TEXAS WINDSTORM INSURANCE ASSOCIATION

Legislative & External Affairs Committee Meeting Materials

April 27, 2022

Table of Contents

Executive Summary

Report Purpose and Requirements

Texas Insurance Code Section 2210.0025 requires the Texas Windstorm Insurance Association (TWIA) Board of Directors to submit to the Commissioner of Insurance, the Senate Committee on Business and Commerce, the House Committee on Insurance, and the Sunset Advisory Commission a written report relating to the operations of the association during the preceding biennium. The report must include:

I. Any proposed changes in the law relating to regulation of the association and a statement of the reasons for the changes; and
II. Any information regarding association operations or procedures that is requested by the department to be addressed in the report.

Process and Materials

The Board of Directors has directed the Legislative and External Affairs Committee (the "Committee") to develop potential legislative recommendations for the Board's consideration.

This document presents a list and a discussion of possible items for inclusion in the Report. The list includes prior Board recommendations not adopted by the 87th Legislature, Regular Session (2020), and new concepts from Board members and Association staff.

These materials also include public policy considerations included in TWIA's 2020 Biennial Report. The public policy considerations relate to the Association's ratemaking process and funding, funding structure, and financial sustainability. This section also includes newly added alternatives, denoted by a blue box, in addition to the considerations and alternatives from the 2020 report.

The Committee will present its final recommendations to the Board for consideration at the August quarterly meeting of the TWIA Board of Directors. If the Board finalizes the Report content at the August meeting, staff will then draft the Biennial Report for submission to the Legislature with the recommendations approved by the TWIA Board of Directors, the required statement of reasons for the changes, and a summary of the Association's accomplishments and operations.

Topics for Consideration

Item	Timing	Topic	Description/Alternative
Items 1-4 are the LEA Committee's recommendations for legislative change from their most recent Biennial Report to the Legislature.			
1	2020 Prior Recommendation to the Legislature	Agent Requirements & Standards	Revise TWIA's statute to enable TWIA to mirror the Texas FAIR Plan Association (TFPA) producer requirements and performance standards.
2	2020 Prior Recommendation to the Legislature	Exclude Commercial Risks from Automatic Renewal Process	Revise TWIA's statute to exclude commercial risks from the automatic renewal process (AAG Request).
3	2020 Prior Recommendation to the Legislature	Expert Panel	Modify statute and regulations to eliminate TIC Section 2210.578 requiring the use of an Expert Panel after the Association's contract to implement the requirements ends in April 2022.
4	2020 Prior Recommendation to the Legislature	FORTIFIED Home Construction	Consider feasibility and possible public funding of FORTIFIED home construction and other mitigation programs.
Items 5-10 are new options for the Committee's consideration and were submitted by TWIA Board members.			
5	New from Board Member	Eligibility Requirements	Require agents to produce three confirmed declinations from private market carriers annually, and exclude applicants with private market coverage or offers from eligibility.
6	New from Board Member	Premium & Maintenance Tax	Exempt TWIA from premium and maintenance taxes.
7	New from Board Member	ACV Policies	Similar to some other residual market property insurers, only offer an Actual Cash Value (ACV) policy.
8	New from Board Member	ACV Policy for Older Roofs	With some exceptions, require ACV policies for properties with roofs older than ten years.
9	New from Board Member	Deductible Requirements	Require higher deductibles in certain circumstances.
10	New from Board Member	Binding Arbitration	Make binding arbitration a mandatory dispute resolution option to vacate an appraisal award and for denied TWIA claims.

Item	Timing	Topic	Description/Alternative
Items 11-17 are new options for the Committee's consideration and are based on operational issues encountered by staff where legislative change could improve Association effectiveness in terms of service or efficiency.			
11	New from Staff	Appraisal Deadlines	Set statutory deadlines for the completion of an appraisal to prevent delays in the process.
12	New from Staff	Appraisal Process	Allow TWIA to have a formal objection process related to issues or concerns with a policyholder's selected appraiser or umpire.
13	New from Staff	Split Appraisal Costs	Revise the statutory provision requiring TWIA and the policyholder to split the cost of their respective appraisers to require each party to pay their own appraisal costs.
14	New from Staff	Discounted Storm-related Advertising	Require broadcast media to provide the Association with a substantial discount to run hurricane preparedness and response information.
15	New from Staff	Earned Premium	Revise cancellation rules and procedures so Association policies may be canceled fully earned for certain reasons.
16	New from Staff	Depopulation	Authorize TWIA to activate and deactivate the Assumption Reinsurance Depopulation Program as necessary according to market fluctuations.
17	New from Staff	Board Vacancies	Repeal the provision requiring TWIA to provide TDI with a roster of recommendations to fill Board vacancies.

2020 Prior Legislative Recommendations

1 Agent Requirements & Performance Standards

Subject: Currently, TWIA does not have express authority to limit an agent's ability to transact business with the Association in the event of audit noncompliance or other inappropriate acts in connection with agents' work on behalf of their clients.

- Any Texas-licensed property insurance agent may submit applications to TWIA.[1]
- TWIA does not appoint agents, nor do they contract with TWIA.
- The Plan of Operation requires TWIA to audit agents' compliance with specific TWIA eligibility requirements. However, it does not have express authority in statute or rule to take any action in response to agent noncompliance.[2]
- In contrast, the statute governing the Texas FAIR Plan Association (TFPA) provides broad guidance for a Plan of Operation. The Plan explicitly directs TFPA to maintain producer requirements and performance standards and authorizes their enforcement.[3]

Possible Solution: Revise TWIA's statute to enable TWIA to mirror the TFPA producer requirements and performance standards.

- Provide TWIA specific authority to enact producer requirements and restrict agents' ability to submit applications to the Association when standards aren't met.
- TWIA would have clear authority to take appropriate action to limit agents' Association activities in response to audit noncompliance and other inappropriate acts or failure to act.
- Agents would continue to represent only the policyholder and would not become agents of the Association.
- Holding agents accountable to specific standards would increase agents' Association knowledge, improve operational efficiency and customer service, and help ensure policyholders' best interests are served.
- This recommendation received support from TWIA's Agent Advisory Group and would have no material fiscal impact on TWIA's operations.

2 Expert Panel

Subject: Although the Expert Panel's recommendations apply to less than 5% of Association policies, the Association has paid more than $11 million over the last five years to implement the recommendations and expects to have annual expenses of about $1.8 million for ongoing software maintenance and data analysis costs.

- Statute requires the Association to use guidelines adopted by the Insurance Commissioner based on recommendations provided by experts ("Expert Panel").
- The purpose of the recommendations is to assist the Association in determining the extent to which wind, waves, tidal surges, or rising water caused a loss to insurable property when very little of the property remains. These losses are referred to as "slab claims."[4]
- TWIA implemented the Expert Panel recommendations as adopted by the Commissioner on June 1, 2018.
- TWIA's contract with the vendors to implement the recommendations expires on April 30, 2022. However, additional annual expenses to maintain the program after the contract expires in 2022 will be approximately $1 million to $1.25 million.

TWIA Expert Panel Costs 2013-2022	
Expert Panel Members 2013 - 2018	$1,441,977
Implementation 2017-2018	$4,517,754
Maintenance 2017-2022	$8,295,812
Total Costs 2013 - 2022	**$14,255,543**

Possible Solution: Modify statute and regulations to eliminate the requirements to use the Expert Panel's recommendations and guidelines adopted by the Commissioner.

- If the Legislature would prefer TWIA to retain and use the Expert Panel's recommendations, consider transferring the costs to the Texas Department of Insurance.
- If the Legislature and TDI repealed the Expert Panel methodology, TWIA would use methods commonly used by the insurance industry to evaluate slab claims, including hiring engineers and weather experts who can help the Association assess the nature of the property damage. Alternative processes would likely create some delays in claim processing.

