12-13-1989

# Hearing on The Loma Prieta Earthquake: An Examination of Earthquake Insurance Property Damage, December 13, 1989

Senate Subcommittee on Earthquake Insurance

CALIFORNIA LEGISLATURE

SENATE SUBCOMMITTEE ON EARTHQUAKE INSURANCE
SENATOR CECIL GREEN, CHAIRMAN

Hearing on

# THE LOMA PRIETA EARTHQUAKE: AN EXAMINATION OF EARTHQUAKE INSURANCE PROPERTY DAMAGE




December 13, 1989
P.U.C. Auditorium
San Francisco, California



472-S

CALIFORNIA LEGISLATURE

SENATE SUBCOMMITTEE ON EARTHQUAKE INSURANCE

SENATOR CECIL GREEN, CHAIRMAN

# HEARING ON

# THE LOMA PRIETA EARTHQUAKE:

# AN EXAMINATION OF EARTHQUAKE INSURANCE

# PROPERTY DAMAGE

DECEMBER 13, 1989

P.U.C. AUDITORIUM

SAN FRANCISCO, CALIFORNIA

# California Legislature

## SENATE COMMITTEE ON INSURANCE, CLAIMS AND CORPORATIONS

ALAN ROBBINS
CHAIRMAN

JIM CATHCART
CHIEF CONSULTANT
SAL BIANCO
PRINCIPAL CONSULTANT
LEAH CARTABRUNO
ASSOCIATE CONSULTANT
MAUREEN BROOKS
COMMITTEE SECRETARY
ROOM 5122
STATE CAPITOL
SACRAMENTO, CA 95814
(916) 445-0825

**SUBCOMMITTEE ON EARTHQUAKE INSURANCE**
**CECIL GREEN, CHAIR**
**December 13, 1989**
**2:00 p.m. - 5:00 p.m.**
**P.U.C. AUDITORIUM**
**505 Van Ness, San Francisco**

**AGENDA**

**SUBJECT: An Informational Hearing on the Impact of the October 17, 1989 Loma Prieta Earthquake on Homeowners, Businesses, Local Government, and the Insurance Industry regarding Earthquake Insurance Coverage**

I. CALL TO ORDER

A. Opening Statement by Senator Cecil Green

B. Remarks by Senator Milton Marks

II. PERSPECTIVES

A. Homeowners and Business Owners

Barbara Miller - San Francisco (Marina District)

Paul Cobb - Oakland

Gloria Fontinello - President, Marina Neighborhood Assn.

Allan Goodman - San Francisco (Marina District)
Radovan Pesusic - San Francisco (Marina District)

California Grocers Association

Don Beaver, President

Don Kaplan, President of Bonfare Markets, Inc.

PUBLIC COMMENT

B. The Local Insurance Marketplace

Scott Hague - Cal Insurance & Associates, San Francisco
Independent Insurance Agents & Brokers of California

C. Local Government

Keith Grand, Risk Manager
City and County of San Francisco

Honorable Warren Widner, Supervisor
County of Alameda

D. Gail K. Hillebrand, Staff Attorney
Consumers Union

III. REGULATORY ROLE - California Department of Insurance

David Stolls, Chief of Claims Services Bureau

Linda Yarber, Senior Insurance Policy Officer

IV. INSURANCE COMPANIES AND TRADE ASSOCIATIONS

A. Personal Insurance Federation of California

Dan Dunmoyer, Vice President of Legislative Policy

Leonard Gelfand, Regional Vice President & Claims Manager
Farmers Insurance

B. California State Automobile Association

Barry Shiller, Manager of Governmental Affairs

C. Association of American Insurers

D. National Association of Independent Insurers

E. Alliance of American Insurers

F. Association of California Insurance Companies

V. UNSCHEDULED WITNESSES

VI. CLOSING COMMENTS

VII. ADJOURNMENT

TABLE OF CONTENTS

PAGE

CHAIRMAN CECIL GREEN: Good afternoon and welcome to everybody. I welcome you here to the hearing. As all of you know, I'm Cecil Green, Chairman of the Subcommittee on Earthquake Insurance. And as Chairman of the Subcommittee, I'm pleased to have the opportunity to hold this hearing and here in San Francisco. And I want to thank Senator Marks and his staff for all their assistance in preparing for this hearing today. Unfortunately, Senator Marks was going to be with us and due to circumstances he couldn't be here this afternoon, but he did leave his testimony and a letter of what he was going to say in the hearing. So that will be made part of the record from Senator Marks.

Before we begin, I want to take a moment to put this hearing in perspective. After the devastating earthquake in '87, we held several hearings in my district on the issue of earthquake insurance coverage. The purpose of these hearings was to find out what type of problems people were having with their insurance company, and to discuss why earthquake insurance was so expensive for the average homeowner.

At that time, we found companies lacking in their response to the victims of that particular earthquake. There were lengthy delays in payment of claims, arguments over the deductible, and many, many problems associated with assessment of overall damage.

In Santa Cruz, a lot of those things were remedied by some of the companies, but today, in this hearing, I think we're going to have a different story. Last week our committee met in Santa Cruz and heard about some positive things companies have done, and that was to assist their policyholders. However, not all the companies were given such high marks.

The purpose of this hearing is to sort out those particular cases where companies are not responsive to the needs of their policyholders. It is our intent to pursue legislation or take other steps to bring these companies more in line with what homeowners and businesses need to help in recovery from this devastating earthquake.

The other point of this hearing is to discuss the problem of high deductibles and the high cost of obtaining earthquake insurance. We hear arguments from homeowners and businesses alike that they would buy earthquake coverage if it was cheaper or the deductible was lower. We hear from the insurance companies that only a federal program can make such coverage more affordable and available.

But I believe we can come up with a better solution for all of California. There has been far too much focus on the catastrophic event and trying to provide coverage for the "big one" and not enough attention to protecting people against earthquake damage, which is coverable. The committee is dedicated to pursuing legislation to address this issue, and to introduce bills which will provide better overall coverage for the people of our state.

But before I begin with the witnesses, I'd like to recognize those Senators here today and ask if they would like to have any opening remarks. And to my right is Senator Jim Nielsen and to the left of him is Dan McCorquodale. Jim, do you have...?

SENATOR JIM NIELSEN: No, Mr. Chairman. Just appreciate your convening the committee on this very important issue. We look forward to the testimony.

CHAIRMAN GREEN: Thank you, Jim. And Dan?

SENATOR DAN McCORQUODALE: No. Ready to go.

CHAIRMAN GREEN: All right. Then let us begin with our witnesses.

(SENATOR MARKS' TESTIMONY INSERTED)

SENATOR MARKS: Good afternoon, Senators Green, McCorquodale, and Nielsen, and members of the public. Welcome to San Francisco — my district and my neighborhood.

I am very proud of the way in which this city conducted itself during and after the October 17, 1989 earthquake. Although we are still recoving from its effects, we must continue constructive discussion on how to best prepare and respond to future earthquakes.

I would like to take this opportunity to thank the Subcommittee for holding this hearing, as well as all those who have come here today to provide testimony.

As Californians, we are just beginning to feel the insurance aftershocks of the October 17 earthquake. We are reading the fine print only to discover the 10 to 20 percent deductibles. We are becoming aware of the fact that even if we would like to purchase earthquake insurance for our homes and businesses it may not be available.

My main concerns involve identifying ways in which the state can help make earthquake insurance work for homeowners, renters, and businesses. Specifically, I hope to examine what the state can do to close current loopholes that allow insurance companies to cancel existing policies or deny coverage altogether in areas like San Francisco's Marina District, and others perceived as vulnerable during an earthquake.

Clearly, the state must be willing and ready to take action. It is my hope that we will be able to take the useful information and guidance you provide us with here today back to our colleagues in Sacramento and construct legislation that will provide insurance relief to those who need it now or may need it in the future.

(HEARING RESUMED)

CHAIRMAN GREEN: If I could ask all the homeowners to come up at one time and sit at the table here, then we'll take their testimony one at a time.

Okay, we have with us today — and I'll introduce them one at a time — those wishing to speak would be Barbara Miller of San Francisco out of the Marina District. If you would begin, Barbara.

MS. BARBARA MILLER: Good afternoon, Senator. I appreciate you holding these hearings. It's been a frustrating two months. I don't quite know where to begin. I theoretically have earthquake insurance but having been almost two months, I still have no determination as to whether or not I have any coverage.

Immediately after the quake, when the City finally allowed us to inspect the property, an adjustor came out with me to inspect it with a structural engineer that I had hired.

CHAIRMAN GREEN: What kind of building do you have? A single family residence, or a condo or what?

MS. MILLER: It's a two flat condo.

CHAIRMAN GREEN: So there are just two of you.

MS. MILLER: There are just two of us, right. And the policy is written as the Jefferson Street Homeowners Association.

After the adjustor came out to inspect the property with me, I hadn't heard from her. I put in a number of calls asking specific questions as to what I was entitled to and what I was covered for. She responded to those calls, always telling me that I was not covered. At the same time, I filed with FEMA and was rejected for assistance with FEMA because I had earthquake coverage. I wrote a letter to FEMA saying that I felt like I was falling through the cracks and got a phone call immediately from somebody in the regional office at FEMA saying that he'd never heard of earthquake insurance not covering temporary living expenses. And so he called my broker and indeed found out that my policy did not cover my — cover temporary living expenses for me. So he is now...

CHAIRMAN GREEN: So that was part of your coverage. In other words, it was excluded in your policy?

MS. MILLER: Apparently it was, yes. He said that he'd never heard of that before, and it's been excluded in my policy. So he is indicating to me that he is continuing to process my claim with FEMA. But meanwhile, I've been living with friends for two months and it's been...

CHAIRMAN GREEN: I see. What company do you deal with?

MS. MILLER: My insurance company is Argon Mutual.

CHAIRMAN GREEN: Argon Mutual. Mr. McCorquodale?

SENATOR McCORQUODALE: Do you have your regular homeowners policy with the same company you have the...

MS. MILLER: No, I don't. I have my personal property covered with Liberty Mutual but it did not have earthquake insurance for my personal property. And so I'm not eligible and I understand that I'm not eligible to receive anything from Liberty Mutual. It's the Argon Mutual people who have not been responsive to my claim.

I finally got a report from my structural engineer as to what the damage was and what needed to be done to repair the building back up to the city code specifications, and at that point called the adjustor, again from Argon Mutual, with a little bit of anger in my voice and she told me to cool myself out. And at that point — this was December 1st, so quite some time after the quake — she indicated to me that it might be possible for me to be reimbursed for my structural engineer's expenses, which is estimated to be anywhere from $2,500 to $3,500, and it might be feasible for me to be reimbursed for the soils test that the structural engineer was recommending which he was saying was anywhere from $2,500 to $4,500. And I said to her, "Might is not going to hack it. I can't have these tests done until I know definitely that you're going to cover me because I can't afford that kind of money for these tests."

So she said that she needed something in writing from my structural engineer before she could validate or verify anything in terms of my coverage. I sent her that last week. I got a call from her today -- actually, she responded back to my call — and has set up a meeting with me on Friday. I asked her if she, at that time, would have specifics for me as to what I would be covered for and I took down the quote because it was such a wonderful one. She said she would have "some definitive guidelines on the possibilities of what I may or may not be covered by." So I said, "Are you going to tell me what you're going to pay for and not pay for?" And she said, "Well, I may have some definitive guidelines for you." So still, two months after the quake, I still have no idea as to what I'm going to be covered for.

The Catch-22 that I find of all of this in terms of giving the committee some guidance in the future about earthquake insurance is that everybody's told me I'm one of the lucky ones, I have a 5 percent deductible. Well, that's $20,000. Twenty thousand dollars out of pocket is a lot of money that I can't afford.

The City is telling me I can't live in the house unless I bring it back up to earthquake code. My structural engineer is estimating that it's going to cost me between $60,000 to $90,000 to bring it up to code.

CHAIRMAN GREEN: Plus the repairs on the house, or is that the overall?

MS. MILLER: The repairs on the house, I already have an estimate. It's somewhere around $20,000 to repair it up to the conditions prior to the quake. So that's the deductible. And then it's $60,000 above that for me to repair it up to the building code requirements. So basically I'm being asked to put $60,000 out of pocket after having put out $2,000 a year for earthquake coverage.

CHAIRMAN GREEN: Okay. Let's bring it into retrospect. The City then is saying when you repair your house you have to bring it up to earthquake standard.

MS. MILLER: That's correct.

CHAIRMAN GREEN: The insurance company is saying they don't cover that part.

MS. MILLER: That's correct.

CHAIRMAN GREEN: I think the key question is was there an exclusion in the contract or the policy you have that says that, that they shouldn't be covering for that phase of the construction?

MS. MILLER: Well, you've asked a seemingly innocent question that has a complex answer to it.

CHAIRMAN GREEN: It's a legal question. Did you have any exclusions that covered that?

MS. MILLER: I currently to date do not have a copy of my policy. I have called my broker and asked for a copy of my policy to be sent to me, because an attorney who is doing some pro bono work in the Marina said that he would look at it for me. I showed him the papers that were sent to me and he said, "This isn't your policy, this is just an indication that you have insurance." And so I have not been able to read the specifics as to what I'm covered because after requesting a copy of my policy, I was not sent one.

CHAIRMAN GREEN: I would ask if you would possibly in the future, as your case develops, that you could share those documents with the committee, because I think that's part of the record that we need. One of the problems we're finding in the various communities is that the city or the counties require the upgrading of the home and then insurance companies on the other side are saying this is not part of the damage and we shouldn't have to pay that. And I think it's a legal question that has to be answered and future legislation has to be directed to that.

MS. MILLER: Yes, I would absolutely recommend that.

CHAIRMAN GREEN: Senator McCorquodale.

SENATOR McCORQUODALE: It seems like this is something that we ought to look at on the — she suffered loss from the earthquake, but from what you're — just getting a rough idea of what you're saying, your biggest loss is going to be caused by the City in having to bring the house up to code, which would not have had any requirement had not the earthquake come along. It seems to me that we've heard a few of those cases in Santa Cruz, but it's interesting to note how much of — get some rough idea of all the earthquake damage, how much of it would be put back on that government added on top of what you're doing. Because from what you're saying, you're going to have to have soils test, you're going to have to have structural tests. That's connected with the earthquake and probably in connection with building the building. Maybe there's nothing you can do on that. You must have a — what do you have? A half million dollar policy but you have a $20,000 deductible?

MS. MILLER: Four hundred thousand.

SENATOR McCORQUODALE: Four hundred thousand. So you probably bought, thinking you were going to well cover yourself.

MS. MILLER: Correct.

SENATOR McCORQUODALE: The truth of the matter is is if you'd only had a $100,000 policy, you'd have been much better off with what your damage was, because with that $20,000 deductible, you've got to do $20,000 worth of work and they're probably not going to allow any credit for the work done for the code work, and if that ends up being $60,000, then you're not covered for that. The real impact on you is going to be some rule that says when the earthquake comes we're going to recapture all the codes that have been adopted since your house was built, which wouldn't have happened if it hadn't been for the earthquake. I doubt if there's anything that the City could just come in and say, okay, you've got to spend $60,000 on your house.

I don't know whether it's the purview of this committee or whether we ought to ask Senator Bergeson to take a look at it from a local government standpoint.

CHAIRMAN GREEN: Well, it could be that it will boil to that, Senator McCorquodale, but right at this point I think this is one of the problems that we have is what the entities, the public entities are causing the policyholder out there.

SENATOR McCORQUODALE: Trying to figure out who it is who's doing what to you.

CHAIRMAN GREEN: Yeah.

MS. MILLER: In fact, you know, I am grateful to the City for imposing some building requirements for my own personal safety as well as for my property value, because I've talked to realtors about selling the house and I can't sell it in the condition that it's in. So I'm in a Catch-22 unless I take a loss and sell it to an investor. I've got to bring it up to the code in order to sell it because nobody will buy property in the Marina now unless it's up to code.

CHAIRMAN GREEN: Well, and then you get into a Catch-22 with energy even because you have to put different insulation in today than you had to do 20 years ago. So that's part of your building costs and that's some of the factors we're talking about.

MS. MILLER: Right.

CHAIRMAN GREEN: If it's a public building or a business, they would have to bring it up to the handicapped as far as the restrooms were concerned and stuff, and until they need a building permit, the local entity cannot put those conditions in place. So it's a way to bring the codes in not just safety but all the other things too. And so it's costing the policyholder double, and this is what somebody has to look at and I think a report will be going to Bergeson and the Local Government Committee of what our findings are here in this committee.

How much was your policy cost per year?

MS. MILLER: A little over $2,000 a year.

CHAIRMAN GREEN: So your cost was $2,000, and that was not very affordable, especially for what it boils down to what you're getting in coverage. How long had the policy run?

MS. MILLER: I've owned the property for four years and we've maintained it for those four years, and I understand that they — the previous owner had also had the policy for quite a number of years as well.

CHAIRMAN GREEN: Now, you say you're having to have temporary housing. What does that cost to you?

MS. MILLER: Well, right now I've been living with friends and splitting their mortgage payments with them, but it's a less than satisfactory situation. I'm an independent consultant and I, in essence, ran my business out of my home. I had a computer and file cabinets. So I've not been able to really run my business the last two months because I just haven't had the facilities to run it as well as the fact that...

CHAIRMAN GREEN: So it's not just housing it's business also.

MS. MILLER: I've been concentrating on this — on the issues. Beyond that, I also had a rental unit on the property and so I've lost my rental income.

CHAIRMAN GREEN: So it puts a heavy load on you.

MS. MILLER: Yeah. It's been quite a burden.

CHAIRMAN GREEN: Well, I appreciate you coming out today and I appreciate your telling of your story because we need all of this documented with the committee, and any paperwork you can get from the insurance company I wish you'd share with the committee and let us know how your case goes along.

MS. MILLER: Thank you. Again, I appreciate you holding these hearings, Senator.

CHAIRMAN GREEN: Thank you very much. Okay, the next is Paul Cobb from Oakland.

MR. PAUL COBB: Senator Green, I want to thank you for the invitation to come and testify. I've had some of the same problems as the previous homeowner. I also want to thank your staff person, Eileen Carroll, because I, quite frankly, wasn't coming until I talked to her on the phone yesterday. This whole situation has made me frightened, probably for the first time in my life. Last night I went before the Oakland City Council to ask for help to go with me to FEMA, because there seems to be some sort of price you pay for speaking out. I live three blocks from the collapsed structure in Cypress and it was probably the loudest, most frightening sound I've ever heard in my life and our neighborhood has been crawling with the media ever since. And so, I mean, the odds were one to one that you were going to get interviewed or asked a question by somebody because there were so many people there.

When I went down to FEMA they recognized me and thought that I really didn't have a legitimate claim, that I was just complaining.

CHAIRMAN GREEN: Well, let me, at this point, say to you, if there is any repercussions to you for your testimony here today, this committee will do everything legislative it can do to protect you and keep your integrity. We don't believe that — we want to hear the true story, we want to hear the accurate story from everyone — both sides — insurance companies as well as the homeowners. And if anyone is using intimidation out there to intimidate what is in this hearing, we can't give you total immunity but we can sure protect you from what you say.

MR. COBB: Yeah, well, I had a phone call from my insurance company an hour before coming, and I've got more help out of them in the last 24 hours than I have...(laughter) I don't know what that means. I just hope you can hold the hearing for about a week. (Laughter.)

CHAIRMAN GREEN: Well, let me say this. This hearing today is just here today, but what this committee is doing is going to be lasting for longer than a week. And so maybe that's why you're getting some action out of your insurance company. Let's hope so. Because they shouldn't have the threat of this type of hearing to do the job for their policyholders because they're selling a — you're buying a product and they should really do what's right.

MR. COBB: Well, I see the list of questions that you and your office sent and I'll answer very briefly and then I would like to close with a quick recommendation. It says, "Do you have earthquake insurance?" Yes. And my insurer is Triple A. They ought to change their name to Triple F because, quite frankly, they do not live up to their advertisement on quick roadside service for your auto; they really don't have the same response mentality for the home. And I think they — we have an auto insurance policy with them and they've done — I've been totally satisfied with their auto insurance over the last 15 years. So I'm not here to trash them per se, but I just think that they have not lived up to their reputation in the auto insurance business. They surely don't have the speedy response, and I can understand that because of the mass devastation.

I understood that there was the deductible but what I didn't understand and what was so difficult was the attitude. It was almost as if you had to hire a lawyer and an engineer and an architect just to have a conversation about the explanation of the policy. The fine print, there ought to be some legislation that literally changes the whole thing about fine print. It ought to be bold print, sort of like some of the prompting notes that you and your colleages have. That's the way the policies ought to be literally written, in that large of language and with the emphasis on that kind of explanation.

The customer orientation is not there. It's as if you have — you feel like you're accused of a crime and you have to prove that you didn't cause the earthquake just to — that was my experience with the person, and which I won't mention the name in public but I'd be happy to give you the name of the person that I've been dealing with.

CHAIRMAN GREEN: If you would do that for the committee record.

MR. COBB: Yes. I don't know if it's appropriate or proper...

CHAIRMAN GREEN: It really isn't. We're not out to make public all of the — but in private, for our record, those names we should have.

MR. COBB: The damage estimates by the insurance company have swung now drastically. At first it was — I have a $12,000 deductible, which is 10 percent, and the first estimate was $14,000. Now, this morning, just to repair the chimney, which I had to get a video camera to show them yesterday — after they looked at the video camera, the video tape — which I'd be happy to send to you -- they realized $20,000 just for the chimney and the cavity of the chimney alone, which means that now the estimate has soared to $50,000. But it doesn't matter whether it's 50, 60, or 70, if you don't have the deductible — but it was the attitude to get them. I had to go out and hire and pay for an additional inspection with a video camera to show them that I was not getting a proper inspection.

CHAIRMAN GREEN: Who did your inspection at first? Did you have a city inspector?

MR. COBB: You want me to name the company?

CHAIRMAN GREEN: It was a consulting company came in.

MR. COBB: It was a consulting company that Triple A had hired. A guy came to the door with a Polaroid camera and said — this is an engineer firm — said I'm only going to be here 10 or 15 minutes, and it takes that long just to get into the attic, then you have to crawl underneath for the foundation. This is a Victorian home. I mean, our neighborhood has been on television, you know, all those Victorians adjacent to the freeway. The house is two-story and it takes 15 minutes just to walk around it.

CHAIRMAN GREEN: So that was an appraiser from the insurance company.

MR. COBB: The insurance company had sent this consulting engineering firm and I asked him why was he doing that. He said, "Well, engineers are busy right now. We're getting so many calls" — and that was understandable — and I said, "Well, you can't do me justice with an analysis" — in my living room there's plaster literally falling off the walls. There's separation of the plaster in the walls so you can run your hand through it, and he's just going to take a few pictures, I guess.

But Triple A had sent someone out within four days after the earthquake to take photographs of the -- I guess to prove the house was still there or not there, whatever, and he's coming behind them to do the same thing. And then they want to send another engineer who's going to just come and take pictures. I have taken the pictures myself. I said, "I'll supply you with photographs."

CHAIRMAN GREEN: How about the aftershocks? What did they tell you about those?

MR. COBB: The — oh, yes. That was the discussion I had with them yesterday. After I showed them the film he said, "Well, that's probably the aftershock." And I said, "Well, why are you emphasizing the word aftershock so much?" He said, "Well, because anything that happens after the aftershock we're not liable for." I said, "Well, since your" — he answered that — that's one question he answered with great rapidity. He knew the answer.

SENATOR McCORQUODALE: The 7.1 that we just had is probably the aftershock from the

1910. (Laughter.)

MR. COBB: Yeah, that's right. I like that. I'm going to have to use that one. That's a good one. Yeah, well, I'm still in — the aftershock is going on when you see the bill and when you try to — that's the real aftershock. And for us, the homeowners, everybody keeps waiting for the big one? Well, we've had it when it comes to our pocketbook. The big one has hit.

And the other problem is how do you get the deductible money? The insurance company, it seems to me — and I would appeal to you, Senator Green, and I don't know how to pronounce your name...

CHAIRMAN GREEN: McCorquodale.

MR. COBB: McCorquodale.

SENATOR NIELSEN: And Nielsen.

MR. COBB: Okay, and Senator Nielsen. I appeal to you to come up with some legislation that in a government declared emergency — when the Governor declared this a disaster or the President declares this a disaster area, that the insurance company ought to broker some kind of large scale financing for everybody where they automatically pay you immediately to fix a government declared disaster, and <u>then</u> let the homeowner acquire their financing through the insurance company and the banks' deal. Maybe there ought to be some kind of enabling legislation that arranges that, because you already have enough headache trying to arrange for emergency shelter, and if you lived in our neighborhood...

CHAIRMAN GREEN: I think that's coming through loud and clear is that the bureaucracy — we have some companies that are paying on a two-party check; in other words, making the homeowner and also his lending company a party to the check, and when they get down to pay the contractor, they can't sign the check because the lending agency won't sign off on it. So here's a check sitting there — yes, they might have had the check issued, but the check's no good to them because they can't pay the bill because the lending institution is not paying off. So yes, some of these hearings we've uncovered some of these things, and what legislation is done in the future, who knows?

I think one of the key questions that I'm hearing from you is how were you treated in Oakland compared to the people here in San Francisco and also like Santa Cruz? Of course, you might not know about the Santa Cruz area. We've had testimony there. But you're from Oakland, how were the people in the Marina District treated compared to the people in Oakland by the companies?

MR. COBB: We are going to change our name to the West Oakland Marina District. (Laughter.) I'm serious. I don't envy the Marina District. You know, it's not a time to have — I don't think there's a pecking order of devastation, but I think that the Marina District got a lot of positive response. I don't know all the reasons. I think it's because of being in San Francisco, which is media -- it has a lot of media headquarters and so forth. I think that was important. But we already -- in my neighborhood we live in a red-lined area which is difficult to get a loan if there wasn't an earthquake. You almost have to be a millionaire just to qualify for financing, and this is even going to further...

CHAIRMAN GREEN: Or does it go into what we term as management? There's probably a different director in Oakland than there is here in San Francisco and in Santa Cruz and it depends on how he did their job for that particular company — or she — if they did a good job for their policyholder on the company side. So it could very well be in management from those particular companies.

MR. COBB: Well, I had told your assistant — I think Eileen Carroll — over the phone that I thought that there ought to be legislation required some kind of sensitivity training. And I know from looking at television programs in the Watsonville area, where there are a lot of Hispanic population and the language problem...(tape turned)...I really do think there ought to be some direction. If you can legislatively regulate that — I don't know if you can do that — but I think that's a major problem. I have been a victim of it.

And what really frightened me about my insurance company, by them being in the auto business, and when I saw the news about how the auto insurance companies were taking on this Insurance Commissioner about 103, I said, well, I'd better not raise any questions because these people don't want to pay for anything, and if I dare join any organization to protest, then I see what their reaction is going to be. They'll take me to the Supreme Court to challenge me. So I don't have a chance with Triple A going in the homeowner business, insurance business. So it was that fear and pressure which I fear in speaking out that they will retaliate the same way they're doing on the Prop. 103. If they don't like what you're doing, they'll come and get you.

CHAIRMAN GREEN: Let us know, and as I say, we'll see what we can do as far as giving you immunity. Appreciate what you've said today. Senator McCorquodale or Senator Nielsen, are there any questions you'd like to ask the witness? Okay. But I appreciate your coming forth today and giving us your problem, and I would ask of you also, as your case goes along, keep our staff — Eileen Carroll or whoever you've been contacting — appraised of your issue as it goes along.

SENATOR McCORQUODALE: Let me ask, what was your — how much was your policy? What was the limit on your policy?

MR. COBB: Well, what is it? If I have to pay $12,000 — the first $12,300 and that's 10 percent...

CHAIRMAN GREEN: That's $120,000.

MR. COBB: But if I go to get a loan, it's not appraised at that value. So it's interesting. Maybe the insurance companies' appraisals ought to be used by S&L's so we can maybe qualify for a loan. But they can tell you the house is worth a lot when they want to get the deductible, but if you take that same appraisal to the S&L to borrow money to fix it, they won't appraise it at the same amount. So that's the other conflict we have.

And now, when I found out that I might have to be moved out — and I'm thankful that we didn't have a lot of rain, because with the big cavity in my roof, if it had rained on it, that damaged brick that we discovered would have — teetering to crash right into our bedroom. And so they are rushing now to get someone to fix the house today or tomorrow, but they told me to be on alert because I might have to move out. And they should have discovered this. Their engineer, I don't see how someone could be a licensed engineer, crawl up there and not take a photograph of that. They took a photograph of everything else but the most damaging problem.

CHAIRMAN GREEN: Okay. Well, thank you very much.

MR. COBB: Thank you.

CHAIRMAN GREEN: Thanks for coming out today. Next we have Allan Goodman from San Francisco in the Marina District.

MR. ALLAN GOODMAN: Probably, Senator Green, and the rest of the panel, we have an apartment building. This is probably a little different situation.

CHAIRMAN GREEN: You own the apartment building?

MR. GOODMAN: Yes. Eighteen apartment building in Marina.

CHAIRMAN GREEN: How many units?

MR. GOODMAN: Eighteen.

CHAIRMAN GREEN: Eighteen. In other words, the two of you together here.

MR. GOODMAN: Right. And we're with I believe a pretty big company. This is Associated International Insurance Company out of Los Angeles and they have about an A rating.

CHAIRMAN GREEN: And the company is what company?

MR. GOODMAN: Pardon?

CHAIRMAN GREEN: What's the company? The insurance company.

MR. GOODMAN: Associated International. We carried earthquake insurance, oh, for many, many years. I've frankly insisted on it. And I've always dealt with A rated companies — A plus preferably. And this is one of the questions I always query my carrier, my agent, because I think it's important.

Also, they have what you call an admitted company where you pay a premium and they have like a fund like the FDIC in case they can't pay.

What I'm seeing here is some of these other people who are having problems, so far we haven't had any. It's very early for us. They have approved the structural engineer, saw the engineer, and the contractor, and right now we have security, our doors, garage door and so forth, and we are shored up as per the City's wishes.

One thing, though, our broker said that he felt we would need a private adjustor and we weren't too happy with that. In fact, I think his rate was very exhorbitant. So we decided we'd better turn him over to our attorney, who, fortunately, we have a good attorney. He's senior partner with a very prominent firm, plus he's a litigation — or a trial attorney and he has represented insurance companies, so he understands the fine print. Plus I do go through the fine print myself.

CHAIRMAN GREEN: Of your 18 units, did they have to vacate the premises or are they still in the premises?

MR. GOODMAN: They're vacated.

CHAIRMAN GREEN: And how about the company as far as the relocation costs? Was that in your policy? In other words, the interim housing for them?

MR. GOODMAN: Well, I guess I fouled up in relocation because I have the homeowners but I didn't put the quake rider. That was probably my fault. So actually, FEMA came up with — they gave so much, it was helpful, and plus whoever stays in a motel they give it as half rate. So I'm not too pressed for that. We also have loss of rents, which is — I think people should, if they have rentals, probably should have that — loss of rents. And also, very important is the cost replacement endorsement which is supposed to be new for old and you have more power to bargain with rather than taking a depreciated basis.

CHAIRMAN GREEN: So you really don't have a horror story at this time with your company. It's pretty well handled your situation. What is your policy limit?

MR. GOODMAN: The limit is $3.3 million.

CHAIRMAN GREEN: $3.3 million and 10 percent or 5 percent policy?

MR. GOODMAN: The problem is is it was a blanket. See, we owned another building and then it was subsequently sold. They would only write us a blanket. I was able to get a good price on that. Something like $8.3 million. Now, we've separated. Through this other company — ironically, it would have been 5 percent deductible in the Marina for $2,000 because they feel the wood frame has soil damage, but they have not — you know, we're not aware of a soil problem. And the other building, which is located in Pacific Heights, there's about a 10 percent deductible as a class C building. So that would have cost 22 — or a total of about $25,000. So I decided to take a blanket, a 3.3 covering either/or or both and that with a 7½ percent deductible. But even then, that's sizable. We're talking $2½ million.

CHAIRMAN GREEN: Now, when you were dealing with your agent purchasing that insurance, did he do a good job explaining what the coverage was, how much it cost, and what they would be covering?

MR. GOODMAN: Well, our broker — I would say no. I've had to — I've had problems with him. In fact, I had to insist on cost replacement endorsement. He said, "Well, it's in there." I said, "It's not in there. You show me where it's at." And I finally got what I wanted. Because without that cost replacement endorsement, they take it on a depreciated basis — maybe 30 percent or more, especially a 60-year-old building. So I had to call him on that. I had to call on making sure I got the binders and on time and that I was covered. I'm still on his tail to do that. You have to. You can't say here it is. But he did give us this private adjustor. We have been happy with him. A lot of talk but nothing else. So we kind of sent him to our attorney for a little treatment and he's kind of shaped up and we rewrote the contract or we were going to get rid of him.

CHAIRMAN GREEN: I see. Have you heard from the City yet what your upgrading will be over and above — in other words, are you going to have to upgrade the building to current earthquake standards?

MR. GOODMAN: Well, I think that's — the City is going to demand the standards. I don't think they're going to let you build to the old standards. Though I think there was something in the paper about the 62 and according to our structural engineer that'd be about three-quarters of the present standards. I was talking to the engineer this morning and he said even those standards are not enough, not with the type of soil we have, and he's talking about a very rich type foundation or a grid, or kind of a grid type foundation and so forth because he says he doesn't feel, in case of a real major one, that would be enough. Well, he's talking about water at eight feet and then you have this very loose type of sand.

CHAIRMAN GREEN: Like jello.

MR. GOODMAN: Yeah. Liquefaction goes to liquefaction.

CHAIRMAN GREEN: So you don't have a price yet as far as the City and the upgrading, so you really don't know where you're at there?

MR. GOODMAN: No, it's too early for this. Right now the City has demanded the shoring and we have excellent shoring — it's really a professional job. This is preliminary. I think the main thing is to start at the bottom and work up rather than — some of them are starting at the top working down. I don't think that — but what I've seen in terms of your contractors here and so forth — you have a section down — some of the contractors gone around — people, you know, are kind of desperate if the building is about to collapse and anybody comes along — it's poor work that they're doing and the charge is very exhorbitant.

CHAIRMAN GREEN: Okay, that was going to be my question, are you having any problem with your contractors...

MR. GOODMAN: No.

CHAIRMAN GREEN: ...because in some of these hearings, we've been hearing about some of the contractors not doing the kind of job they should be doing.

MR. GOODMAN: We have an excellent contractor. Excellent.

CHAIRMAN GREEN: So you yourself. How about the other witnesses? Have you got good contractors or are they...

MR. COBB: No.

CHAIRMAN GREEN: You've had a bad one?

MS. MILLER: I've received estimates from two contractors, and a friend of the family who lives in Novato asked to see those estimates and he said he thought I was being charged at least $7,000 to $10,000 more than was the appropriate going rate.

CHAIRMAN GREEN: I see. How about you?

MR. COBB: No. And in fact, because of the media attention really hurt us, those houses so close to the freeway — there were pickup trucks of people just coming by putting 3x5 cards in our mail slot. So if they saw an insurance car or someone go there, they would — there were so many people crawling through the neighborhood that you would get the impression that the insurance company had just sent this person and they would ask you for $500 cash or whatever and they could get started immediately. And so in that sense publicity hurt us.

So I would like to ask you a question that I heard you ask her in the first testimony, and that is if it's a legal question between — whether the City's codes requirements you raised, the concern about the legality on that? Well, it seems to me it's a simple concept of law and order. If the City is a legal entity of the state and the code is a law and if the insurance company says they're not going to bring it up to code, then why should they be sanctioned as an insurance company if they are not going to obey the law? And if you are not going to require them to do that, aren't you contributing to an illegal act, to deliberately not obey the law?

CHAIRMAN GREEN: Well, I wouldn't phrase it just that way...(laughter)

MR. COBB: Well, but the insurance guy told me — he was very quick to tell me, almost with rote memory, of all the things they could not do. So when you asked him what you could do he got foggy, he'd have to go back and do research, or I would have to supply documentation and do some research on my own.

CHAIRMAN GREEN: All right. Any questions? Thank you very much, all of you, for coming today. Be in touch with this committee because we're here to help. Thank you.

Okay, we have then — we go into California Grocers Association, Don Beaver, who is the President.

MR. DON BEAVER: Mr. Chairman, members of the Subcommittee, my name is Don Beaver and I'm President of the California Grocers Association. We represent nearly 8,000 retail grocers throughout the state, including all the supermarkets, independent chains, convenient stores, mom and pops, wholesale grocery houses, suppliers, and brokers.

I want to thank you for giving us the opportunity to be here today and present our remarks. As an industry, we've spent many hours in developing emergency preparedness plans in the state for the grocery industry to protect their employees, their physical plants, and to be ready to be back in business as soon as possible to distribute food and water and other necessities as needed, and the industry did do an excellent job in donating millions of dollars worth of those products.

We would like to be able to respond to your list of questions that you had put out. Unfortunately, we can't get — the majority of the industry cannot get earthquake insurance, at least in the areas where there are earthquakes. The problem is really quite simple: The availability of the earthquake insurance is woefully inadequate and in rare instances where insurance is available, the premiums and the deductibles are certainly not affordable.

Homeowners can get earthquake insurance, grocers can't. We can get tornado and hurricane insurance, but we still can't get the earthquake insurance. Homeowners and retailers used to be subject to flood and not be able to get insurance but now we can get insurance on floods. And that's only after the federal government has finally stepped in to provide it.

Now, homeowners can get earthquake insurance, but we're still without it. Of course, the solution to this dilemma is why we're here today. Insurance companies that do offer earthquake insurance, they offer it on a very limited amount. Companies may put out $2 million worth of earthquake insurance available and that can be snapped up by one company and the rest of the industries around that deal with that company cannot get earthquake insurance.

The bottom line is in the past that most policies have — that are written have specific exclusions for earthquakes, and there used to be exclusions for the flood, but again, that flood insurance is now available because it is on a pooling with the federal government.

We'd like to offer just some recommendations maybe for the committee. I do have with me Don Kaplan who also wants to make some comments. He is a retailer and he wants to talk about his insurance problems with you on specifics.

We'd like to suggest somehow to work with the federal government if it's necessary. We're not trying to say move the insurance industry out of coverage for business and homeowners. Our position has been though if the industry cannot provide coverage for business and homeowners, then I think it has to be the responsibility of government, either federal or by state government. There's a variation that — excuse me. I wanted to bring your attention to that map on the back that shows you that this is not a California problem. If you look at that map where earthquakes have occurred — now, unfortunately, I could only get a map that's been updated through 1970, but you can see on there that there's as many earthquakes east of the Mississippi as they are west of the Mississippi. So it is a national problem, not just a California or a Western United States problem. And we feel very strong that the federal government ought to do what they do with flood insurance if the insurance industry is unable, for one reason or another, to provide that kind of coverage.

We'd like to see in that line the Legislature introduce a concurrent resolution calling on the federal government to implement an earthquake insurance program; again, if it cannot be done on an insurance basis. We certainly can use organizations such as yourselves as the grass roots to try to get Congress to act. Should the federal government not be responsive, then sponsor legislation at least to get a study going in California on how government and the insurance industry can provide insurance. Business — at least the grocery industry in California — is willing to pay a premium for earthquake insurance. It's just a matter it's not available at any price. But we certainly feel it's got to be somewhat within a reasonable deductible and a reasonable premium. We're not asking anyone to come in and bail us out. We're willing to pay for it but it's got to be available before we can do that.

We'd like to see, you know, the state look in some kind of a study on the risk pooling, that the build-up of pool somehow either through premiums on current policies and then businesses and homeowners can buy policies direct that would be self — at least funding for any kind of a major disaster.

And these are only conceptual ideas and they've got to be fleshed out by the experts in the field. But just as a reminder that we feel that there can be some creative solutions and they can and need to be found. Business in California, again, are willing to pay a reasonable premium for earthquake insurance and if the insurance industry is unable to supply it, then we feel very strongly that government has got to step in and make it available in some form to the industry. I know that the agents and brokers and Department of Insurance will be speaking later today, and certainly our industry is willing to help to try to develop some kind of a program that will cover businesses.

Thank you.

CHAIRMAN GREEN: Thank you. Any questions? Thank you very much for coming today. All right, Don Kaplan, President of Bonfare Markets, Inc.

MR. DON KAPLAN: Senators, I'm here in two capacities: I'm President of Bonfare Markets, which is a chain of franchise small grocery stores. Each store is owned by a family who has its whole life and energies tied up in one store. I'm also here as Chairman of the California Convenience and Small Store Association speaking on behalf of that association.

CHAIRMAN GREEN: Pictures are always worth a thousand words and they really...

MR. KAPLAN: I thought I'd share with you those pictures. That was taken at our store just outside the villages in Mr. McCorquodale's district in San Jose. Our stores in San Jose suffered the most damage. Some damage spread up through Milpitas and Fremont store and along the Bay and Oakland also. An earthquake hits, you never know which side of the street it's going to attack, and it's a strang thing. There's no explanation of it.

In 22 years of my building this company, the one thing that scared me the most is an earthquake. Everything else I'm insured for, I'm prepared for, I pay for that coverage, but if a major earthquake occurs — and this was not the major earthquake — I could be wiped out. Not only me but every member of my firm. Every store could not recover from the damage. Luckily — if we can call it that — this earthquake caused merchandise damage, the bulk of it in bottles like beer, wine, liquor, mayonnaise — anything coming in a bottle — and that which happened to be close to the bottles when it hit. We had one store that had a great deal of bottles over an ice cream freezer. When that happened, they just hit each other and the ice cream melted and the power went off and everything went in. So it's a big mess to clean up. All our families just got together and for days worked at cleaning it up.

CHAIRMAN GREEN: I found two years ago, or even going a little further back, the Coalinga quake and also the Whittier quake, that 25 percent of the small businesses after the quake did not survive. What — in other words, you're a small businessman.

MR. KAPLAN: Yes.

CHAIRMAN GREEN: What would your suggestion be so that what we could do — I guess most of the problem is why you're out of business because you have a cash flow problem.

MR. KAPLAN: Yes.

CHAIRMAN GREEN: When that's interrupted your expenses continue, but yet, you haven't any money to pay for it for the time you're down. Would that be the best thing to do for small business is provide a cash flow while they're down?

MR. KAPLAN: That would be of tremendous help but also the replacement of the inventory, or should we have a big one, which is projected on the Hayward fault — there's a 36 percent chance that in the next 30 years there'll be a 7.5 on Hayward, and from what the experts say, that'll be a more serious rubbing effect than on the San Andreas and all my stores would go then; in fact, including my house. So I wouldn't have much to worry about as far as what I would put together.

But I did try, Senator, to answer your question, the letter I gave you a copy of was from our broker. That broker handles the Northern California Grocers Association insurance. I could not get earthquake insurance on physical damage — building or equipment — or inventory. So I asked him if I could possibly get it on business interruption. As you probably know, business interruption is covered only if the loss is covered. And the answer was no. We have no provision for earthquake business interruption insurance, because as you say, a good risk, a big risk is the time the store is down.

This quake, although it was very severe, and especially for those people here that got hurt personally or with their homes, it was still minor compared to what's going to happen or can happen. And we suffered merchandise damage. Mr. Beaver tried to get relaxation of the ABC laws so that suppliers, brewers and so on could replace merchandise should they wish to do so, and they fought the relaxation of those laws, hiding behind the fact that it's against the law to give anything away free. So the small merchant took it. The major chains got hurt too, but with the major chains you have a diversity of risk. When you own one little store 2,500 feet and everything is in it, if that collapses you've lost it all, you've got no diversity of risk at all.

What I had thought of, and it's no magic, is that if every policyholder in the state, preferably in the nation, were assessed a dollar — maybe it's 70 cents, maybe it's $1.20 — and that fund was allowed to build up — and we probably would have several years without any major claims — the interest on it alone would be so huge that if we could keep that fund separate, that could be used to provide or subsidize, if you will, any insurance the insurance industry would like to provide. And if they don't like to provide it, if they don't want the risk, because we understand one of these quakes could wipe out a company no matter what size it is, then maybe the government itself would use this fund. But it would be something that everyone would pay for, and those of us that are in the business would pay a regular premium for a deductible that would be reasonable.

My stores, as small as they are, are insured for $150,000 each. We can't buy any insurance; I don't have much choice. But I was prepared and I have been each and every year for the last nine years. I had insurance about nine years ago and then it went away, it disappeared. But I'd be willing to pay, even with a deductible of $15,000 which means you're paying for nothing unless you get a real bad one and it's even worth it then, but the premiums are high, the deductible is high — both of those have to be corrected — but it isn't available anyway. It's not even a decision whether I want to do it or not. We are willing to do it. But if we could spread the risk over all policyholders, then I think residences as well as businesses will not be in this terrible situation, and it really is the only risk other than insurrection or war that is not covered. Everything else in an all-risk policy such as we have is covered except earthquake, flood, and as Mr. Beaver pointed out, flood is now protected.

CHAIRMAN GREEN: So you have an all-risk policy but with the exclusion of earthquake.

MR. KAPLAN: That's correct. It specifically excludes earthquake and flood. In the Bay Area, flood is not a problem so we don't have the problem that they would have in the valley. But there is government federal insurance to take care of the flood. There is absolutely nothing to take place — to take care of the earthquake risk.

The pictures I've given you are just of one store. I stand ready to help the committee. I stand ready to spend as much time as needed. Mr. Beaver and his association — I'm part of his association - would also like to help in any way we can. It's true, a lot of people lost their lives and lost their houses and it's probably more serious than losing a business, but still, if you work 15, 20 years in the business and lose everything, I don't know how much you can differentiate between the two losses.

If you have any questions of me, I'd be glad to answer them.

CHAIRMAN GREEN: I don't have any questions. I think just a little matter of explanation. I think basically what you're requesting is what the committee is attempting to do. All of us feel there should be a risk pool and that we should make insurance affordable with the lesser amount of deductible. And that's what we'll probably be coming up with like in February. So you'll see some legislation this year on just what you're asking. And we're hoping that these committees, these committee meetings and the hearings that we've been holding throughout the state for basically the last two years are now generating enough facts and figures for the underwriting, and then to put a program in place in the State of California.

The testimony saying let's do a resolution in joining Congress and do something on the federal level, I'm not against that and we might do that. However, I think California needs to stand on its own, too. So we cannot afford to sit and wait for the federal government; we have to act in the State of California to protect our business and our homeowners because this is a family affair we have here. So that's what this committee is attempting to do.

MR. KAPLAN: Thank you very much for your time, Senator. Really appreciate it.

CHAIRMAN GREEN: Okay, on this phase so far do we have anyone from the public that would like to speak at this given time? Anyone in the audience? Public, private, whatever.

SENATOR McCORQUODALE: Senator Green, I just thought that since this seems to be a market here, I think we ought to...(tape turned)...and if we just keep it quiet that it's going to have a 20 percent deductible of that amount, he'll never know that he won't get a nickle paid off on it.

CHAIRMAN GREEN: Well, that's...

SENATOR McCORQUODALE: (Inaudible.)

CHAIRMAN GREEN: That's some of the problem that we've had, and we've experienced with the committee in testimony is that when people buy earthquake insurance, there's not enough education to the people to know what they're buying. And in your case, it's not even there to buy. So that's a different situation of what we find with some of the homeowners is that they buy a product and they really don't know the product they're buying. It is a very comparative view in the hearings we've been holding so far is that it's not totally across the whole spectrum of companies, but it's across the spectrum of certain ones of the companies out there guilty of that. And some of the companies do a fine job and some of the companies do a very bad job. And why does that happen? Well, that's then maybe the Department of Insurance, maybe it's legislation. Maybe we have to control the companies a little more so that they'll be universal throughout the State of California and not territorial in aspect.

And we're seeing, for instance, in the City of Santa Cruz, they dropped their building codes, they allowed tents down there for the businesses to operate in. The City went gung ho to help the business person that was wiped out. We're seeing here in San Francisco testimony that the City Hall is not helping those people quite as much in the Marina District as they did in Santa Cruz and smaller cities. So they operate quicker and faster. So we can't put fault. We can just say this is a problem down there after a devastating thing like an earthquake. The City of Whittier, a small city, did not allow those businesses to operate in a tent, for instance. That was innovative by Santa Cruz. I thought that was a terrific thing Santa Cruz did. But there are 25 percent of the businesses failed in Whittier now because of the earthquake. Cash flow.

SENATOR McCORQUODALE: I would just like to add something positive. Even though these folks were, it was pointed out, not even able to get insurance, earthquake insurance — a lot of people like Mr. Kaplan suffered a lot of loss — the grocers responded tremendously just in the days after the earthquake, because a lot of the food that fell on the floor and splattered on it couldn't be sold and if it hadn't been for their willingness to help get the food moved to places like Watsonville and Santa Cruz, Los Gatos, other places, there would never have been any way that people could have had adequate food.

CHAIRMAN GREEN: Not only did they furnish the product, but they furnished the transportation to get it there, and I think that's outstanding.

SENATOR NIELSEN: Not only that but all over the state stores cooperated. You are indeed to be commended.

CHAIRMAN GREEN: Thank you so much for being here today and congratulations on the fine job you did getting the food to those homeless people during that period of time.

We have next local insurance marketplace and it's Scott Hague for California Insurance & Associates from San Francisco. Now, they're independent insurance agents and brokers of California.

MR. SCOTT HAGUE: Thank you. My name is Scott Hague. I'm the owner of the Cal Insurance & Associates. I have an office in San Francisco as well as an office in Redwood City. I also am the President of an organization called the Small Business Network which is thirteen associations in San Francisco representing about 11,000 businesses. And I'm on the Small Business Advisory Commission. So I do feel I have a fair amount of knowledge as far as the impact on small businesses in San Francisco regarding the quake.

As far as our agency, and it's my understanding that the direction — what I propose to provide to you is information about what our agency did and what the companies did, what some of the problems were, and that's the direction that I wanted to cover.

CHAIRMAN GREEN: You write small businesses though and not homeowners.

MR. HAGUE: Yes. Well, we write both. Our agency represents approximately ten insurance companies. We have in the personal lines homeowners/auto area. We represent about 3,000 customers. In commercial lines about a thousand small businesses. So we do have both the personal and the commercial lines.

CHAIRMAN GREEN: And do you offer earthquake insurance?

MR. HAGUE: Yes, we do. As far as the earthquake insurance is concerned, all of our clients -- of course it is required on residential to make an earthquake offer to the clients and we do that and give an earthquake projection for them if it is determined that the client does not want it. And that's required by our insurance companies. In the commercial lines we do the same thing, although that is not formally required.

CHAIRMAN GREEN: Let me question on that, if you would, and I'm sorry to break in but at these hearings you get a thought in the head. By law, you must offer earthquake insurance to homeowners.

MR. HAGUE: Yes.

CHAIRMAN GREEN: And also by the same law you have to offer it when they buy and then a restructuring or the second year. Then by law you don't have to offer it after that, the same person?

MR. HAGUE: It's the initial — when the company initially takes on the coverage, they have to make that offer.

CHAIRMAN GREEN: But, for instance, they buy it at that given time.

MR. HAGUE: Yes.

CHAIRMAN GREEN: You don't have to go and contract with that person by law for a two-year period?

MR. HAGUE: I apologize, I...

CHAIRMAN GREEN: Or can you cancel after the second year?

MR. HAGUE: Well, they can take it off at any point if they don't want the coverage. They only have to make the offer the first year.

CHAIRMAN GREEN: As you at the company though, if they purchase and then you decide you want to slow down on your insurance coverage, you can say then not reinsure that person after the second year.

MR. HAGUE: The company can't make that choice. The insurer could, but the company can't.

CHAIRMAN GREEN: Thank you, that's clear.

MR. HAGUE: I'm sorry. As far as our broker business, approximately 20 percent — and I'm using rough numbers but eyeballing it — approximately 20 percent of our personal clients' homeowners buyer policies have earthquake insurance. On the commercial side it's significantly less. I would estimate under 10 percent of our clients have purchased the earthquake insurance.

As far as our response to the earthquake, and a little background, we, with the numbers of clients that we had, we submitted approximately 70 claims to our insurance companies, both personal and commercial. Our directives from our insurance companies was anyone that had a claim, whether it was covered or not, that was not our determination and we did not make that determination. Every claim was filed with the insurance company for their review. Of the claims that we filed that clearly had earthquake insurance, there was approximately 20 to 25 of our accounts that had earthquake insurance clearly spelled out in their policies.

