



The Florida Senate

Revised

Interim Project Summary 2000-03

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Committee on Banking and Insurance

Senator James A. Scott, Chairman

AVAILABILITY AND COST OF RESIDENTIAL HURRICANE COVERAGE

SUMMARY

Despite significant improvement, the residential property insurance market continues to pose major problems, now 7 years after Hurricane Andrew. These problems include: (1) limited availability and high cost of private market coverage in high risk areas, particularly in coastal areas of Dade, Broward, and Palm Beach Counties; (2) the exposure of the Florida Windstorm Underwriting Association to a multi-billion dollar hurricane loss that would trigger significant premium assessments on all residential policyholders in Florida; and (3) the likelihood that problems of cost and availability of coverage will significantly worsen after another major hurricane.

The Legislature has created two insurance entities to sell property insurance coverage to persons who cannot obtain coverage in the private voluntary market. The Florida Residential Property and Casualty Joint Underwriting Association (RPCJUA) offers standard homeowners coverage in all areas of the state. The Florida Windstorm Underwriting Association (FWUA) offers only windstorm coverage, and only in designated coastal areas. These two insurers depend upon debt financing to pay claims in the event of a major hurricane, secured by premium assessments on all property insurance policies in the state.

At the end of July 1999, the RPCJUA insured 113,488 residential structures, a significant decrease in policies over the past 3 years from the 936,837 policies in force in September 1996. However, the FWUA has grown to 456,958 policies with an insured value of \$88 billion, more than one-half of which is concentrated in Dade, Broward, and Palm Beach Counties, and faces an estimated loss of \$5.3 billion from a 100-year storm. A major hurricane striking south Florida would trigger significant assessments on all property insurance policyholders in the state.

The Legislature and the Department of Insurance should consider options to reduce the exposure of the FWUA in a manner that does not unfairly impact FWUA policyholders. Options for reducing the exposure of the FWUA include the following:

- Specifying the standards and procedures that must be followed if an insurer makes an offer of coverage that would disqualify a policyholder from maintaining FWUA coverage, including adequate notice to the policyholder, agent, and other peril insurer; providing the other peril insurer with the option of writing the windstorm coverage; and authorizing the department to approve the take-out insurer's financial capacity to meet its obligations.
- Eliminating or reducing coverages that are not typically covered under a standard homeowners policy, such as tiki huts and gazebos;
- Limiting coverage for personal lines residential risks to a specific value, such as \$1 million, if a determination is made that such coverage is generally available from authorized insurers or the surplus lines market.

The current law requires that rates for the FWUA be actuarially sound and not be competitive with approved rates charged in the admitted voluntary market. The law also provides the FWUA board with the option for arbitration of a rate filing that is disapproved by the department, and provides that hurricane loss projection models are admissible and relevant in a rate hearing if they have met the standards approved by the Florida Commission on Hurricane Loss Methodology. These standards and procedures should be sufficient to address concerns regarding the adequacy or excessiveness of the FWUA rates.

The Legislature should consider imposing an outside limit on the annual liability of the FWUA to its policyholders, comparable to the practical limits

imposed on policyholders of authorized insurers. The limit could be equal to the estimated probable maximum loss for a 100-year storm (currently \$5.3 billion), as annually determined by the board and the department, with a minimum guarantee of \$300,000 per claim and pro rata reduction of claims beyond this limit.

The Legislature should consider requiring authorized residential property insurers to maintain adequate surplus and reinsurance to cover their estimated probable maximum loss for a 100-year storm, as estimated by at least one of the models meeting the standards approved by the Florida Commission on Hurricane Loss Methodology.

The Legislature should consider amending the definition of *hurricane coverage* to provide a more specific determination of when a hurricane deductible applies. One option is to require that the damage occur in a county in which the Division of Emergency Management of the Department of Community Affairs, based upon official forecasting information from the National Weather Service, declares that an area in the county sustained winds that were part of the storm system.