3 Exclude Commercial Risks from Automatic Renewal Process

Subject: Commercial policy underwriting can be complex, and it may not be in policyholders' best interest to renew commercial policies directly with TWIA through the automatic renewal process.

- TWIA implemented a new automatic renewal process in January 2020 due to legislation passed by the 86th Legislature, Regular Session.
- If there are no changes in coverage, residential and commercial policyholders can remit payment directly to TWIA and renew their policy without agent involvement.

Possible Solution: Eliminate the option for commercial risks to renew automatically.

- Due to the complexities of commercial properties and the more dynamic nature of property and coverage needs, commercial policyholder needs may be better served by a traditional, non-automatic renewal process that requires the assistance of an agent.
- TWIA's Agent Advisory Group supports this recommendation.

4 Fortified Construction

Subject: TWIA does not have any programs associated with FORTIFIED construction.

- FORTIFIED is a nationally recognized building method that goes beyond building codes to strengthen residential and commercial buildings against specific natural hazards such as high winds and hurricanes. FORTIFIED standards are based on more than 20 years of scientific research and real-world testing by the Insurance Institute for Business & Home Safety (IBHS).
- More resilient construction can improve both the availability and affordability of insurance coverage and can lead to less community damage, reduced costs of emergency management and disaster recovery resources, and lower insurance losses after a catastrophic event.
- Other coastal states, notably Alabama and North Carolina, have encouraged FORTIFIED construction for both new and existing homes through a combination of public grants and policy endorsements covering upgrades to the FORTIFIED construction standards.

Updated Possible Solution: Consider providing funding support from the State of Texas, the Catastrophe Reserve Trust Fund, or other sources for FORTIFIED home construction.

Alternatively, given recent discussions among the TWIA Actuarial & Underwriting Committee and the TWIA Board of Directors, consider expanding the scope of this recommendation to include TWIA incentives or public funding support for all types of wind mitigation efforts, such as retrofitting existing construction with upgraded opening protections, roof attachments, and other certified improvements. In the absence of a request for public funding, implementing this possible solution would not require a legislative change.

Appendix A includes the relevant statutory language related to the following citations:

[1] Texas Insurance Code (TIC) Section 2210.202 (b)

[2] Texas Administrative Code (TAC), Chapter 28 Section 5.4902 (d)

[3] TIC Section 2211.054, the contents of TFPA's Plan of Operation, and 28 TAC 5.9913 (d).

[4] TIC Section 2210.578

New from Board Members

5 Stricter Eligibility Requirements

Subject: TWIA's declination requirement may be insufficient to encourage policyholders to explore other wind and hail coverage options in the private insurance market.

Possible Solution: Adopt eligibility requirements similar to the Texas FAIR Plan Association (TFPA).

Discussion
Adopting stricter eligibility requirements ensures that TWIA continues to operate as the insurer of last resort and not as an inadvertent competitor in the private market, contrary to its statutory mandate. Possible changes to TWIA's declination requirements include:

- Change the number of required declinations of coverage from one to three insurance companies.
- Deem ineligible for TWIA coverage those applicants who have a current homeowners or other residential property policy that covers wind and hail, a renewal offer, or a valid offer of comparable residential wind and hail property insurance.
- A policyholder must reapply for coverage in the voluntary market every year.

For reference, the following sections list TWIA and TFPA's current eligibility requirements related to declinations:

TWIA's Current Requirements
- Applicants must have been denied coverage by at least one authorized insurer writing or renewing windstorm and hail coverage in the designated area.
- Evidence of one declination is required every two years to renew an Association policy.

TFPA's Current Requirements
- Applicants must have been denied coverage by at least two insurance companies licensed to write and actually writing residential property insurance in Texas.
- Applicants are not eligible for coverage if the applicant has a current homeowners or other residential property policy, has a renewal offer, or has received a valid offer of comparable residential property insurance from an insurance company licensed in Texas.
- A policyholder must reapply for coverage in the voluntary market every two years.

Statutory and Rule References
Texas Insurance Code Section 2210.202, 2211.151, 28 TAC 5.9917

6 Premium & Maintenance Tax

Subject: Texas premium and maintenance taxes impact rate indications and lessen the affordability of TWIA policies.

Possible Solution: Exempt TWIA from paying premium and maintenance taxes.

Discussion

TWIA has spent $7-8 million in premium and maintenance taxes annually for the past five years. Before 2017, when policy counts and, therefore, written premiums were higher, TWIA incurred more than $9 million in some years. Appendix B includes the premium and maintenance tax TWIA has paid between 2010 and 2022.

A reduction in expenses has a corresponding impact on rate indications. Elimination of premium and maintenance taxes would reduce TWIA expenses by roughly 1.86% of the annual written premium.

7 Actual Cash Value (ACV) Policies

Subject: Minimize exposures and avoid inadvertent competition with the private market.

Possible Solution: Amend the statute to eliminate the insurance-to-value requirement for replacement cost coverage and only offer an ACV policy, similar to some beach and FAIR Plans.

Discussion

In many cases, residual market carriers are not designed to offer the most comprehensive coverage on the market. To this end, some other residual market property insurers do not provide replacement cost coverage. Eliminating replacement cost coverage would likely reduce annual premium costs for policyholders and encourage policyholders to explore other options for wind and hail coverage in the private insurance market, reinforcing TWIA’s role as an insurer of last resort and avoiding competition with the private market.

8 ACV Policy for Older Roofs

Subject: Minimize exposures and avoid inadvertent competition with the private market.

Possible Solution: With some exceptions, require ACV policies for properties with roofs older than ten years.

Discussion
With some exceptions, such as metal roofs, older roofs can be more susceptible to wind-driven rain and direct physical damage, causing more interior damage.

In many cases, residual market carriers are not designed to offer the most comprehensive coverage on the market. Requiring an ACV policy on the home if the roof is older than ten years would minimize coverage levels keeping them in line with the original intent and purpose of a residual market carrier. Further, it would encourage policyholders to explore other wind and hail coverage options in the private insurance market. For those policyholders who must remain with TWIA, it would encourage policyholders to take an active role in the ongoing maintenance of the property. It would also allow TWIA to avoid offering products that unintentionally compete with the private market.

9 Deductible Requirements

Subject: Encourage policyholders to take an active role in both the long-term maintenance of the insured property and proactive participation in the claims process.

Possible Solution: Require higher deductibles in certain circumstances.

Discussion
Some plans only offer percentage deductibles, e.g., 1%, 2%, 5%, and 10%. This recommendation would require a 5% or higher deductible in some instances, such as when ACV roof endorsements are applied. This solution could potentially lower premium costs for policyholders who may not realize that higher deductibles typically result in lower premiums. Greater financial participation at claim time incentivizes policyholders to keep maintenance up to date and to play a proactive role in helping TWIA assist the policyholder in documenting their loss.

10 Binding Arbitration

Subject: Further reduce expenses associated with claim disputes.

Possible Solution: To further reduce the costs associated with TWIA claim disputes, make binding arbitration a mandatory method for policyholders to vacate an appraisal award and dispute the denial of their claim.

Discussion
Legislative and operational reforms established after Hurricane Ike have significantly reduced TWIA's litigation ratio, associated expenses, and overall claim dispute ratio. However, implementing a binding

arbitration process under certain conditions could further reduce expenses associated with TWIA claim disputes.

The existing statute allows policyholders to purchase a binding arbitration endorsement voluntarily for an actuarially justified premium discount. There are currently no TDI rules related to the binding arbitration endorsement or process, which is a prerequisite for TWIA to offer it as a claim dispute option.

This possible solution contemplates mandatory binding arbitration for all claims that have been denied in whole or in part and for disputes over appraisal awards. By making binding arbitration mandatory for disputing a TWIA claim or appraisal, Association expenses and lawsuits may be reduced.

