

U.S. SENATE COMMITTEE ON COMMERCE, SCIENCE, AND TRANSPORTATION

OVERSIGHT OF THE PROPERTY AND CASUALTY INSURANCE INDUSTRY

April 11, 2007

Overview

Good morning, Mr. Chairman and members of the Committee. Thank you for inviting me here today to discuss the availability and affordability of property and casualty insurance in the Gulf Coast and other coastal regions. My name is Jim Hood, and I am the Attorney General for the State of Mississippi. I am encouraged by the Committee's attention to this urgent matter.

We cannot solve the problems that face the insurance industry without understanding the true nature of those problems. The citizens of Mississippi are experiencing first-hand the overwhelming power of the insurance industry, an industry that cannot be effectively regulated by state insurance commissioners. Short of federal criminal prosecutions, the industry is not, in practice, limited in any meaningful way by the federal government. The insurance industry is running wild.

Much of this debate has centered on the sanctity of contracts. For example, State Farm has complained that their policies are "now being reinterpreted by the courts and certain elected officials." [See Exhibit A] That would indeed be a problem, if it had actually occurred. What really happened is much different.

The Mississippi Attorney General's Office (hereinafter "MSAG") has learned that State Farm acted after Hurricane Katrina to create and implement three different tactics for denying coverage. These tactics are not set forth in the policies themselves. Homeowners could not agree to those conditions, because they were never made aware that requirements outside of their policies would be used to deny their coverage. On information and belief, these policies were not presented, for review, to our state's Insurance Commissioner. **State Farm's policies on the Mississippi Gulf Coast are not being "reinterpreted" by the courts and elected officials—they are being ignored altogether by the "good neighbors" who issued them.**

What remedy do these citizens have? Tens of thousands of Mississippians have failed to get any relief from State Farm's agents, catastrophe team members or mediators. To add insult to injury, our citizens are then criticized as being litigious when they turn to the courts for relief after they

have been unable to get it any other way. Their former homes are ridiculed by disparaging references to houses built on sandbars. Somehow the homeowner's expectation of payment is preposterous, but the industry's decision to issue a policy on what they later decide is a risky property and collect premiums is not questioned. An honest assessment would acknowledge that Mississippians do not live on sandbars and hold insurers accountable for honoring policies they write. We also have to question the quality of the actuarial data used to set rates if the premiums charged are not related to actual risk.

Defenders of the industry brag that only 1% of Katrina claims are currently disputed, but fail to mention that the insurance industry defines "claim" as a demand for payment under an applicable policy. This definition conveniently omits the common scenario in which a homeowner reports wind damage for coverage under a wind policy, and State Farm denies that any wind damage occurred. The industry definition of a "resolved" claim seems, in many instances to be synonymous with "closed." Homeowners who participated in mediation and received ten cents on the dollar for their damages may have their cases counted as closed, but these are hardly satisfied customers. Self-reporting of customer satisfaction by the insurance industry cannot be taken at face value.

The MSAG has worked diligently to reach an agreement with State Farm that would encourage them to continue doing business in the State of Mississippi. Insurance Commissioner Dale's recent announcement of an agreement with State Farm to re-examine approximately 35,000 claims represents more than a third of the claims recognized by State Farm in Mississippi. However, no extraordinary deals should be required here at all. State Farm has had nineteen months to evaluate and pay these claims. They do not need a deal with either the MSAG or the Insurance Commission in order to pay what they owe.

The remainder of this report will briefly outline the following:

- * tactics State Farm used to circumvent contractual obligations;
- * the impact of those tactics and other conduct on the National Flood Insurance Program (NFIP);
- * lessons learned from Hurricane Katrina.

I. TACTICS USED BY STATE FARM TO CIRCUMVENT CONTRACTUAL OBLIGATIONS

A. A Combination of Tactics: Selective Application of Anti-Concurrent Causation Clauses and the Adoption of a Wind/Water Protocol

Legal gymnastics in the form of anti-concurrent causation clauses and a wind/water protocol

were employed by State Farm after the storm to deny coverage. Policy exclusions should be understandable to the agents selling the policies, the customers buying them, and the personnel interpreting them when a claim is made. The so-called "anti-concurrent causation clauses" and the water exclusions featured in Homeowners policies that became disputed after Katrina are excessively convoluted and confusing. Members of the Committee are urged to review Exhibit B for the comprehensibility of these provisions.

In August of 2006, the Honorable Judge L.T. Senter, Jr. of the U.S. District Court for the Southern District of Mississippi, Southern Division, found Nationwide's anti-concurrent causation clause to be unacceptably vague in the *Leonard* case, pointing out that "[t]his reading of the policy would mean that an insured whose dwelling lost its roof in high winds and at the same time suffered an incursion of even an inch of water could recover nothing under his Nationwide policy... I do not believe this is a reasonable interpretation of the policy."¹ An honest and realistic assessment of whether this language is likely to be applied consistently and fairly by employees and vendors with varying degrees of training and experience working under challenging circumstances, yields little certainty.

State Farm may have recognized this problem. A wind/water protocol issued September 13, 2005, instructed CAT workers, in under three pages, how to make coverage decisions. The protocol was prefaced with this explanation:

Because of the combination of wind and water damages many homes sustained from Hurricane Katrina, the following materials have been developed and are intended for use as a guide for handling various wind and/or water claims in Louisiana, Mississippi and Alabama.

[See Exhibit C]

Surely Homeowners policies issued by State Farm already contemplated that in a hurricane, a combination of wind and water damages could and would occur. The wind/water protocol was not available for policyholders' review but it was, by its very language, designed to evaluate their right to coverage.

Notably, the protocol maintained the anti-concurrent causation clause, but only in certain situations. The second page of the protocol features the following language:

Damage to Property Caused by Flood Waters with available Flood Policy : Where wind acts concurrently with flooding to cause damage to the insured property, coverage for the loss exists only under flood coverage, if available...

[See Exhibit C]

Stated differently, the protocol dictates that if damage is caused by both wind and water, the policyholder only gets paid if they have a flood policy. If they have a wind policy, they get nothing. Thus, the anti-concurrent causation clause is applied to deny claims of policyholders who have no flood insurance, and is used to shift the burden to the federal government through the NFIP. The burden on the NFIP is discussed at length in the next section.

The insurance industry is quick to cite the need for predictability as a reason to exit the Mississippi market, but policyholders deserve predictability too. At the very least, their rights should be interpreted under the policies they sign, not protocols developed after the storm.

B. The third tactic: introducing new terminology after the storm

The most generic definition of a hurricane is a "tropical cyclone." Thus the event of a hurricane is defined by a combination of wind and water. Reducing claims to a question of "wind versus water" is a simplification that reflects the insurance industry's approach to claims and has little or nothing to do with the actual experience of a hurricane.

It is easy enough to neatly sort out which policyholders have purchased wind coverage, flood coverage, or both. Looking at a concrete slab that used to be a family home and determining with any reasonable degree of certainty that 50% of the damage was caused by wind and 50% was caused by water is a tall order, not to be undertaken lightly by under-qualified adjusters and/or rookie, or even seasoned, engineers. Individual lawsuits filed since Katrina have inevitably featured a battle of weather experts, but the actual decisions regarding causation of damage were not made on site by professional weather experts. **Soliciting the advice of adjusters and engineers to determine whether a home was destroyed by "wind or water" makes any ensuing "investigation" more closely correlated with the availability of coverage than the factual findings of damage.**

After the storm, the MSAG received complaints from homeowners who were advised by State Farm employees or vendors that they could not recover for wind damage unless they demonstrated "discernible wind damage." Placing the burden on the policyholder to prove the

nature of the damage represents a departure from long-standing Mississippi law. The term "discernible wind damage" is not included in policy language or Mississippi law, which makes it a disturbing standard to use when determining whether a family will have their coverage denied and live indefinitely in a FEMA trailer. This is yet another illustration of how policyholders were unable to rely on the language in their actual policies because State Farm changed the rules.

II. IMPACT OF THESE TACTICS ON THE NFIP

Wind and water occur together naturally in a hurricane, but not in insurance policies. Part of the challenge of keeping the NFIP and private insurers viable is untangling our understanding of these two forces of nature and either imposing a somewhat artificial division in order to allocate risk and assess damages or developing a unified approach that accurately reflects the reality of the destruction a hurricane can cause.

In our investigation, we found evidence that adjusters for E.A. Renfroe, working for State Farm, were dispatched to damage sites and instructed to determine whether the damage could be categorized as a slab, "popsicle stick," or "cabana." "Popsicle stick" is industry slang for a foundation with support pilings intact; a "cabana" is industry slang for a structure that maintains some degree of post and lintel support but is otherwise a skeleton due to water washing through.

Not much effort beyond riding past the property in a car and looking out the window would seem to be required to make this determination, but the fees for this adjusting "service" were passed along to the NFIP. Adjusters were instructed that if they found the property to be in one of these three conditions, they were to request that an engineering inspection be ordered to provide additional guidance in assessing the damage. This subsumes that the adjusters were not considered qualified or sufficient to make a final determination as to the cause of damage. However, many of these adjusters at this stage, without the benefit of an engineering report and often without the benefit of proper flood training and certification themselves, would go ahead and recommend maximum payment of flood coverage and contents through the NFIP.

So, to illustrate, a home is insured by State Farm under a homeowner's policy for \$500,000 for structural damage and \$250,000 for contents; in addition the homeowner purchases \$250,000 of protection against structural damage due to flood and \$100,000 for contents due to flood pursuant to NFIP policies. An adjuster visits the damage, and determines that maximum coverage is available under the NFIP.

Software programs used by the industry to price home repairs and reconstruction are admittedly not regulated by the NFIP². This can result, for example, in a claim against an NFIP policy, with a calculation of \$1.00 per square foot for drywall repair, and a companion claim under a Homeowners policy for the same property, calculating a drywall repair at \$0.60. The MSAG is

also aware of at least one instance in which a list of contents submitted by the insureds bore no resemblance to the list of contents ultimately submitted by their insurance provider for payment on that same claim to the NFIP. On the second list, items had been added, and values had been elevated to bring the claim up to the amounts needed to trigger coverage through the NFIP.

Continuing our illustration, the adjuster then advises the homeowner that further investigation will be needed to assess the extent of wind damage. However, by approving payment through the NFIP, the adjusters have already made a decision about the ratio of damage attributable to wind and that attributable to water. Unfortunately, the ratio is not based on the actual damage. It is based on the availability of coverage. Damage should be assessed first, then the availability of coverage. Reversing this order turns the entire premise of insurance on its head.

The claims adjusting process continues as an engineer may then visit the property and submit a report of damage to State Farm. The homeowners were not allowed to see these reports. Even though the report was requested in order to assist the adjuster's evaluation, the reports were not given to adjusters. The reports were not given to the claim representatives or even openly circulated within State Farm catastrophe offices. Records of whether and when engineering reports had been ordered and received were accessible only to a limited number of catastrophe employees, and the reports themselves were reviewed by only a handful of people.

The MSAG is not aware of any instances in which a professional engineer's conclusion established a ratio of wind to water damage that contradicted the initial assessment of flood damage by an adjuster. In fact, the engineering reports usually did not separate wind and water damage out into any sort of ratio or proportion at all. How then, is a relatively untrained adjuster considered qualified to do a perfunctory inspection and determine that the proportion of damage correlates with the limits on federal flood policies?

Clearly State Farm is willing to spend the NFIP's money with only nominal investigation, but is much more deliberate and hesitant to spend its own. This may explain why the industry experienced record-breaking profits last year and the NFIP is on track to be bankrupt by September of this year.

III. LESSONS LEARNED FROM KATRINA

What is the appropriate response of state and federal government when an insurance company simply disregards its contractual obligations? How can anyone accurately assess whether or not an insurance company can reasonably be expected to continue doing business in coastal areas without getting to the truth of how much a private insurer actually owed, and how much of that was improperly passed on to the NFIP? If another hurricane hits, and the insurance industry uses the same tactics they did after Hurricane Katrina, who can stop them? If the industry's anti-trust

exemption if not revoked, we will probably be asking ourselves these same questions after the next disaster.

Insurers want to argue both that it is unreasonable to expect them to cover coastal areas and that government involvement is not warranted because it would "displace" private capital. If private industry continues to abandon the 130 million Americans who live in coastal regions, one could hardly say that private capital has been displaced. It has been withdrawn, and a vacuum exists that threatens the housing market and economic viability of significant parts of our country. One of the biggest benefits the insurance industry has to offer, the ability to capitalize risk and spread it globally, is completely absent in areas that have been abandoned after natural disasters. The industry opposes government intervention on the grounds that it will simply shift risk around, rather than spreading it, but Hurricane Katrina has shown us the industry's willingness to shift its own obligations onto the taxpayers supporting the NFIP.

The insurance industry has also asserted that the 2005 hurricane season wiped out premiums and underwriting for the last several years in Mississippi and Louisiana. If the premiums charged in Mississippi were not enough to cover the policies, then perhaps the inquiry should be into whether or not State Farm's actuaries anticipated implementing this scheme to maximize coverage under the NFIP when they recommended the rates in effect when Katrina hit.

Further, if homeowners can only expect to recover the amounts they paid in through premiums, what is the difference in what a private insurer can offer and a government-backed catastrophe savings account? Many of our citizens would have been overjoyed to recover the amounts they have paid in through premiums, but were denied even that modest a benefit of their bargain with insurance companies.

According to recent publicity by State Farm³, they have "handled" about 84,000 claims and paid out "over one billion dollars" in Katrina claims in Mississippi, excluding all payments made through the NFIP. That averages out to less than \$12,000 per claim and covers claims from an undisclosed number of Mississippi's eighty-two counties. Insurance Commissioner Dale's agreement, under which State Farm will "re-examine" approximately 35,000 claims and "make millions of dollars available" may give the appearance of relief, but guarantees policyholders nothing but another opportunity to be exploited by State Farm⁴. If State Farm could not make an accurate determination of the cause of damage right after Hurricane Katrina, how will they do a better job after nineteen months of cleanup and rain?

The industry's reverence for contracts is again belied by this widespread practice of engaging policyholders in wrangling for months or years to eventually have a small portion of their claim paid as a "settlement." People who have survived natural disasters are in no position to negotiate their insurance coverage after the fact, but this is exactly what they are being required to do.

Payment of claims is a contractual obligation but is frequently treated as a benevolent gift from the insurer to the insured. Katrina has shown us that the regulatory status quo is not adequate to protect policyholders' contractual rights.

IV. CONCLUSION

The MSAG's office has, in good faith, engaged in tireless efforts to work with State Farm to make insurance affordable for our citizens. However, we recognize that accepting premiums is not the same thing as "doing business." If a State Farm insurance policy is nothing more than a meaningless security blanket, then Mississippians do not benefit from having them stay in the state to collect premiums. As the struggle in our state and throughout the country demonstrates, insurance companies are free to take the money and run from the market whenever they choose. At the same time, prospective homeowners are unable to get federally-backed mortgages without purchasing homeowners insurance. It is for this reason that a discussion of free markets is not entirely appropriate when applied to a product that people are legally required to buy.

No easy reconciliation of the competing interests in this discussion can be made, but Congress urgently needs to take actions to keep homeowners from losing faith in the insurance industry altogether. Consumers who faithfully pay their premiums should not have to wonder why, after nineteen months of inspections, mediations, phone calls and letters, they are no better off than those who did not buy insurance at all. If the industry wants to serve coastal areas, they must be held accountable, just as any other business would be. The antitrust exemption provided by McCarran-Ferguson has yielded outrageous results. If the industry pulls out of coastal areas, it cannot then object to the government's response in assisting an abandoned segment of the population. Thank you for inviting me today. I look forward to your questions.

Endnotes:

1. Leonard v. Nationwide Mutual Insurance, 438 F. Supp.2d 684, 689 (S.D. Miss. 2006).

2. Associated Press. *Isabel claims under scrutiny*, Baltimore Sun, March 12, 2004, "NFIP claims director James Shortley said the program does not regulate the software that adjusters use, explaining, 'We would have to verify prices in every little town'."

3.State Farm® Announces It Will Suspend Writing Homeowners and Commercial Policies in Mississippi. http://www.statefarm.com/about/media/media_releases/mississippi_home.asp.
4/2/2007

4. Associated Press, *Insurance regulator says State Farm agrees to re-examine hurricane cases*. USA Today, March 19, 2007.

Exhibit List:

- Exhibit A- Letter issued to State Farm customers stating it will no longer offer new homeowners policies to Mississippians.
- Exhibit B- Anti-Concurrent Causation language found in homeowners insurance policies issued by Allstate, Nationwide and State Farm.
- Exhibit C- Wind/Water Protocol issued by State Farm on September 13, 2005.

State Farm Insurance
11350 Johns Creek Parkway
Duluth, GA 30098



Lynn Gunn
110 Lauderdale Rd
Pelahatchie, MS 39145-2713



Dear Lynn,

Recently, State Farm® announced it will no longer offer new homeowners or commercial insurance policies in Mississippi. This decision certainly didn't come easily or quickly - it's unfortunate, but necessary. The unpredictable legal and political environment in the state leaves us unable to accept any additional risk in the Mississippi homeowners market. Simply put, we cannot continue to write new policies under a contract that is now being reinterpreted by the courts and certain elected officials.

We've built our business by talking to people and by establishing relationships and helping them protect what they value most. Rest assured, that's what we will continue to do.

You are a valued customer with whom I'm proud to call this state home. We want to work with you to make Mississippi stronger and more vibrant than ever before. While we cannot offer homeowners or commercial insurance policies in addition to the ones you already own, we look forward to meeting your insurance and financial services needs through the more than 70 other products State Farm offers. These include auto, life and health insurance, as well as a variety of financial services.

I invite you to call your State Farm agent with questions you may have about what I've shared in this letter, or about what you may read or hear in the news.

It is an honor for us to serve you. I appreciate your business and your loyalty.

Sincerely,

A handwritten signature in black ink that reads "Webb Howell".

G. Webb Howell
State Farm Vice President - Agency

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GENERAL

EXHIBIT A

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EXHIBIT B

Taken from Allstate Property and Casualty Insurance Company Deluxe Homeowners Policy, *Elmer and Alexa Buente v. Allstate Insurance Company et al*, Civil Action 1:05CV712 LTS-JMR, U.S. District Court, S.D. Miss., Judge Senter's Memorandum Opinion, March 24, 2006.

With respect to the insured dwelling (Section I, Coverage A) and other structures (Section I, Coverage B):

Losses We Do Not Cover...

We do not cover loss to the [insured] property consisting of or caused by:

1. Flood, including but not limited to surface water, waves, tidal water, or overflow of any body of water, or spray from any of these, whether or not driven by wind.

4. Water or any other substance on or below the surface of the ground, regardless of its source. This includes water or any other substance which exerts pressure on, or flows, seeps or leaks through any part of the residence premises.

21. Weather conditions that contribute in any way with a cause of loss excluded in this section to produce a loss.

23. We do not cover loss to property...when:

- a) there are two or more causes of loss to the covered property; and
- b) the predominant cause(s) of loss is (are) excluded under Losses We Do Not Cover, items 1 through 22 above.

With respect to personal property (Section I, Coverage C, Personal Property Protection):

Losses We do Not Cover...

We do not cover loss to [insured personal] property caused by or consisting of:

1. Flood, including, but not limited to surface water, waves, tidal water or overflow of any body of water, or spray from any of these, whether or not driven by wind.

4. Water or any other substance on or below the surface of the ground, regardless of its source. This includes water or any other substance which exerts pressure on, or flows, seeps or leaks through any part of the residence premises.

13. Weather conditions that contribute in any way with a cause of loss excluded in this section to produce a loss.

15. We do not cover loss to [insured personal] property when:

- a) there are two or more causes of loss to the covered property; and
- b) the predominant cause(s) of loss is (are) excluded under Losses We Do Not Cover items 1 through 14 above.

Exhibit B continued...

Taken from Nationwide homeowners insurance policy, *Paul Leonard and Julie Leonard v. Nationwide Mutual Insurance Company*, Civil Action No.1:05 CV475 LTS-RHW, U.S. District Court, S.D. Miss., Judge Senter's Memorandum Opinion, August 15, 2006

Section 1, Property Coverages

Coverage A-Dwelling

Coverage B- Other Structures

Coverage C- Personal Property

Property Exclusions, Section 1

1. We do not cover loss to any property resulting directly or indirectly from any of the following. Such a loss is excluded even if another peril or event contributed concurrently or in any sequence to cause the loss.

b) Water or damage caused by water-borne material. Loss resulting from water or water-borne material damage described below is not covered even if other perils contributed, directly or indirectly to cause the loss.

Water and water-borne material damage means:

(1) flood, surface water, waves, tidal waves, overflow of a body of water, spray from these, whether or not driven by wind.

n) Windstorm or hail to any

(1) structure, other than a building, including the supports and screens, with a roof-like covering of cloth, metal, plastic or fiberglass, whether or not the structure is attached to a building.

(2) screens, including their supports, around a pool, patio or other areas.

(3) property lines and similar walls, including seawalls, greenhouses, hothouses, slathouses, trellis, pergolas, cabanas and outdoor equipment used to service the residence premises.

(4) structure, including property in or on the structure, which is in whole or part, in or over water.

2. We do not cover loss to any property resulting directly or indirectly from the following if another excluded peril contributes to the loss:

c) Weather conditions, if contributing in any way with an exclusion listed in paragraph 1 of this Section.

Exhibit B continued...

Taken from State Farm homeowners policy, *John Tuepker and Claire Tuepker v. State Farm Fire & Casualty Company*, Civil Action No. 1:05CV559 LTS-JMR, Judge Senter's Memorandum Opinion, May 24, 2006

Section I, Losses Insured
Coverage A–Dwelling
Coverage B–Personal Property

Section I –Losses Not Insured

1. We do not insure for any loss to the property described in Coverage A which consists of, or is directly and immediately caused by, one or more of the perils listed in items a. through n. below, regardless of whether the loss occurs suddenly or gradually, involves isolated or widespread damage, arises from natural or external forces, or occurs as a result of any combination of these:

a. collapse, except as specifically provided in Section I Additional Coverages, Collapse.

2. We do not insure under any coverage for any loss which would not have occurred in the absence of one or more of the following events. We do not insure for such loss regardless of: a) the cause of the excluded event; or b) other causes of the excluded event; or c) whether other causes acted concurrently or in any sequence with the excluded event to produce the loss; or d) whether the event occurs suddenly or gradually, involves isolated or widespread damage, arises from natural or external forces, or occurs as a result of any combination of these:

c. Water Damage, meaning:
(1) flood, surface water, waves, tidal water, tsunami, seiche, overflow of a body of water; or spray from any of these, all whether driven by wind or not;

3. We do not insure under any coverage for any loss consisting of one or more of the items listed below. Further, we do not insure for loss described in paragraphs 1 and 2. immediately above regardless of whether one or more of the following: a) directly or indirectly cause, contribute to or aggravate the loss; or b) occur before, at the same time, or after the loss or any other cause of the loss:

c. weather conditions.

However, we do insure for any resulting loss from items a., b., and c. unless the resulting loss is itself a Loss Not Insured by this Section.

Date: September 13, 2005
To: State Farm Claim Associates handling CAT PL in the Central and Southern Zones
From: Property and Casualty Claim Consulting Services
Subject: Wind/Water Claim Handling Protocol

*****ACTION REQUIRED*****

Summary

Because of the combination of wind and water damages many homes sustained from Hurricane Katrina, the following materials have been developed and are intended for use as a guide for handling various wind and/or water claims in Louisiana, Mississippi and Alabama.

Action:

The protocol below outlines the process that should be used for determination of coverage in these locations.

Protocol Detail

Each claim should be handled on its merits. A causation investigation should be conducted and appropriate claim file documentation is required. Any available information should be considered in making a coverage determination. This information will include, but is not limited to:

- Evidence gathered at the on site inspection. This includes documentation of physical evidence such as water lines, an examination of the debris, and an analysis of the physical damage to the structure.
- Evidence gathered at neighboring locations.
- Data obtained from reports describing damage to the area.
- Information from witnesses and policyholders.
- Input from experts that may be retained to provide guidance.

The damage to insured properties will fall into the following categories and should be handled as detailed below:

- Damage to the property was caused by windstorm.
- Damage to separate portions of the property can be attributed to either windstorm or excluded water.
- Damage to the property was caused by excluded water with no available coverage.
- Damage to the property was caused by flood waters; covered by an available flood policy.

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EXHIBIT C

Damage Caused by Windstorm

When the investigation indicates that the damage was caused by windstorm, the claim will be handled under the applicable provisions of the involved property policy. Consideration should be given to determine if a hurricane deductible or a windstorm or hail exclusion endorsement is involved and the claim handled accordingly.

Damage to Separate Policies with Disruptible Wind or Excluded Water

Each type of damage should be documented in the claim file. The claim representative should calculate the separate damage attributable to each part and handle the adjustment accordingly. In those cases where the policyholder has policies for both a windstorm and a flood, payments should be issued under the applicable policy.

Damage Caused by Excluded Water

When the investigation indicates that the damage was caused by excluded water and the claim investigation does not reveal independent windstorm damage to separate portions of the property, there is no coverage available under the homeowners policy pursuant to the following language in Section 7 Losses Not Insured:

"2. We do not insure under any coverage for any loss which would not have occurred in the absence of one or more of the following excluded events. We do not insure for such loss regardless of: (a) the cause of the excluded event; or (b) other causes of the loss; or (c) whether other causes acted concurrently or in any sequence with the excluded event to produce the loss; or (d) whether the event occurs suddenly or gradually, involves isolated or widespread damage, arises from natural or external forces, or occurs as a result to any combination of these:

a. Water Damage, meaning:

- (1) flood, surface water, waves, tidal water, tsunami, seiche, overflow of a body of water, or spray from any of these, all whether driven by wind or not . . ."

Other Losses Not Insured may be applicable, including 2.0(2) & (3), 6.(a), (b) & (c).

Damage to Property Caused by Flood Water with available Flood Policy

Where wind acts concurrently with flooding to cause damage to the insured property, coverage for the loss exists only under flood coverage, if available. The flood damage claim should be handled consistent with the terms of the flood policy providing coverage as outlined in Operation Guide 71-00.

Claims where the causation investigation is ongoing

Payment can be made under a reservation of rights for ALE or Loss of Income until the property policy until the final coverage decision is made. The policyholder should be advised in writing that:

- The investigation is ongoing.
- No coverage decision has been made.
- In the event it is determined that there is no covered damage, no further payment will be made on ALE or Loss of Income.
- They may undertake an independent investigation.

All claims in this category must be reviewed by the Claim Team Manager before a final decision is made. Management should be involved in any claim where it is deemed necessary to retain an expert to assist in the determination of causation.

For More Information
Any question on this protocol should be directed to your Claim Team Manager.

- P & C Claims Executive
- Southern Zone Executive & Claim Managers
- Central Zone Executive & Claim Managers
- P & C Claims Directors and Consultants
- Catastrophe Services Chair, Managers
- Catastrophe Services Section & Team Managers
- Zone Section Managers

Transcript of Exhibit C

Date: September 13, 2005
To: State Farm Claim Associates handling CAT FL in the Central and Southern Zones
From: Property and Casualty Claim Consulting Services
Subject: Wind/Water Claim Handling Protocol

Action Required

Summary

Because of the combination of wind and water damages many homes sustained from Hurricane Katrina, the following materials have been developed and are intended for use as a guide for handling various wind and/or water claims in Louisiana, Mississippi and Alabama.

Action

The protocol below outlines the process that should be used for determination of coverage in those locations.

Protocol Detail

Each claim should be handled on its merits. A causation investigation should be conducted and appropriate claim file documentation is required. Any available information should be considered in making a coverage determination. This information will include, but is not limited to:

- Evidence gathered at the on site inspection. This includes documentation of physical evidence such as water lines, an examination of the debris, and an analysis of the physical damage to the structure.
- Evidence gathered at neighboring locations.
- Information from witnesses and policyholders.
- Input from experts that may be retained to provide guidance.

The damage to insured properties will fall into the following categories and should be handled as detailed below:

- Damage to the property was caused by windstorm.
- Damage to separate portions of the property can be attributed to either windstorm or excluded water.
- Damage to the property was caused by excluded water; with no available coverage.
- Damage to the property was caused by flood waters; covered by an available flood policy.

Damage Caused by Windstorm

When the investigation indicates that the damage was caused by windstorm, the claim will be handled under the applicable provisions of the involved property policy. Consideration should be given to determine if a hurricane deductible or a windstorm hail exclusion endorsement is

involved and the claim handled accordingly.

Damage to Separate Portions with Distinguishable Wind and Excluded Water

Each type of damage should be documented in the claim file. The claim representative should calculate the separate damage attributable to each peril and handle the adjustment accordingly. In those cases where the policyholder has policies for both a windstorm and a flood, payments should be issued under the applicable policy.

Damage Caused by Excluded Water

When the investigation indicates that the damage was caused by excluded water and the claim investigation does not reveal independent windstorm damage to separate portions of the property, there is no coverage available under the homeowners policy pursuant to the following language in Section I Losses Not Insured:

"2. We do not insure under any coverage for any loss which would not have occurred in the absence of one or more of the following excluded events. We do not insure for such loss regardless of: (a) the cause of the excluded event; or (b) other causes of the loss; or © whether other causes acted concurrently or in any sequence with the excluded event to produce the loss; or (d) whether the event occurs suddenly or gradually, involves isolated or widespread damage, arises from natural or external forces, or occurs as a result to any combination of these:

c. Water Damage, meaning:

(1) flood, surface water, waves, tidal water, tsunami, selche, overflow of a body of water, or spray from any of these, all whether driven by wind or not..."

Other Losses Not Insured may be applicable, including 2.c.(2) & (3), 3.(a), (b) & ©.

Damage to Property Caused by Flood Waters with available Flood Policy

Where wind acts concurrently with flooding to cause damage to the insured property, coverage for the loss exists only under flood coverage, if available. The flood damage claim should be handled consistent with the terms of the flood policy providing coverage as outlined in Operation Guide 71-06.

Claims where the causation investigation is ongoing

Payment can be made under a reservation of rights for ALE or Loss of income under the property policy until the final coverage decision is made. The policyholder should be advised in writing that:

- The investigation is ongoing.
- No coverage decision has been made.
- In the event it is determined that there is no covered damage, no further payment will be made on ALE or Loss of Income.
- They may undertake an independent investigation.

All claims in this category must be reviewed by the Claim Team Manager before a final decision is made. Management should be involved in any claim where it is deemed necessary to retain an expert to assist in the determination of causation.

For More Information

Any question on this protocol should be directed to your Claim Team Manager.

- C. P & C Claims Executive
 - Southern Zone Executive & Claim Managers
 - Central Zone Executive & Claim Managers
 - P & C Claims Directors and Consultants
 - Catastrophe Services Claim Managers
 - Catastrophe Services Section & Team Managers
 - Zone Section Managers