BACKGROUND

Florida Windstorm Underwriting Association (FWUA)
The FWUA was formed nearly 30 years ago, in 1970, in response to problems of availability of property insurance in certain coastal areas. The FWUA offers coverage only for windstorm and hail losses, and only in those areas where the department determined that windstorm coverage was unavailable and that certain economic conditions existed. Coverage now includes coastal areas in 29 of Florida's 35 coastal counties. In Dade, Broward, and Palm Beach counties, the entire area east of Interstate 95 is eligible for FWUA coverage, and all of Monroe County is eligible, but in other counties eligibility is typically limited to about 1,000 to 1,500 feet from the coast. By act of the Legislature in 1998, further expansion of the eligible boundaries of the FWUA is now prohibited. The boundaries of the FWUA directly affect the obligation of private market insurers to provide windstorm coverage. Outside of FWUA eligible areas, insurers must include windstorm coverage in every residential property insurance policy it writes. Inside FWUA areas, insurers are free to write policies that exclude windstorm coverage.

The FWUA is authorized to assess all Florida property insurers and their policyholders to fund a deficit if premiums are not sufficient to cover claims payments. *Regular assessments* may be made against property insurers, up to 10 percent of the FWUA's deficit, or 10 percent of property insurance premiums in the state, whichever is *greater*. Insurers may then recoup these assessments from their policyholders after getting a rate filing approved. If the deficit exceeds the maximum regular assessment, *emergency assessments* may be imposed on all new and renewal property insurance policies in the state, also limited to the greater of 10 percent of the deficit, or 10 percent of the prior year's statewide premium for property insurance. An insurer can obtain credits against regular assessments by voluntary writings in FWUA-eligible areas, but not credits against emergency assessments. The board of the FWUA may pledge emergency assessments to secure debt financing.

Like all residential property insurers, the FWUA must buy reinsurance from the Florida Hurricane Catastrophe Fund, which reimburses insurers for a portion of their hurricane losses. Reimbursement generally provides funding to the FWUA after regular assessments are imposed, but before debt financing and emergency assessments would be necessary.

In 1997, legislation provided that a FWUA policyholder is no longer eligible for coverage with the FWUA if an offer of coverage is made by an authorized insurer to cover the risk at the insurer's approved rates under a policy that includes windstorm coverage. These provisions were modeled on similar provisions in the RPCJUA law. One significant practical difference, however, compared to the situation of an insurer taking a policy out of the RPCJUA, is that requiring a FWUA policyholder to accept a policy from a take-out insurer effectively forces the policyholder to also lose their "other perils" policy with a private market insurer, if the take-out insurer is offering full coverage, not just windstorm coverage.

The FWUA has received offers from insurers to take policies out of the FWUA. However, the board of the FWUA has determined that it will not move forward with any insurer's take-out offer until depopulation procedures have been approved by the department. Depopulation procedures have been adopted by the board of the FWUA and submitted to the department, and are reportedly close to approval (August 1999). The issues include financial standards for take-out companies, adequate notice to the policyholder, agent, and current other perils insurer, requiring that policies

only be taken out upon renewal, approval of the rates and benefits for the take-out insurer's replacement policy, and others. In May 1999, the department approved the first take-out of FWUA policies.

Florida Residential Property and Casualty Joint Underwriting Association (RPCJUA) - The legislative enactment of the RPCJUA in Special Session of December 1992, was a direct response to the severe market disruption following Hurricane Andrew. The RPCJUA provides residential property insurance statewide, insuring all perils covered under a standard residential policy (except in FWUA-eligible areas, where a RPCJUA policy excludes windstorm coverage). The RPCJUA must charge the same rates charged by the insurer with the highest rates in the county, among the top twenty insurers in the state by premium volume. This requirement was enacted in 1995 and amended in 1996 in an effort to assure that the RPCJUA would be the insurer of last resort, at a time when the RPCJUA was experiencing rapid growth in policies and exposure.