Statutory and Rule References
Texas Insurance Code 2210.554
Texas Insurance Code 2210.363 (a)(2) and (b)

New Topics from Staff

11 Appraisal Deadlines

Subject: Current statutes and rules define deadlines for beginning the appraisal process, for a policyholder to demand appraisal after receiving TWIA's Notice of Claim Acceptance, and for informing the other party of the fees to be charged when hiring an appraiser. However, there are no deadlines for completing an appraisal.

Possible Solution: Set statutory deadlines to complete an appraisal to prevent delays in the process.

Discussion
In the Association's experience following Hurricane Harvey, several factors led to appraisers and appointed umpires causing unnecessary delays. The average duration of an appraisal for a residential claim was nearly 200 days, while appraisals for commercial claims took up to 40% longer or 277 days on average.[1]

Policy Type	Number of Appraisals	Average Duration (in days)
Commercial	109	277
Residential	748	199
Total	**857**	**209**

Incentives to complete an appraisal timely and/or requiring the parties involved to agree to extend the duration of an appraisal will benefit both policyholders and the Association and lead to a timelier resolution of disputes. As there are variations in the size and complexity of losses, applying deadlines to the appraisal process should be flexible to allow for an adequate investigation of the claim and preserve the independence of the appraisers involved.

Statutory and Rule References
Texas Insurance Code Section 2210.574
Texas Administrative Code Chapter 28 Section 5.4211

[1] Based on a preliminary analysis of a sample of 857 appraisals for Hurricane Harvey claims (2017).

12 Appraisal Process

Subject: TDI rule requires appraisers to disclose potential conflicts of interest when appointed, but it does not disqualify appraisers with conflicts of interest from engaging in an appraisal. Additionally, there are no methods by which an appraiser can be challenged or disqualified before the appraisal's completion.

Possible Solution: Allow TWIA to have a formal objection process related to issues or concerns with a policyholder's selected appraiser or umpire.

Discussion
The appraisal process is based partly on the appointed appraisers' independence and disinterest. TDI rule requires appraisers to disclose potential conflicts of interest when appointed. Many potential conflicts in the rule focus on the appraiser's financial motivations to minimize or maximize the claim's value regardless of its merits. However, none of the potential conflicts outlined in the TDI rule disqualifies the appraiser from engaging in an appraisal. As a result, policyholder appraisers appointed to Hurricane Harvey claims rarely followed the disclosure rules, and even when potential conflicts existed, they continued to engage in the appraisal process. For example, several Public Adjusters and repair contractors routinely appointed themselves or their employees as the appraiser for their clients, despite having a financial interest in the outcome of the claim.

Moreover, an appraiser cannot be challenged or disqualified before the appraisal's completion. Instead, the parties can only raise an appraiser's misconduct by filing a suit to set aside the award and begin a new appraisal.

TWIA proposes adding an objection process to the current rules governing appraisal to balance the need to remove those who participate in the process in bad faith with the imperative of keeping the appraisal process streamlined and inexpensive for the policyholder. The Association proposes referring objections to the TDI Ombudsman, and to the extent this would add additional expense to the Ombudsman's budget, TWIA would bear that expense.

Statutory and Rule References
Texas Administrative Code Chapter 28 Section 5.4212

13 Payment of Appraisal Costs

Subject: Statute requires TWIA and the policyholder to split appraisal costs. But, the overall cost of an appraisal can be imbalanced, with the policyholder paying a higher share than they would if they were only responsible for the costs of their appraiser.

Possible Solution: Revise the statute to require each party to pay for their appraiser instead of splitting the total cost of both appraisers.

Discussion

The appraisal process for handling TWIA claims is established in Texas Insurance Code and states, "*the claimant and the association are responsible in equal shares for paying any costs incurred or charged in connection with the appraisal, including a fee charged under Subsection (e).*"

The appraisers TWIA hires charge an hourly rate for their service. As the appraisal process is designed to be separate and independent from TWIA's claim handling, TWIA provides little direction and oversight of appraisers. TWIA often experiences situations in which the amount of work that a TWIA appraiser performs on a file exceeds the amount of work performed by the policyholder's appraiser. The TWIA appraiser may also charge a higher rate than the rate charged by the policyholder's appraiser. The result of these scenarios is that the cost of TWIA's appraiser is often higher than the cost of the policyholder's appraiser, sometimes substantially so.

In Hurricane Harvey appraisals on residential claims, TWIA's appraisal expense averaged about $500 higher than the policyholder's. If the appraisal award is a nominal amount, payment of the fees may significantly reduce the policyholder's final payment. This difference in costs can also cause disputes with the policyholder and may be detrimental to TWIA's efforts to settle a claim. Allowing TWIA and the policyholder to pay their own appraisal costs may eliminate the negative issues incurred in the appraisal process.

Statutory and Rule References

Texas Insurance Code Section 2210.574 (d)(2)

28 Texas Administrative Code Section 5.4221

14 Discounted Storm-related Advertising

Subject: Some forms of advertising, such as television and radio spots, can be cost-prohibitive for the Association to use effectively after a storm. It is in the best interest of policyholders after a catastrophe for the Association to be able to reach as many people in impacted areas as possible.

Possible Solution: Require broadcast media to provide the Association with a substantial discount to run hurricane preparedness and response information.

Discussion
Staff has a preliminary understanding that some disaster response agencies in Florida may have legislative provisions that require advertising entities to provide airtime at a substantial discount for storm-related television and radio spots.

The high costs associated with running storm-related TV and radio ads after a catastrophic event has been a barrier to using this form of advertising to reach policyholders after a storm. The average rate for a 15 second TV spot in the Houston area can range from $125 to $2,440 during primetime hours. It would cost TWIA nearly $300,000 to run ads for 30 days on one station.[2] To effectively reach as many policyholders in impacted areas, we would ideally want to run ads on multiple TV and radio stations for 2-4 weeks at different points during the claim handling process.

Legislation requiring media outlets to grant substantial discounts to TWIA for disaster preparedness and response messaging would help ensure policyholders receive crucial claim filing and recovery information when they need it most.

15 Earned Premium

Subject: TWIA does not have a mechanism to discourage policyholders from obtaining a policy at the start of storm season and then canceling the policy in December and receiving a pro-rata refund amount.

Possible Solution: Revise cancellation rules and procedures so the Association may cancel policies on a pro-rata basis for the following reasons only:

- Coverage is replaced by another company (Evidence must be provided)
- The property is sold (Evidence must be provided)
- There is a total loss of the property (Evidence must be provided)
- TWIA determines that the property is no longer insurable under TWIA rules and procedures

Discussion
Seasonal cancellations create additional operating expenses for the Association and reduce the income available for paying claims or contributing to the Catastrophe Reserve Trust Fund.

The Mississippi Windstorm Underwriting Association's Plan of Operations includes similar cancellation provisions. TWIA currently uses a 90-day minimum earned premium (MEP) to prevent short-term issuance and cancellation of policies. The Legislature reduced the MEP from 180 days to 90 in 2011.

[2] Based on rates for nine available hourly segments.

Cancellation for any reason other than the above reasons would result in a fully earned, non-refundable premium to TWIA.

16 Depopulation

Subject: Participation in the Assumption Reinsurance Depopulation Program ("Assumption Program") has dramatically declined over the past five years. Regardless of the volume from year to year, TWIA must perform the same complex steps.

Possible Solution: Authorize TWIA to activate and deactivate the Assumption Reinsurance Depopulation Program as necessary according to market fluctuations.

Discussion

Senate Bill 900 (84th Legislature, Regular Session) authorized the Assumption Program in 2015. The law seeks to provide TWIA policyholders with alternative wind and hail insurance options in the private market. The program functions in the following manner: TWIA provides policy data to participating companies, who then make offers to assume, or transfer, TWIA policies. The participation of insurers, agents, and policyholders in the program is entirely voluntary.

