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TO THE SENATE COMMITTEES ON
AGRICULTURE AND ENVIRONMENT
AND
WATER AND LAND

TWENTY-NINTH LEGISLATURE
Regular Session of 2018

Wednesday, February 14, 2018
1:15 p.m.

TESTIMONY ON SENATE BILL NO. 2327, RELATING TO INSURANCE.

TO THE HONORABLE KARL RHOADS AND MIKE GABBARD, CHAIRS, AND MEMBERS OF THE COMMITTEES:

The Department of Commerce and Consumer Affairs ("Department") appreciates the opportunity to testify on S.B. 2327, Relating to Insurance. My name is Gordon Ito, and I am the Insurance Commissioner for the Department's Insurance Division. The Department provides the following comments.

The purpose of this bill is to require authorized property insurers to establish environmental reserve funds out of policy premiums to pay for losses resulting from environmental events occurring along shoreline property in the State.

The Department appreciates the concerns of global warming and erosion that this State faces, but is unsure of the mechanics and operation of these proposed reserves.

If a policyholder has insurance coverage for shoreline environmental risks, then a claim against the policyholder's insurance policy may be made according to the terms in the contract. However, section 431: -H(a) states that an insurer shall release its reserve when "it" incurs qualifying losses. By the plain reading of this bill, the only way for an insurer to incur a qualifying loss means that a covered loss on an existing policy already exists. There is a contractual relationship under an existing policy to pay and the insurer already has a reserve to pay for it. The end result is that the additional reserve proposed by this bill will not be affected or used.

If the purpose of this reserve fund is to make a payment for an environmental claim which is not covered by a current policy, then this is not insurance as there is no contract for the coverage of that claim. The funding of an environmental reserve and the mandatory payment of a claim not under a contract under this scenario is problematic.

It is not clear whether these additional costs to insurers are to be considered taxes or fees. Additionally, the establishment of mandatory global warming and erosion reserves for all property insurers in this State will raise all property insurance premiums making the purchasing of all property insurance more expensive.

Thank you for the opportunity to testify on this measure.

HAWAII INSURERS COUNCIL
A trade association of property and casualty insurance companies

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1003 Bishop Street
Honolulu, Hawaii 96813
Telephone (808) 525-5877

Alison H. Ueoka
President

TESTIMONY OF MICHAEL TANOUE

COMMITTEE ON AGRICULTURE AND ENVIRONMENT
Senator Mike Gabbard, Chair
Senator Gil Riviere, Vice Chair

COMMITTEE ON WATER AND LAND
Senator Karl Rhoads, Chair
Senator Mike Gabbard, Vice Chair

Wednesday, February 14, 2018
1:15 p.m.

SB 2327

Chair Gabbard, Vice Chair Riviere, and members of the Committee on Agriculture and Environment, and Chair Rhoads, Vice Chair Gabbard, and members of the Committee on Water and Land, my name is Michael Tanoue, counsel for the Hawaii Insurers Council. The Hawaii Insurers Council is a non-profit trade association of property and casualty insurance companies licensed to do business in Hawaii. Member companies underwrite approximately forty percent of all property and casualty insurance premiums in the state.

Hawaii Insurers Council **opposes** this bill. This bill creates a new article, ñGlobal Warming or Erosion Insurance Reserve.ò Its purpose is to require authorized property insurers to establish reserve funds out of premiums of policies covering risks located or resident in this State. The reserve fund shall be used to pay for losses resulting from certain environmental events occurring along shoreline property in the State.

The bill seeks to mandate authorized insurers to set aside monies to pay for losses that are undefined but appear to be those which are normally excluded from insurance policies. Furthermore, the losses are only those which occur along the stateôs shoreline areas. It creates an unlevel playing field against those insurers authorized to do business in Hawaii by mandating monies be set aside that no other insurer in the United

States is required to do. The bill also requires these reserves to pay for losses that are normally not covered, for instance, losses that could be caused by seawater action. The bill is specific to shoreline property which includes commercial and residential property. The bill provides an incentive for people and businesses to purchase properties along the shoreline if all other property policyholders will pay for their loss of land due to erosion or from higher water levels attributable to global warming. The value of these types of losses could be enormous and property premiums in Hawaii could not withstand a surcharge large enough to pay for them.

