CHAPTER 35

INSURANCE

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"Why is insurance so expensive and hard to get in Hawai'i?"

With regard to auto insurance, this has long been a fair question. State-by-state figures, compiled by the National Association of Insurance Commissioners, show that Hawai'i motorists paid an average of $999 in 1991 to insure one vehicle for one year. Only New Jersey ranked higher at $1,081. We'll get into why in a moment.

By contrast, Hawai'i residents have gotten a home insurance bargain for years. The last general movement in rates came in 1987, and that was a *decrease*.

Iniki's impact. Hurricane Iwa in 1982 caused a blip in insured losses—$175 million—but that was viewed as something of a freak. Otherwise, losses in Hawai'i have run low. But that changed on a frightening Friday in September 1992 when Hurricane Iniki devastated the island of Kaua'i. Iniki caused $1.6 billion of insured losses and forever changed how property insurers regard Hawai'i. When all accounting is done, companies will have ended up paying in claims more than they collected in premiums over the previous twenty years!

Before Iniki, a Hawai'i resident could obtain $300,000 of property insurance for a premium payment of about $953 a year. That compared with $1,634 for the same coverage in Chicago, $2,422 in Houston, and $2,477 in Miami. Insurance companies were making profits from homeowners in Hawai'i and actively sought new business here.

After Iniki, property insurers lump Hawai'i with the Gulf Coast and

Florida as high hurricane-risk locales. One company —the Hawaiian Insurance Group (HIG)—quit the business entirely, unable to cover more than a third of its $200 million losses from Iniki. Two other companies phased out their homeowners business, citing inability to line up reinsurance. Consequently, starting in late 1992, and for at least a matter of several months, homeowners insurance did indeed become difficult or impossible to get, primarily because of a reinsurance crisis.

Reinsurance crisis. Property insurers purchase reinsurance to bring in others, such as Lloyd's of London, to share risks of catastrophic loss. As the HIG case illustrates, lack of sufficient reinsurance can prove ruinous. By itself Iniki would have driven up the cost of reinsurance for companies doing business in Hawai'i. But coming in the same year as Miami's Hurricane Andrew, the Los Angeles riots, and winter storms in the Northeast, Iniki made reinsurers reluctant to extend coverage at any price.

In an attempt to fill the gap, and with support from the insurance companies, the 1993 state legislature created a hurricane insurance "pool," called the Hawai'i Hurricane Relief Fund. After the pool is up and running, it will cover losses from storms officially designated as hurricanes up to $750,000 per home. The collective liability of insurance companies will be capped at $500 million. Companies choosing to participate will continue to write homeowners policies as before, insuring for fire, sub-hurricane wind, theft, and comprehensive personal liability. All or at least most companies are expected to participate.

Despite the new pool, premiums for basic homeowners will rise. Data developed by the Hawai'i Insurance Bureau and submitted to the State Insurance Division clearly will support increases, in part because of the high cost of reinsurance.

Auto insurance. Can we simply blame Hawai'i's high cost of living for lofty auto insurance premiums? Not really. If it were that simple, why was homeowners insurance so reasonable here for so long?

Hawai'i's 20-year-old no-fault auto insurance law deserves much of the blame. In national comparisons, it is in many ways unusual, in some ways unique.

Here's how Hawai'i-style no-fault works. If you or your passengers are injured in an accident, your insurance company pays for medical, rehabilitation, loss of income, and certain other costs. Fault is irrelevant, but the ability to sue kicks in if an injured person dies or suffers serious disfigurement, or if medical and rehabilitation costs exceed a dollar limit (the "threshold"). The legislature intended that the threshold be set such that no more than 10 percent of all injury cases would end up in lawsuits.

As of mid-1993, the threshold had risen to $10,000 from the original $1,500. Observers believe many accident victims have deliberately run up medical and rehabilitative costs just to reach the threshold and thus be able to sue. Insurance companies are widely perceived as being willing to offer cash settlements well above threshold limits, just to avoid the ridiculously high cost of litigation.

High settlement costs. Indeed, insurance settlements in Hawai'i run much higher than national averages. According to a study by an industry-backed research group, the average bodily injury liability settlement in Hawai'i was $35,705 in 1990, about six times the national average.

To some extent that average was high because Hawaii's threshold is the highest for any state having a no-fault law, and that limits the number of lawsuits. But the same 1990 study showed that 28 percent of all bodily injury cases in Hawai'i that year were eligible for lawsuits, far above the 10 percent target. One reason: in 1985 the legislature, seeking administrative simplicity, tied increases in the threshold to an inflexible formula based on annual increases in the cost of living.

Now comes some hopeful news. In 1992, the legislature mandated a return to the concept of limiting lawsuit-eligible cases to 10 percent. Equally important, it also adopted a system of medical fee schedules for specific services, much like those long used in workers compensation insurance. As a result, a party injured in an auto accident will now find it more difficult to run up big medical bills. Any increase in the allowed number of chiropractic visits, for example, will require special approval through a peer review process.

The 1992 reform package also called for insurance companies to reduce their premiums by 15 percent in 1993. Few did so, however, invoking their rights to "fair and reasonable" rates of return. The State Insurance Division, with an eye to court decisions in California and Nevada, determined it couldn't enforce the 15 percent rollbacks.