Assumption Reinsurance Depopulation Program Participation					
Program Year	**2016-2017**	**2017-2018**	**2018-2019**	**2019-2020**	**2021-2022**
Participating Carriers	4	3	2	2	1
Policies Selected by Carriers	102,171	109,356	75,039	64,380	32,318
Agent-Approved Offers	18,047	3,091	3,967	1,866	210
Policies Assumed	11,164	1,634	2,080	1,002	125

The Sunset Commission staff detailed the complexity and inefficacy of the Assumption Program in their 2018-2019 report. That report explains in more depth the following findings:

1. The Assumption Reinsurance Depopulation Program is administratively complex, creating unnecessary confusion.
    a. Policyholder confusion delays claim payments.
    b. The complexity of the program requires logistical and financial gymnastics.
2. The industry's interest in the Assumption Reinsurance Depopulation Program is limited and the benefits to policyholders are questionable.
3. Insurance agent interest in and ability to participate in the Assumption Reinsurance Depopulation Program is limited.
    a. Insurance agents have expressed concerns about the program's viability.

b. Many insurance agents contractually cannot sell depopulation policies.

While Sunset staff recommended that the Sunset Commission eliminate the Assumption Program, the Commission elected to modify certain logistical elements of the program's timeline to make it less complex.

Statutory and Rule References
Texas Insurance Code Subchapter O (2210.701 - 2210.705)

17 Board Vacancies

Subject: The Association has been unable to compile the slate of nominees required by statute to fill an insurance industry representative vacancy on the board of directors.

Possible Solution: Repeal the provision requiring the Association to provide a slate of nominees to the commissioner to fill a vacancy on the Board of Directors that is reserved for an insurance industry representative.

Discussion
The TWIA Board of Directors includes three members who are representatives of the insurance industry. When one of those positions becomes vacant, TWIA's governing statute establishes a process for filling the vacancy. The process requires the Association to solicit nominations from member insurers and to provide a slate of nominees to TDI for the commissioner's consideration. The slate of nominees submitted to the commissioner must include at least three more nominees than the number of vacancies. The commissioner may, but is not required to, appoint an industry representative from the slate of nominees.

TDI routinely requests a slate of nominees when the term of an industry representative is expiring. The association sends a solicitation to all members companies requesting nominees, as required by statute. The Association has not received the required number of nominees to meet the statutory requirement in the past four years, (2019, 2020, 2021, and 2022). In each of those years, TWIA sent multiple solicitations and/or staff contacted companies to request candidates.

Because the member insurers have routinely not provided a sufficient number of nominees to provide a slate as required by the statute and because the commissioner is not required to appoint a nominee from the slate requested from the Association, elimination of the requirement to provide a slate of nominees would not be detrimental to the process of appointing industry representative to the Board of Directors.

Statutory Reference
Texas Insurance Code Section 2210.102 (f)

Public Policy Considerations

In the 2020 Biennial Report, the TWIA Board of Directors, at the recommendation of the Legislative & External Affairs Committee, elected to present the issues of Association rates and ratemaking and the funding, funding structure, and financial sustainability of the Association as matters of public policy.

While the Board identified several areas of improvement related to the Association's ratemaking and funding, they agreed addressing the issues is most appropriately undertaken by the Texas Legislature.

The 87th Texas Legislature (2021) passed some reforms impacting the Association's ratemaking process and the process to secure the Association's annual catastrophe funding. However, the COVID-19 pandemic ultimately delayed interim studies of the Association's funding by the Windstorm Funding and Funding Structure Legislative Oversight Board and a potential merger of TWIA and the Texas FAIR Plan Association by the Windstorm Insurance Legislative Oversight Board. Created by House Bill 1900[3], the interim studies had been due to the 87th Texas Legislature prior to the start of the 2021 session. Senate Bill 1448[4], consolidated both studies under the Windstorm Insurance Legislative Oversight Board and extended the due dates of the studies.[5]

The information the Board included in the 2020 Biennial Report about the Association's ratemaking and funding is included on the following pages. The first section contains information regarding the challenges of the existing ratemaking process and several options the Legislature might consider to address those challenges. The second section details challenges with the existing funding structure and a list of possible alternatives for the Legislature as well as information on the Association's funding methodology and history. Staff has also added a small number of new options and alternatives related to the Association's ratemaking process and funding for the Legislative & External Affairs Committee's consideration.

Action Needed: Determine whether to use the same approach in presenting rate and funding issues and alternatives as was taken in the 2020 Biennial Report.

[3] 86th Texas Legislature, Regular Session
[4] 87th Texas Legislature, Regular Session
[5] The statute related to the Windstorm Funding and Funding Legislative Structure Oversight Board has expired. The interim studies by the Windstorm Insurance Legislative Oversight Board are due prior to the 88th legislative session.

TWIA Ratemaking

Issue: The current ratemaking process makes it difficult to meet the statutory requirements that "rates must be reasonable, adequate, not unfairly discriminatory, and nonconfiscatory as to any class of insurer" while balancing stakeholder concerns regarding affordability of Association premiums.

- The 2021 TWIA rate adequacy analysis indicated that its residential and commercial rates were 39% and 46% below adequacy, respectively.
- Inadequate rates may jeopardize TWIA's ability to issue public securities to fund catastrophic losses, or repay the debt once issued.
- The Association's annual, statutorily required rate filing process has come under considerable public and political pressure since Hurricane Harvey. The 5% rate increase effective January 1, 2022 is the first rate increase implemented since 2018.
- Recently passed legislation now prohibits the TWIA Board of Directors from voting on a proposed rate increase if there has been a vacancy on the board for at least sixty days and all rate increases now require approval of two-thirds of the board to be filed.

Proposed Change: Review the TWIA ratemaking process and modify the statute as necessary to address these concerns. Some alternatives to the current process identified by TWIA include:

- Requiring that rate inadequacy be addressed through a "glidepath" approach consisting of a series of smaller rate increases over time;
- Holding an administrative hearing before an Administrative Law Judge who would submit a rate change proposal to the Commissioner of Insurance;
- Creating a separate rating bureau or similar entity to assess TWIA's rate adequacy and propose or implement rate changes;
- Modifying statutory ratemaking standards and requirements to address concerns about policy affordability; and/or
- Addressing concerns about actuarial fairness by specifically authorizing the Association to implement territorial rating.

Additional information on possible implementation of these alternatives is presented below.

Historical information on how TWIA has approached the process of rate filings over time is included in Appendix C.

Glidepath Approach:

- This approach would involve smaller incremental annual rate increases intended to move toward rate adequacy while avoiding larger sudden rate increases. Since there are a number of variables impacting rate adequacy, including storm frequency and severity, inflation impacts, etc., the glidepath approach may not close the gap depending upon the nature of these and would require an annual evaluation by the Board.

Administrative Hearing:

- Another approach to consider is requiring a hearing through the State Office of Administrative Hearings (SOAH) to set rates. The hearing would be before an Administrative Law Judge (ALJ) who would submit a rate change proposal to the Commissioner.
- SOAH hearings are currently used when certain TWIA actions are appealed by policyholders and/or member insurers.
- Interested parties would be allowed to provide written and oral comments, as well as empirical evidence, at the ALJ hearing. TWIA would provide data, which would include staff's rate adequacy analysis, to the ALJ for consideration.
- The statute should include a timeline for required actions. The Commissioner's Order setting the rates would be based on acceptance or modification of the ALJ's proposal.
- There is likely a fiscal note to the State with this approach.

Rating Bureau:

- A third possible change to the current process would be to create an independent rating bureau or other entity, similar to what some other states have established.
- The bureau would analyze rate need and set rates for the Association independently.
- This would limit TWIA's role to providing statistical data such as catastrophe modeling results and loss and expense information.

As an example, the North Carolina Rating Bureau sets rates for several types of insurance in North Carolina, including property, auto, and workers compensation. Texas could implement a similar model specifically focused on TWIA rates.

The NCRB enabling statute can be found at:
https://www.ncleg.net/enactedlegislation/statutes/pdf/byarticle/chapter_58/article_36.pdf.

It provides a methodology for ratemaking; requirements for filing proposed rates with the Department of Insurance; and a process for Department approval or disapproval, including public inspection, comment, and hearing.

Affordability:

- The current statutory requirements for Association rates are that "rates must be reasonable, adequate, not unfairly discriminatory, and nonconfiscatory as to any class of insurer." There is no language in statute specifically addressing affordability, even though this is a key issue for many coastal stakeholders.
- One way to address this issue would be to include statutory guidance as to how to define and address affordability as it relates to Association rates.

Territorial Rating:

- Actuarial analysis indicates that rates for Association policies could vary materially geographically, with some areas potentially seeing rate decreases.
- In order to promote fairness among TWIA policyholders, a possible change to current statute would be to revise Texas Insurance Code section 2210.355(i) to make clear that TWIA continues to have the authority to implement rating territories.

Funding

The following information outlines challenges with the existing funding structure and a list of possible alternatives to the Legislature. A new possible alternative related to the depletion of the CRTF post-event and increased insurance costs is highlighted on page 27.

Additionally, Appendix D includes an overview of the funding structure and its individual components as well as stakeholder suggestions for funding changes.

Issue: Current statute provides funding for TWIA losses and expenses in excess of its premium and other revenue up to a set amount and includes the requirement that TWIA secure funding for a catastrophe year with a probability of one in 100 through the purchase of reinsurance with an attachment point in excess of all statutory funding sources. The Association has identified several challenges associated with the current funding structure:

- **Public securities may not be fully marketable or funded sufficiently quickly.**
    1. Proceeds issued after a catastrophic event may not be available for up to six months after a catastrophic event, potentially delaying claim payments.
    2. Not all proceeds are available to pay claims due to reserve accounts required by bond investors.
    3. Securities may not be able to be issued in their full, authorized amount due to general financial market conditions or the uncertain financial condition of TWIA and the economic conditions on the Texas coast following a major hurricane.
- **The current structure imposes a financial burden on TWIA and its current and future policyholders in the years following a catastrophic event.**
    1. A depleted CRTF would require TWIA to purchase more reinsurance to meet the minimum funding requirement, increasing costs after an event.
    2. Reinsurance itself will most likely be more expensive after an event.
    3. TWIA policyholders may not be able to afford policy surcharges that may be required to repay multiple Class 1 issuances.
- **There is no statutory provision for funding in excess of the 100-year minimum funding level (plus any additional reinsurance funded through member company assessments).**

Proposed Change: Modifications to improve the Association's funding, funding structure, and financial sustainability are matters of public policy to be undertaken by the Legislature in coordination with the

Legislative Funding and Funding Structure Oversight Board (LOB) created by House Bill 1900 (86th Legislature, Regular Session). The LOB is tasked with completing a study of the Association's current funding and funding structure and developing recommended changes for consideration by the full Legislature.

TWIA has included additional information on the challenges noted above and possible alternatives for consideration, individually or in combination, below.

Public securities may not be fully marketable or funded quickly enough

Challenge 1: Proceeds issued after a catastrophic event may not be available for up to six months after a catastrophic event, potentially delaying claim payments.

Most sources of funding are available to pay claims within days or weeks after a catastrophic event. Post-event public securities, however, may take up to six months after an event to become available to pay claims, due to the lengthy process of issuing this type of debt. At up to $1 billion, this represents a significant portion of TWIA's overall funding.

TWIA has addressed this concern by purchasing a line of credit, which allows TWIA to borrow against public security proceeds during the issuance process. The line of credit has become increasingly expensive and this quick source of cash to pay claims may not be reliable in the long-term.

Possible Alternatives:

- Allow TWIA to collect from its policyholders a CRTF surcharge separate from premiums to fund the CRTF directly.
- Authorize a statewide policy surcharge to build the CRTF to a minimum level.

Building the CRTF balance reduces the likelihood that public securities will be necessary to fund claims and allows TWIA to deposit more of its premiums in the CRTF due to reduced reinsurance costs.

- Reorder TWIA funding to place post-event securities "higher up".
- Provide a temporary source of funds that could be used to pay claims until proceeds from public securities become available.

Challenge 2: Not all proceeds are available to pay claims due to reserve accounts required by bond investors.

A portion of the proceeds from public securities is not available to pay claims. Investors require various reserve accounts to ensure the Association's ability to repay the debt, and these accounts must be funded directly from bond proceeds. Reserve amounts and issuance costs both reduce the total amount available to pay claims, resulting in a potential funding shortfall.

Possible Alternatives:

- Provide additional funding from assessments or other sources to fund any difference between the $1 billion of authorized public security issuances and the actual amounts available to pay claims.
- Authorize issuance of public securities in amounts over $1 billion such that the net amount available to pay claims is $1 billion.
- Allow flexibility in the attachment point of reinsurance to address the potential gap created by issuance costs and/or debt reserve amounts.

Challenge 3: Public securities may not be able to be issued in their full, authorized amount due to TWIA's financial condition or general financial market conditions.

In general, the issuance of debt is subject to the availability of capital in the financial markets and the creditworthiness of the borrower. For TWIA specifically, this means that general market conditions may restrict the amount of public securities that can be issued as part of the Association's funding. Being authorized in statute to issue up to $1 billion in public securities does not guarantee that the financial market will be willing to provide those funds.

In addition to general market conditions, the perceived ability of TWIA to repay any debt is a significant factor in both the amount of debt that can be obtained and the cost of that debt, in terms of the interest rate charged. Existing debt service obligations from previous catastrophe years, the collectability of TWIA and coastal policyholder surcharges, and the uncertainty of future legislative or regulatory changes are all concerns that have previously been raised by investors. These concerns impact the interest rates charged to TWIA and could possibly limit the amount of public securities that could be issued.

Possible Alternatives:

- Allow for the issuance of public securities guaranteed by the State of Texas.
- Allow for the issuance of public securities on a tax-exempt basis for investors.
- Allow TWIA to account for the balance in the CRTF as surplus.

Each of these would increase the marketability, and potentially reduce the cost, of public securities.

- Provide additional funding from assessments or other sources to fund any difference between the $1 billion of public securities authorized and the actual amounts issued.

TEXAS WINDSTORM INSURANCE ASSOCIATION

Financial burden on TWIA and its policyholders following a catastrophic event

Challenge 1: A depleted CRTF requires TWIA to purchase more reinsurance to meet the minimum funding requirement, increasing costs after an event.

Hurricane Harvey resulted in an ultimate loss estimate of $1.71 billion, which completely depleted the $737 million in the CRTF. Current statute requires the Association to exhaust the CRTF before using any other funding sources.

As the Association must provide for funding to a 1-in-100-year event each year, a smaller amount in the CRTF requires TWIA to purchase additional reinsurance to meet the minimum funding requirement. Reinsurance also attaches at a lower level because of the diminished CRTF, making the cost of reinsurance more expensive.

Possible Alternatives:

- Allow TWIA to charge its policyholders a CRTF surcharge separate from premiums.
- Authorize a statewide policy surcharge to build the CRTF to a minimum level.
- Allow flexibility in the minimum required funding level after a catastrophic event to reduce the amount of reinsurance required to be purchased.
- Establish a public reinsurance facility for TWIA and the private market similar to the Florida Hurricane Catastrophe Fund.

Challenge 2: Reinsurance itself will most likely be more expensive after an event.

In years following a significant storm, the Association can also expect the price of reinsurance to be higher than normal due to a reaction from the market, further straining available premium revenue.

Possible Alternatives: Each of the alternatives above also addresses this challenge.

Challenge 3: TWIA policyholders may not be able to support repayment of multiple Class 1 issuances.

Hurricane Harvey also required TWIA to use the amounts available from the $500 million in pre-event public securities issued in 2014. TWIA's premiums earned in subsequent years must be shared among paying the principal and interest on the outstanding bonds, Association operating expenses (including payment of routine non-catastrophe claims), and reinsurance costs. This leaves little left over for deposit into the CRTF.

Another catastrophe year requiring the issuance of Class 1 public securities could require TWIA policyholder surcharges of over 20% to repay the additional bonds.

Possible Alternatives:

- In addition to the alternatives above, allow a contingent source of funding for Class 1 public securities similar to existing sources for Class 2 and Class 3 public securities.
- Provide a cumulative maximum amount of public securities to be repaid by TWIA premiums and policyholder surcharges at any one time.

Revise the existing bond repayment surcharge on TWIA policies to apply at renewal, rather than during the policy term.

Appendix A: Statutory References

[1]Texas Insurance Code (TIC) Section 2210.202 (b)

Sec. 2210.202. APPLICATION FOR COVERAGE; DECLINATION REQUIREMENT. (a) A person who has an insurable interest in insurable property may apply to the association for insurance coverage provided under the plan of operation and an inspection of the property, subject to any rules established by the board of directors and approved by the commissioner. The association shall make insurance available to each applicant in the catastrophe area whose property is insurable property but who, after diligent efforts, is unable to obtain property insurance through the voluntary market, as evidenced by one declination from an insurer authorized to engage in the business of, and writing, property insurance providing windstorm and hail coverage in the first tier coastal counties. For purposes of this section, "declination" has the meaning assigned by the plan of operation and shall include a refusal to offer coverage for the perils of windstorm and hail and the inability to obtain substantially equivalent insurance coverage for the perils of windstorm and hail. Notwithstanding Section 2210.203(c), evidence of one declination every three calendar years is required before renewal of an association policy.

(b) A property and casualty agent must submit an application for initial insurance coverage on behalf of the applicant on forms prescribed by the association. An application for initial coverage must contain:

> (1) a statement as to whether the applicant has submitted or will submit the required premium payment from personal funds or, if not, to whom a balance is or will be due; and
>
> (2) a statement that the agent acting on behalf of the applicant possesses proof of the declination described by Subsection (a) and proof of flood insurance coverage or unavailability of that coverage as described by Section 2210.203(a-1).

[2]Texas Administrative Code (TAC), Chapter 28 Section 5.4902 (d)

TITLE 28	INSURANCE
PART 1	TEXAS DEPARTMENT OF INSURANCE
CHAPTER 5	PROPERTY AND CASUALTY INSURANCE
SUBCHAPTER E	TEXAS WINDSTORM INSURANCE ASSOCIATION
DIVISION 10	ELIGIBILITY AND FORMS
RULE §5.4902	Additional Requirements

(d) The Association shall implement an agent audit procedure to verify that agents possess and maintain proof of the declination and flood insurance as required under §5.4903 of this division and, if applicable, §5.4904 of this division.

[3]TIC Section 2211.054, the contents of TFPA's Plan of Operation, and 28 TAC 5.9913 (d).

Sec. 2211.054. CONTENTS OF PLAN OF OPERATION. The plan of operation must:

(1) provide for a nonprofit association to issue residential property insurance under this chapter and distribute the losses and expenses in writing that insurance in this state;

(2) provide that all insurers that write residential property insurance shall participate in the association in accordance with Sections 2211.101(b) and (c);

(3) provide that a participating insurer is entitled to receive credit in accordance with Section 2211.101(d);

(4) provide for the immediate binding of eligible risks;

(5) provide for the use of premium installment payment plans, adequate marketing, and service facilities;

(6) provide for the establishment of reasonable service standards;

(7) provide procedures for efficient, economical, fair, and nondiscriminatory administration of the association;

(8) provide procedures for determining the net level of participation required for each insurer in the association;

(9) provide for the use of deductibles and other underwriting devices;

(10) provide for assessment of all members in amounts sufficient to operate the association;

(11) establish maximum limits of liability to be placed through the program;

(12) establish commissions to be paid to the insurance agents submitting applications;

(13) provide that the association issue policies in the association's own name;

(14) provide reasonable underwriting standards for determining insurability of a risk;

(15) provide procedures for the association to assume and cede reinsurance; and

(16) provide any other procedure or operational matter the governing committee or the commissioner considers necessary.

[4]TIC Section 2210.578

Sec. 2210.578. EXPERT PANEL. (a) The commissioner shall appoint a panel of experts to advise the association concerning the extent to which a loss to insurable property was incurred as a result of wind, waves, tidal surges, or rising waters not caused by waves or surges. The panel shall consist of a number of experts to be decided by the commissioner. The commissioner shall appoint one member of the panel to serve as the presiding officer of the panel.

(b) Members of the panel must have professional expertise in, and be knowledgeable concerning, the geography and meteorology of the Texas seacoast territory, as well as the scientific basis for determining the extent to which damage to property is caused by wind, waves, tidal surges, or rising waters not caused by waves or surges.

(c) The panel shall meet at the request of the commissioner or the call of the presiding officer of the panel.

(d) The panel shall investigate, collect, and evaluate the information necessary to provide recommendations under Subsection (e). The cost and expense incurred by the panel associated with the work of the panel under this section shall be paid or reimbursed by the association.

(e) At the request of the commissioner, the panel shall recommend to the commissioner methods or models for determining the extent to which a loss to insurable property may be or was incurred as a result of wind, waves, tidal surges, or rising waters not caused by waves or surges for geographic areas or regions designated by the commissioner.

(f) After consideration of the recommendations made by the panel under Subsection (e), the commissioner shall publish guidelines that the association will use to settle claims.

(g) A member of the panel is not individually liable for an act or failure to act in the performance of the official duties in connection with the individual's work on the panel.

(h) In any review of a claim under this subchapter, and in any action brought against the association under Section 2210.575, the guidelines published by the commissioner under Subsection (f) govern the claim and are presumed to be accurate and correct, unless clear and convincing evidence supports a deviation from the guidelines.

Appendix B: Historical Premium & Maintenance Tax

Year	Premium Tax	Maintenance Tax & Other	Total
2010	$6.2 Million	$1.2 Million	$7.3 Million
2011	$6.5 Million	$1.2 Million	$7.7 Million
2012	$7.1 Million	$1.3 Million	$8.4 Million
2013	$7.6 Million	$1.4 Million	$9.0 Million
2014	$7.9 Million	$1.5 Million	$9.4 Million
2015	$8.1 Million	$1.5 Million	$9.6 Million
2016	$7.8 Million	$1.5 Million	$9.3 Million
2017	$6.8 Million	$1.3 Million	$8.0 Million
2018	$6.3 Million	$1.2 Million	$7.5 Million
2019	$6.0 Million	$1.1 Million	$7.1 Million
2020	$5.9 Million	$1.1 Million	$7.0 Million
2021	$6.3 Million	$1.2 Million	$7.5 Million

Appendix C: Historical TWIA Ratemaking

Below is an outline of the various processes by which TWIA rates have been set in the past.

I. **TWIA filed rates with State Board of Insurance/Department of Insurance**
   a. TWIA Board of Directors filed rates with the State Board of Insurance (SBI). SBI could approve, modify or disapprove the filed rates. Rates were deemed approved if not modified or disapproved within 30 days of filing.
      i. Secondary requirement that rates could not be more than the maximum rates set by the Board for similar risks or classes of risks
      ii. Commissioner could request additional information from TWIA
      iii. Commissioner required to have a hearing on the rate filing before acting on the filing

II. **State Board of Insurance promulgated rates for the insurance industry and TWIA was based off the promulgated rate.** Process was used for commercial and non-commercial. TWIA Board of Directors did not make a rate filing but provided experience to be used in the rate hearings
   a. State Board of Insurance set a benchmark rate and TWIA's rate could not exceed rate set by SBI for **non-commercial** lines or the manual rate promulgated by the Board.
   b. State Board of Insurance promulgated a rate for commercial risks.

III. **TWIA Board of Directors required to make an annual rate filing no later than August 1 of each year for commercial risks.**
   a. Filings were submitted to the Commissioner of Insurance.
   b. The Commissioner could approve, disapprove, or modify the filing.
   c. Rate change limited to 15%.

IV. **Annual Rate Filing – Current Process**
   a. Must be submitted no later than August 15 for all types and classes of risks written by TWIA.
   b. Association may use the rate if the rate change
      i. does not exceed the rate in effect on the date the rate filing is made,
      ii. and
      iii. is filed not later than 30 days before the date of use
   c. If the rate change does not meet the criteria of IV., B.
      i. Commissioner shall provide interested parties opportunity to review the filing and provide comments
      ii. Commissioner shall approve or disapprove the filing not later than October 15 otherwise the filing is considered approved
      iii. Commissioner does not have express authority to modify the filing submitted by TWIA

iv. A rate change is limited to 10% average rate change and 15% for an individual rate class.
v. Any proposal to increase the current rate must be approved by two-thirds of the Board of Directors
vi. The Board of Directors may not vote on a proposed rate increase if there is a vacancy on the Board and the vacancy has existed for at least 60 days when the vote is taken.

V. Other Rate Filings – Current Process

a. Rate change must be filed with the Commissioner for approval
b. Commissioner must approve or disapprove as soon as reasonably possible
c. A filing not disapproved on or before the 30th day of filing is considered approved
d. TWIA may use the filed rate if the rate:
    i. does not exceed the rate in effect on the date the filing is made,
    ii. is filed not later than 30 days before the date of use, and
    iii. the commissioner has not disapproved the filing

Commissioner does not have express authority to modify the filing submitted by TWIA
    iv. Any proposal to increase the current rate must be approved by two-thirds of the Board of Directors

The Board of Directors may not vote on a proposed rate increase if there is a vacancy on the Board and the vacancy has existed for at least 60 days when the vote is taken.

Appendix D: Funding Overview

Funding Overview and Recent Legislative Changes

Texas Insurance Code Chapter 2210 provides the funding structure to be used to pay TWIA's insured losses and operating expenses. Prior to 2009, the Association funded losses through premiums and potentially unlimited assessments on insurance companies. House Bill 4409, enacted in 2009, significantly changed Association funding, providing for the issuance of up to $2.5 billion in Class 1, 2, and 3 public securities.

Senate Bill 900 (84th Legislature, Regular Session), effective September 1, 2015, further modified the sources of funding and requires overall funding to cover at least a 100-year season, a storm or series of storms with a 1% or less chance of occurring. TWIA's current funding structure is, in order:

- TWIA premiums and amounts in the CRTF
- $500 million in Class 1 public securities
- $500 million in Class 1 member company assessments
- $250 million in Class 2 public securities
- $250 million in Class 2 member company assessments
- $250 million in Class 3 public securities
- $250 million in Class 3 member company assessments
- Reinsurance or alternative risk financing in an amount sufficient to achieve total funding not less than a 100-year hurricane season.

Under Senate Bill 900, all Classes of public securities are intended to be backed solely by TWIA revenues and are not obligations of the State of Texas. Class 1, 2, and 3 public securities are repaid by TWIA premiums and surcharges on TWIA policies. However, Class 2 and 3 public securities, after a finding by the Commissioner of Insurance, may also be repaid by surcharges on coastal property and auto policies if premiums and TWIA policy surcharges are insufficient.

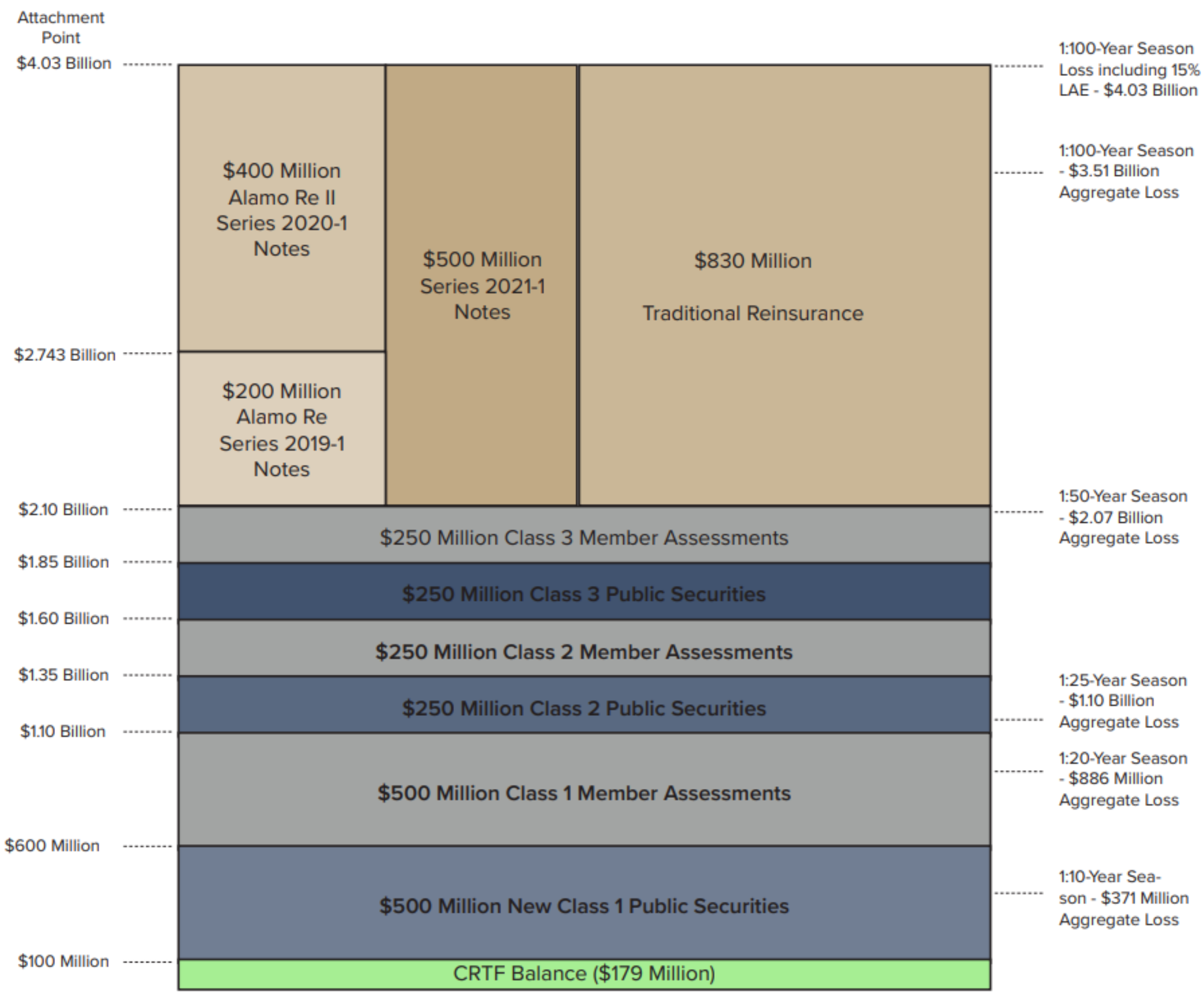
House Bill 1900, effective June 10, 2019, clarified how TWIA can use its funding sources to repay losses. House Bill 1900 prohibits TWIA from paying excess losses from a catastrophe year with premium and other revenue earned or reserves available or accrued in subsequent years. The bill also requires TWIA's purchase of reinsurance above its minimum required funding level to be paid for by an assessment on member companies.

Most recently, House Bill 769, effective September 1, 2021, made changes to how TWIA completes its annual purchase of reinsurance. The law prohibits TWIA from purchasing reinsurance from an insurer or broker that provides the catastrophe modeling TWIA uses to determine the probable maximum loss or make rate decisions.