The bill mandates that everyone who purchases property insurance pay for targeted coverage which is presently excluded from policies. This is likely to result in very large property insurance premiums for homeowners and businesses. If there is a mortgage or commercial lessor, lender-based insurance may be imposed, also at a very high cost. If policyholders abandon the local insurance market to self-insure or purchase insurance from unauthorized insurers, there will be nothing in reserves as a result.

We ask that you hold this bill.

Thank you for the opportunity to testify.

PCI

Advocacy. Leadership. Results.

To: The Honorable Mike Gabbard, Chair
The Honorable Gil Riviere, Vice Chair
Senate Committee on Agriculture and the Environment

The Honorable Karl Rhoads, Chair
The Honorable Mike Gabbard, Vice Chair
Senate Committee on Water and Land

From: Mark Sektnan, Vice President

Re: SB 2327 – Relating to Insurance
PCI Position: OPPOSE

Date: Wednesday, February 14, 2018
1:15 p.m., Conference Room 224

Aloha Chairs Gabbard and Rhoads, Vice Chair Riviere and Members of the Committees:

The Property Casualty Insurers Association of America (PCI) is opposed to SB 2327 which would require insurers to establish special reserves funds. In Hawaii, PCI member companies write approximately 42.3 percent of all property casualty insurance written in Hawaii. PCI member companies write 44.7 percent of all personal automobile insurance, 65.3 percent of all commercial automobile insurance and 76.5 percent of the workers' compensation insurance in Hawaii.

SB 2327 creates a new article, "Global Warming or Erosion Insurance Reserve." Its purpose is to require authorized property insurers to establish reserve funds out of premiums of policies covering risks located or resident in this State. The reserve fund shall be used to pay for losses resulting from certain environmental events occurring along shoreline property in the State. The bill seeks to mandate authorized insurers to set aside monies to pay for losses that are undefined but appear to be those which are normally excluded from insurance policies. Furthermore, the losses are only those which occur along the state's shoreline areas. It creates an unlevel playing field against those insurers authorized to do business in Hawaii by mandating monies be set aside that no other insurer in the United States is required to do. The bill also requires these reserves to pay for losses that are normally not covered, for instance, losses that could be caused by seawater action. The bill is specific to shoreline property which includes commercial and residential property. The bill provides an incentive for people and businesses to purchase properties along the shoreline if all other property policyholders will pay for their loss of land due to erosion or from higher water levels attributable to global warming. The value of these types of losses could be enormous and property premiums in Hawaii could not withstand a surcharge large enough to pay for them.

The bill mandates that everyone who purchases property insurance pay for targeted coverage which is presently excluded from policies. This is likely to result in very large property insurance premiums for homeowners and businesses. If there is a mortgage or commercial lessor, lender-based insurance may be imposed, also at a very high cost. If policyholders abandon the local insurance market to self-insure or purchase insurance from unauthorized insurers, there will be nothing in reserves as a result.

PCI asks the committee to hold this bill.

REINSURANCE ASSOCIATION OF AMERICA
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OPPOSE: Hawaii SB 2327
Global Warming and Erosion Insurance Reserve Act for Property Insurance Companies

The Reinsurance Association of America ("RAA") submits the following comments in opposition to the "Hawaii global warming and erosion insurance reserve act," SB 2327. The Reinsurance Association of America is the leading trade association of property and casualty reinsurers doing business in the United States. RAA membership is diverse, including reinsurance underwriters and intermediaries licensed in the U.S. and those that conduct business on a cross border basis. The RAA represents its members before state, federal and international bodies.

While we appreciate the efforts to put serious thought into catastrophe insurance issues, the RAA does not believe the Hawaii global warming and erosion insurance reserve act (the "Act") will achieve the ultimate objective of increasing the availability and affordability of insurance in catastrophe prone areas. First, the RAA believes the Act will significantly disappoint policymakers, as our understanding of Hawaii law, regulations and policies convinces us that the potential reserve that it would create would be negligible in relation to the potential losses that policymakers hope to address. Second, as we have mentioned in prior testimony, the RAA is concerned that a mandatory catastrophe reserve fund will not work as intended. And, since the Act would only apply to licensed insurers and reinsurers, it would have no effect on non-US reinsurers and could have the unintended consequences of providing a market advantage to unlicensed reinsurers.

Will the Proposed Reserve Create a Material Pool of Funds for Future Losses?

The RAA believes the Act, at best, will create a reserve with a negligible balance in relation to the climate change and erosion risks the legislature seeks to address.