The RPCJUA may impose regular and emergency assessments to fund deficits and may pledge emergency assessments to secure debt financing, under the same limitations that apply to the FWUA. It must also obtain reinsurance from the Florida Hurricane Catastrophe Fund at the same level as the FWUA. Beginning in 1995, the Legislature, Department of Insurance, and the RPCJUA focused on depopulation of the RPCJUA by encouraging insurers to take policies out of the RPCJUA, including cash bonuses and exemptions from assessments. Depopulation of the RPCJUA is discussed in Findings, below.

Florida Hurricane Catastrophe Fund - The Florida Hurricane Catastrophe Fund, commonly referred to as the "Cat" Fund, is a state trust fund administered by the State Board of Administration (SBA), created in 1993 to reimburse residential property insurers for either 45 percent, 75 percent, or 90 percent of their hurricane losses, as selected by the insurer, above a certain retention, which is about \$3.1 billion for all insurers combined. The FWUA and RPCJUA must buy coverage at the 90 percent reimbursement level.

Significant changes were made to the Cat Fund by 1999 legislation in order to preserve its claims-paying capacity for subsequent seasons after a major hurricane. The 1999 act limited the total amount that the Fund may pay all insurers for hurricane losses to \$11 billion for any one year and limited each insurer's annual payment from the Cat Fund to the insurer's

minimum guarantee, which generally equals each insurer's proportionate share of Cat Fund premiums. However, the FWUA and the RPCJUA are *not* subject to the latter limitation. The 1999 act also increased the maximum assessment that can be imposed on property and casualty policies in any one year from 4 percent to 6 percent to fund bonds issued by the SBA to fund Cat Fund obligations, but limited to 4 percent for hurricane occurring in any one contract year. The Cat Fund will have approximately \$3 billion in cash reserves at the end of 1999 and it is estimated that the SBA would need to impose an assessment of about 3.7 percent on property insurance premiums to issue an additional \$8 billion in revenue bonds, if necessary to pay the maximum \$11 billion reimbursement to insurers for hurricane losses in 1999.

Rate Regulation; Arbitration - Florida's insurance laws require insurers to file property and casualty insurance rates for approval with the department either 90 days before the proposed effective date or 30 days after the rate filing is implemented. Under the latter option, however, the department may order the insurer to refund that portion of the rate determined to be excessive, so it is rarely utilized. If the department disapproves a rate filing, the insurer may request an administrative hearing under the Administrative Procedures Act. In 1996, the law was amended to allow insurers to request arbitration of a rate filing as an alternative to an administrative hearing. After the department issues a notice of intent to disapprove a rate filing, the insurer may request arbitration before a panel of three arbitrators. The panel is chosen as follows: one is selected by the insurer, one by the Department, and the third is chosen by the two other arbitrators. An arbitrator must be certified by the American Arbitration Association and may not be the employee of any insurance company or insurance regulator.

Hurricane Loss Projection Models; Methodology Commission - Insurers and regulators have become increasingly dependent on hurricane loss projection models to estimate the expected losses from hurricanes, particularly after Hurricane Andrew. The premiums that insurers are required to pay for coverage from the Florida Hurricane Catastrophe Fund are based on models that have been approved by the Florida Commission on Hurricane Loss Projection Methodology, which was created by act of the Legislature in 1995. Also, the Department of Insurance requires insurers to use hurricane models to determine the amount of surplus and reinsurance needed in order for the insurer to be approved for taking a block of policies out of the RPCJUA or FWUA. The

Commission has adopted standards and specifications of acceptable computer models and as of August 1999 has approved five different models as having met these standards. The current law provides that the findings and models approved by the commission are *admissible and relevant* in the department's consideration of a rate filing or in any administrative or judicial review of the department's actions.