Other factors. While high claims and settlement costs have been the primary villains in past years, other factors also help explain why auto insurance in Hawai'i is so costly.

• Hawai'i's law requires insurance companies to accept any applicant presenting a valid driver's license and the money to pay the premium. This "take all comers" rule bars a company from rejecting an applicant it feels poses an unacceptable risk. An example would be a young male driver with a record of tickets, an accident or two, and perhaps a drunk-driving conviction.

• In submitting premium schedules to the state for approval, a company can't charge different rates based on age, sex, or marital status. This means, assuming a clean driving record, that a 19-year-old unmarried male pays the same premium as a 45-year-old married female. That's so even though statistics show that the young male is far more apt to cause a loss for the insurer.

• Crowded highways produce more accidents, and in Hawai'i the ratio of miles driven to miles of highway runs almost four times the national average.

• In Hawai'i, every welfare recipient gets basic liability insurance for free, compliments of the insurance-buying public. As of early 1993, about 10,000 welfare recipients were enjoying this benefit, the cost of which adds to the cost of each auto insurance buyer's policy.

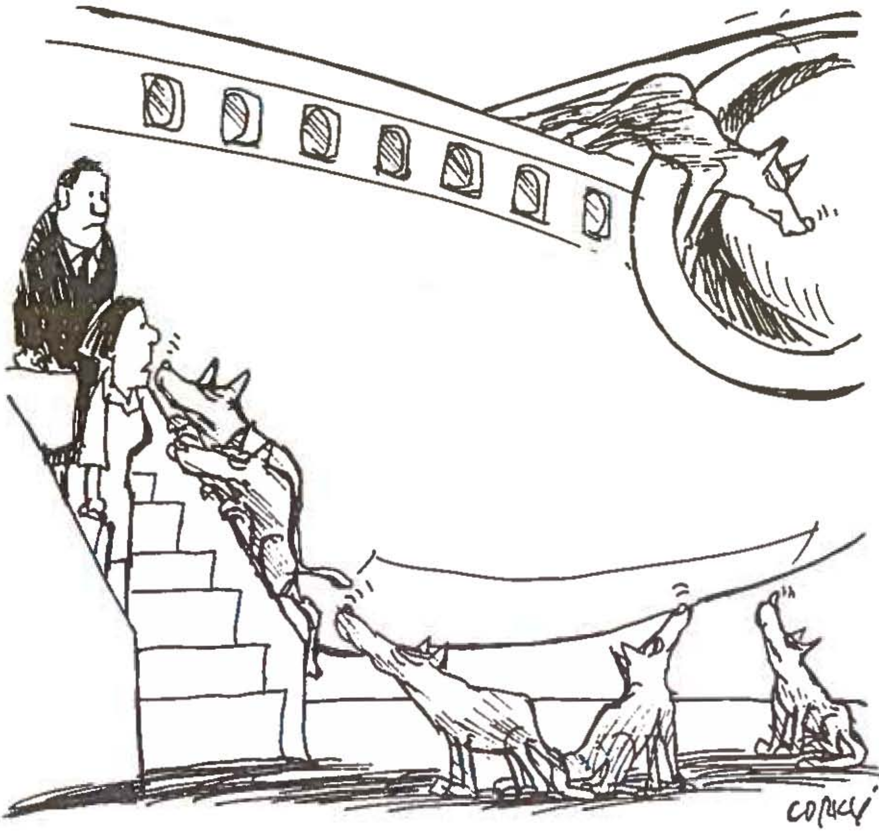
• As many as 20 percent of the more than 670,000 vehicles on Hawai'i's roads lack insurance, according to Insurance Division estimates. That's so even though coverage is mandatory. Also, drivers with low limits of coverage—$25,000 of bodily injury liability is the minimum written—may lack enough coverage to meet judgments against them. This is why insurance companies offer coverage for uninsured motorists and underinsured motorists. If every driver were adequately insured, there would be no need to buy either.

Reform. The 1993 legislature, in its regular session, repealed "take all comers" and went so far as to allow companies to drop up to 2 percent of their insured drivers from their books at renewal time. Governor John Waihee called the repeal "an idea whose time has come" but vetoed it anyway, citing technical flaws in how key provisions were drafted. But then in its special session later that year, the legislature passed reform again, having corrected the flaws.

Insurance regulators say that companies eyeing entry into the Hawai'i market have cited "take all comers" as a principal reason for balking. If more companies were to operate here, competition would rise and, if theory holds, premiums would become more reasonable.

Many believe the insurance companies should be allowed to charge different rates based on age, sex, and other criteria. This would bring Hawai'i more in line with most other states. It would also encourage into the market companies specializing in good or substandard risks. By specializing, a company is better able to control and plan for its risks—and thus lower its premiums.

Finally, if the legislature deems that welfare recipients and other low-income people should get free auto insurance, it—the state—should pay. Forcing the insurance-buying public to subsidize others is a hidden tax. If a tax is in order, it ought to be labeled a tax.



"SOMEDAY WE'LL THANK THE BROWN TREE SNAKE PATROL..."