First, the RAA understands that the risk of erosion is typically not covered or is excluded under private property insurance policies.

As the risk of erosion is typically not covered, insurers do not include a charge for the excluded risk of erosion in their policyholder premiums. Further, it is our understanding that the Hawaii insurance department would refuse to approve a rate that included a charge for an excluded risk if an insurer made such a filing. Accordingly, the potential catastrophic reserve for losses caused by erosion is likely to be negligible.

Second, while a changing climate is a material concern, property insurers typically write annual policies. The premiums charged reflect the risk of loss that the policyholder is exposed to in the ensuing twelve month period. As we understand the science, climate change impacts are supposed to manifest themselves over several decades and further into the future. Further, it is our understanding that scientists are currently unable to identify if a particular weather event is due to natural weather variability or to climate influenced events.

The difference is timing is quite significant. Insurance rates charged are based upon the probability of loss during the policy period. They do not contemplate losses and the changing climate for periods that occur after the policy has expired.

Because of the timing difference, it is the RAA's understanding that the rates filed by insurers with the insurance department do not include a risk charge for the potential impacts of climate change. Instead, the rates charged reflect the probability of losses for the covered policy period.

As insurance rates do not contemplate loss impacts decades into the future, the potential reserve fund for climate change risks would likely be immaterial or smaller.

Assuming the Act is applied as the RAA anticipates, it would be largely ineffective due to (a) the coverage issues mentioned above and (b) the fact that it would incrementally increase insurer expenses to comply. If the Act is applied to require insurers to establish a reserve for risks not covered due to policy terms and conditions or because the loss impacts are expected after the policy period, the Act would have significant market implications for insurers and Hawaii property owners. Unless insurers are able to obtain a rate that compensates them for their risks, expenses and an opportunity to potentially earn a reasonable profit, the RAA anticipates that insurers would look less favorably on the Hawaii property market at existing rates, terms and conditions.

Will the Proposed Reserve Have a Positive Impact?

As the RAA has previously testified regarding a catastrophe reserve proposal, the RAA is concerned that the Act's provisions that require the establishment of a segregated reserve for particular risk types will have significant unintended consequences and will likely interfere with the way companies underwrite risk and allocate capital. Contrary to its stated purpose, the Act is likely to increase market instability and unlikely to result in a more stable, abundant supply of affordable insurance.

Currently, insurers writing Hawaii catastrophe risks participate in pooling risks globally, directly and through reinsurers. To have a significant positive impact, the proposed reserve would need to reduce insurer concerns about events causing extremely large losses. The RAA does not believe the proposed reserve addresses the extreme event issue.

Further, if it is determined that a climate change reserve should be imposed, insurers are unable to rely upon their ability to draw from the reserve in the event of a catastrophe. As noted above, it is the RAA's understanding that scientists do not have the ability to discern whether a particular weather event was caused by normal weather variations or climate change impacts. As such, the proposed benefit of such a reserve would be negated by the uncertainty of being able to access it after a catastrophe.

On an annual basis, insurers must evaluate their exposure to catastrophe losses and how they will pay for such losses. Uncertainty regarding the ability to draw upon a climate change reserve requires insurers to ensure that their other claims paying resources, including reinsurance, are adequate to pay losses under a variety of loss scenarios. As uncertainties about being able to use a restricted reserve are likely, insurers will have to maintain the reserve and purchase reinsurance to enable them to pay their entire losses in the event a catastrophe is deemed to be natural variability and not a climate change event. In such an event, maintaining a climate change reserve arguably increases insurer costs as their reinsurance could be structured to pay without regard to the level of climate change influence on the loss event. Such a scenario is not beneficial to insurers or consumers.

In recent years, competition in the reinsurance industry due to an increase in reinsurance capacity has resulted in very significant reinsurance price decreases for insurers. Competition in the private (re)insurance market for natural catastrophe risks is beneficial for insurers and, ultimately, consumers. The RAA believes it is in Hawaii's best interest to permit insurers to access the full spectrum of reinsurance options and to choose those that best fit their individual needs.

A climate change reserve will interfere with insurer risk management decisions and is not likely to have a positive impact on either pricing or availability. For a catastrophe reserve to be effective, the RAA believes it must: (a) be limited to the rare, very large events; (b) be tax deferred; and (c) be voluntary so that insurers can choose whether a catastrophe reserve or reinsurance is a better risk management tool from an individual company perspective.