2021 Hurricane Season Funding

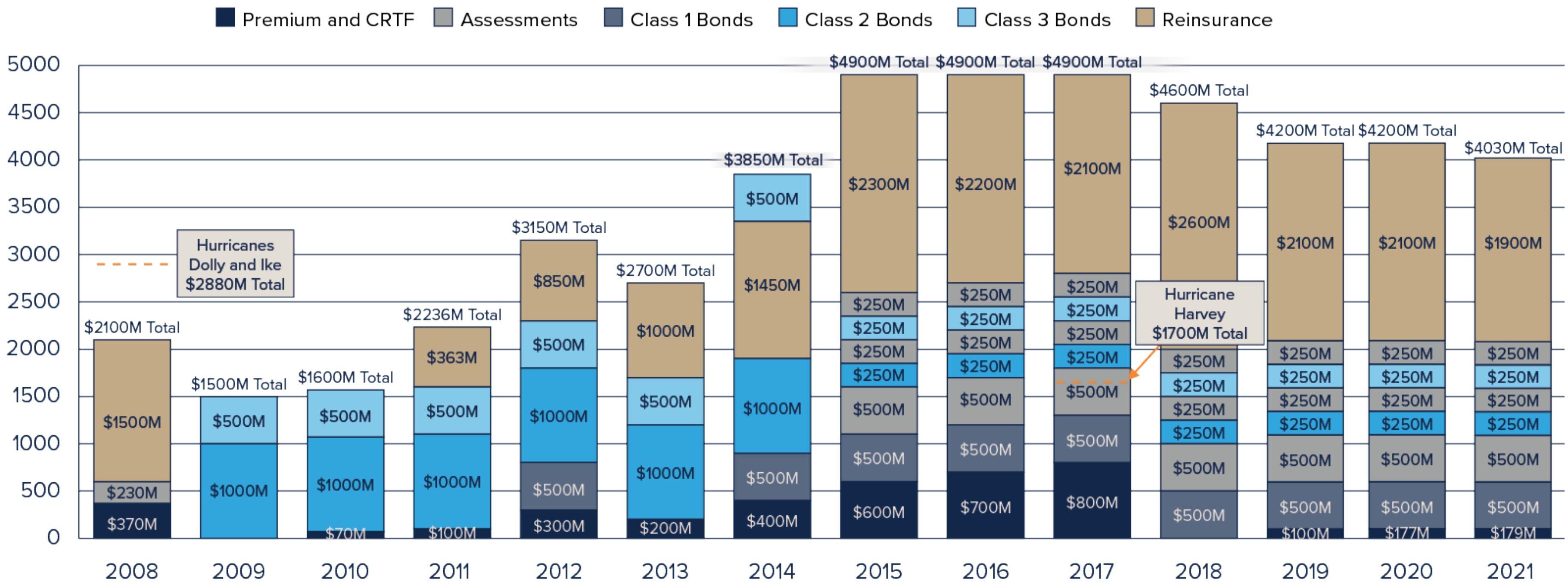
TWIA's 2021 catastrophe funding program, effective June 1, 2021 to May 31, 2022, provides access to $4.03 billion in total funding. The reinsurance program includes $830 million of traditional reinsurance and $1.1 billion in new and previously outstanding catastrophe bonds placed atop the $2.1 billion of total statutory funding sources. The traditional reinsurance program provides coverage on an aggregate basis, meaning multiple hurricane events would be covered under the same reinsurance program. TWIA did not contribute to the Catastrophe Reserve Trust Fund (CRTF) from net gains from operations in 2020, primarily reflecting losses from the active hurricane season. The current CRTF balance is $179 million.

TWIA's funding for the 2021 hurricane season is illustrated by the chart below followed by historical funding for the past 14 years:



Storm frequencies based on an average of AIR and RMS modeled losses using TWIA exposures as of 11/30/20

Historical Funding (2008-2021)



Funding for 2008 shown as it existed for Hurricane Ike, post-Hurricane Dolly; unlimited additional funding available via reimbursable assessments
Funding for 2009-2011, 2013 assumes $0 Class 1 Public Securities issuable; 2012, 2014-2015 include $500 Million pre-event Class 1 Public Securities
Funding for 2015 shown as of September 1, 2015, incorporating SB 900
Funding for 2015-2016 incorporate bond funding sources that differ from prior years
Funding for 2018 was impacted by the depletion of the CRTF to pay losses from Hurricane Harvey
Funding for 2019 includes approximately $100 Million in the CRTF from 2018 net gains from operations
Funding for 2020 includes deposits totaling $177 million in the CRTF
Funding for 2021 is effective from June 1, 2021 – May 31, 2021

Association Funding Sources

TWIA funding has historically been provided from the following general sources, each with differing benefits and challenges:

TWIA Premiums

The premiums paid by TWIA policyholders in the current year are always the first source of funding for both catastrophe and non-catastrophe claims. The other sources of funding are only utilized if a catastrophe or series of catastrophes results in losses and expenses in excess of premium and other revenue.

Premiums paid by TWIA policyholders are immediately available to pay claims and are a guaranteed source of funds but are limited in amount to those premiums earned in the current year.

Catastrophe Reserve Trust Fund (CRTF)

In most years, TWIA premiums are greater than losses and expenses. Every year, TWIA transfers all remaining premiums into the Catastrophe Reserve Trust Fund (CRTF), a separate account administered by the Comptroller on behalf of TDI. Certain TWIA policy surcharges are also transferred to the CRTF. In this regard, the CRTF represents premiums and surcharges paid by TWIA policyholders in prior years. Funds in the CRTF may only be used for purposes directly related to the funding of insured losses, as described in statute.

Like current year premiums, the CRTF is available immediately after an event and is a guaranteed source of funds. As the entire balance of the CRTF may be used after a catastrophic event, the amount available in any given year is limited to the premiums and surcharges transferred since the most recent catastrophic event.

Public Securities

The Texas Public Finance Authority is authorized to issue up to $1 billion in public securities to fund TWIA losses. There are three different classes of securities available, each in differing amounts and with different sources of repayment. Public securities are effectively a means for TWIA to borrow funds from the financial market to pay losses and to repay those funds over a maximum of 14 years through premiums and surcharges on TWIA policies and, if necessary, all property and auto policies in the catastrophe area. Class 1 public securities may be issued either pre- or post-event; Class 2 and 3 securities may only be issued post-event.

The process of issuing public securities is lengthy and expensive. Proceeds from public securities may not be available to pay claims until months after an event. Additionally, the ultimate availability of securities is dependent on general financial market conditions, which are highly variable.

Member Company Assessments

TWIA has the authority to assess its member companies, comprising all insurance companies authorized to write property insurance in Texas with limited exceptions, up to $1 billion to fund losses. These assessments are levied by the TWIA Board of Directors with approval by TDI and may not be directly recouped by companies through premium surcharges or tax credits. In practice, companies generally include a provision for potential assessments in their rates.

Assessments are due from companies 30 days after receipt of the notice of assessment and are limited to amounts specified in statute. Payment of assessments is enforced by TDI, and there have, historically, been very few uncollected assessments. The ultimate source of assessment funds are the premiums paid statewide by insurance company policyholders, to the extent companies have included this potential expense in their rates.

Reinsurance

Reinsurance is a form of insurance purchased by insurance companies from specialized reinsurance companies. TWIA may purchase catastrophe reinsurance to cover its losses and expenses after a catastrophic event. The costs associated with reinsurance can be significant. Reinsurance in an amount in excess of other funding sources, up to the estimated amount of a catastrophe with a probability of one-in-100, is purchased directly by TWIA. Any additional reinsurance purchased beyond the minimum funding level is paid by assessments to member companies.

TWIA also utilizes catastrophe bonds as an additional source of funding. These function identically to traditional reinsurance, except the reinsurance is offered by capital market investors on a collateralized basis, rather than by reinsurance companies. This allows TWIA to more effectively manage the cost of reinsurance and mitigate any credit risk associated with reinsurance companies being unable to pay.

Funds from reinsurance and catastrophe bonds are available immediately after a qualifying event, as determined contractually.