



April, 2009

Sent via Email to all U.S. Insurance Commissioners:

Dear Commissioners,

Demand surge refers to an increase in the cost of property repair claims following a catastrophe. It has been assumed by catastrophe modelers that higher repair costs following a catastrophe resulted from increased demand for labor and materials because of the large number of claims in a particular area.

Demand surge has been used to justify higher catastrophe loads and, consequently, higher rates for property insurance based on the premise that the cost of repair will rise after a catastrophe event due to demand surge. Demand surge has been a relatively unexamined component of catastrophe models, even though assumptions about demand surge can increase catastrophe loads in rates by 20%, 30% or more.

The attached article from the National Underwriter reports on new research on demand surge and find demand surge has little to do with rising prices for labor and materials after a large catastrophe but, rather, is related to the quality of insurance adjustments. The researchers conclude that labor and material costs did not rise after major catastrophes in the past decade, but that higher claim costs were a result of inexperienced adjusters. This research raises questions about assumptions used in computerized catastrophe models and the reasonableness of catastrophe loads in rate filings based, in part, on demand surge models.

To charge consumers for expenses due to incompetent cat claim adjusting and payouts to make up for having underinsured properties at the point of sale is wrong and should be stopped. Demand surge costs that are attributable to insurer malfeasance should be excluded from ratemaking and not allowed to be passed along to homeowner or business policyholders. In addition, to the extent that it exists, demand surge should be preventable through the action of government in partnership with insurers through the stockpiling of materials, contracting for stand-by labor and the enactment and enforcement of anti-gouging regulations. Insurers should not be provided incentives to ignore mitigation efforts by padding catastrophe models with demand surge assumptions.

This research once again highlights the importance of a few key assumptions affecting the output of computer catastrophe models and the wisdom and need for the NAIC's efforts to develop a public catastrophe model with complete transparency about these key assumptions.

Board of Directors

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We respectfully request your action to:

*In Your State: * Review property insurance rate filings to require insurers to make clear the key assumptions underlying catastrophe loads and take action to eliminate unjustified and unreasonable demand surge provisions in the rates; and;

At the NAIC: Continue support for the public catastrophe model under development at the NAIC to ensure that regulators and the public have access to catastrophe modeling with transparency of key assumptions.

Sincerely,

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