The Pitfalls of State-By-State Reserves

While the proposal may not have a significant positive impact, it may have a negative impact. Through the concepts of risk spreading and diversification, insurers and reinsurers are able to more cost-effectively offer insurance products. Part of the cost effectiveness arises from the ability to support differing risks through the efficient use of the same capital base. The Act dedicates a portion of an insurer's policyholder surplus for certain types of Hawaii only risk, as defined. Particularly if other catastrophe exposed states follow suit, dedicated pockets of capital will make capital management inefficient – reducing the flexibility of companies to be able to use their policyholder surplus funds when and where they are needed to pay losses and eliminating the benefits of geographical diversification. This inefficiency may result in the need to raise capital or otherwise maintain a greater capital base. The increased capital charges associated with writing catastrophe exposed business in such an environment are likely to be counter-productive to the goal of more affordable and available insurance in catastrophe prone areas of the state. The proposed catastrophe reserve may also cause some companies to reduce their exposure to catastrophic risks, reducing the capacity for such risks - clearly not the intended outcome.

Tax Considerations

The lack of tax benefits for the reserves presents a problem. As the reserves are not tax deductible, reserves must be funded with after-tax dollars (profits) that are not available for other uses for a period of up to 10 years. Any consideration of catastrophe reserves must be dependent upon federal tax law changes or an offset to state premium or franchise taxes.

Additional Concerns from a Reinsurance Perspective

While the Act enables insurers to continue to make their own decisions regarding the amount and types of reinsurance and risk transfer they believe is beneficial to their individual circumstances, the Act requires licensed insurers and reinsurers to establish the required reserve. Since unlicensed and non-U.S. reinsurers are not required to establish the reserve, the Act may unintentionally create an unfair market advantage to this sub-set of the global reinsurance market, creating a market imbalance that could alter the cost-benefit risk evaluation analysis that reinsurance underwriters utilize in competing for Hawaii risk. Because reinsurance rates charged to Hawaii insurers are dependent upon the number of competitive reinsurers vying for such risk, if licensed reinsurers are unable to be as competitive vis a vis as unlicensed reinsurers, Hawaii insurers and consumers will be disadvantaged.

Summary

The RAA believes that the Act is likely to be ineffective as the reserve and reserve contributions are based upon risk charges that the insurance market does not currently include in their rate filings.

If the Act is applied to require reserve contributions without regard to coverage and timing considerations, the Act is likely to have significant unintended consequences. It will likely interfere with the way companies currently underwrite and price risk, and allocate capital. As a result, the Act is likely to increase market instability and it is unlikely to result in a more stable, abundant supply of affordable insurance.

Dennis C. Burke
Vice President, State Relations
Reinsurance Association of America

SIERRA CLUB OF HAWAIʻI
MĀLAMA I KA HONUA. Cherish the Earth.

SENATE COMMITTEE ON AGRICULTURE AND THE ENVIRONMENT

SENATE COMMITTEE ON WATER AND LAND

Wednesday, February 14, 2018 1:15PM Conference Room 224

In SUPPORT of SB 2327 Relating to Insurance

Aloha Chairs Gabbard and Rhoads, and members of the AEN and WAL Committees,

On behalf of our 20,000 members and supporters, the Sierra Club of Hawaiʻi, a member of the Common Good Coalition, **supports SB 2327**, establishing the global warming and erosion reserve branch within the insurance division of the Department of Commerce and Consumer Affairs, requires property insurers to set aside funds for the payment of property losses due to climate change.

This bill is important to implement key recommendations from the "Hawaiʻi Sea Level Rise Vulnerability and Adaptation Report[1]" (the Report) prepared by the Hawaiʻi Climate Change Mitigation and Adaptation Committee. This report details the slow-moving catastrophe confronting the Hawaiian Islands as temperatures rise more than 2 degrees, sea levels rise more than three feet, and the intensity of storms dramatically increase in the next 30 years.

The Report estimates more than $ 19 billion in property damage and 6,500 structure loss due to chronic flooding across the Hawaiian Islands in the next 30 years. This number applies only to structures, and does not include critical infrastructure like sewers, water mains, and utilities.

