

SECOND ANNUAL REPORT TO THE LEGISLATURE

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**COMMONWEALTH OF PENNSYLVANIA
DEPARTMENT OF ENVIRONMENTAL PROTECTION**

**COAL AND CLAY MINE SUBSIDENCE INSURANCE PROGRAM
MSI**

SECOND ANNUAL REPORT

**STATE FISCAL YEAR
2004-2005**

PREPARED BY

**DEPARTMENT OF ENVIRONMENTAL PROTECTION
BUREAU OF MINING AND RECLAMATION**

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visit DEP directly at www.dep.state.pa.us or visit MSI directly at www.paMSI.org

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I. EXECUTIVE SUMMARY

This report provides information about the Commonwealth of Pennsylvania's Coal and Clay Mine Subsidence Insurance (MSI) Program and its experience with mine subsidence insurance sales through insurance producers (insurance agents, brokers and agencies who are licensed in Pennsylvania to sell property and casualty insurance). Section 20 of the Act of August 23, 1961 (P.L.1068 No. 484), as amended, (52 P.S. §§ 3201-3225) (Act), provides that the Department of Environmental Protection (DEP) submit this annual report to the Environmental Resources and Energy Committees of the Senate and House of Representatives. This reporting requirement was added to the Act as part of the December 9, 2002 amendments that also provided that, in addition to the sales of policies made by the MSI Program, the insurance producers may also submit MSI applications to the MSI Fund and be paid commissions for their applications that become policies.

Established in 1961, Pennsylvania's MSI Program was the first MSI program in the nation. In terms of numbers of subscribers, Pennsylvania's MSI Program (Program) has always been the most successful MSI program of any of the elective MSI programs in the nation. Only states that mandate MSI coverage have programs with more subscribers. In June of 2003, just prior to the date when insurance producers began to offer coverage, subscriptions totaled 53,379. However, there were still more than one million uninsured structures in Pennsylvania that are at risk from mine subsidence damage. Given the insurance producers the ability to sell MSI coverage to their customers who are at risk was intended to greatly increase MSI subscriptions. Those results have not yet been achieved.

The efforts made by DEP to encourage insurance producers to register to use the MSI systems have been successful. With input from the insurance producers, online registration and application systems were developed by DEP. Over 1,500 of the estimated 2,500 active insurance producers that are located in the coal and clay mining regions have registered to use the application systems. During FY 2004-05 those insurance producers sold 2,144 policies. This was during a time when all the marketing to the public that was conducted by DEP specifically encouraged property owners to contact their insurance producers to purchase MSI. On average, each registered insurance producer sold less than two MSI policies per year, which indicates that, with only a few exceptions, the insurance producers are not promoting MSI coverage.

To address the low number of sales by the insurance producers, DEP will increase the marketing efforts that are intended to encourage the insurance producers to promote MSI coverage. At the same time DEP will enhance the online systems it provides to property owners so that they will be able to more easily apply directly to the MSI Fund for coverage. Both these systems have been provided by DEP via a short domain name, www.paMSI.org

II. CONCLUSION AND RECOMMENDATIONS

The MSI Program continues to be the most successful mine subsidence program in terms of the numbers of subscribers of any MSI program in the nation that is not associated with state mandated coverage. However, over one million **uninsured structures** continue to be at risk in Pennsylvania, and mine subsidence causes substantial losses each year to uninsured structures. Sales by insurance producers

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are intended to dramatically increase the number MSI subscriptions. However, despite extensive marketing efforts to inform the insurance producers about the need for coverage, the development of online application systems and the establishment of generous commissions, the expected increase in the number of policies written by the insurance producers has not been achieved. On average, each registered insurance producer is selling less than two MSI policies per year. That performance indicates that, with only a few exceptions, the insurance producers are not promoting MSI coverage. The pattern of sales by the insurance producers appears to be directly related to the marketing efforts of DEP that have directed property owners to their insurance producers or by news coverage of subsidence events in which DEP spokespeople encourage property owners to contact their insurance producer for MSI coverage. In essence, the insurance producers, as a body, do not appear to be promoting MSI coverage, as the amendments to the Act intended. To address this situation, DEP will increase marketing efforts to encourage the insurance producers to promote MSI coverage. Efforts are underway to enhance the tools provided to the insurance producers include the following:

- Additional surveys of the insurance producers to better identify their needs.
- Improved marketing material and increased marketing efforts to encourage MSI sales.
- Continued improvements to the online application systems.
- Development of electronic payment capabilities.

III. BACKGROUND

There are over one million structures in Pennsylvania that are located above old abandoned coal and clay mines. The subsidence of those mines causes millions of dollars of property damage each year. The MSI Fund was created in 1961 to provide a reliable source of insurance to compensate for losses caused by the collapse of old abandoned underground coal and clay mines. The legislature created the MSI Fund because, in the late 1950's, mine subsidence coverage became so costly that it was excluded from standard homeowners insurance policies. Premium rates had risen to prohibitively high levels because of the excessive costs associated with the investigation of claims and the subsequent inability of the private industry to manage losses. Mine subsidence is highly unpredictable and the damage it causes can be very costly to repair. The absence of mine subsidence coverage exposed property owners to personal financial losses and negatively impacted the economic vitality of the coal regions by also exposing the mortgage industry to the risk of uninsurable losses. Such exposure limited the ability of lenders to fund mortgages, which resulted in suppressed property values. The legislature determined that a special proprietary fund organized within and utilizing the resources of state government would allow those at risk to mutually insure against the risk of mine subsidence losses, and do so at affordable premium rates.

