

The 'Earthquake Crisis' Is an Insurance Hoax



The court has ensured that Prop. 103 will keep companies from exploiting disasters to get unjustified rate hikes.

By HARVEY ROSENFELD

The California Supreme Court's unanimous ruling on Proposition 103 means much more to consumers than the long-delayed payment of \$1.5 billion in premium rollbacks. By upholding the insurance commissioner's authority to limit the profits and expenses of insurance companies, the decision enforces 103's provisions protecting California consumers against industry greed and abuse in the future.

Nothing better illustrates the importance of these Proposition 103 protections than the looming confrontation between consumers and insurance companies over the Northridge earthquake.

Last month, State Farm, Farmers and Allstate, which collectively control about 60% of the California market for homeowners' insurance, predicted an "insurance crisis." Unhappy that they will have to pay out about \$4 billion in claims from the January quake, the companies (whose assets total more than \$90 billion) complained, remarkably, that they never anticipated such a disaster. And, they said, they could no longer insure against future earthquakes. The carriers then made their announcement a self-fulfilling prophecy by halting or restricting the sale of new homeowners' and earthquake policies. Many current policyholders have had their coverage canceled. Dozens of other insurance companies have followed suit.

The companies' demands? They want state law to be changed to relieve them of the responsibility to offer earthquake insurance with homeowners' policies. They want legislators to establish a taxpayer or policyholder subsidized "insurance pool" that would provide earthquake coverage. Insurance companies would sell the policies at a profit but take none of the risk. And they want immediate rate increases for homeowner as well as earthquake policies.

Ten years ago, insurance companies fabricated a similar crisis, blaming what they claimed was an "explosion" in lawsuits. The companies sharply limited the availability of business, municipal and auto liability policies, which led to huge premium increases. Independent studies showed there was no surge in litigation. But California's insurance regulators—political appointees beholden to the industry—had neither the power nor the desire to restrain the industry. Legislators quickly passed laws to limit how much compensation insurers would have to pay under their liability policies, and the "crisis" abruptly ended—with skyrocketing profits for insurers.

Like the "liability crisis" of the 1980s, today's "earthquake crisis" is a hoax concocted by the industry to mask dwindling profits. When interest rates are low and the stock market is down, as they are today, the insurers' investment income declines and companies look for an excuse to raise rates in order to maintain their bloated profits. Natural disasters are the perfect foil, and insurers have no compunctions about exploiting the public's misery for private gain. On the August, 1992, morning that Hurricane Andrew hit the Florida coast with deadly force, a top executive of the world's largest insurer, American International Companies, circulated a memo to company executives that "this is an opportunity

to get price increases now . . . get it moving today." The same greed, not the Northridge temblor, motivates the industry's present actions.

Ten years ago, California consumers were powerless to protect themselves against such brazen mistreatment, but not today. It was the devastating economic impact of the last "crisis" that led voters to enact Proposition 103 in 1988.

Proposition 103 gives an elected insurance commissioner the power to alleviate shortages by forcing companies in the state to sell the coverage. And the initiative requires every insurer to open its books to prove that rate increases are justified. This will be hard to do for many companies, which made enormous profits selling homeowner and earthquake coverage for the 23 years between the 1971 Sylmar quake and this year's Northridge temblor.

Take, for example, Woodland Hills-based 20th Century Insurance Co., the hardest hit of any insurer in the state. Its practice of "cream skimming"—avoiding all but the best risks—made huge profits for its shareholders. In

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1991, the company defied the commissioner's order to roll back its rates under 103, disputing voters' right to regulate its premiums. But the company's over-concentration of lucrative San Fernando Valley customers proved to be a financial disaster after the Northridge quake.

Insurance Commissioner John Garamendi acted quickly to assist the depleted company, giving it a 17% increase in homeowners' rates in June. But now 20th Century wants its auto insurance policyholders to pay an otherwise unjustified 9.2% increase to bring the company's capital to secure levels—with no requirement that the policyholders be reimbursed, with interest, for being forced to invest in the company. An audacious proposal, considering the company reported a profit for the second quarter. Our lawyers have urged Garamendi to reject any plan that does not include full reimbursement of the policyholders, as well as payment of \$119 million in rollbacks, before shareholders begin to earn profits.

Regulatory actions, authorized by 103, also have blocked \$6 billion in rate increases since 1988. Auto-insurance premiums have dropped in California, while the rest of the nation's have risen an average of 20%. California used to have the seventh fastest-growing auto rates in the nation. Now it ranks 48th.

And the Supreme Court's decision upholding Garamendi's stringent rate controls means that future commissioners will be able to deliver similar savings.

For six years, the insurance industry spent more than \$200 million trying to block every part of Proposition 103 in the courts, hoping that the public would eventually give up. They were wrong. The Supreme Court's decision is a vindication not only of 103, but also of the people's control over democracy.

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