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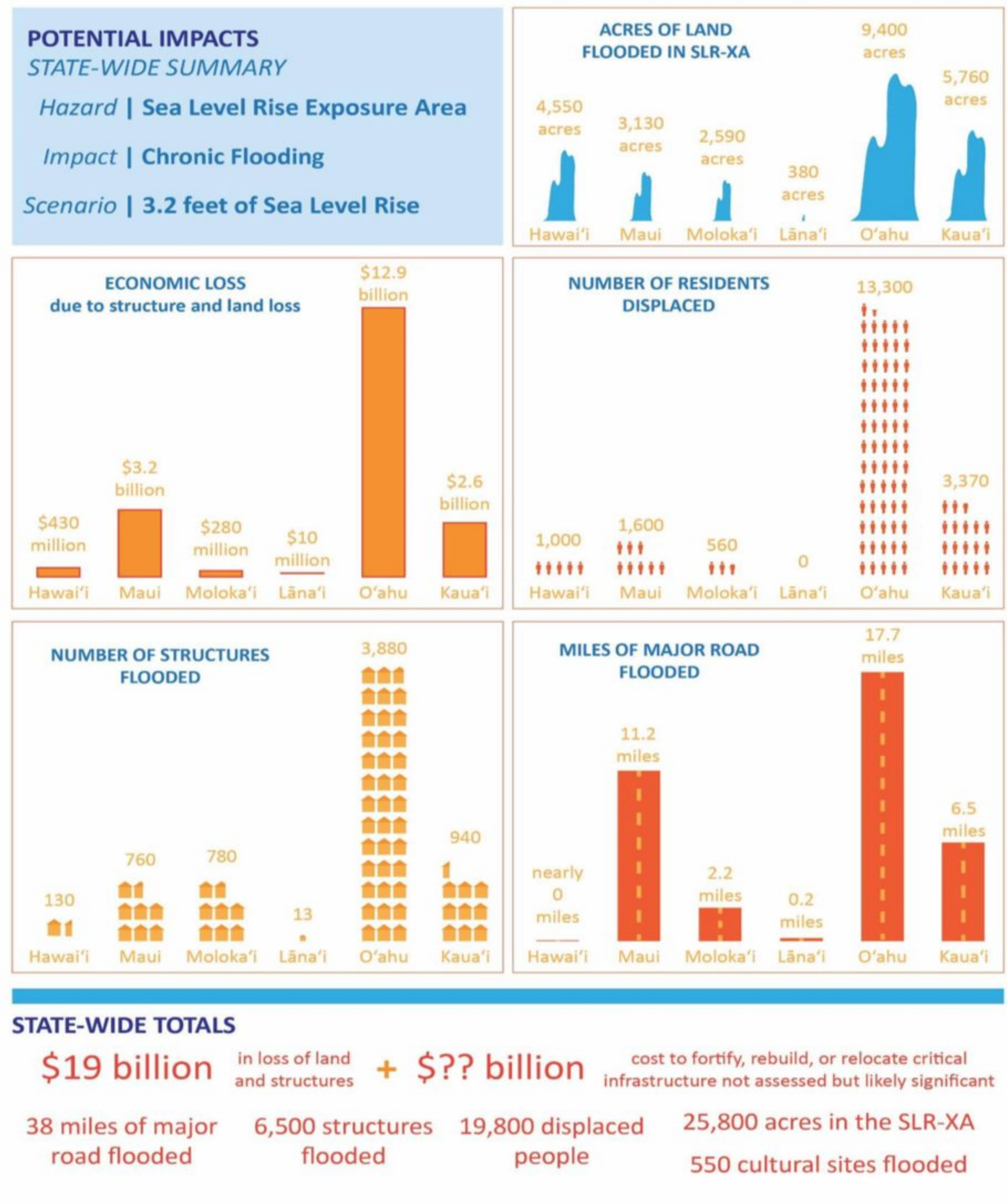
[1] https://climateadaptation.hawaii.gov/wp-content/uploads/2017/12/SLR-Report_Dec2017.pdf

P.O. Box 2577 Honolulu, Hawaiʻi • 808-538-6616 • www.sierraclubhawaii.org



Summary of potential impacts in the SLR-XA with 3.2 feet of sea level rise (chronic flooding) in Hawai'i

To minimize this loss, the Report makes specific recommendations to encourage a managed retreat from our shorelines.

