

CASUALTY ACTUARIAL AND STATISTICAL (C) TASK FORCE

U.S. Homeowners Insurance Rate Regulation

Draft Exposed: 6/26/26

A Regulatory Perspective on Cross-State Subsidization, Consumer Protection, and Market Dynamics in the Modern Era

NAIC Property and Casualty Insurance (C) Committee | 2026 Spring National Meeting Charge

What We'll Cover



01

The Regulatory Foundation

How state-based rate regulation works, and the three-part legal standard.



02

Building & Reviewing Rates

Prospective ratemaking, catastrophe modeling, and reinsurance allocation.



03

Defining Cross-State Subsidization

What it would actually require – and common mischaracterizations.



04

Testing the Hypothesis

Enterprise capital, indirect effects, and CIPR's empirical case studies.



05

Conclusion

Rate regulation as layered, evidence-based consumer protection.

The Question Behind This Paper

"Imagine a multi-state insurer tries to charge more premium to homeowners in a state with lower disaster risk to make up for heavy losses in a state with higher risk."

Legislators, researchers, media, and consumer advocates have asked: **do insurers spread catastrophic losses across their entire book of business, raising premiums in low-risk states to offset losses elsewhere?**

CASTF Charge:

Draft a white paper that explains how homeowners' insurance rates are regulated across states, with particular attention to public questions and academic claims regarding potential cross-state subsidization of catastrophic losses.

The Paper's Conclusion

Under the state-based system of insurance regulation, homeowners rates are designed and reviewed to reflect the expected future cost of risk in the state where the policy is written – not to shift costs from one state's policyholders to another's.



Legal Constraints

State rating laws require rates to be supported by state-specific actuarial analysis – not another state's losses.



Regulatory Review

Filings are scrutinized before and after taking effect; market conduct exams catch real-world deviations.



Market Discipline

Insurers pricing above local risk lose business to competitors, making artificially high rates unsustainable.

SECTION 1

The Regulatory Foundation

How state-based rate regulation works, and the legal standard every homeowners rate must meet.

I. WHAT IS HOMEOWNERS RATE REGULATION?

State-Based, Not Federal

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- 1944** **United States v. South-Eastern Underwriters Association**
Supreme Court holds insurance crossing state lines is interstate commerce, subject to federal regulation.
 - 1945** **McCarran-Ferguson Act**
Congress preserves state primacy: no act of Congress may invalidate state insurance regulation.
 - Today** **Commissioner-Led Oversight**
Each state's Insurance Commissioner, Superintendent, or Director holds broad authority over rates, forms, and solvency.

The Three-Part Rating Standard

Derived from the All-Industry Bills and the NAIC Model Rating Law – adopted, with variations, across most states.



Not Excessive

Rates must not result in unreasonably high profits or financial gains to the insurer.



Not Inadequate

Rates must be sufficient to cover expected losses and expenses and maintain insurer solvency.



Not Unfairly Discriminatory

Rates must not differentiate among similarly situated risks without an actuarial or justifiable basis.

Two Complementary Layers of Oversight



Rate Regulation

Reviews the prospective rates insurers propose to charge, before – and often after – they take effect.

- Prior approval
- Modified prior approval
- Flex rating
- File and use
- Use and file
- No file



Market Conduct Regulation

Checks whether insurers, in practice, charge the rates they filed and treat consumers fairly in claims handling, underwriting, marketing, and billing.



Catches misapplied rating factors or unfiled surcharges



Can require consumer refunds, fines, or practice changes



Triggers notice to other states where the insurer does business

The Market Is a Backstop, Too

Insurers that price above the risk of the market in a state will lose business to competitors – making it difficult to sustain rates that are artificially high.



Consumer Shopping

Competition works best with many active insurers and consumers who shop around for coverage.



Real Limits

Comparison is hard given policy complexity and disruptions – withdrawals, insolvencies – which can limit efficiency.



A Complement, Not a Substitute

Regulatory engagement fills the gaps competitive markets leave, especially where availability and affordability are strained.