Moratorium on Non-renewing Residential Policies - Since 1993, Florida law has either prohibited or limited the number of residential insurance policies that an insurer may cancel or non-renew for the purpose of reducing hurricane exposure, referred to as a moratorium on cancellations and nonrenewals. The current restrictions are scheduled to be repealed on June 1, 2001, and apply only to policies that were in effect on June 1, 1996. The current law prohibits insurers from non-renewing more than 5 percent of their residential property insurance policies in the state in any 12-month period, or more than 10 percent of their policies in any one county in any 12-month period, for the purpose of reducing hurricane exposure, subject to certain exceptions.

Hurricane Deductibles - Florida law limits the maximum and minimum hurricane deductibles that may be offered by residential property insurers and requires that certain deductibles be offered. In practice, this results in most homeowners being given two options for a hurricane deductible -- either 2 percent or 5 percent of policy limits.

METHODOLOGY

The property insurance laws enacted since Hurricane Andrew in 1992 and previous legislative reports on this subject were reviewed. Numbers of policies, insured value, estimated losses, current financing plans, and historical depopulation activities for the RPCJUA and the FWUA were obtained for each of these associations. Average statewide percentage increases in residential property insurance rates since 1992 for the top ten insurers in the state in 1994 were obtained from the Florida Department of Insurance. The department also provided the percentage rate increase filed and approved for all rate filings submitted to arbitration, and a premium rate comparison for hurricane rates in Broward, Dade, Palm Beach, and certain other counties, for the FWUA, RPCJUA, State Farm, Allstate Floridian, and the two insurers that charge the highest and lowest rates among the top 18 writers in those counties. Interviews were conducted with representatives of the Florida Market Assistance Plan

(FMAP) and with insurance agents regarding the availability of property insurance in south Florida.

FINDINGS

Growth in FWUA Policies and Exposure - The FWUA experienced significant growth in policies and exposure after Hurricane Andrew in 1992, leveling off in December of 1998, and in June and July of 1999 the policy count dropped, due to the first approved take-out plan. The FWUA reports that it is currently writing about 2,100 new policies per month. As of July 31, 1999, the FWUA had 456,958 policies in force, with a total insured value of \$88 billion. Approximately one-half of both the policies and exposure are concentrated in Dade, Broward, and Palm Beach counties.

A significant factor in the growth that occurred during 1997 and 1998 were non-renewals of wind coverage in FWUA areas by the state's two largest voluntary market insurers, State Farm and Allstate. These two insurers received approval from the Department of Insurance for an "accelerated exposure reduction plan," pursuant to a statutory exemption from the percentage moratorium limitations on nonrenewals. More recently, in June and July of this year, Clarendon Insurance Company removed about 37,000 policies from the FWUA, becoming the first insurer to obtain approval from the department to do so. Clarendon also removed a large number of RPCJUA policies and received the largest cash bonuses awarded to date, discussed in more detail, below.

Estimate of FWUA Losses; Financing Claims - The FWUA estimates its projected hurricane losses, by contracting with an actuarial firm that has developed hurricane loss projection models that meet the standards approved by the Florida Hurricane Loss Methodology Commission. It is estimated that the *average annual loss* for the FWUA for 1999 is \$317,892,294, which is greater than the estimated *annual premium* of \$305,401,993, which indicates that current funding may not be at adequate levels. Premiums should be expected to cover average annual hurricane losses plus amounts necessary to cover non-hurricane wind losses, agent commissions, and other expenses of administration.