Recommendation 7.2 Develop a multi-pronged financing strategy at federal, state, county, private sector, and philanthropic levels to address costs of adaptation to sea level rise

> As part of this strategy, the Hawaiʻi Legislature could adopt laws enabling state and local governments to develop tax incentive programs and special tax districts. Incentives could be used to encourage landward relocation, retrofitting to increase flood resiliency, siting of new development in upland areas, conservation of open space along the shoreline, and preservation or restoration of natural flood buffers. Although tax incentives may lack support in times of budget shortfalls, they are a proven policy tool to achieve key social, economic, and environmental objectives. Creating financial incentive programs for sea level rise and other climate change impacts, however, would require decision-makers to establish clear priorities regarding the type of development (e.g., new or existing, critical infrastructure, and residential development) to be encouraged or discouraged in particular areas.

Surprisingly, the insurance industry has been slow to adapt to the new challenges posed by climate change. Adopting this statute will help to set in motion the right financial incentives to move critical property and infrastructure away from shorelines. This is a critical step to protecting public safety and valuable property investments.

Thank you for the opportunity to testify in support of SB 2327.

SB-2327
Submitted on: 2/13/2018 12:08:41 PM
Testimony for AEN on 2/14/2018 1:15:00 PM

Submitted By	Organization	Testifier Position	Present at Hearing
Melodie Aduja	OCC Legislative Priorities	Support	No

Comments:

PRESENTATION OF THE

OAHU COUNTY COMMITTEE ON LEGISLATIVE PRIORITIES

DEMOCRATIC PARTY OF HAWAII

TO THE COMMITTEE ON AGRICULTURE AND ENVIRONMENT

AND

THE COMMITTEE ON WATER AND LAND

THE SENATE

TWENTY-NINTH LEGISLATURE

REGULAR SESSION OF 2018

Wednesday, February 14, 2018

1:15 P.m.

Hawaii State Capitol, Conference Room 224

RE: **Testimony in Support** of SB 2327, RELATING TO INSURANCE

To the Honorable Mike Gabbard, Chair; the Honorable Gil Riviere, Vice-Chair and the Members of the Committee on Agriculture and Environment

To the Honorable Karl Rhoads, Chair; the Honorable Mike Gabbard, Vice-Chair and the Members of the Committee on Water & Land:

Good afternoon. My name is Melodie Aduja. I serve as Chair of the Oahu County Committee ("OCC") Legislative Priorities Committee of the Democratic Party of

Hawaii. Thank you for the opportunity to provide written testimony on Senate Bill No.2327 relating to insurance to cover losses that result from global warming and erosion and establishes a mandatory reserve fund.

The OCC Legislative Priorities Committee is in favor of Senate Bill No.2327 and supports its passage.

Senate Bill No.2327 is in accord with the Platform of the Democratic Party of Hawai'i ("DPH"), 2016, as it establishes the global warming and erosion reserve branch within the insurance division of the department of commerce and consumer affairs. Beginning June 1, 2019, requires authorized property insurers that cover losses resulting from an environmental event, including global warming, erosion, or both, to establish a Hawaii mandatory global warming and erosion reserve, to fund the payment of claims associated with global warming and erosion in the State's shoreline areas.

The DPH Platform states that "[w]e know that climate change is a real threat to our islands and the world. We strongly urge our candidates and elected officials to take immediate action to mitigate and adapt to the consequences of climate change. This includes funding adaptation measures including coastal retreat, effective participation of indigenous peoples in climate change governance, and recognition that indigenous, local, and traditional ecological knowledge is key in climate change adaptation solutions." (Platform of the DPH, P.8, Lines 435-438 (2016)).

Given that Senate Bill No.2327 establishes the global warming and erosion reserve branch within the insurance division of the department of commerce and consumer affairs and requires authorized property insurers that cover losses resulting from an environmental event, including global warming, erosion, or both, to establish a Hawaii mandatory global warming and erosion reserve, to fund the payment of claims associated with global warming and erosion in the State's shoreline areas, it is the position of the OCC Legislative Priorities Committee to support this measure.

Thank you very much for your kind consideration.

Sincerely yours,

/s/ **Melodie Aduja**

Melodie Aduja, Chair, OCC Legislative Priorities Committee

Email: legislativeprorities@gmail.com, Tel.: (808) 258-8889

SB-2327
Submitted on: 2/10/2018 10:31:30 PM
Testimony for AEN on 2/14/2018 1:15:00 PM

Submitted By	Organization	Testifier Position	Present at Hearing
Erica Scott	Cuddle Party	Support	No

Comments: