Hurricane Deductibles: Legislative and Regulatory Restrictions Threaten Benefits for Coastal Markets

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The utilization of hurricane deductibles by property insurers has been the subject of legislative, regulatory and generally political actions that threaten their viability in enhancing the affordability and availability of insurance coverage.

Insurers operating in coastal states potentially subject to Atlantic storms have increasingly used hurricane deductibles (as well as named-storm deductibles and windstorm deductibles) in recognition of the extent of their exposure to catastrophic losses. Such deductibles are based on a percentage of a home's insured value rather than a flat dollar amount.

Widespread Use

According to the National Association of Insurance Commissioners, hurricane deductibles have been approved for use in as many as 20 states.[1] At least seven states (Connecticut, Florida, Louisiana, Maryland, New Jersey, New York, and Rhode Island) have enacted laws and/or regulations addressing insurers' use of such deductibles. Typical provisions of such measures include notice requirements and limitations on what circumstances can trigger the application of deductibles.

The applicability of hurricane deductibles was the subject of considerable attention following Hurricane/Tropical Storm Irene in 2011 and "Superstorm" Sandy in 2012. Following both storms, insurance commissioners and governors issued declarations and proclamations regarding whether insurers could apply deductibles.

An early and extreme case took place in Connecticut following Irene when Governor Dannel Malloy issued a press release stating that the administration was "working closely" with insurers and that, as a result, most companies would be waiving deductibles even if they were applicable by their terms.[2]

Storm Sandy, which was a hurricane as it churned across the Atlantic but was reclassified as something other than a hurricane by the National Weather Service, was in any event a storm of historic proportions, with total insured losses reaching some $19 billion to make it the third-most costly storm in U.S. history.[3]

Executive Branch Pronouncements

Following the storm, the governors of Connecticut,[4] New York,[5] and New Jersey[6] all issued pronouncements indicating that insurers would not be allowed to apply hurricane deductibles to Sandy-related losses. A similar bulletin[7] was issued by the Maryland Insurance Administration.

The announcements may have been technically accurate due to the storm's characteristics and classification, but they carried with them the erroneous implication that governors possess the power to make binding declarations regarding matters of insurance policy coverage. Illustrating the misconception, CNN Money published a news story with the headline "Governors say no to hurricane deductibles," with a lead sentence stating, "Homeowners in New York, New Jersey and Connecticut will save thousands of dollars in insurance costs after several state governors declared that Sandy did not make landfall as a hurricane, exempting them from insurers' hurricane deductibles."[8]

Issue Brief

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Viability Questions

The statutory and regulatory restrictions combined with the political forces that were made evident following Irene and Sandy provide grounds to question the viability of hurricane deductibles in the Northeast. This is a cause of concern because hurricane deductibles and similar percentage deductibles were introduced by the industry as a means of maintaining the affordability and availability of coverage. If they are not available in a meaningful way for insurers to use as a tool to manage risk of exposure to catastrophic losses, there could be negative consequences that affect coastal insurance markets to the detriment of insurance consumers.

In NAMIC's view, insurers' use of hurricane and other percentage deductibles should not be subject to undue legislative or regulatory restrictions. And the applicability of hurricane deductibles should be determined solely by the contractual language of the policy and not subject to political pressures following a potentially triggering event. An absence of restrictions provides optimal flexibility for insurers. However, NAMIC has also recognized that, from a public relations and political perspective, it can be seen as necessary to have consistent triggers established in legislation and/or regulation. In light of such political realities, while engaged in legislative and regulatory deliberations over hurricane deductible triggers in several states, NAMIC has not opposed legislative and regulatory proposals that meet certain criteria.

The following kinds of provisions are generally acceptable:

- Limitation of the application of deductibles to a set time period starting with the issuance of a hurricane warning for any part of a state and ending some time period (such as 72 hours) after the expiration of such warning.

- Limitation of the application of deductibles to instances in which hurricane conditions (such as sustained wind speed exceeding 74 miles per hour) exist in the state.

- Provisions that require insurers to inform policyholders about a policy's deductible(s) and provide examples to explain how they work.

The following kinds of provisions are generally problematic:

- Limiting the use of deductibles to specific regions within a state (such as specific counties).

- Restrictions that use the term "landfall." Hurricane conditions can occur regardless of whether or when a storm makes landfall.

- Overly restrictive caps (such as below 5 percent) on what percentages can be offered.

- Provisions to prevent a deductible from being applied more than once in a calendar year.

Endnotes

[1] "The Debate Over Hurricane Deductibles," NAIC Center for Insurance Policy & Research Newsletter, April, 2013, at http://www.naic.org/cipr_newsletter_archive/vol7_hurricane_deductibles.pdf.

[2] "GOV. MALLOY, INSURANCE COMMISSIONER PRAISE CARRIERS FOR WAIVING HURRICANE DEDUCTIBLES," issued Sept. 2, 2011, at http://www.governor.ct.gov/Malloy/cwp/view.asp?A=4010&Q=486154.

[3] http://www.iii.org/press_releases/over-90-percent-of-the-new-jersey-and-new-york-sandy-insurance-claims-have-been-settled-likely-to-be-third-largest-hurricane-ever-for-us-insurers.html

[4] "GOV. MALLOY ANNOUNCES INSURERS CANNOT IMPOSE HURRICANE DEDUCTIBLES IN CONNECTICUT," issued Nov. 1, 2011, at http://www.governor.ct.gov/malloy/cwp/view.asp?A=4010&Q=513366.

[5] See "Illinois Lawmakers Reject Firearm Liability Insurance Bill," March 21, 2013, at http://www.insurancejournal.com/news/midwest/2013/03/21/285431.htm.

[6] "Christie Administration Takes Action to Protect Storm-Impacted New Jersey Homeowners from Higher Insurance Deductibles," issued Nov. 2, 2012, at http://www.nj.gov/governor/news/news/552012/20121102e.html.

[7] BULLETIN 12-24, issued Oct. 30, 2012, at http://www.mdinsurance.state.md.us/sa/docs/documents/insurer/bulletins/bulletin-12-24.pdf.

[8] At http://money.cnn.com/2012/11/01/real_estate/sandy-hurricane-deductible/.