The *probable maximum loss* is also estimated for the FWUA and used to determine the funding needed to pay claims for the single largest storm that is likely to occur over a specified time period. It is estimated that for 1999 the FWUA has a one percent chance of having a \$5.3 billion loss, also referred to as its 100-

year probable maximum loss. An insurer is generally expected to have the ability to pay claims, from its surplus and reinsurance, in an amount sufficient to covers its estimated loss for a 100-year storm in order to obtain an acceptable insurance rating from private rating organizations and as a condition of obtaining approval from the Department of Insurance for a take-out plan to write policies out of the RPCJUA or FWUA. For 1999, the FWUA has secured access to debt financing that would enable it to pay up to \$5.361 billion in claims. The FWUA has \$60 million cash on hand, as its first source of funding, which is a small figure compared to the loss estimates. Relatively minor hurricane losses would trigger regular assessments against insurers of up to \$448 million, which is 10 percent of premium, which would be recouped from their policyholders, and the FWUA would impose equivalent market equalization surcharges of \$60 million on FWUA policyholders. These three sources, combined, generate a total of \$568 million, which is below the estimated losses for a 10-year storm of \$671 million, and well short of the estimated losses from a 20-year storm of \$1.8 billion. Storms of such magnitude would trigger the next layer of funding, which is an estimated \$2.2 billion recovery from the Florida Hurricane Catastrophe Fund for 1999. This is a significant layer of funding, and when added to underlying sources, comes close to funding the 50-year storm loss estimate of \$3.2 billion. But, this would trigger Cat Fund assessments on property insurers of 3 to 4 percent of premiums, assuming proportionate losses by other insurers, and would also require use of \$250 million in pre-event notes that the FWUA has obtained (funds that have already been borrowed) to pay for the 10% retention of claims not paid by the Cat Fund. Beyond about \$3.0 billion in losses, the FWUA funding is solely dependent upon debt financing, including \$1.5 billion in pre-event notes and an \$800 million line of credit that it has obtained, secured by premium revenue and emergency assessments, completing its 1999 financing package for covering a \$5.36 billion loss. Payment for losses beyond this amount are limited only by what the capital markets will bear as secured by additional emergency assessments.

RPCJUA Policy Count and Exposure - After its creation in 1992, the Residential Property and Casualty Joint Underwriting Association grew to a peak of 936,000 in-force policies in September 1996. Since that time, the policies and exposure of the RPCJUA have been steadily reduced to its July 31, 1999, total of 113,488 policies with \$18.4 billion of insured value (exposure). The RPCJUA is heavily concentrated in the

three counties of Dade, Broward, and Palm Beach, which together account for 92% (104,844) of its policies and 96% (\$17.7 billion) of its insured value.

RPCJUA and FWUA Depopulation Programs- During the 1995 session, legislation was enacted establishing statutory guidelines for the depopulation of the RPCJUA. The Legislature had become concerned about the dramatic growth of the RPCJUA and the potential deficit assessments against insurance companies and their policyholders. The legislative findings and intent specifically noted that “extraordinary measures” were needed to reduce the number of policies in the RPCJUA and thus a “variety of financial incentives” were necessary to encourage replacement of RPCJUA policies with policies written by admitted insurers at approved rates.

Under the statutory scheme, companies could receive up to a \$100 per policy bonus for take-outs of at least 25,000 policies subject to approval by the association board. Such bonuses would be funded through premium revenues and the take-out insurer would be required to provide coverage for at least 3 years. Additionally, the Legislature gave the association the authority to offer a limited exemption from regular assessments, which would apply to the policies an insurer removed from the RPCJUA and would decline over time. In the first year, 100% of the premium was excluded from the insurer’s assessment liability; in the second year, 75% was excluded; and, in the third and final year, 50% was excluded. The RPCJUA approved 3 companies to participate in this incentive program and collectively the companies removed approximately 183,387 policies.

Under a separate section of the 1995 bill, the Legislature granted the RPCJUA broader general authority to develop additional depopulation incentives to reduce both new and renewal policies than the specific depopulation criteria outlined in s. 627.3511, F.S. The 1999 Legislature repealed the provision that prohibited the association from offering take-out bonuses and assessment exemptions when the policy count of the association falls below 250,000. Utilizing these legislative authorizations, the association has been able over the past several years to implement a series of take-out programs that offer a variety of cash bonuses and assessment exemptions as incentives for insurance companies to remove policies.