SECTION 2

Building & Reviewing Rates

Prospective ratemaking, catastrophe modeling, and reinsurance allocation – the mechanics regulators examine.

Premiums Are Prospective, Not Retrospective

Rates fund the expected cost of coverage during a future policy period – they are not a mechanism to recoup past losses.



Expected Losses

The largest component – also called pure premium or loss cost – derived from trended historical data.



Loss Adjustment Expenses

The cost of investigating, defending, and settling claims.



Underwriting Expenses (Incl. Premium Taxes/Licenses)

The cost of issuing, servicing, and administering the policy.



Profit & Contingencies

A reasonable return for the risk undertaken, influenced by expected investment income.

State-Based, With Some Broader Inputs



Mostly State-Specific

- Local peril exposure & geographic concentration
- Construction characteristics & roof type
- Legal environment & claims settlement patterns
- Credit-based insurance score, home age

ASOP No. 13 governs trending: adjusting historical data to reflect expected future rebuilding costs.



Some Broader Influences

- Repair-and-rebuild cost inflation (labor, materials)
- Reinsurance market conditions
- Countrywide underwriting expense analyses
- Capital market conditions & investment income

Regulators examine each input: historical period adequacy, credibility blending, trend selection, and expense justification.

Catastrophe Risk Needs Special Treatment

Low-frequency, high-severity, spatially correlated losses can't be reliably measured with a short historical window alone.



Wildfire



Hurricane



Severe Convective
Storm



Flood-Adjacent
Perils

Actuarial Standard of Practice ASOP No. 39

Defines a catastrophe as an infrequent event producing unusually large aggregate losses, requiring separate ratemaking treatment.

ASOP No. 38

Filings based on these models must disclose which model was used, what exposure data went in, and how secondary perils and uncertainty were handled.



Catastrophe Models

Computerized simulations of scientifically plausible catastrophic events, estimating financial impact on a portfolio. Filings using model output should disclose which model, what exposure data, and how secondary perils, demand surge, and uncertainty were addressed (ASOP No. 38).

Reinsurance Cost Is Allocated By Risk Contribution



A single enterprise-level reinsurance program may cover multiple states. Its cost is not spread evenly – it's allocated based on each state's modeled catastrophe losses, exposure, and contribution to reinsured layers.

Per-Risk / Per-Occurrence

Excess-of-loss treaties responding to large single-event losses.

Aggregate Covers

Respond to the accumulation of smaller losses over a policy period.

Catastrophe Bonds

Capital-market instruments providing additional protection against tail events.

A consumer in a low-catastrophe state pays for the portion of the reinsurance program that protects against losses in their own state – not someone else's.

SECTION 3

Defining Cross-State Subsidization

Precision matters: what would structural cross-state subsidization actually require – and what doesn't qualify?

Two Conditions Must Both Be Met

Structural cross-state subsidization: policyholders in one state systematically pay rates inadequate for their own expected costs, while policyholders in another state pay more than their expected costs to offset it.



1. Market-Wide Distortion

Structural cross-state subsidization is a market-wide phenomenon. If one company's portfolio shows it in isolation, that alone does not meet the definition of cross-subsidization between states.



2. Not-Actuarially-Justified Rates in Both States

If rates in either state are actuarially justified, structural cross-state subsidization has not occurred. A truly cross-subsidized market would show inadequate rates in some states and excessive rates in others, simultaneously.

What Often Gets Mistaken for Cross-State Subsidization



Differing Actuarial Assumptions

Credibility treatments, catastrophe loadings, and trend selections reasonably differ state to state while both remain actuarially justified.



Filing Timing Differences

Insurers may absorb cost fluctuations or sequence filings due to resources – creating temporary gaps that aren't structural.



Mix-of-Business Shifts

Rapid growth or shrinkage in a state's book can call for different conservatism in assumptions, unrelated to other states.



Regulator Disapproval

A filing rejection often reflects insufficient support or procedural gaps – not evidence of cross-subsidization.



