LIEUTENANT GOVERNOR JOHN GARAMENDI

May 1, 2008

The Honorable Steve Poizner
Insurance Commissioner, State of California
300 Capitol Mall, Suite 1700
Sacramento, CA 95814

Dear Commissioner Poizner:

I am sure you will not be surprised to hear how disappointed I am in the actions that you have taken to undermine important consumer protections embodied in the "Prop 103 prior approval rate regulations" promulgated by the department during my tenure as Insurance Commissioner.

I am more than disappointed; I am alarmed that after making such substantial changes to a complex set of regulations, you are proposing that they be hastily adopted as emergency regulations. My understanding is that some of the most significant changes were made as late as Monday, and have barely seen the light of day, leaving no opportunity for public analysis or reaction.

Members of your staff have repeatedly argued against the use of emergency regulations when the criteria of Section 11342.545 have not been met. This is clearly not an action that is necessary to protect the "public, peace, safety or general welfare." A lack of action on the part of the agency does not constitute an emergency. If these changes were so important why did you not subject the changes to public comment?

My administration's prior approved regulations were adopted after years of reflection, meetings, public hearings, and negotiations. The process was public and thorough, and intended finally to end years of struggle and acrimony over the proper balance between the voters' intentions as expressed in Proposition 103 and the legitimate needs of a competitive insurance market place. This debate had lasted through three Insurance Commissioner's terms. And in spite of insurers' attempts, the voters' legitimate interest in economic regulation was upheld in several major court challenges.

I believe my administration properly struck the balance that was called for. The regulations which we adopted and which went into effect in April of 2007 (during your administration), were never challenged by the industry, evidencing the fact that while the

industry may not have found them to be ideal, they could not mount a meritorious legal challenge.

Apparently, the industry found a more productive route to further their interests, through jaw boning and rewriting the regulations outside of the discipline of public scrutiny and comment.

Even without adequate time to completely analyze the impact of these changes I am certain that you have opened the door to abuse by insurers. Some of your modifications to the prior approval regulations create gaping exceptions that undermine the spirit and the intent of Proposition 103

Specifically, changes to Section 2644.7 claim to allow "flexibility" by permitting companies to use expanded historical periods to develop loss and premium trends. Even worse the regulations allow companies to selectively cherry pick from these longer periods those that they feel are most "actuarially appropriate." It will come as no surprise that actuaries will justify higher rates with this opportunity. While the regulation states that the Commissioner may require a different selection, you know as well as I do, that the agency lacks resources to adequately scrutinize these choices in the thousands of filings that will come in utilizing this provision. The burden of justification should be on the carrier not the department. This is the reason for having "standards" in the first place.

Your modifications to Section 2644.16 still provide for a return equal to the risk free rate plus 6%, but now allow adjustments of up to 2% when the Commissioner determines that "the difference between the risk free rate and the cost of capital is significantly different from its historical average." Frankly, it is unclear what this means, and requires the application of a level of discretion and macroeconomic analysis that should be far beyond the scope of generic regulations. It is also conveniently similar to the 8% adjustment the industry has been advocating for years.

Section 2644.25 (d) departs dramatically from my administration's policy and allows the costs of reinsurance to be used when setting rates. We had determined that this course would allow an untenable pass through of unregulated rates from the reinsurance market. While we specified exceptions for earthquake and medical malpractice insurance because of some level of regulatory oversight in these areas, we prohibited the pass through of reinsurance from unauthorized sources. Inexplicably you have eliminated this prohibition.

Your regulations make many other changes that I am sure have potential adverse impacts for consumers, including changes in the efficiency standards, and alterations to the standards for granting a variance. Unfortunately because of the haste with which you have promulgated these changes, I have not had time to fully analyze them. I wanted to react to your precipitous process you are following with the same immediacy with which you have embarked upon it.

Commissioner, you were elected to enforce a law enacted by the voters in the way that most closely manifests their interest in enacting it. I believe that these recent changes represent an attempt to undermine the law in significant ways and I must register my objections.

While I have no objection to legitimate technical fixes that would allow a "better mouse trap" these changes clearly do not fit into that category. And if they did they would not have to be enacted on an emergency basis.

In spite of endless insurer objections, the work that we have done over the past two decades has saved ratepayers $62 billion according to the April 24, 2008 report by the Consumer Federation of America. I am disappointed to see you embark on a course of action intended to reverse that direction. I am even more disappointed to see that this action has been rationalized as an emergency.

Sincerely,

JOHN GARAMENDI
Lieutenant Governor
Insurance Commissioner 1991-1995; 2002-2006