In November 1995, the RPCJUA launched its Open House Program which included the following take-out incentives: (1) three-year, 100% exemptions from

RPCJUA regular deficit assessments by removing a minimum of 1,000 policies; and (2) eligibility for receiving a \$40 per policy bonus for removing 5,000 to 12,499 policies, a \$60 per policy bonus for removing 12,500 to 24,499 policies and a \$100 per policy bonus for removing 25,000 policies in certain geographic locations. Under this program twelve companies collectively removed approximately 421,839 policies from the RPCJUA. In February 1997, the RPCJUA initiated the Market Challenge Program which offered the same incentives as those offered under the Open House Program. However, the association offered companies a flat rate of \$100 per policy to remove at least 10,000 mobile home policies. Twelve insurers collectively removed approximately 360,104 policies, of which 58,000 were mobile home policies.

The RPCJUA inaugurated the Coastal Countdown Program in February 1998 in order to specifically depopulate the three counties in which the RPCJUA had a high concentration of policies, namely Dade, Broward and Palm Beach. Increased take-out incentives were offered which included a \$200 per policy bonus for removing Dade county policies; a \$150 per policy bonus for Broward and Palm Beach county policies; and a \$100 per policy bonus for other coastal county policies. Insurers were given options to remove at least 5,000 policies pursuant to several options. It soon became evident to the RPCJUA that companies could not meet these policy requirements, thus, the association revised the requirements to allow insurers to take-out 1,500 policies from Dade County and 3,500 policies from Broward and/or Palm Beach counties. Companies were also eligible for the 3-year, RPCJUA regular deficit assessment exemptions as well as the 3-year FWUA regular assessment exemptions. Pursuant to this program, seven insurers collectively removed approximately 67,198 policies.

In late May 1999, Clarendon National Insurance Company entered into a Consent Order/Agreement with the Department of Insurance wherein the insurer agreed to remove up to 100,000 of the 195,000 policies remaining in the RPCJUA and up to 48,029 policies from the FWUA. In return, Clarendon would receive a \$300 per policy take-out bonus which was higher than the \$100 and \$200 bonuses paid to companies under the previous take-out programs. According to representatives with the Department of Insurance, this large bonus was because all of the policies were in "extremely hurricane-prone areas." Clarendon agreed to write the policies at 3 percent below the current RPCJUA base rate for homeowners policies and 5 percent below the RPCJUA base rate for mobile home

policies. Clarendon will assume the FWUA's existing rates for the wind-coverage policies it removes. Additionally, the company must implement a keep-out program to facilitate placement of at least 10,000 new policies that would otherwise come to the RPCJUA. The RPCJUA is also setting aside a contingency reserve of \$210 per policy which would be paid out to Clarendon only if hurricane claims on these specific RPCJUA take-out policies exceed \$22.5 million per year in the next 3 years.

Since the inception of the depopulation program in 1995, the RPCJUA has approved 33 insurance companies to remove more than 1.1 million policies through its take-out programs and has ultimately awarded more than \$109 million in bonus moneys to these take-out insurers.

Although the RPCJUA had been concentrating on its take-out program for several years, by 1998 it was averaging more than 11,000 new policies each month. In response, the RPCJUA launched two programs during 1998 which were designed to prevent policies from coming into the association. As a result of the two programs, the amount of new business coming into the RPCJUA declined to between 4,000 and 5,000 policies a month.

FWUA Depopulation - The FWUA, unlike the RPCJUA, lacks statutory authority to offer either cash bonuses or exemptions from assessments in its depopulation program. In 1998, the FWUA developed a broad depopulation rule which included both "take-out" and "keep-out" procedures. The Department of Insurance approved the keep-out procedures in January 1998, but still has under review the take-out provisions.

In May of this year, Clarendon National Insurance Company became the first company to formally enter into an agreement with the FWUA to remove wind only policies from the association. The insurer assumed 37,312 FWUA wind only policies, with 40 percent of the policies from Monroe, Dade, Broward, and Palm Beach counties. The company made what is referred to as a "me to" filing, which meant that all coverage and terms are the same as the FWUA. As of July 1999, several other insurers have contacted the FWUA about taking out more policies.

Pursuant to the FWUA "keep-out" program, insurance companies provide quotes for coverage of FWUA applicants, and the FWUA then rejects the application for FWUA coverage if the insurer makes an offer to cover a particular property. Representatives with the

FWUA report that the keep-out program is expected to keep-out between 10 and 20 applications a week.

Availability of Coverage in the Voluntary Market - The growth pattern of the RPCJUA and FWUA are indicative of the availability of coverage in the voluntary, private market. In most areas of the state, coverage is generally available from authorized insurers. The RPCJUA is writing very little new business outside of Broward, Dade, and Palm Beach counties. In these three counties, however, coverage remains difficult to obtain, particularly in the FWUA-eligible area, east of Interstate 95. Interviews with representatives of the Florida Market Assistance Plan and insurance agents in that area indicate that windstorm coverage with authorized insurers is extremely limited, but is more generally available for high value property and for locations that are least 1,500 feet from the coast, and there is greater availability of coverage from surplus lines insurers.

Residential Property Insurance Rates- The Department of Insurance reports that since Hurricane Andrew (August 24, 1992), residential property insurance rates have increased 108.5 percent, on a statewide basis, weighted for market share, for the insurers that were the top ten writers in 1994.

In 1996, the FWUA had its first rate increase in 13 years, averaging 31 percent statewide. In 1998, the FWUA obtained an average statewide increase of 12 percent, as determined by an arbitration panel after the FWUA had filed for a 61 percent increase to be phased in over a 3-year period, that was disapproved by the department. A new rate filing was filed by the FWUA in May 1999, which was disapproved by the department. The FWUA has filed for arbitration of the rate filing, which is pending. The FWUA rate filing would increase rates by a statewide average of 128 percent, with a maximum annual increase of 40 percent. The filing is based on all five models approved by the Florida Commission on Hurricane Loss Methodology, which generally varies rates by distance from the coast. The filing also provides premium credits for homes that meet or are retrofitted to meet certain construction design standards that mitigate against hurricane losses, so that the rate increase would be in the 60-80 percent range if a policyholder meets these standards.

The Department of Insurance was asked to provide a rate comparison to the committee of the hurricane rate and the non-hurricane rate (which must be separately identified by insurers) in Dade, Broward, Palm Beach,

and certain other counties, for the FWUA, RPCJUA, State Farm, Allstate Floridian, and the two insurers that charge the highest and lowest rates among the top eighteen writers in those counties, for homes valued at \$75,000, \$150,000, and \$300,000 with hurricane deductibles of \$500 and 2 percent of policy limits.

The FWUA provides windstorm coverage only, so the most relevant comparison is between the hurricane rates for the FWUA with the hurricane rates of other insurers. However, the FWUA charges a separate premium for appurtenant structure coverage for screened enclosures, which makes the comparison difficult. The FWUA reports that only about 3 percent of its policyholders elect this coverage. Most companies include this coverage as part of the standard policy, but State Farm does not provide coverage for detached buildings in five counties, including Dade.

With these factors in mind, in Dade County, the hurricane rate for the FWUA *with* appurtenant structure coverage is \$1,554, which is lower than the \$2,352 rate for the highest priced insurer (Florida Farm Bureau), and lower than the \$1,742 rate charged by Allstate Floridian, but higher than the \$1,260 rate charged by State Farm and the \$507 rate charged by the lowest priced insurer, Prudential. However, the FWUA rate *without* appurtenant structure coverage is \$865, which is lower than the rates of each of these insurers except the lowest priced insurer. This pattern holds true for Broward and Palm Beach counties.

RECOMMENDATIONS

The current exposure and expected losses of the FWUA create a likely possibility that significant assessments will be imposed on all property insurance policyholders if this exposure is not reduced. The Legislature and the Department of Insurance should consider options to reduce the exposure of the FWUA in a manner that does not unfairly impact FWUA policyholders. Options include the following:

- Specifying the standards and procedures that must be followed if an insurer makes an offer of coverage that would disqualify a policyholder from maintaining FWUA coverage, including adequate notice to the policyholder, agent, and other peril insurer; providing the other peril insurer with the option of writing the windstorm coverage; and authorizing the department to approve the take-out insurer's financial capacity to meet its obligations.

- Eliminating or reducing coverages that are not typically covered under a standard homeowners policy, such as tiki huts and gazebos;
- Limiting coverage for personal lines residential risks to a specific value, such as \$1 million, if a determination is made that such coverage is generally available from authorized insurers or the surplus lines market.

The current law requires that rates for the FWUA be actuarially sound and not be competitive with approved rates charged in the admitted voluntary market. The law also provides the FWUA board with the option for arbitration of a rate filing, and provides that hurricane loss projection models are admissible and relevant in a rate hearing if they have met the standards approved by the Florida Commission on Hurricane Loss Methodology. These standards and procedures should be sufficient to address concerns regarding the adequacy or excessiveness of the FWUA rates.

The Legislature should consider imposing an outside limit on the annual liability of the FWUA to its policyholders, comparable to the practical limits imposed on policyholders of authorized insurers. The limit could be equal to the estimated probable maximum loss for a 100-year storm (currently \$5.3 billion), as annually determined by the board and the department, with a minimum guarantee of \$300,000 per claim and pro rata reduction of claims beyond this limit. Under current law, after a major hurricane, the FWUA will be forced to use the debt financing that it has secured, and if that is not sufficient, attempt to issue revenue bonds or other means of additional debt financing to pay its contractual obligations to policyholders. Such additional financing may not be available or would, at best, carry high interest rates and debt service. This potentially unlimited liability would be borne by all policyholders in the state. Failure of the FWUA to aggressively pursue and obtain debt financing for the full extent of its liability could lead to lawsuits against the association and the state. The FWUA board has followed a policy of securing debt financing sufficient to cover its estimated 100-year

storm loss. Similarly, the Department of Insurance requires an insurer to have surplus and reinsurance to cover its estimated 100-year storm loss, as a condition of approval to take policies out of the RPCJUA or FWUA. If an authorized insurer becomes insolvent, the Florida Insurance Guaranty Association guarantees payments of policyholder claims, but only up to \$300,000 per claim. For condominium association policies, the limit is \$100,000 multiplied by the number of units. FWUA policyholders should be assured of these same minimum recoveries, but not more. Since the FWUA cannot technically become insolvent, it would be equitable to its policyholders to impose an outside limit on the FWUA's liability equal to the 100-year storm financing that financially sound voluntary insurers are expected to obtain.

The Legislature should consider requiring authorized residential property insurers to maintain adequate surplus and reinsurance to cover their estimated probable maximum loss for a 100-year storm, as estimated by at least one of the models meeting the standards approved by the Florida Commission on Hurricane Loss Methodology. Despite the fact that this standard is generally accepted by insurance rating organizations and required by the Department of Insurance as a condition of approval for insurers taking policies out of the RPCJUA or FWUA, it is not a statutory requirement for all residential property insurers.

The Legislature should consider amending the definition of *hurricane coverage* to provide a more specific determination of when a hurricane deductible applies. One option is to require that the damage occur in a county in which the Division of Emergency Management of the Department of Community Affairs, based upon official forecasting information from the National Weather Service, declares that an area in the county sustained winds that were part of the storm system.

COMMITTEE(S) INVOLVED IN REPORT (*Contact first committee for more information.*)

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MEMBER OVERSIGHT

Senators Geller and Childers