Credibility & Non-State Data

Blending state data with a credibility complement is standard actuarial practice (ASOP No. 25), not cost-shifting.

SECTION 4

Testing the Hypothesis

Enterprise capital deployment, indirect market effects, and what the empirical evidence actually shows.

Enterprise Capital Is Not Cross-State Subsidy



A national insurer maintains a single pool of surplus capital backing obligations in every state. When a hurricane causes billions in Florida losses, the same surplus that backs Ohio policies is drawn upon if needed.

That capital is the insurer's own, contributed by shareholders – not premium dollars transferred between states' policyholders.



Diversification Benefit

The insurer pools the uncertainty of State A's results against State B's, not the losses themselves. The benefit reduces required capital and improves stability.



Who Benefits?

Primarily shareholders, through reduced capital requirements, and policyholders, through improved insurer financial stability – not State B paying State A's losses.

Real Indirect Pathways, Distinct From Subsidization

These are legitimate, economically rational channels, not regulatory or actuarial mechanisms for cost-shifting.



Rebuilding-Cost Inflation

Demand surges for lumber, roofing, and labor after a major catastrophe, raising claim severity nationwide, even for repairing damages caused by an unrelated burst pipe in Indiana.



Global Reinsurance Pricing

A severe hurricane season or large wildfire loss can raise reinsurance costs for the next policy year, reflected in filings even in states untouched by the event.



Catastrophe Model Updates

New science learned from one state's event can update models used nationwide, raising rates in other states exposed to the same peril, not because of cost-shifting, but better science.

CIPR's Empirical Test: No Supporting Evidence for Cross-State Subsidization

The Center for Insurance Policy and Research examined rate filings before and after major catastrophes to test whether out-of-state losses crept into the indication.



Minnesota Hail (2017) → Iowa Filings

11 Iowa filings examined (5 before / 6 after the Derecho).
No Minnesota or other out-of-state losses reflected. No methodology shift designed to indirectly raise indications.



Harvey, Irma & 2018 CA Wildfires → Virginia Filings

8 + 16 Virginia filings examined before/after. No out-of-state losses included; no methodology changes suggesting indirect allocation of loss experience.

Where indications rose post-event, drivers were in-state loss trends, updated catastrophe models, and routine profit-provision updates, not out-of-state losses.

Four Pitfalls That Distort the Debate



Rate Filings Are Not Exact Rate Needs

Indications are point estimates within a plausible range, not certainties – single-snapshot research can mislead.



Claim Count Definitions Vary

Insurers count claims differently; unadjusted comparisons can produce false conclusions about frequency or severity.



Indicated vs. Implemented Rate

Filing below the full indication is common and reflects competition or compliance, not a gap that must be 'recovered' elsewhere.



Catastrophe Pricing Is State-Level

Models calibrated to one state's exposure may be updated using science learned elsewhere, which is improved science, not cross-subsidization.

SECTION 5

Layered Consumer Protection

Bringing it together: why this architecture protects consumers without permitting cross-state cost shifting.

Four Layers, Working Together

1



Legal Standard

Rates must be not excessive, not inadequate, not unfairly discriminatory, backed by state-specific data.

2



Front-End Filing Review

Regulators scrutinize loss projections, catastrophe loadings, and expenses before rates take effect.

3



Back-End Market Conduct

Exams catch real-world deviations, like misapplied factors or unfiled surcharges, after rates are in force.

4



Competitive Market Pressure

Insurers pricing above local risk lose business, making artificially high rates unsustainable.



Premiums are forward-looking estimates of future cost, not a vehicle for recovering one state's past losses from another state's policyholders.

State-based rate regulation is a holistic core consumer protection system: it ties rates to risk, subjects them to rigorous review, and helps ensure insurance remains both available and financially sound.

Casualty Actuarial and Statistical (C) Task Force | 2026



Questions & Discussion

Thank you for your time and engagement on this important topic for homeowners insurance regulation.

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