); other commercial automobile liability; or commercial automobile physical damage.

(b) On a written request from the department, an insurer must provide the department with a premium surcharge reconciliation report for the year specified by the department in its request.

(c) Reconciliation reports must be provided to the department within 15 working days after the date the request is received by the insurer.

(d) Reconciliation reports must consist of information concerning premiums written and surcharges collected, separately for each applicable surcharge period, including periods in which no premium surcharges were in effect, within the specified year for:

(1) premium written at policy issuance for policies effective within the year, including anniversary dates within the year on multiyear policies, separately for:

(A) premium on policies subject to a premium surcharge, including premium attributable to insured property located both in and outside of the catastrophe area; and

(B) premium on policies not subject to a premium surcharge, including premium attributable to insured property located both in and outside of the catastrophe area;

3302

(2) premium written due to midterm coverage changes occurring within the specified time period separately for:

(A) premium increases on policies subject to a premium surcharge, including premium attributable to insured property located both in and outside of the catastrophe area;

(B) premium decreases on policies subject to a refund or credit of the premium surcharge, including premium attributable to insured property located both in and outside the catastrophe area; and

(C) premium on policies not subject to a premium surcharge, including premium increases and decreases attributable to insured property located both in and outside of the catastrophe area;

(3) unearned premiums returned due to midterm cancellations occurring within the specified time period separately for:

(a) return premium on policies subject to a premium surcharge, including return premium attributable to insured property located both in and outside the catastrophe area; and

(b) return premium on policies not subject to a premium surcharge, including return premiums attributable to insured property located both in and outside the catastrophe area;

(4) total premium due to post term premium changes occurring within the specified time period, including adjustments caused by premium or exposure audits,

3302

retrospective rating adjustments, or other similar adjustments that occur after policy expiration, separately for:

(A) premium on policies subject to a premium surcharge, including premium attributable to insured property located both in and outside of the catastrophe area; and

(B) premium on policies not subject to a premium surcharge, including premium attributable to insured property located both in and outside of the catastrophe area;

(5) separately for paragraphs (1)(A), (2)(A), and (4)(A) of this subsection, the amounts of premium surcharges collected;

(6) separately for paragraphs (2)(B), (3)(A), and (4)(A) of this subsection, the amounts of premium surcharges refunded or credited to the policyholder;

(7) the total amount of premium surcharges claimed as offsets by the insurer under §5.4187 of this division (relating to Offsets); and

(8) the total amount of written premium for policies written in the State of Texas as reported in the Annual Statement, Exhibit of Premiums and Losses (Statutory Page 14), Texas.

(e) Nothing in this section limits the department's authority to obtain information from insurers under the Insurance Code.

(f) A report provided to the department under this section may be provided to the association.

§5.4192. Data Collection.

(a) The department may request from each insurer the information necessary to enable the department to determine the premium surcharge percentage applicable to policyholders with insured property located in the catastrophe area.

(b) For lines of insurance subject to this division for policies in force on or after October 1, 2011, each insurer must maintain sufficient records to report, for policies where the premium surcharge was, or would be determined under this division, the total written premium attributable to insured property located in the catastrophe area.

(c) When possible, and practical, the department will obtain information from the Texas Surplus Lines Stamping Office prior to requesting information from affiliated surplus lines insurers.

(d) Nothing in subsection (c) of this section should be read to mean that subsections (a) and (b) of this section do not apply to affiliated surplus lines insurers.

(e) Nothing in this section limits the department's authority to obtain information from insurers under the Insurance Code.

8. CERTIFICATION. This agency certifies that legal counsel has reviewed the adoption and found it to be a valid exercise of the agency's legal authority.

Issued at Austin, Texas, on May 16, 2014.

3302

TITLE 28. INSURANCE
Part I. Texas Department of Insurance
Chapter 5. Property and Casualty

Adopted Sections
Page 87 of 87



Sara Waitt
General Counsel
Texas Department of Insurance

The commissioner adopts amendments to 28 TAC §§5.4171 - 5.4173, 5.4181, 5.4182, 5.4184 - 5.4187, and 5.4189 - 5.4192.



Julia Rathgeber
Commissioner of Insurance

COMMISSIONER'S ORDER NO. **3302**