As established in the Act, the MSI Board (Board) administers the MSI Fund. The Board is comprised of the heads of three departments of state government. The Secretary of the Department of Environmental Protection (DEP) chairs the Board and the Insurance Commissioner and State Treasurer are members. The Board establishes provisions of the insurance policy, promulgates regulations, and establishes premium rates, which are to be adequate to provide reserves sufficient to maintain the solvency of the MSI Fund. The expertise provided by the Board members and their staffs contributes greatly to the economic and efficient operations of the MSI Fund and Program. The Insurance Department contributes actuarial and insurance policy expertise. The Treasury, the mandated custodian of the MSI Fund, invests the Fund's reserves. DEP, the agency mandated to administer the MSI Program, contributes mining expertise that allows for the economical investigation of damage claims and also provides operational support through the use of its computer aided systems, which further provides for the economical administration of the MSI Program.

Historically, the Program has had a statewide staff of about 10 representatives who would respond to requests and write MSI policies. Surveys of the residents of the mining communities indicate a general awareness of the need for and availability of MSI, but only about 5% of those at risk have insured. As a result, many of the structures damaged have been uninsured. To improve the outreach to the owners of the more than one million uninsured properties, routine advertising campaigns were initiated by DEP in the late 1990's. Although the campaigns were effective in increasing subscriptions, they did not

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appreciably improve the market share. Allowing the private insurance industry to offer MSI coverage was intended to dramatically improve the numbers MSI subscriptions because the insurance producers would be able to directly inform their customers of the availability and need for MSI coverage and then encourage them insure against that risk.

IV. MSI FUND AND PROGRAM PERFORMANCE OVERVIEW

The MSI Fund is a proprietary fund of the Commonwealth constituted from the retained premiums of the MSI policyholders. It continues to remain solvent with an unreserved fund balance at the end of State Fiscal Year (FY) 2004-05 of \$38,345,724 that stands against the potential losses of its policyholders. At that same time it had 54,749 structures insured and very close to \$6 billion in underwritten coverage. During FY 2004-05, 4,136 new MSI policies were created, of which the insurance producers submitted 2,144 and the Program submitted 1,192. More statistical and financial information is provided in the **STATISTICAL/FINANCIAL SUMMARY** Section of this report.

V. DEP AND MSI BOARD EFFORTS

DEP uses its mining expertise and program resources to economically manage the operations of the Program especially as it relates to the investigation of damage claims. These resources allow DEP to successfully manage claim losses. DEP also uses its extensive computing systems to further add efficiency and economy to the operation of the Program.

To promote and assist in the efforts of the insurance producers, DEP had meetings with the insurance producers prior to and during the development of the systems that are intended to best serve them and the Program with their MSI sales efforts. DEP has ongoing surveys to promote feedback from the insurance producers, which supports the ongoing efforts to improve the support for their sales. Among the products and services developed to support their sales are the following:

- Internet based application systems that include animated tutorials and complete marketing and sales kits.
- Online systems to determine underground mining conditions and customer risk.
- Support systems including a toll free help line and extensive information about mine subsidence.
- Direct marketing to inform and encourage all insurance producers located in the mining regions to sell MSI and make generous commissions (50% of the first years premium, as established by the MSI Board)
- Mass marketing campaigns that directed the residents of the coal regions to contact their insurance producers for MSI coverage.
- Special news letters to the insurance producers sent via email that update them on mine subsidence events and new tools being provided by DEP.

VI. INSURANCE PRODUCER IMPACTS

Over 1,500 of the estimated 2,500 active insurance producers that are located in the coal and clay mining regions have registered to use the application systems. During FY 2004-05 those insurance producers sold 2,144 policies. This was during a time when all the marketing to the public that was conducted by DEP specifically encouraged property owners to contact their insurance producers to purchase MSI. On average, each registered insurance producer sold less than two MSI policies per year, which indicates that, with only a few exceptions, the insurance producers are not promoting MSI coverage.

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VII. STATISTICAL/FINANCIAL SUMMARY

The statistical and financial information in this summary demonstrates the operational and financial performance of the MSI Fund and Fund and documents the contributions made by the insurance producers. The data is tracked on a fiscal year (FY) basis. To provide a historical perspective, the summary begins with data from FY 1995-96. The first fiscal year that insurance producers were eligible to submit MSI applications was FY 2003-04, and their first full fiscal year was FY 2003-04.

STATISTICAL/FINANCIAL SUMMARY								
STATE FISCAL YEAR	POLICIES IN FORCE	UNDER-WRITTEN COVERAGE IN \$ MILLIONS	UNRESERVED FUND EQUITY	POLICIES CREATED BY MSI PROGRAM	POLICIES CREATED BY INSURANCE PRODUCERS	REGISTERED INSURANCE PRODUCERS	PRODUCER GENERATED PREMIUMS	COMMISSIONS PAID
1995-96	42,083	\$3,222,915	\$13,152,997	4,047	0	0	\$0	\$0
1996-97	43,589	\$3,478,793	\$15,039,743	3,203	0	0	\$0	\$0
1997-98	44,319	\$3,640,974	\$17,149,560	3,117	0	0	\$0	\$0
1998-99	44,574	\$3,746,272	\$19,927,027	2,743	0	0	\$0	\$0
1999-00	45,420	\$3,945,403	\$22,759,927	2,481	0	0	\$0	\$0
2000-01	52,395	\$4,754,237	\$27,187,788	7,217	0	0	\$0	\$0
2001-02	53,309	\$4,950,738	\$30,375,641	3,554	0	0	\$0	\$0
2002-03	53,280	\$5,134,789	\$33,211,797	2,943	9	35	\$2,539	\$0
2003-04	53,487	\$5,484,411	\$34,935,305	1,980	1,405	791	\$178,424	\$67,446
2004-05	54,749	\$5,972,256	\$38,345,724	1,992	2,144	1,520	\$271,392	\$124,767