As far as an agency, our response, we did open immediately the next day (that being Wednesday) after the earthquake and our response was immediately to put together a letter to all of our insureds, whether they were in an earthquake area or not, indicating that we were obviously concerned about their situation but asking that all damage be reported to us immediately so that we could forward it on to their company. We also tried to provide the information that we could obtain regarding the FEMA loans. We recommended that they consult a licensed contractor and gave some of the builders' exchange numbers around the Bay Area for them to contact. We then identified zip codes that would be in earthquake areas and contacted every one of our clients in those particular zip codes to try to determine who had problems, whether they were insured with earthquake or not.

We found that the majority of the claims that we submitted were pulled out of our system by us rather than the client contacting us. So we were there before they got to us, understandably so. Their first concern was not submitting a claim. Their first concern was taking care of the immediate family.

We also, in the days that followed, acted as a clearinghouse of information — this coordinated with my small business efforts — but we continued to update them on funds that were available from both the federal, state, and local basis. If there were in fact funds available for our businesses, we gave them information regarding tax considerations and things like that. We got involved in setting up alternate delivery times for some of our insureds, coordinating to try to break — relieve the congestion in various areas around the city.

We put together a trauma seminar, which I did through the chamber of commerce and the small business network, to advise small business clients about the effects on their employees and themselves on earthquake.

One of the major problems that occurred was the lack of business where there was no physical damage, but because of the earthquake and the message that was getting out in the media, I individually, and a number of people in the agency made every effort to get out into the media and encourage people to get out and shop in their local areas because that, quite frankly, was where most of the economic loss was. It was the Marina District where the customers weren't coming in. It was Fisherman's Wharf where there were no customers but there was no damage.

We also took the names of — during the time that the moratorium was on, we took the names of all clients that called in and wanted earthquake insurance, and we have subsequently followed up with those people when the moratorium was pulled up — pulled off to see if they were interested in purchasing earthquake insurance. We've done this for about the last 5 or 6 years and interestingly enough, we have never had more than a 10 percent response in actually effectuating the insurance of people that have called and initially after the quake ask for it when the initial shock has gone passed. Most of the people that we have called back have opted not to take the quake insurance.

As far as our companies' response, as I've said, we represent about ten insurance companies. Not all of them did we have situations where we submitted claims to them. However, the major companies that we did submit claims to was the Fireman's Fund, the AETNA, the Safeco, the Kemper, and the Uniguard as our major carriers that we submitted claims to. In my opinion, all the companies responded extremely well. The Safeco — well, the Fireman's Fund, Safeco, and AETNA offered to put a claims person in our office. We didn't feel that was appropriate because we didn't have enough claims to justify one individual, but they did make the phone call. The Royal Insurance, which we didn't have any claims with, called me at 9:30 in the morning to ask for an immediate list of anyone that may have had earthquake damage so they could make contact with them that day if it was at all possible.

The Safeco insurance, during the course of the following two to three days after the earthquake, their general manager was out handing out checks in areas down in Santa Cruz.

CHAIRMAN GREEN: On these checks, were these checks issued to the claimant and the bank?

MR. HAGUE: I did not see the checks. I would make an assumption that they probably, because they are a loss payable, that the banks would be listed on the check. That would be an assumption of mine.

CHAIRMAN GREEN: Well, that's my assumption too, but we found that a lot of the banks weren't signing off on their signature and so the check was sitting there and the claimant then didn't actually have anything but that piece of paper. Did you hear of that here...

MR. HAGUE: I did not personally hear of that, but I could see where that could occur.

CHAIRMAN GREEN: Thank you.

MR. HAGUE: The Safeco also had their marketing representatives going out and literally going door to door to their clients trying to identify clients that had earthquake damage that were their policyholders. I know that to be true in the Marina area and other areas of San Francisco and the Bay Area.

The Fireman's Fund, their response was also very good in getting back to us and advising us of the status of claims that had been submitted, what actions they were going to take. They responded very well, in my opinion, as did the AETNA. They flew in people from around the country to assist them.

CHAIRMAN GREEN: Okay, for the record, the companies that you're listing are companies that are very big. In other words, do you have any smaller companies, or do you use any smaller companies?

MR. HAGUE: Well, I don't know exactly what you define as a smaller company. Most of the companies that I represent are major carriers, the Uniguard Insurance carrier and so on.

CHAIRMAN GREEN: Well, companies like Oregon Mutual or Associated International.

MR. HAGUE: I don't represent those companies. The Uniguard I do represent and they had a situation where we had a client whose building had collapsed and he did not have earthquake. He called me on Wednesday morning. It suffered significant damage. We didn't know the exact extent because he couldn't get into his building, but there was a pipe that broke and there was water damage. Subsequently what happened, and this was what I found a number of companies — this is the best example or the most outstanding example — where the water was turned off the day after and clearly, that portion of the damage caused by the water would not have been covered because it was caused by the earthquake. But subsequently, someone turned the water back on and it ran for nine additional days and the Uniguard is now paying the majority of that claim under the auspices of it was damaged after the quake, after the water was turned off. And in my opinion, the companies did make every effort to try to find — from my experience — tried to find coverage where it was not clearly outside the demands of the policy.

The major problems that I encountered, the deductible was an item. What we experienced on one client where we indicated in a letter that the coverage was — I'm not sure the number exactly — but $400,000 subject to a 10 percent deductible, and our insured indicated to us that he read that meaning 10 percent of the claim deductible, not 10 percent of the value that I stated. So there was some confusion, although I only had a couple of people in that area. But there were some insureds that suffered $5,000, $10,000 worth of damage which we submitted to the carrier anyhow.

CHAIRMAN GREEN: Did this earthquake teach you anything?

MR. HAGUE: Excuse me?

CHAIRMAN GREEN: Did this earthquake teach you anything for using as a sales tool for the future?

MR. HAGUE: Well, I guess you can never be too explicit, I guess is what the message is.

CHAIRMAN GREEN: That's what I wanted. In other words, you were educated to the point of explaining to your client exactly what the policy is and what it covers.

MR. HAGUE: Well, we do that, and when the policy was sold, I did go over with this client how the deductible worked. But I will say that on the letter that was sent out, I did not say "equalling X number of dollars." I said "10 percent of" or there's a "10 percent deductible." So we've changed our internal procedures. That deductible situation was a problem.

The most glaring problem in the commercial area was the lack of understanding in the business interruption area. What we found is we had a number of people contact us and say "I know I didn't have any earthquake but I suffered a business interruption" and did not understand, even though I did go back and look over my letters, and it was pretty clear that they mentally did not coordinate the two, did not understand that you had to have earthquake business interruption and that it was not simply a business interruption situation. And that probably was the most frequently misunderstood area that I encountered, not just within my own agency, but in speaking before small business groups around the city, that was probably the most common misunderstanding that I did encounter.

I'd be happy to answer any questions that you may have. I do want to go back to the aspect of the loss as a result of the media attention and the perception that San Francisco and other areas (but most commonly San Francisco) was suffering severe damage and as a result the loss of tourists for the city and the loss of people going into the Marina area, Fisherman's Wharf, in my opinion was the major cause of the loss for the small businesses around the city. I'm estimating, but my talking to people, I would not be surprised if 70 to 80 percent of the businesses in San Francisco suffered — small businesses — suffered a loss of some sort, most likely in the loss of business. But I think it is very, very prevalent throughout the city.

CHAIRMAN GREEN: Being a broker, what would be your thoughts on improving the product the insurance companies offer to the public on earthquake insurance?

MR. HAGUE: Well, I would like to see some mechanism whereby — the problem right now is very clearly, in my opinion, the way it's structured and adverse selection type of situation where the only people that'll buy earthquake insurance are the ones that, whether they in reality are or aren't, they perceive themselves to be in an earthquake area. So you have an adverse selection situation. I believe that the way to make the product respond to these type of situations is to broaden the base, be it state or federal through the insurance association.

CHAIRMAN GREEN: If you broaden the base, would it make added cost to the product or less cost to the product?

MR. HAGUE: Because you're taking people that would not be clearly taking earthquake because they're in an earthquake zone, you're spreading it throughout the country — or the state...

CHAIRMAN GREEN: And it would cost less for the product.

MR. HAGUE: It would cost less, and you could also, in my opinion, take a look at that closely.

CHAIRMAN GREEN: We've had two answers that yes, it's going to cost more if we have more people. We've had other answers saying no, it would cost less. So we're getting confused.

MR. HAGUE: I don't understand why it would cost more, especially if you're getting dollars from people who are not clearly — I mean, there are areas that have tornadoes and hurricanes and if they paid a little bit for earthquake, they're getting the wind damage if you spread the risk. At least in theory it should reduce the claim.

CHAIRMAN GREEN: Well, but we're looking at the State of California which almost anywhere in the state you have the risk of insurance — I mean of earthquake here. There are some areas that is -- probably people don't take — because there's no faults.

MR. HAGUE: Well, and that's the point. You would get some premium dollars from those areas.

CHAIRMAN GREEN: Yeah, so, in other words, we can't look at it like from the federal aspect because we're talking about the state. We're hoping the federal will do something but we're not going to wait for them. So your answer is that it would cost less because it would spread the risk.

MR. HAGUE: Yes.

CHAIRMAN GREEN: See, that's my view but we've had some witnesses saying that it would cost more for the product from the insurance company.

MR. HAGUE: We differ.

CHAIRMAN GREEN: Any questions?

MR. HAGUE: I would like to make one — I'd like to wear my small business hat for a moment. The one problem — you mentioned cash flow and that is a very serious problem for a lot of small business. Most of them, as the grocery store individual indicated, they don't have the spread of businesses, they operate in one location. If that's down they're suffering a loss. They don't have any revenue whether they've suffered a physical loss or not. The monies available on an immediate basis -- they need immediate money. They don't need money in six months, maybe two to three months with FEMA, but they need immediate money from the cash flow situation, and there's got to be some way of addressing that immediate crunch where there's not two, three months of long-term waiting while paperwork is going through. The people are going to be severely hurt financially and there's got to be a mechanism set up to get those funds in some way to the small businesses on an immediate basis.

The state loan program has been put together; unfortunately, it's going through a mire of problems right now with the banking industry and whatever, and the bottom line is it's not getting to those small businesses that desperately need their funds. And there's not a lot of money available on a city basis. San Francisco only has $450,000 which isn't going to go too far, and FEMA is taking an awful long time to get it processed. So I would like to encourage some way of addressing that immediate cash flow problem.

CHAIRMAN GREEN: Okay, thank you. And we do have SB 8. That's slow also. So FEMA and SB 8...

MR. HAGUE: When I said FEMA I mean SB 8.

MR. BEAVER: Could you ask the gentleman, for the record, which of his carriers do offer earthquake insurance and what are the deductibles?

CHAIRMAN GREEN: Well, I think — I was going to follow up with another question. He offers earthquake insurance. He didn't clarify it. Does he offer commercial earthquake insurance like the business.

MR. HAGUE: Yes, we do.

CHAIRMAN GREEN: You do. What company is that?

MR. HAGUE: All our companies...

CHAIRMAN GREEN: All of your companies.

MR. HAGUE: ...provide it now.

CHAIRMAN GREEN: Why don't you give him your card and maybe he...

MR. HAGUE: Okay, I...

MR. BEAVER: Because I'm going to disprove this. I've checked with every one of those companies but they do not offer it. So if he has a way of doing it, I'd like to give him my business.

CHAIRMAN GREEN: Well, that's what I'm suggesting.

MR. HAGUE: You asked the question, "Do they offer it?" The two things I would say is right now our companies do offer it. They were on a moratorium for a period of time. That's one comment. So I don't know when you asked them. The second situation is they may offer it but that doesn't mean they offer it to all people in all areas with all building — I mean, it varies by the risk. If they...

CHAIRMAN GREEN: In other words, you don't have a universal offering and possibly in an earthquake fault area you don't offer it.

MR. HAGUE: That's very well the case and that's the point. Again, I don't mean to be playing games with you, but...

MR. BEAVER: We know we're talking in Sacramento but there's no earthquakes there.

CHAIRMAN GREEN: Yeah. Well, on this map that you gave us that was one of the areas that didn't have earthquake on a fault.

MR. BEAVER: That's why they offer it.

CHAIRMAN GREEN: Well, but they have earthquakes there but it's an aftershock of some other place. In other words, you didn't pick areas that the companies want and that's where they offer it, and so that was why...

MR. HAGUE: Well, it also depends if it's unreinforced masonry building as opposed to a reinforced building. So there are other factors.

CHAIRMAN GREEN: Thank you. That clarifies that for the record.

MR. HAGUE: Thank you.

CHAIRMAN GREEN: Next we have from local government Supervisor Warren Widner from the County of Alameda.

SUPERVISOR WARREN WIDNER: Senator and other members of the committee, I'm Warren Widner, Supervisor for the 5th District of Alameda County. I'm happy to be able to come here this afternoon and respond to some of the questions that you specifically asked about the county's experience in obtaining earthquake insurance...

CHAIRMAN GREEN: I don't mean to be hard on the cities and the counties. I come as a mayor of the City of Norwalk and 14 years on the city council, and I'm seeing a difference in what some of the cities are doing to help their people within their city. And I understand and I fully agree that you can't totally forget bringing buildings up to earthquake standard, because your duty is to look at the safety. Sometimes though the safety is up to state laws so your hands are tied to some respect. But what Santa Cruz did was innovative and I haven't seen that happening in any other city or county.

SUPERVISOR WIDNER: Well, the specific questions that we're responding to — the ones that you asked — were the county government's experience in obtaining earthquake insurance for the county's property, including some of our shelters. And generally, that's been very good. I think it's much due to the aggressive manner in which our risk manager goes after insurance as anything else. So I decided that I would bring the risk manager here, Nancy Johnston-Billard, and ask her to make a presentation on...

CHAIRMAN GREEN: You're a good supervisor because you bring your brains with you.

SUPERVISOR WIDNER: Right. And then, of course, we'll be happy to answer any questions.

CHAIRMAN GREEN: Thank you very much. And your name is Nancy...?

MS. NANCY JOHNSTON-BILLARD: Nancy Johnston-Billard, Risk Manager, County of Alameda. Honorable committee members, as Supervisor Widner has stated, we are responding to the questions as outlined in your letter. If there are any other questions that you would like to ask or information after we finish the presentation, we'd be delighted to answer them.

Alameda County's experience in obtaining earthquake coverage has been very good, I would say. There have been periods when insurance was not available or in small amounts. But because of the size of the County of Alameda and because of our past track record of constantly buying earthquake coverage, we've always been able to have some coverage, even in small amounts. As the marketplace expanded, the County of Alameda, through it's broker, was able to purchase earthquake insurance in increments of $10 million.

I have a very aggressive broker who constantly shops the marketplace here and abroad to determine where insurance might be available. She will give me a telephone call and say, "I found $10 million, do you want it?" And I'll say, "What's the price? What kind of deal can we work out?"

We many times have been able to get earthquake coverage without paying a whole lot of money on our existing premium, and let me explain that. We don't have our buildings insured building by building. We have a blanket policy that covers all of our buildings. So when we go for earthquake coverage it fits in on top of that blanket. This allows us more flexibility. I cannot guess where an earthquake will hit or what buildings will be damaged, so I always say, "Can I have a floater for my earthquake coverage?" and they respond "Yes." We're never quite sure what that means, except we found out during this earthquake. What it meant was that every building that was damaged had earthquake coverage with a 5 percent deductible. We're not yet sure of what our total damage will be.

But the market conditions for Alameda County have been soft. We've had no difficulty, the price has been good. There've been frequent window periods where we could pick up small amounts of earthquake coverage.

Presently, our earthquake insurance limits are $60 million — that is up from last year — with a 5 percent deductible of the values at risk. We're structured with a primary and three excess layers covered through 15 companies. So there are a lot of companies that are taking a piece of the action. And it's, as I said, a package rather than per building which works to our advantage.

The cost was $834,260 for the total insurance package. That's the general insurance plus the earthquake coverage. Now, this is down from $1.2 million on the previous year. Here again, remember we have an aggressive broker who searches the market, and because of our past history and the size of Alameda County, we are able to negotiate situations where other people might not be able to.

Also, during the earthquake we had boiler and machinery coverage. We have recently upgraded this area of coverage because we had a gap at Highland Hospital. Had anything happened there, we would have had some difficulties. We had a transformer catch fire. The insurance company will cover that, including any business interruption as a result of that transformer going under that boiler and machinery policy. Had we had a generator go down at Highland Hospital and blood had been damaged that was in storage, that would have been paid for and replaced.

As far as the general damage to the County of Alameda, looking at our territorial spread, and I brought it with me just so you can see the — about 10, 15 pages — we have approximately 63 buildings that were damaged. We're not finished with our survey yet. Type of damage ranges from hairline cracks to something that we think <u>might</u> be something. The highest estimate in this log is $3.6 million. Here again it is an estimate.

We're estimating the total cost in soft figure approximately $8 million. Now, with the 5 percent deductible and the damage spread throughout the various numbers of buildings, we may or may not go beyond the deductible on each building, which means it is possible...(tape turned)...deductible and the insurance would come in to pick up the rest.

Moving into your question about insurance for temporary shelters, the County of Alameda has had a policy in place for several years that all shelters have to be inspected by the Health Department, Fire Department, Building and Codes. After the earthquake, we decided to send in teams of engineers, structural engineers, along with the other types of specialists. Because it was a disaster we set priorities. Normally we are very concerned about shelters having insurance. We use it as a risk transfer mechanism. Because of the disaster, we set priorities and said it is more important to house people who have no homes, <u>but</u> for a good faith effort we will still require that all the inspections be done. That meant that maybe one or two — possibly two shelters passed the inspection but did not have insurance. We said if a problem arises, we'll face that later. In all the other instances, the owner of the buildings had insurance, so the insurance went into place, no problem.

Shelters without insurance coverage may still present a problem. One of the things we have been noticing for the last several months is that churches are used for homeless shelters, and they took people in during the disaster. We're beginning to see insurance companies who previously insured under the sanctuary clause now beginning to raise questions as to the liability, whether they really want to insure churches for homeless shelters at all in the future. That is an issue we don't have the answer for. We're just now beginning to see it.

Since the earthquake, I have asked my broker to search the market to see what insurance she could find. She asked how much I wanted; I first said $10 million. She called back in a few days and said, "What was your figure?" I said, "$10 million." She said, "How about $30 million?" I said, "I'll take it." She called back a few days later and said somewhere in Texas she had found $45 million in earthquake coverage, that if the County of Alameda wanted to take it could.

Now, this does not mean that the market is open and free for all and that everyone can buy. The gentleman prior to me spoke about the qualifying criteria. Let me state again that because of the size of Alameda County and the track record that we have in purchasing earthquake coverage over the long haul has helped us during whatever crisis there was in pricing of earthquake coverage and in the purchasing of that earthquake coverage.

CHAIRMAN GREEN: Thank you. Very good testimony. Any questions? I appreciate your coming down today — thank you, Mr. Supervisor — giving us what has happened in Alameda County. One question comes to mind is you brought up the thing with this church and shelters and so forth. Have you given any thought in your giving coverage during that type of emergency?

MS. JOHNSTON-BILLARD: We did not come out directly and say we will cover you, because the County of Alameda has no liability insurance. We do have property but it does not necessarily extend to the other owners.

CHAIRMAN GREEN: You're self-insured as far as liability.

MS. JOHNSTON-BILLARD: Yes. We were prepared to do whatever we had to do should a problem arise. Now, don't ask me what that meant. I haven't decided.

CHAIRMAN GREEN: I understand.

MS. JOHNSTON-BILLARD: We just decided — we just said we would help out, do whatever we could. If it meant committing dollars we would do it.

CHAIRMAN GREEN: Uh huh. To help the people.

MS. JOHNSTON-BILLARD: To help the people.

CHAIRMAN GREEN: To get them housed, because that's our job.

SUPERVISOR WIDNER: Our liability insurance is several million dollars, and usually in these circumstances it's not a lot of damage or liability that would be involved. So although we don't advertise, we just sort of — we know that we do have funds in a reserve for liability, and if it becomes necessary to spend some in order to do our job, which is to help homeless and poor people, then that's what we'll do.

CHAIRMAN GREEN: Good for you. Okay, thank you so very much. And let's hope that we don't have a big one for the next 70 years.

SUPERVISOR WIDNER: Thank you.

CHAIRMAN GREEN: Thank you. Okay, next we have Keith Grand, who's Risk Manager from the City and County of San Francisco. And Jane Keegan, who is the Risk Manager, Port of Oakland. If you could come up also.

MR. KEITH GRAND: Thank you, Senator Green, and members of the committee. My name's Keith Grand, Risk Manager, City and County of San Francisco. Among my duties are handling the insurance needs of the city and county, and the handout I've given you is my attempt to summarize a few of the specific experiences the City's had with attempts to obtain earthquake insurance, what our current situation is, how our request to get reimbursed from FEMA for the October earthquake create insurance questions. It may be a little difficult for the audience to follow without the handout but in essence, what I'm saying here in our first example, this is an example where we attempted to insure a major building in the city for earthquake insurance. And over a period of three years — in the middle '80s — essentially what we ran into is this situation. The value of the property didn't change except by appreciation in the neighborhood of $120 million. The first year we were able to buy that fully insured for all risks, including earthquake, with only a million dollar deductible for a premium of $97,000.

The next year the market started to turn. The risk was identical to what it was before. But now the deductible went from a flat million dollars to 5 percent of the value of the building. At $120 million, 5 percent is $6 million deductible. The premium jumped from $97,000 to $1,080,000 -- more than a tenfold increase in the premium and a sixfold increase in the deductible.

The following year is the last year we bought earthquake insurance on that building. The value had only appreciated another $5 million to $125 million. The earthquake sublimit, or the maximum amount of earthquake coverage we could find on the building that year dropped from $120 million down to $50 million. The deductible was still at 5 percent, but because the value of the building had appreciated, the deductible now was $6¼ million, but the annual premium estimate was $2.1 million. At that point, before we bought the coverage, we had an independent seismic study done of the building, which told us that if there was an 8.0 quake on the Richter scale, we would suffer less than $6 million damage to that building. Well, the deductible was greater than $6 million, the premium was $2.1 million. We decided we were going to self-insure from that point on.

That's an example of our recent experience with property insurance on a building; let's say commercial property insurance. The next example is just the reverse. We buy a considerable amount of property insurance on the city's fine arts collections. In the last two years our experience has been as follows: The value of the art is probably in excess of a billion dollars. Nobody has an exact figure because it's changing everyday. A year ago we had earthquake insurance with a limit of $50 million on a collection worth over a billion. The earthquake insurance deductible was only $15,000, although the limit was $50 million. And the annual premium for that $50 million of coverage was $90,000. A year later, we were able to increase the limits on that fine arts insurance from $50 million to $300 million — a sixfold increase in the limit insured. The deductible didn't change; it's still $15,000 -- in our case per earthquake. And the annual premium went up slightly from $90,000 to $115,000.

CHAIRMAN GREEN: Okay, now this was fine arts. For instance, you've got a Rembrandt in the museum and you've got it insured for $5 million. Then if the building collapses and it ruins that Rembrandt, you can't replace it so they pay off the $5 million.

MR. GRAND: Right. We have a provision in the policy that says they pay whatever we value the art to be worth. They don't even have a choice of deciding what it's worth. In some cases with some of the artists it's very difficult to even determine what it's worth. So our provision gives us the right to decide what the number is.

But the point I'm trying to make here is that there's a huge contrast in availability and cost between commercial earthquake insurance on a building where we were largely dealing with domestic insurers in the first instance, and there was some foreign insurance as well.

CHAIRMAN GREEN: That doesn't make sense, does it?

MR. GRAND: And then in the second instance we've been entirely in the London Market for fine arts insurance and the London Marine Market, which is in effect some of the same underwriters who deal with the Hurricane Hugo and the Phillips Petroleum explosion. A lot of those kinds of losses, there's been almost no difference in pricing or availability. In fact, it's become more available.

The third example is, again, back to the building — commercial insurance. This is a survey I'm currently in the process of doing for our negotiations with FEMA on our earthquake reimbursement, but as recently as today, I got some information from our insurance brokers that is summarized in what I call Example 3. What I did was I took a cross-section of City properties that were damaged in the recent earthquake. The amount of damage to those buildings — in sum there was over 100 buildings — the amount of damage is estimated to be somewhere in the neighborhood of $16 million. But in looking for earthquake insurance, what the insurance companies typically require is that you insure the properties for the full replacement value of the property, not the amount of damage. So in our case that hundred buildings represents $1.4 billion in replacement value. And as you heard before, the typical deductible is 5 percent. So we're talking about 5 percent of $1.4 billion. The insurance deductible for us then is $70 million and we've had damage in the neighborhood of $16 million to those buildings, and in order to get that coverage, the rough estimate of the annual premium would be somewhere from $2½-3 million for that coverage.

Now, the difficulty that this creates for us, let's say, as a local government, is I mentioned we're in the process of dealing with FEMA. FEMA, in essence — part of the regulations on insurance says that if they give us money to repair damage, we have to agree to insure against the peril which caused that damage — in this case earthquake — and we have to insure for either the life of the repair or the life of the property. We have to insure that amount equal to their grant for the repair and the only waiver is if the State Insurance Commissioner decides that such coverage is not reasonably available.

So on the example I gave you, in essence, if we were to go to FEMA now to apply for our $16 million to repair the damage to a hundred buildings, insurance companies won't insure the value of a portion of the building. We can't tell them, well, we only had $16 million of damage, we want $16 million worth of earthquake insurance. The typical response is you have to insure the full replacement value. So we buy a policy with a limit of $1.4 billion, 5 percent deductible, given the most generous reading of how the deductible applies.

And there's some question here that typically says 5 percent of the value at risk at the time of loss. Does that mean the value of the entire schedule of properties or only the value of the properties which were damaged? Well, when you have a blanket policy that covers all your properties, it could be read either way, and there's some question about how the deductible would apply. But given the most generous reading of the deductible, we would apply a 5 percent deductible only to the buildings which suffered damage — we're back to the $70 million deductible — and if we were to follow this course, we'd be paying, assuming the marketplace stayed the same, $2½-3 million a year for the coverage for the life of the repair or the property in order to qualify with FEMA's requirement to recover $16 million worth of damage.

CHAIRMAN GREEN: So you're caught in a Catch-22. It costs you more to accept the money than if you didn't accept it at all.

MR. GRAND: That's right. Well, obviously, we're in the process of preparing our case to go to the Insurance Commissioner to get a certification that such coverage is not reasonably available. Given the terms — largely the deductible and how it applies and what the premium is, we feel it's not reasonably available, but that's for the Commissioner to make and certify to FEMA.

CHAIRMAN GREEN: And can't you establish a risk pool of so many dollars per year — somewhere less than the premium — to go into a fund as your own risk pool of City and County of San Francisco?

MR. GRAND: Yeah, in fact, that's exactly what we did. Following example one, when the premium went to $2.1 million, we decided to quit buying commercial insurance and take the money we would have spent on insurance and put it into the fund to self-insure against exactly that kind of loss.

CHAIRMAN GREEN: Well, actually you have already become your own company, so that wouldn't be part of your case-making to the Insurance Commissioner, that you actually have a risk sharing with the funds you already have built up.

MR. GRAND: That's correct. One last item that I just — just to illustrate one of the problems with the commercial insurance, Item C on my little handout refers to an attached chart, and the only reason I give you this is this attachment is simply a diagram of the separate insurance policies that would have been placed on that one building had we decided to buy the insurance that cost $2.1 million. As you can see, there are 33 companies there. Not all of the companies have exactly the same terms and conditions. It takes months to put something like that together for the brokers, especially in a hard market like it was then. And one of the other difficulties that I want to point out is once you've got the insurance in place, you can't really rest easy even then.

As happened in our case in the year prior, the last year we had insurance, one of the insurance companies in that jigsaw puzzle decided to cancel mid-term. We found a replacement company but they wanted to charge a little more premium than the company that had canceled. Well, once — and we put that piece of coverage in place because we felt we needed it — once that happened, all the other companies in that excess layer insisted on getting an adjustment in their premium because the new player was getting a little more than all the others had originally agreed to.

So we went along with that because we felt at the time we had a legal obligation to maintain the insurance. And I suppose I could rationalize to myself why all the players in the same layer should be paid an equal rate, but what happened next was that the players, the underlying carriers, the primary layer of insurance, those players also then came in and asked for an adjustment in their layers of insurance because of that one player in the upper layers got an increase.

So over a period of a year, this complicated structure of insurance was never really solid and the costs tended to change as we went through the year. We finally finished the year, and like I said, we got that seismic study and decided it was cost effective not to buy insurance anymore, because given the deductible and the seismic qualities of the building, insurance would probably never pay a loss. So by and large, the City, from that point, has become — has been largely self-insured both for property and liability risks.

That's everything I wanted to say about our experience with earthquake insurance. I'd be happy to answer any questions you might have.

CHAIRMAN GREEN: Well, thank you. Any questions? Dan?

SENATOR McCORQUODALE: Have you experienced or heard about any proposals to cover situations like yours with insurance that you were buying now but would have been effective — would have become effective July 1st of this year?

MR. GRAND: Oh, a retroactive effective date.

SENATOR McCORQUODALE: Yes.

MR. GRAND: I've heard of that being done. I mean, it's not something we've tried to find. But occasionally you hear of something like that. Probably the most famous first example I know of was the MGM Grand fire where they in effect insured the liability of the hotel after the fire had happened. But there it's almost a question of trading dollars. It's a question of estimating what is the loss going to become since you know you have a loss — you just don't know what its magnitude is — and the premium nearly approaches what people think the loss is going to be.

SENATOR McCORQUODALE: Well, in your case, as an example, the example you use in Number 3 is the type of thing that I've heard, that if you get — the Insurance Commissioner doesn't relieve you of the requirement to have insurance, so you get FEMA and you then get — so you're required to provide the insurance, that if you — the gamble would be is there going to be an earthquake in the next five years. If there's not going to be an earthquake in the next five years or say ten years, they're going to sell you the premium for $3 million. They offer you $16 million and then if you have a long-term agreement on the $3 million, it would be a way to get the insurance — provide the insurance on a long-term basis. I would assume you would be a good payer and would structure that payment, some upfront and some stretched out. I just wondered if anybody has approached you in that.

MR. GRAND: No. I've not heard of something like that. The only other thing I might add is again, part of this current survey we're doing is that — and I've talked to several major brokers here in San Francisco and they all tell me the same thing. My impression was the earthquake insurance market might have vanished after the October earthquake, but for commercial risks, there's probably as much capacity today, they tell me, as there was two or three years ago when we last decided to buy some insurance. And the estimates I got — as I mention in Example 3 — there's $120-150 million limit, according to two of the brokers. This is maximum worldwide earthquake capacity. If you search the globe and come up with earthquake insurance, you could probably buy that amount of insurance, even though we've had the earthquake. But it's the application of the deductible and the high premium that, in my view, makes it not worth buying.

CHAIRMAN GREEN: Okay, well, thank you very much. Next we've got Jane Keegan, Risk Manager, Port of Oakland.

MS. JANE KEEGAN: Good afternoon, Senator Green and committee members. I did not make a formal packet for you to discuss some of the Port of Oakland's problems, but I definitely concur with the risk manager for the City of San Francisco and some of the frustrations in buying earthquake insurance and dealing with FEMA after the fact if you haven't totally insured.

The Port of Oakland does not insure our buildings for earthquake damage currently. We dropped it a few years ago when it really got unaffordable, largely because of the premium and the high deductible and also the number of property that's excluded. An awful lot of our property is uninsurable, that what you can buy insurance on is buildings, contents, but you can't buy land, which is what marine terminals are; you can't buy it on dykes, you can't buy it on runways because of the susceptibility.

Where we did buy it about two years ago when the market started softening up was on our cranes, because once again, the marine market in London had softened. In our renewal that year, we were able to buy earthquake for the same price as last year. The crane rate was the same with earthquake as the prior year had been without earthquake. So we will have a claim under that policy this year which will include the damage to the cranes, some loss of income, and some additional expenses. The policy covers extra expense. That's the additional cost of getting back in business. One of our marine terminals is shut down so we had to truck the cargo to a different location and we have ongoing additional expenses at that location.

So our frustrations right now are trying to buy it to meet FEMA's requirements. We have approximately $105 million worth of damage but very little of that was to buildings. Mostly it was to the runway and to ground. The question is do we have to buy it, to what extent? The manual states to the amount of the grant. Does that mean I need to buy $100 million worth of earthquake, or do I have to buy it for 5 or 10 million, which is probably what our damage to our buildings was. So even if we had bought earthquake insurance, it probably wouldn't have responded on the buildings because it would have been under the deductible. We have approximately half a billion dollars worth of values. I've recently found that it might be available, earthquake insurance, but it's not affordable. And I called the Insurance Commissioner to ask for determination that it's not affordable and been advised that she was not going to be make a blanket statement.

A quote that I received approximately six months ago for a fairly low limit of $10 million on our buildings was $250,000. A quotation I received this week was $4.6 million for that same coverage, which is obviously what the insurance industry is saying is we don't want to write it right now. I've been told that after the first of the year, things will calm down in the marketplace. But I certainly don't think it's ever going to go back to where it was a few months ago pricing-wise.

So the question is right now what do we do with FEMA? We're supposed to give them assurances that we will buy it, but we still question if it's really — considering our mix of business and property — if it's still the best thing to do. And the first thing FEMA wants to do is to come in and get copies of all your insurance policies because anything you insure you can't collect from FEMA for, which certainly makes sense. So the question is, you know, what should we do now, and I think right at this point we have to wait until after the first of the year to see if the market calms back down.

But even then, as with the City of San Francisco, if our damages were only a few million, should we be paying several million upwards a year for earthquake insurance? I've heard about some possibility of some companies being set up which are policy-owned insurance companies, which I think it might be a good route to go if something was going soon. But I'm not sure if FEMA would accept that, rather than just paying the insurance company that much money every year.

CHAIRMAN GREEN: You don't belong to any joint powers insurance authority.

MS. KEEGAN: No, we don't. We don't have some of the problems other public entities have in purchasing insurance. Because our operations are a lot narrower, we don't have any police and fire, which are the major reasons that most public entities can't buy insurance.

CHAIRMAN GREEN: Okay. That would be the only suggestion I would have is look around for a risk pool out there and join it and then FEMA will accept that since you are in a risk pool. I think we have some hearing — this testimony we still have some work to do with FEMA, and so far we haven't seen too many good marks. They've done better here than they did in Whittier but they still have a lot to be desired in doing and we haven't been getting into that phase of what happened in the earthquake was with the problem with FEMA. But I'm sure that there's going to be a lot said down the line somewhere. Senator Mello is pretty unhappy with FEMA and what they've done, and there were promises made to him in Washington and they weren't kept.

So thank you very much. Any questions? Thank you very much for coming today. Okay, next we have Gail Hillebrand, Staff Attorney for the Consumers Union.

MS. GAIL HILLEBRAND: Thank you, Senator Green, members of the Subcommittee. I'm going to switch the focus back to the situation the individual homeowner faces, and I think you heard it described here pretty well this morning.

Homeowners see high costs and severe limits on the coverage they can get. Because of the current practice of most companies in California, often a 10 percent deductible, occasionally a 5 percent deductible, it's impossible for the average homeowner to fully protect the equity they have in their home, particularly for people who've purchased recently who are perhaps first-time home buyers or trade-up buyers. If they have a 90 percent mortgage, that 10 percent deductible may represent all or nearly all of their equity. If they have an 80 percent mortgage, that deductible may represent half their equity.

I'd like to tell you what can be done about this problem, but I'm not prepared to do that and I don't think any of us are yet. It's going to require a great deal of further study. I do agree with the concern expressed by Senator Green that consumers need availability of coverage not only for the "big one" but also for more moderate damage that they would probably choose to insure for if that were available. It's as if a person could insure themselves for a terminal cancer but not for a broken leg, and that's what people face today.

I would express a caution we'd be interested in looking at, legislative measures and working with the Subcommittee, but I would express a caution about any state pool program, that it'd be adequately capitalized so that the representations being made to people when they pay those premiums in fact will come true when the earthquake hits and there'll be money there to stand behind the claim.

We submitted a letter to the committee in advance suggesting some questions that should be asked of the insurers and I won't go through all of those here. I would however stress the importance of matching up the data on the claims with the data on the monies received as to type of coverage. We've seen a lot of news reports, X amount of dollars in losses, X amount of claims expected. It's important to tie those in: how many of those claims will be for homeowners versus how much of homeowners paid over a fairly long period of time. And I would just urge you as you hear from members of the insurance industry to ask those questions.

Something we've been thinking about that we haven't seen yet in the market and perhaps we'll see in the future is the issue of insurance companies taking a role in prevention of loss. In other types of insurance coverages, you do have a dollar incentive for people to take preventative steps. A good example of that is the discount that homeowners get from many companies for burglar alarms and smoke alarms — 5 percent off your policy, 10 percent off your policy if you have a burglar alarm. I'm not aware of any companies operating in California that have a different price structure for earthquake insurance if the homeowner has bolted their home to the foundation — a very basic step many people can take if it's a wood frame home — that would be very helpful — or has installed T-stress bars, which the diagrams that have been appearing in our local newspaper tell us help distribute the stress among the house so that you're less likely to have collapse. And that's something that perhaps the industry should take the lead on. It may be something that your committee can consider further.

I'd like to comment on a couple of issues that the homeowners raised this morning, in particular the issue of the payment of the replacement cost. I think that's an issue that there's further exploration because it may impact not only on people who buy earthquake insurance but on people who purchase other kinds of homeowner insurance. If a person's home is destroyed tomorrow in a fire and they have replacement cost coverage, they would reasonably expect that the insurance company would pay the entire cost to replace their house, including if your house was built in 1930 — very common in the Bay Area, 1925 — and not up to current building codes. A person would think, and I think rightfully would think replacement cost in the ordinary homeowner's policy means the cost to replace it today consistent...(tape turned)...

CHAIRMAN GREEN: ...building permit to do that, so who pays that? The homeowner or the insurance company?

MS. HILLEBRAND: That — I'm not sure about that. I believe...

CHAIRMAN GREEN: Well, that's the key question.

MS. HILLEBRAND: ...that there may also be a situation where the person has to bring the part of the house on which work is being done up to code. For example, it would take $20,000 to bring it up to where it was last year. It would take $60,000 to bring the part which is being corrected up to code.

CHAIRMAN GREEN: Yeah, but you see, they're not allowing building permits to rebuild that section of the house unless they bring the rest of the house up to code. That's the key question here is why? — in other words, who pays for it? And we don't have an answer to that yet.

MS. HILLEBRAND: I think that's a question that bears further study, and in part because at least in the East Bay jurisdiction with which I'm most familiar, they...

CHAIRMAN GREEN: That's true. Yeah, we know who pays but we don't know who should. That was Dan's remark and I think it's a good one, because that's been the testimony in various places. Some of the entities are requiring them to come up to par. So maybe a $200,000 building suffered $40,000 worth of damage, but it's going to cost them 80 or 90 or 100 thousand to bring the rest of the building up to par.

MS. HILLEBRAND: I think that — from the consumer standpoint, you might say that the person -- if the person is being sold a policy, which is called a replacement policy, they would have a reasonable expectation that it's going to pay to replace their house and a person can't replace their house without getting a building permit.

CHAIRMAN GREEN: But is it legal and what are the companies doing, that's I think where we're after. Go ahead.

MS. HILLEBRAND: In addition, we do urge the passage of SB 94 to close a loophole that we've never believed could exist with respect to homeowners' earthquake coverage, and that's the potential for a loophole if the company chooses to nonrenew after a person has accepted the offer of earthquake coverage. It's always been our position that the requirement to offer means to make a real offer and not something that's only good for one year and they cancel or refuse to renew, but that's an issue that's been the subject of some debate.

Finally, I would urge the committee to inquire from the insurance companies about the types of complaints they've received from consumers. And I don't mean to imply that all of those complaints will be well-founded, but I think that the volume and types of complaints and inquiries will go a long way toward helping us all determine whether consumers really understood the policies they were buying; because particularly if the complaint is I have cracks and I'm not covered, that may indicate there's been a problem in the marketing and in the communication where people are not really understanding the limited nature of the earthquake coverage in any quake other than a very large quake.

I'd be happy to answer questions.

CHAIRMAN GREEN: Thank you. Any questions? Thank you very much for your testimony. Okay, next we get into regulatory role and that's the California Department of Insurance. We have with us today David Stolls and Linda Yarber, and if both would come up, please. We saw you in Santa Cruz and you did testify and we appreciate that. Is there anything new happened since then?

MS. CHARLENE MATHIAS: Senator, I'm Charlene Mathias with the Department of Insurance. We have no new testimony to give you. We were asked to be here for both hearings and we'd be glad to repeat the testimony or just leave the record.

CHAIRMAN GREEN: Oh, no, don't repeat it because we put it in there last time but I don't think there's — I think the key question that came up here today though is like the public entities that we heard from and with FEMA and they have to provide insurance: How do you determine insurance and is it available and affordable to those public entities? I mean, you heard the testimony this morning.

MS. MATHIAS: We heard the testimony and we were not prepared to address that. Apparently the Insurance Commissioner does make some sort of ruling and it sounds as though she's going to do this on a case-by-case rather than make a blank statement.

CHAIRMAN GREEN: Well, I would say it has to be case-by-case because each case is different. But like San Francisco here with the amount of dollars of coverage they might be getting, or \$4 million or \$5 million in aid from FEMA and over a very short period of time they'd be paying that back to the company, then it wouldn't be worthwhile. So somehow if you could provide it, how you're going to look at it, to this committee, we would appreciate it.

MS. MATHIAS: We can do that — give it to your consultants for the record at a later time, Senator.

CHAIRMAN GREEN: Yeah, that's it. Question, Dan?

SENATOR McCORQUODALE: Well, I just wondered if they could respond a little to that deductible. Is there any other type of insurance that's sold where the deductible is a fixed amount based on the value of the policy?

MS. MATHIAS: There may be, Senator. I wish you'd address that to the insurance industry. They may be more familiar with it. But the earthquake insurance is a catastrophic coverage and it is not intended to cover lesser amounts. It's intended to prevent a person from losing their entire investment. The deductible is at a fairly high percentage in order to make the policies affordable, for one thing, and as I say is intended to be a catastrophic coverage.

SENATOR McCORQUODALE: It just seems like there's — I keep trying to find the logic in it. I'm sure it's there but I haven't quite found it.

MS. MATHIAS: Well, for one thing, it makes the coverage more affordable to have a higher deductible. For another thing, there is a limited capacity with respect to earthquake within the industry, depending on how extensive the damage is. It's also intended to spread the number of people who can recover.

SENATOR McCORQUODALE: But it seems like from a consumer standpoint it would make more sense that the policy be — unless it was trying to disguise it — it'd be better to say okay, we're going to sell you a policy that will cover from $20,000 to $100,000 from your loss; the first $20,000 is your responsibility. That seems a more common thing. I can buy health policies, as an example, that will pay the deductible in my basic health policy, but I know that it doesn't — it's clear. That's something that I come in contact with frequently. I can buy surplus coverage for — based on cancer, Alzheimer's disease. I can buy excess coverage on my automobile. I can cover the deductible on my automobile. I can do a lot of different things. The thing that seems to me to be strange, and we keep hearing it not only in the hearings but also among people that I've talked with, they have a hard time comprehending that they can buy so much insurance, because they wanted to cover every possibility related to an earthquake, but it pushes the deductible up to where it's above the value of the property. And maybe they would do that and nobody would ever even point it out to them.

MS. MATHIAS: Well, the statute does specify what has to be in the policy, the policy language, with respect to the deductible. Now, perhaps one of the things that you'd want to consider is revising that statutory language. And I think the gentleman from the agents association indicated that perhaps a better explanation at the time of the sale of the policy or the offering of the policy is in order as well.

SENATOR McCORQUODALE: If you deal with it on the — I mean, you could stamp something else on the front of the policy but we've got so much on the front of the policy now that there's more there than on the other 14 pages of the policy. But I wonder if — I'm trying to think of what would happen if we just said, as an example, there can't be any deductible on it. Don't you think they would still sell it but would offer it — they'd offer a range: we'll cover from the amount that your loss is from $20,000 to $100,000 or we'll cover the loss on your house from $10,000 to $120,000. I mean, that seems like that wouldn't create any problems for them. Maybe we ought to inquire...

MS. MATHIAS: Well, Senator, I think you ought to address that to the insurance industry. Under the statute they must offer it but you might address your question to them and have them tell you what it would do to the prices of the policy.

SENATOR McCORQUODALE: I know that the press keeps reporting that the insurance industry ran the Department of Insurance always in the past, but I thought with Prop. 103 maybe that had changed. So I think — would it change your philosophy that the insurance company is the one that's advising the Legislature? We think that maybe you ought to have a role in that.

MS. MATHIAS: Well, we do have a role, Senator, and I think that you are aware that earthquake insurance is now covered under Proposition 103. So the Commissioner will be approving the price of the policies but it's going to depend on what the policy covers, among other things. The actuaries in the industry, and our actuary unfortunately is in New Zealand attending a symposium on earthquake at this particular time so we can't ask him, but the insurance industry has the actuaries that can tell you what changing the deductible would do to the price of the policy that they would submit to the Commissioner for approval. And then you would have to decide, you know, whether you want more coverage with a lower deductible or a more affordable policy.

CHAIRMAN GREEN: I think the question that I'd like to have answered, and I don't remember if I asked it in Santa Cruz or not, the amount of complaints that you've had from the various communities. Do you have any handle on that?

MS. MATHIAS: Mr. Stolls is here. We kind of tailored our information. We did give you the specific area information the other day and Mr. Stolls has information on our complaints in the Bay Area.

CHAIRMAN GREEN: Yeah, that's — what he passed out last time, was that the complaints or just...

MS. MATHIAS: That was the — well, let him tell you.

CHAIRMAN GREEN: Like you had the hot line and some of those people just called in to ask questions what to do on what to do it.

MS. MATHIAS: That's correct.

CHAIRMAN GREEN: But I think what I'm looking for is what kind of complaints have you had against what companies.

MR. DAVID STOLLS: Senator Green, Dave Stolls, and we did talk about that a little bit at Santa Cruz. I had indicated at that time that the numbers of complaints were inconsequential, despite our hope for visibility of the Department to the consumer out there. We did receive quite a number of hot-line calls on our 800 number, but as far as written complaints, we received less than 15. But I also acknowledge to you that there is quite a long tail with respect to claims complaints. Most of the consumers try to resolve the matters directly with their agents and/or companies and it's only when they do reach that impasse, if they reach an impasse, and are totally frustrated that they do seek our assistance. But up to date, we've received less than 15 complaints; but again, I invite those sitting out in the audience and, again, I'll address the committee that we stand ready to investigate each complaint on its individual merits and take whatever action is necessary to resolve the matters.

I do want to take a moment also to indicate the first lady that testified this morning, for your information, one of her problems where she did not have her policy at all for contract, that's presently on its way over here. We've had it faxed over already and that'll be going out in tonight or tomorrow morning's mail to her...

CHAIRMAN GREEN: Good for you.

MR. STOLLS: ...for step number 1. As far as the other kinds of inquiries, of the 15 complaints, I think we had three with respect to delays, and I have testified that I thought the industry as a whole had responded — there were exceptions of course — very well as far as their visibility and availability to the consumer out there. But then again, there is a long tail and we do anticipate there'll be complaints.

CHAIRMAN GREEN: Because in the two hearings, we had two complaints in Santa Cruz, or two people complaining, had three here today so that's five. That's a third of all the complaints?

MR. STOLLS: The nature of the problem was the misunderstanding of the deductibles or not understanding if they had earthquake insurance or if they did not what was covered under any kind of policy they might have. We had encouraged the consumer to file a claim with their insurance company regardless of the policy they had because various companies did pick up certain limit-at-allperils and extended their coverages. So we did properly advise the consumer to file the complaints. They did not know. That was our purpose, availability over the hot line and as well as at the disaster centers which we staffed.

CHAIRMAN GREEN: Is the hot line still operating?

MR. STOLLS: Yes, it sure is. It operates all the time. And as I indicated last time, we are very -- you can get through. We have less than a 1 percent busy signal rate now so it's very easy to get through. We have 27 officers on the hot line every day.

CHAIRMAN GREEN: Very good. Okay, well, thank you. Any other questions? I guess everybody else is gone. Thank you very much for coming out again today, and your information is in the packet that we have here. Thank you very much.

Okay, we have then from the insurance companies and trade associations, Personal Insurance Federation of California, Dan Dunmoyer and Leonard Gelfand, if both of you would come up, please.

MR. DAN DUNMOYER: Thank you, Mr. Chairman, members if you do come back. Once again, we are glad to be here today. On behalf of the Personal Insurance Federation, we make up basically companies that sell predominantly personalized insurance: residential and auto.

Today, we have with us the Farmers Insurance Company. We have four representatives from the company here. Just let me introduce them to you for your information so if you have specific questions you'd like to address it'll make it easier for you.

To give testimony to answer the 17 questions you provided as best we can at this time will be Leonard Gelfand, Regional Vice President. He'll do most of the discussion. Also, just for your information, we have Wes Whitamore, Regional Claims for Farmers for the region that was involved by the earthquake; and also Linda Jorgensen from Farmers as well, a claims manager as well. For your information too, we have invited Jeff Beyer from the executive office in Los Angeles, Vice President for Public Affairs, Public Relations, just to answer any questions you may have on our communication mechanisms and how we responded on a global sense throughout the state. So I'll turn it over at this time to Mr. Leonard Gelfand, Regional Vice President, to give testimony.

MR. LEONARD GELFAND: Good afternoon. Chairman Green, we thank you for giving us the opportunity to testify here today. As officer in charge of our Pleasanton office, I'm responsible for all of Farmers operations here in the Bay Area. And let me begin by saying how very proud I was of our agency force, our employees and our district managers, for the job they did in assisting our customers and other quake victims which followed this major catastrophe.

In the next few minutes I'd like to address the specific issues and questions the committee asked us to consider in advance of this informal hearing. Certainly, the October 17th earthquake was the largest catastrophe of its kind in the California industry that we've ever faced. As of the first 11 days in December, Farmers has received about 600 — excuse me, 6,650 claims relating to physical damage to property and another 350 involving damage to automobiles. To date, there've been only four worker compensation claims reported. We have no reports of life or health claims.

Of the nearly 7,000 claims that have been reported, 5,200 (or 74 percent) of them have already been closed out. Most of the claims still pending involve situations where advanced payments for additional living expenses have been made, but the payments for repair work have not been finalized.

CHAIRMAN GREEN: On that issue, when you write a check from Farmers to your client, do you write it as a two-party check with a lending institution and him?

MR. GELFAND: It depends on what kind of check. For additional living expenses, no, we make those out payable directly to our insured.

CHAIRMAN GREEN: I think what we've had in past testimony is that some of the clients were having problems getting them cashed so they could pay their contractor for the construction as they go along, the progress payment, because some of the lending institutions refuse to sign the check until it's a completed project.

MR. GELFAND: Okay, on those type of payments where it's for structural damage, we are required by the Legislature and by the Insurance code to include the mortgagee on the draft if they are named as an additional insured on the policy.

CHAIRMAN GREEN: I know that but we wanted to get that in the record.

MR. GELFAND: It's in the record.

CHAIRMAN GREEN: Thank you.

MR. GELFAND: But that's only on losses. The small repair type losses, those involving less than a few thousands dollars even if it's on a structure, we are not double naming, we're just paying those directly.

CHAIRMAN GREEN: Thank you.

MR. GELFAND: Forty-six percent of the claims that have been closed were closed without any type of payment, and those were where there was either no earthquake coverage available or the loss was below the deductible. In both cases, our customers needed an insurance company denial for either IRS or FEMA purposes, and we assisted each of our policyholders in this respect whether they had earthquake coverage or not.

The estimated total dollars that we will pay to satisfy these earthquake related claims is going to be substantial. At this time we are projecting that a total of $50.6 million will be paid to our policyholders in satisfaction of their claims, along with an additional $6 million in adjustable(?) expenses.

To put the situation in perspective, the '87 Whittier quake down in Los Angeles resulted in a total payout of $12 million in total claims in the Farmers group. So that means the quake up here, we're going to be paying out four times the size of that one.

The vast majority of these payments of the $50 million will be for property claims. The remaining $600,000 will cover physical damage to the automobiles and a small number of worker compensation losses.

With the loss projections of $50.6 million, our reinsurance treaties will come into play. We retain the first $40 million in loss for any one catastrophe plus an additional 5 percent on all sums over that amount. So in this particular loss we're expecting our reinsurance treaty now to cover about $9½ million, or a little less than 20 percent of the projected loss.

We've established catastrophe procedures to respond to disasters such as the one that occurred on October 17. Within hours after the quake we had plans that were activated already to bring in an additional 150 adjustors from around the country into our Bay Area in the Central Coast/Santa Cruz area. A catastrophe center was opened the next day at our regional facility in Pleasanton which served as a command center and clearinghouse for all earthquake activities. Our 14 Bay Area branch claims offices also assisted in the catastrophe operation and they all operated on extended hours and also on weekends.

During the hours and days following the quake, there were obviously public confusion over what to do next. We utilized statewide network news services which were linked to newspapers, radio, and television to communicate with our policyholders. Our message included word that we had established a catastrophe center and our insureds should contact a Farmers agent for information and assistance. A toll-free 800 number was established to further offer assistance to our insureds, and that was in our catastrophe center in Pleasanton.

Our 750 Bay Area sales agents reponded quickly to this catastrophe, and their primary role was to secure loss reports from our insureds that suffered earthquake damage. The agents then personally delivered these reports to our 14 claims offices or they even delivered some of them to our catastrophe center directly. So all officers were able to reach the catastrophe center within 24 hours of being reported to us.

Our agency force was not asked to assess or estimate any of the damage. We did ask that they help their policyholders by advising them to make temporary repairs and if possible, to begin inventorying any damaged items which was going to help in the settlement process once they were contacted by the claims adjustors.

Once the insured's damages were assessed, he or she was free to choose any contractors they liked to complete the repair work. If the policyholder requests, our claims staff will provide a listing of reputable and licensed contractors in the area who do that type of work, but the policyholder always had the right to determine which contractor was going to eventually work on their own home.

From all we've been able to determine, the overall claims handling function has operated effectively under the extremely difficult circumstances which were presented by this catastrophe. We are aware of very few unusual delays in handling any of the nearly 7,000 claims that we incurred.

In broad terms, our Farmers earthquake insurance provides coverage for accidental physical loss to an insured dwelling or mobilehome, separate structures, personal property, and loss of use of the resident premises which was caused by an earthquake. Named losses are not insured, and when I talk about named losses I'm talking about losses which are caused by fire, explosion, nuclear hazard and likes of that nature. The fire policy does cover those type of direct physical losses by fire and explosion even though they did result from an earthquake.

In the area of commercial insurance coverage, we do offer loss of income protection that can be attached to our commercial earthquake policy if the insured chooses to purchase that coverage. If it's not part of the basic coverage offered on our — it is not part of the basic coverage we offer on our commercial earthquake policy but it is an option.

We continue to write homeowners policies before, during, and after the October 17th quake.

However, we did implement an earthquake moratorium immediately following the quake in our six Bay Area counties only. The moratorium was cancelled on November 10th and earthquake insurance was subsequently offered to all new policyholders written during that moratorium period.

We have not altered either our rates or our underwriting rules since the earthquake. This applies to both commercial as well as our homeowner coverages.

CHAIRMAN GREEN: So you do offer commercial insurance for earthquake.

MR. GELFAND: Yes, we do.

CHAIRMAN GREEN: Do you give the same answer as the last — the broker that was here in that you exclude certain areas from your coverage, or do you cover the whole State of California?

MR. GELFAND: We cover the whole State of California but we do not write certain type of risks in commercials, such as an entire masonry type structure built out of brick. That would be ineligible for commercial earthquake coverage, irrespective of where in the state it was.

CHAIRMAN GREEN: But this gentleman that was here from the food company — in other words, he could go through your company for his store and get earthquake insurance here at the Marina area?

MR. GELFAND: Definitely. Unfortunately, I'm in the wrong end of the business. If I was one of our agents, I would have contacted him outside right after his call. But yes, that is available through our company.

CHAIRMAN GREEN: We have his name and address so you can contact him.

MR. GELFAND: I wrote it also.

CHAIRMAN GREEN: Okay.

MR. GELFAND: We extend earthquake coverage in compliance with the California Mandatory Offer of Earthquake Insurance law. Under the law, we offer earthquake coverage on every fire policy, covering the dwelling and/or contents of one, two, three or four units which also include mobilehomes and condominiums. This offer is extended without regard to location, soil type, or construction type. We will write earthquake coverage only as an added coverage to or in conjunction with the fire policy. We will not write it as a stand-alone policy by itself.

Our earthquake rates are based on two construction types: frame, which includes frame and stucco, and masonry. And masonry rates are about five times greater than the regular frame and stucco rates are. We do not subscribe to rate setting practices which would effectively prohibit the purchase of earthquake insurance.

As a service to our policyholders, we have developed and will soon publish an earthquake safety guide which provides information to reduce or prevent damage to the home, including tips on personal safety while either at home or away at the time of the quake.

For our commercial insurance customers, we continue just as we have for many years to provide loss control services which include inspections and recommendations to reduce exposures to earthquake damage.

Finally, the committee has expressed interest in the amount of premium revenue generated over the past ten years for earthquake coverage. I think Consumers Union also asked that you look into that. Well, the 10-year period beginning in 1979 has, not surprisingly, showed a steady increase in premiums written. In 1979 our member companies in the Farmers Group wrote a total of close to $560,000 in earthquake premium. Due to dramatic increases in both property values and construction costs, along with a greater awareness by the public on their need to protect their investments, the 1988 annual premium written was $29.3 million. The 10-year total of earthquake premium for all of the Farmers Group combined has been $128 million.

It's important to note that this 10-year total reflects premium from the entire State of California. At the time of the October 17th quake, our member companies had 200,000 policies statewide with earthquake coverage written on them. Seven thousand reported claims from this disaster represents slighly more than 3½ percent of the policies in force at the time.

The economic realities of a major earthquake in California are staggering as this recent unfortunate experience shows. Claims were filed by only 3½ percent of our earthquake policyholders, yet the projected $50 million in claims is nearly twice the amount of earthquake premium paid to our company in 1988, and nearly 40 percent of the earthquake premium we've collected statewide in the last 10 years as totaled(?). Had a 7.1 quake struck the Southern California area where we have the majority of our earthquake business, the claims figures would have been even greater.

Farmers is ready to work with all interested parties, both public and private, to promote earthquake safety and preparedness. We look forward to reviewing the findings and recommendations of your committee. And we thank you, Mr. Chairman, and we'll be glad to answer any questions you or anybody else may have at this time.

CHAIRMAN GREEN: It's become quite clear to me, sitting here listening to the complaints, that it's a certain few companies — and possibly I might say certain reasonable companies — not responding to their policyholders as kind of painting the whole industry with a broad brush. What would you suggest within the industry that would bring these companies more in line with the companies like that you represent?

MR. GELFAND: Jeff, you might want to handle that from a public relations aspect. (Laughter.)

CHAIRMAN GREEN: I know it's a broad question.

MR. GELFUND: I, like some of the others, also brought staff.

MR. JEFF BEYER: If I understand your question, it's what could the industry do as to improve the overall...

CHAIRMAN GREEN: Well, what could we do statewide or what could be done. For instance, there's maybe four or five of the majors — which you represent one of them — that have done a comparatively good job. Sure, you have complaints too, but we find most of the complaints that I've heard of and most of the mishandling by the insured out there from some of the smaller regional companies that are carrying some of this insurance. Is there any answer to that?

MR. BEYER: I guess that's a tough question to answer. It's a competitive industry...

CHAIRMAN GREEN: Well, it's a competitive industry but you have the giants and you have the little guys; yet, the giants are doing a pretty good job, the little guys are not. That brings it right into retrospect.

MR. BEYER: It's a gray thing because one of the restrictions placed on companies and industry after 103 came about were the antitrust violations and almost prohibiting companies from even discussing many aspects of their business claims — handling, rating and so on — with each other. So this may even fall into that area that's precluded us from getting involved with many of the other companies.

CHAIRMAN GREEN: No, I didn't say that. You're in a committee meeting today and I'm asking for an answer — not getting together with another company — what you see as helping the industry, from your viewpoint, or is there any?

MR. BEYER: I guess it's difficult in terms of service to policyholders. Now, we can only speak to our company and how we handled it, and I think we're very competitive on service as well as on rates, and this is the kind of situation where we try and respond as quickly as we possibly can. I guess I'm not sure how to answer your question in terms of what could be done to improve the claims handling and response of the entire industry, and I think that's a difficult question for a company to answer. We might ask the federation to consider that question and provide some kind of response to you because we'd certainly like to think about that.

CHAIRMAN GREEN: We want our small people in the state to operate as well too, but maybe because of the size of your company, the economics of your company and the amount of agents you have in your company compared to somebody that has a tenth the amount of personnel, maybe you can do a better job because of your size.

MR. GELFAND: This points out one of the major differences among all insurers and that's the type of service that enable — to bring to their policyholders in time of a loss.

MR. BEYER: If I might suggest, perhaps we could follow up through with the federation which brought us here today and ask them to provide some thought to the committee.

CHAIRMAN GREEN: It's possible, and see, even though we're just having testimony, we would be happy if you would give us any written documentation or anything that we could use for our record.

I think another thing that's been coming out of these hearings is the delay of claims. Is it clear by the head — like if it's a large claim, is that delayed more than like a little claim or is it just the policies of the company of what you have to do to get the claim out there?

MR. GELFAND: When you talk of a delay we're talking about two different types of delays. We're talking about an initial reponse delay in getting out there and getting it started, and then a delay before the claim was totally concluded.

CHAIRMAN GREEN: Well, like we heard here today one person is still, here some months after the quake, he still hasn't got his claim all put together.

MS. LINDA JORGENSEN: My name's Linda Jorgensen. I was responsible for setting up the catastrophe center and I saw the initial claims being handled. Within the first two weeks, most of the closed claims that we saw were from the East Bay/Contra Costa area as being basically cosmetic minor damage — cracks in the sidewalk or a retaining wall — something small that once the adjustor was out there was capable of estimating and closing and getting agreement out on the spot and then close it. The larger ones, particularly in the South Bay/Los Gatos area...(tape turned)...we had to have better estimates. There was a lot we could do before we could even determine whether those houses were even repairable, let alone starting to get the repair costs.

So just by the very nature of the size and the complexity of the claims, those types of claims are going to take longer. And those are the ones that we still have out and not settled. We know that we owe them but we don't know how much the bill is.

CHAIRMAN GREEN: As part of this factor in what you're doing, the upgrading of insurance — like, you know, it's a $400,000 building today, but when you put the seismic current building standards into it, then it might be a $500,000 building — and the difference, is your client paying or are you paying? How are you handling that?

MR. GELFAND: It depends on the type of policy. The majority of our homeowner policies have what we call full-value protection. So in case of a total loss, we will pay, irrespective of the policy limits, whatever it costs to replace that structure if they have earthquake coverage.

CHAIRMAN GREEN: Yeah, but what we're finding is there's a portion of the building damaged but they're going to have to bring the other part of the building up to code before you pay that part of that claim.

MR. GELFAND: That's the same testimony we've heard earlier today about these problems? Nobody has brought up the fact yet that that type of insurance coverage is available in the industry, and that coverage protects an insured, whether it be a commercial insured or a residential insured, from purchasing coverage which will pay for the upgrades not covered under a basic policy. That's fully available. You can insure purchases that yes, they will be protected and pay for that difference.

CHAIRMAN GREEN: What kind of educational thing are you giving to your insureds that it is available or are your agents...

MR. GELFAND: All of the agents are aware that the coverage is available. Now, all of the agents work on commission. The more coverage they sell the more money they get. And I think where we're torn with a basic philosophy that when agents are competing in an open marketplace to sell insurance, they come in and want to compete and come at the lowest price. You could keep adding coverages onto a basic policy and be out of sight. I don't think that the general population has ever been made aware of this type of insurance. And this is one of the things we have found as an insurance company is that the further education of our agency force from this day forward is going to change quite a bit.

CHAIRMAN GREEN: In other words, what you're testifying to is what — a question I asked in Santa Cruz — what did you learn from the current earthquake?

MR. GELFAND: Oh, definitely.

MR. BEYER: If I could just address that for a minute, Mr. Chairman. Education of both our policyholders and our agency force is something we've spent a lot of time discussing since the quake. I mean, it did teach us some lessons and one of them was the value of more education on the various coverages that are available, helping the policyholder determine whether those coverages are necessary for them, and we are right now planning a major re-education campaign material that will be mailed to all our ten million policyholders throughout the United States, because we feel most of those people live in some degree of earthquake prone areas, and at the same time, a major re-education program of our agents so that they are in a better position to deal with their policyholders whenever the question of earthquake coverage comes up to fully explain the various coverages that are available from Farmers. And we think they do a good job now but we're trying to improve that. In January and February, many of these materials will be going out both to our customers — not just in California but across the country — and our agents at the same time.

MS. JORGENSEN: One of the adjustment problems that we encountered with all the major carriers was when they started actually inspecting the damage to these houses. This is very unusual damage. It's not a normal fire loss or a water loss. We're seeing damage that we've never seen before and it is very difficult to inspect the amount of damage. What appears to be cosmetic may in fact be life threatening, and it is very difficult on the surface without getting a very thorough inspection of the cross base underneath the house as well as the attic, any number of different areas of damage that may be indicative of further damage and that being the difficulty that the adjustors face because there are very few adjustors that have experience in earthquake damage. And I think that's probably a problem that all of the carriers are suffering right now.

MR. BILL GAGE: Okay, I want to thank you for your testimony. We have one more question that the Senator was going to ask. First is do you apply the deductible to the value of the property or the amount of the damage?

MR. GELFAND: The value of the property.

MR. GAGE: The second was what are policyholders required to do to meet the deductible? We've had testimony that they had problems in trying to actually come up with the amount of the deductible in determining both personal property damage or structural damage. Is it just structural damage or is it both personal property and structural that's considered?

MR. GELFAND: Within that deductible?

MR. GAGE: Right.

MR. GELFAND: It depends upon which type of policy your coverage is taken out. If it's on a — it's an easy question with a complex answer. If it's on a homeowner type policy with an earthquake type endorsement added to that policy which covers all of those coverages, then the deductible is an aggregate — it's a separate deductible on each type of coverage. For example, if it's a 10 percent coverage on a building, that building coverage applies separately. If it's 10 percent coverage on — then it would be a 10 percent deductible on the contents which applies separately.

Now, aside from that there are separate earthquake policies that you can purchase in conjunction with a fire policy, and that's an aggregate deductible, which means that the total loss, if the total loss of contents, additional living expenses, building, permanent structures exceeds the aggregate deductible, then there's coverage. So there's a couple of plans the insured has.

MR. GAGE: We also have with us representatives from the Senate Insurance Committee. I wanted to ask if Jim or Sal have any questions?

MR. SAL BIANCO: Well, there's a basic one we'd like to ask. When you were talking about upgrade coverage and you were talking about your basic policy, could you tell us what the cost of those two coverages are?

MR. GELFAND: I don't know. I don't have that available.

MR. BEYER: We'd be happy to make that available.

MR. GELFAND: But I think we'll all be surprised how inexpensive it's going to be, and it can be purchased — I know it can be purchased in increments of a thousand dollars. You can purchase $5,000, $10,000, $100,000 worth of coverage.

MR. BIANCO: Next you were talking about your aggregate earthquake policy. I may not have given the name of the policy correctly. Did you submit that to us? I don't have that document, and could you do so if we don't have it?

MR. BEYER: Certainly.

MR. BIANCO: It's interesting, the State Farm Insurance company's policy that they submitted to us — on the second page — indicates that California law requires them to indicate to each policyholder how they can file a complaint with the Department of Insurance. The policy that you submitted to us did not contain that same page. Is it your understanding that that's a requirement under the current statute or perhaps the competitor has done something that is beyond what the scope of the statute is?

MR. BEYER: The question again was that State Farm has...

MR. BIANCO: The State Farm policy given to us, which we have right here, simply says "and per notice, California law requires us to provide you with information for filing complaints with the State Department of Insurance regarding the coverage and service provided under this policy. Complaints should be filed etc.," and then gives the address for the Department of Insurance. Under your policy you submitted to us, that particular information is not there, and I was just wondering, from your perspective, perhaps State Farm may have done something beyond the statute or perhaps the statute doesn't include that.

MR. GELFAND: That clause is now contained on all new fire policies, and the copy that was submitted to you may not be the most current edition, hopefully.

MR. BIANCO: So therefore the November 8, 1989 document we have is not the most recent document. Is that correct?

MR. GELFAND: We'll get a response back to you on that. It may be on the declaration sheet which is attached as part of the policy.

MR. BIANCO: Okay.

MR. GELFAND: But we do have some good news. We do have a package wrap-around earthquake policy here for you. Without the wording on it.

CHAIRMAN GREEN: I know we learned a lesson and I think we're hearing different things this year than we did two years at the Whittier, and we've got the soil condition now as a factor. Will there be a coverage change in your policies because of the situation like here in the Marina area?

MR. GELFAND: I am not aware of any contemplative change in coverage right now as a result of this. The extent of our exposure in loss in those areas is extremely minimal.

CHAIRMAN GREEN: Of course, we've got other areas of the state too that has the liquefaction factor. Now, I guess I'm just asking what will be your policy as far as the liquefaction on the future of earthquake policies?

MR. GELFAND: I have no idea. I couldn't even begin to guess.

CHAIRMAN GREEN: Question?

MR. JIM CATHCART: Yeah, I have a couple of questions, if I might. First, if I am a Farmers policyholder and when I initially got the homeowners policy and was offered the earthquake and was rejected, and upon my renewal I now desired to have earthquake coverage, will Farmers write me or will they not?

MR. GELFAND: Yes, they will write you.

MR. CATHCART: Is that standard company policy?

MR. GELFAND: Yes.

MR. CATHCART: Second, you indicated your amount of reinsurance, the reinsurance treaty that you have for your earthquake coverage limits your exposure in case of loss, is that generally available? Have you ever had any difficulty getting that, one? Two, is that in the London Market or is that elsewhere? And three, if you have greater exposure in writing the policy, will it be difficult to get additional reinsurance?

MR. GELFAND: No, yes, and probably. In answer to your first one — go ahead and paraphrase, if you would, the first one, the...

MR. CATHCART: I've probably forgotten them now. (Laughter.)

CHAIRMAN GREEN: With your treaty on coverages.

MR. GELFAND: We had no problem obtaining the reinsurance.

CHAIRMAN GREEN: You know, that's kind of like — if you'll equate their treaties to bookies. You know, they have so much in their pool and they go to other bookies to get the rest of it, so they pass it off.

MR. GELFAND: Right now, the reinsurance market is such that we could probably purchase as much reinsurance per catastrophe as we wanted. We carry right now $275 million total on our catastrophe treaty. And the availability for more is there. We don't see a problem if we wrote ten times more earthquake by extending that treaty. And it is through the market. The market is through — there's always an open market.

MR. CATHCART: Now, when you mentioned that — you gave us various data about the number of claims and the number of loss that you paid out and the amount of premiums that you collected. Is it possible to get a breakdown on that at a later time between that which was for homeowners' endorsements or if the coverage in that was for commercial buildings?

MR. GELFAND: Yes.

CHAIRMAN GREEN: Thank you. Appreciate that. And thank you for coming out today. We appreciate your being here.

MR. GELFAND: Thank you, Senator.

CHAIRMAN GREEN: All right. Next we have California State Automobile Association. We had one of your complainers here. How would you answer our first individual that was — or one of our clients that was here today...

MR. BARRY SHILLER: Mr. Cobb? Mr. Chairman, Barry Shiller for Triple A. Obviously his comments are disturbing, and I know from the claims people that I've talked to, we've been working with him since the second day after the earthquake on his claim. And Eileen Carroll of your staff and I are going to continue talking about that claim and continue to update you and your staff on its status until it's settled. And we are as committed to settling his claim as we are every claim, and it's unfortunate to hear his concerns and we're going to work to resolve them.

CHAIRMAN GREEN: Well, good. Is your report at this hearing about the same as it was over in Santa Cruz?

MR. SHILLER: Yeah, I was going to offer to merely offer to you the changes in the numbers that we broke down for the Bay Area which we've offered to you and to the committee staff. Beyond that, perhaps I could simply address the same questions that you've been asking of others. I might need to have you repeat them since there've been a number of them, but that's fine, we can do that.

CHAIRMAN GREEN: Well, I think that basically yes, you have been one of the larger companies that have handled things well over there. I was surprised to hear today of this person that was after Triple A because I've heard a lot of good glowing reports in Santa Cruz, but we're not in Santa Cruz now.

MR. SHILLER: That's right.

CHAIRMAN GREEN: So I guess my question is with your company, do you have a different person in charge here than you have over there, or do you work in districts in this type thing and would that be your answer to maybe what his problem is?

MR. SHILLER: Well actually, Senator, I will tell you very simply. We have offices in so many of the communities that were affected by the earthquake that there are — for example, in Mr. Cobb's case, our Oakland district office is located maybe two miles from his home. So we are as close to him as we were to most of the people in the Santa Cruz area. No, in fact our claim management, which has been collaborating and organizing all of the efforts regarding earthquake claims, all operate out of three-and-a-half blocks from here here in San Francisco. So I would hope — I really would hope that his experience was an exception to what otherwise was the experience of our policyholders, and I would hope that the Department and others will be able to report on how many concerned policyholders there were, because obviously those sorts of comments don't help anyone. They don't help us and we don't like having unhappy policyholders.

CHAIRMAN GREEN: Okay. I guess the question I had, the major question was some of the regional companies, as you heard earlier, we seem to see more complaints, more problems with the claims and the delays and the cause than the major carrier. Do you have any answer to that, or is it what we sort of conjectured with Farmers?

MR. SHILLER: You know, I thought about one of the questions that was asked on Friday, which was should other companies offer the same extended coverage that — I think Sal Bianco might have asked the question. I thought about it later and I realized that you know, in a great sense, the fact that some companies fare better than others in terms of the public perception might be the stimulus to get other companies to compete with them by offering service, because obviously, when you buy the product, that's not really when you get the test of whether the product you buy is good. It's when you have a problem, when a disaster occurs.

I really can't offer any comments to you on ways to make companies behave more responsibly than they did. I think your oversight and the Department of Insurance's oversight as to how companies perform is probably the only step that can be taken, and then from there you can determine what kinds of patterns of things are occurring and deal with it.

CHAIRMAN GREEN: How about this soil conditions problem that's going to pop up? It wasn't so much a factor in Santa Cruz but it is here and in other parts of the state.

MR. SHILLER: Well, as was the case for us in the Santa Cruz area, our underwriting guidelines haven't changed a bit. We began to offer earthquake insurance the morning after the quake, and the only thing that we do with respect to any policy is go out and look at the home to determine what condition it's in. I think I mentioned at the other hearing that there are some people who are worried that until a lot of rain falls on some of these areas — and it may not be as true in San Francisco as it was in the South Bay — there were going to be some concerns about what happens to the soil and whether or not it's able to support rebuilding. But we aren't, at this point, contemplating any changes in the decisions we make or the underwriting standards.

CHAIRMAN GREEN: Yeah. And another thing that was brought out here today, not in Santa Cruz, was what the municipalities are requiring of their — to bring the houses up to code for the seismic. Partial damage of the house, they've got to bring the whole house up to seismic. What is your company going to do on that?

MR. SHILLER: Well, I'll tell you what we're doing with regard to claims now. If we find in a home that has earthquake coverage that the foundation is damaged sufficiently that we've got to get involved, we are repairing the foundations up to current code. The policy does not require that that be the case. Our experience is if we're going to spend thousands of dollars to repair the foundation anyway, we are taking the position that we are going to go ahead and spend what is not dramatically more money to do updates to code. You know, I can't comment on the practices of other carriers, I don't know what they're doing, and I don't know enough about municipal code requirements to be able to comment intelligently, but that's the position we're taking with our claims. We are bringing them up to code when we get involved in them and we can do so.

CHAIRMAN GREEN: Okay, good. I don't have anything else. Do you have something?

MR. CATHCART: Yeah. I would like to ask Mr. Shiller a question. We know that you've taken a pretty big hit — 50 billion plus dollars. We know that the homeowners line is a relatively small line for your company, that you're largely dominated by insuring automobiles. My question is the loss that you're going to take on this, will this adversely affect the automobile insurance rates that your company offers to Northern Californians?

MR. SHILLER: I would suspect that to the contrary we would be in a position to not face inordinate damage. In fact, I will tell you that we very recently announced to our policyholders that we are increasing the dividend on their auto policies from 10 percent to 15 percent. So I would not suspect at this point that we are going to have deleterious impact.

MR. CATHCART: You have enough of a surplus to take it out of, in effect, the auto rates.

MR. SHILLER: I'm not an actuary, but my perception is that although we are paying out more than we've collected in earthquake premium, earthquake is not a real major line for us. We have about 220,000 policies total. Twenty percent or so of those have earthquake endorsements. You know, it's conjecture. It's a fair question. Obviously, the real answer won't be known for a while, but at this point I would suspect that what I see as an inexperienced nonactuary is that that wouldn't be a major problem.

MR. BIANCO: Mr. Shiller, I have a question for you, if I might. Mr. Cobb's testimony earlier in the afternoon talked about earthquakes and the number of earthquakes and whether or not he had coverage. You were kind enough to supply the committee with your homeowners policy and of course were able to find the definition of earthquake. Maybe you might be able to get back to us later if you don't have the answer, that's just fine, except for the record the committee ought to know that earthquake is defined as anything occurring within a 72-hour period, meaning after the initial shock. I think it would be of interest to us is whether or not your company, after the 72nd hour has passed, would consider those tremors — and I'm changing the term now for a reason — earthquake shocks. I also didn't find in this booklet a definition of earthquake shock, so there must be some kind of a generic term that's used and maybe you could let us know later about that.

MR. SHILLER: Sure. On the first issue, on the first question, with respect to Mr. Cobb, we are not interpreting what may have been subsequent damage to his chimney as a separate event. We have committed to him already; in fact, we committed to him before today to replace his chimney under his policy subject his deductible, and I would dare say that the biggest problem we have had is in misinterpreting some things that were conveyed, I guess.

The second question, I will get an answer and we will provide it to the committee. I don't have an answer now to that issue.

CHAIRMAN GREEN: Fine. Thank you very much. Then if there's no further questions, thank you for coming.

MR. SHILLER: Thank you.

CHAIRMAN GREEN: All right, then next we'll have the Association of American Insurers, and National Association of Independent Insurers, and the Association of California Insurance Companies; if you'd all come forward, please, and take a seat at the table. They're not here. Okay, that puts us down to then Alliance of American Insurers. We'll make testimony part of the record which we have in writing. Isn't that true? So we will accept this — it's a statement of Alliance of American Insurers and before this Subcommittee. It's dated December 13, 1989. So that will be made part of the record.

(ALLIANCE OF AMERICAN INSURERS' TESTIMONY INSERTED)

The Alliance of American Insurers is a national property and casualty insurance trade association representing 170 member insurance companies. In California in 1988, Alliance member companies wrote $121 million in homeowners insurance premiums, or 5.5 percent of the market in that line; and $160 million in commercial multi-peril premiums, or 5.3 percent of the market in the state.

We appreciate this opportunity to provide comments regarding insurers' experience following the October 17 earthquake. At this time, the Alliance is not prepared to specifically address the questions and issues posed to the industry by the Subcommittee on earthquake insurance in the memorandum on November 22. However, the Alliance will submit additional comments to the Subcommittee in the future once our member companies have been surveyed.

In order to quickly respond to the needs of their policyholders in Northern California, many insurers dispatched claims units to the San Francisco area immediately following news of the October 17 earthquake. These individuals made an initial survey of the damages and determined the number of adjustors needed to quickly settle claims. Since most of the initial news reports centered around the San Francisco area, a number of companies located their claims headquarters in San Francisco. Later, when it was determined that much of the damage was south of San Francisco, companies relocated their claims headquarters in order to better respond to their policyholders' needs.

A number of companies ran newspaper, radio, and television advertisements informing their policyholders how and where to report claims, while other companies contacted their agents in the area and relied on their assistance in claims reporting. Some companies even chose to personally contact their policyholders in order to determine whether any damage had been experienced. The lack of telephone communication sometimes made claims reporting difficult and also prevented insurers from contacting their claimants in order to notify them of the time when an adjustor would be available to visit the damaged site.

While insurers tried to handle all claims following the quake as quickly and as efficiently as possible in order to indemnify their policyholders, some delays were unavoidable. First, bad weather and subsequent landslides, particularly in the Santa Cruz, Watsonville, and Hollister areas, often prevented adjustors from visiting claimants at the earliest possible time. In addition, some municipalities found it necessary to limit outside access to a particular area for safety reasons which also limited insurers' ability to quickly respond to their policyholders' needs.

Second, delays also resulted because builders and contractors often concentrated on the large losses following the earthquake. Smaller claims settlements were often delayed until a contractor became available to provide estimates or repair damage. Finally, some homeowners were encouraged to submit claims even if they had no earthquake coverage as a means of providing some proof of damage to the Internal Revenue Service or to the Federal Emergency Management Agency for disaster assistance purposes. These additional claims may have created some delays for those who had earthquake coverage since companies needed to investigate all claims to determine whether or not there was any coverge under the homeowners policy. The increased volume of claims likely to be denied may have created delays for homeowners who had earthquake coverage and were entitled to indemnification.

In general, insurers handled claims for the earthquake victims as quickly as was possible. In many instances, on-the-spot payments or cash advances were possible once the adjustor was able to visit the damaged site. In some instances, insurers were also helpful in identifying property damage that was not readily detectable by the property owner.

Industrywide estimates or insured earthquake losses range from about $1 billion to $4 billion, depending on the source. While the dollar amount of insured losses is still somewhat unclear, one thing is clear: This was not the catastrophic earthquake scientists predicted would strike in the United States within the next 20 years. Such a catastrophic earthquake could result in an estimated $50 billion in insured losses.

In an effort to prepare for the inevitable event, the Earthquake Project, a coalition of property and casualty insurers, has prepared a legislative proposal to create a program which would permit insurers to offer affordable earthquake insurance coverage to homeowners across the nation and would provide insurers with federally-backed reinsurance against truly catastrophic earthquakes. The program would be national in nature because the earthquake problem extends beyond the borders of California. According to a report by the U.S. Department of Commerce, all 50 states are vulnerable to the hazards of earthquakes and at least 39 are subject to major or moderate seismic damage. The economic consequences of a catastrophic earthquake are not limited to those individuals and businesses in the area directly affected by the quake. Therefore, the solution for the earthquake problem must reach beyond state boundaries.

The Alliance of American Insurers supports the Earthquake Project's federal proposal for earthquake coverage as a means to prepare our country for a truly catastrophic earthquake. Members of the Earthquake Project are currently preparing a legislative proposal for introduction into Congress in early 1990.

(HEARING RESUMED)

CHAIRMAN GREEN: So that takes us through the hearing for all of those people. We do have at the door a sign-up sheet for additional testimony, and Charles LeKamp from San Francisco Apartment Association.

MR. CHARLES LeKAMP: My name is Charles LeKamp.

CHAIRMAN GREEN: You've been very patient all the way through this hearing.

MR. LeKAMP: I've enjoyed it immensely. I'm a Vice President of the San Francisco Apartment Association. It's been a very enlightening hearing. I have a couple of comments that I hope might be helpful. I happen to be — this is in a hearing regarding how well insurance worked in this earthquake.

CHAIRMAN GREEN: Are you representing the owners of Apartment or...

MR. LeKAMP: I am representing the owners of apartment buildings in San Francisco who are members of our association.

CHAIRMAN GREEN: So this could be essentially the "Apartment Owners Association."

MR. LeKAMP: Right. There are two things that I'd like to comment on. We had two occasions where we used the Marina and held public meetings for both tenants and owners — homeowners and apartment owners. One of the things that was most striking in those meetings — we had an average -- I think the first meeting we turned out about 600 people and the second one we had around 300, 400 people — was how few people had insurance. And perhaps that particular question needs to be addressed.

Most of those people looking back on it wished perhaps that they had had insurance, and when you're looking at a major claim, a major loss, you're thinking well, could you afford it. But one of the real problems that consumers and perhaps carriers need to address is how to broaden that base, that base of customers, to reach so that the — perhaps the best analogy, if you know that there are three men in a room and there's a certainty that a 500-pound weight is going to fall on one of them, I don't think you'd have a hard time convincing all three of them they should buy the product.

San Francisco is a community that's got a record of a major quake. How come it's so hard to sell insurance here? Possibly because the carrier looks to trying to protect themselves in this particular market, which is very difficult. Sacramento, I don't think people worry particularly about earthquake insurance. You don't have the problem over there. We do, and yet we're still looking at this 7.2 quake. When you look at the amount of damage compared to the potential for damage, the number of policies that are actually triggered and paid, the losses here were phenomenally small.

That tells me personally, and I happen to be contractor and I am not a structural engineer but I had the privilege of looking at about 75 different apartment buildings following the quake in the couple of weeks for immediate hazard — this was the request of a property manager and I did this at a very nominal rate so that we could remove risks to tenants and keep people in place — buildings need to have a hard look at what their real risks are. Newer structures came through beautifully. Older structures, it depended a lot on the area and the soils conditions.

The types of policies that you're offering is another consideration. Right now we're looking at -- well, I just had a customer of mine look at a new insurance policy for a $1 million building approximately. He had full insurance based on fire, etc. — $4,500 was his annual premium. This was two days ago. The earthquake insurance on that same building was $15,000 and his deductible is $100,000.

Now, I do have some trouble with that in trying to convince — if I were a carrier — I would have some trouble in trying to convince that owner who had just gone through a 7.2 quake with minor cracks that he should spend $15,000 a year so that in all probability he would then have the privilege of paying for most of the damage himself if that building wasn't one of those few that was wiped out. We lost about 90 buildings. That's the ones on the red tag right now in San Francisco that are up for grabs on whether they're going to be torn down or fixed. It's out of the market where we have over 220,000 apartment buildings. It's a very small percentage. We need to look at the numbers better.

I think the insurance company has already recognized this and the fact that — with all due regard to their feelings — that everybody seems to feel that they can afford to insure against future earthquakes, it seems to indicate to me that there's perhaps a little bit of fat in some of those figures. In the actuarial tables that I'm sure you're going to be looking at should bear that out.

Our coverage, we did not have extensive complaints from members regarding insurance coverage. There may be the exceptional case. The insurance company, where their coverage kicked in, seemed to do — at least our perception of it was — did a very good job and made every effort to cover the claims. The problem is simply getting enough base so that if we are hit in a worse situation there is a financial pool available that doesn't wipe out the consumer and doesn't wipe out the carrier.

Thank you.

CHAIRMAN GREEN: Thank you. That's basically what the direction of the committee is going for is affordable earthquake insurance.

MR. LeKAMP: And I commend you for it. Thank you.

CHAIRMAN GREEN: Well, let's hope we can get it put together. Thank you for your testimony. Any other testimony, come in front of the committee.

Well, again, thank everyone for coming out today. It's been very informative again, and we look forward to seeing you next time, and watch us, because we're going to be in February, at our next hearing, announcing what this committee will be doing.

Thank you all very much. And thanks to staff and to the State Building here furnishing the facilities.

—oo0oo—