

# **Task Force on Long-Term Solutions for Florida's Hurricane Insurance Market**



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## Summary Findings and Recommendations

Senate Bill 1486, Section 24, created the Task Force on Long-Term Solutions for Florida's Hurricane Market and charged the Task Force with gathering information and making recommendations for ways to ensure that hurricane insurance is available for Floridians. Over the course of meetings from August 2005 through January 2006, the Task Force gathered information, heard expert testimony and received public testimony. The report that follows characterizes the issues examined, the information and testimony received, and provides a number of recommendations that the task force believes will help to address the short-term and long-term availability problems.

Because of the absolute size of the economic losses that are possible due to hurricanes in Florida, the private market, public mechanisms, and even the state itself simply do not have sufficient capacity to provide recovery from a truly mega-catastrophic hurricane event. Modelers have suggested that the worst case hurricane event for Florida would be a strong category 5 storm traveling westward that crosses the heavily populated areas of South Florida and then turns to the northeast and re-enters Florida crossing Hillsborough and Pinellas counties, continuing through the heavily populated central Florida and north Florida areas before exiting back into the Atlantic Ocean. Any long-term solution to the Florida hurricane insurance market should include a rational, comprehensive national catastrophe plan, such as is being currently debated in several arenas. The Task Force strongly recommends that Florida's leadership continue to put forth significant efforts in this area for the sake of the continued sustainability of the Florida economy.

Any long-term solution to the Florida hurricane market must also use current Building Codes and effective mitigation (action taken to reduce or eliminate the long-term risk to people and property from hazards and their effects) as a bedrock element. The evidence presented to the Task Force clearly demonstrated that safe homes can be built without prohibitive cost increases. Because of the age of the Florida housing stock, particular emphasis on meaningful mitigation retrofits to existing homes is critical in order to make people safer in their homes, to allow them to shelter in place, and to reduce their risk of loss. By reducing their risk of loss, they reduce the likelihood of having to pay their deductible and the disruption caused by relocating to temporary housing. The Task Force also heard testimony that the stock of mobile homes, in particular, presents a unique problem for the Florida market.

Key overall findings of the Task Force include:

- The hurricane losses of 2004-2005 have seriously strained the resources of both the voluntary market and the public sector mechanisms of Citizens Property Insurance Corporation (Citizens) and the Florida Hurricane Catastrophe Fund (FHCF). Following the 2004 season, the voluntary market recapitalized in large part, but a number of insurers re-evaluated their hurricane exposure, reducing market share in some cases. The same is true following the 2005 season, though new firms are entering the market. However, the re-trenchment by the large insurers has not been offset by the new companies. Since the 2004 hurricane season, Florida insurers have

infused approximately \$1 billion of new capital into the market. However, given the 2005 hurricane season and projections for future hurricane activity in Florida, it is recognized that without sufficient rate increases and other changes that provide greater pricing certainty in the property insurance marketplace (e.g., mitigation), it is likely that the Florida marketplace will suffer severe limitations on investor resources for continued recapitalization and have future limitations.

- Attracting new capital to the Florida market will remain a critical priority for the foreseeable future, based on projections of current and future needs.
- The FHCF fulfilled its purpose in the face of the 2004 hurricane season, as well as the 2005 hurricane season. The stability and availability of capital in the FHCF has served as the cornerstone for market recovery and as the catalyst for attracting new companies and additional new capital to Florida. However, the combined losses and experience of the 2004-2005 hurricane seasons have strained the cash resources of the FHCF, as well as the resources of the voluntary market.
- Any meaningful long-term solution must recognize that there are hurricane events possible that are beyond the capacity of the voluntary market, the public mechanisms and the state's financial wherewithal. For these reasons, any successful long-term solution to the capacity problems in the Florida property insurance market should include a federal backstop. State leaders should continue their efforts to develop a comprehensive national catastrophe program.
- It is imperative that any program focus strongly on ensuring that homes in Florida are wind resistant through mitigation, which is defined as a construction activity that fortifies or hardens the envelope of residential structures by using a variety of techniques. Strong, enforced building codes are the foundation for a sustainable market for Floridians. In addition, recognizing the age of the Florida housing stock, meaningful mitigation measures must be promoted. Mitigation reduces the amount of loss, permits homeowners to shelter in place and is a valuable investment for individuals and governments.

Regarding Building Codes, the Task Force recommends:

- Eliminating the designation of the wind-borne debris region for the panhandle of Florida from Chapter 200-141, Laws of Florida, subject to final determination by the Florida Building Commission, and allow the wind-borne debris region for that area of the state to be determined by the Florida Building Commission.
- Supporting the Florida Building Commission adoption of the 2006 International Residential code that will lead to removal of the option to design buildings as partially enclosed.
- Removing the Exposure Category C definition from law, thereby authorizing the Commission to develop and adopt a new definition within the code by administrative rule.

Regarding Mitigation, the Task Force recommends:

- Establishing Mitigation Public Awareness/Education as a major public priority which continues enhanced promotional campaigns to educate Floridians about the effectiveness of retrofitting and incentive opportunities to stimulate demand for safe homes.
- Considering creation of a Mitigation Consumer Advocate to report annually to the Executive and Legislative branches on the state of mitigation funding and program performance.
- Encouraging local government to provide property tax credits or rebates if homeowners perform mitigation.
- Continuing an expanded emphasis on the importance of professional education and training of contractors, the construction workforce and design professionals on mitigation issues, retrofitting, and technologies.
- Establishing Mitigation Consumer Assistance Programs including (1) free consumer mitigation retrofit inspections by trained and qualified inspectors, (2) provision of retrofit grants for low-income families and (3) provision of low- or no-interest loan programs for established, effective mitigation techniques (openings and roofs) should be made available, at least initially in the most high-risk areas of the state. A pilot program to establish individual residential building sturdiness index scoring should be developed using the data from the free inspections.
- Enhancing the Building Code Effectiveness Grading System (BCEGS) to provide greater incentives with appropriate discounts and surcharges.
- Implementing a pilot project to require that licensed Florida certified contractors or other Florida licensed inspectors provide written documentation in the form of a checklist so that real estate transactions include disclosure by the seller on the existence or absence of mitigation features in a property at the time of sale.
- Developing a uniform Hurricane Resistance Grading Schedule that would assign a grade to structures (houses or condominiums) based on the existence of windstorm loss mitigation features/construction techniques. This schedule, including reasonable discounts, could probably be either determined by or in conjunction with the Department of Community Affairs (DCA) or the Florida Building Code Commission. The DCA should probably also be responsible for determining the appropriate credentials necessary for licensed inspectors to perform the inspections used to determine grades.

Regarding the mobile home insurance market, the Task Force recommends:

- Conducting a more rigorous study of the mobile home market. As a first step, appropriate state agencies and other institutions should be called into a group to determine a systematic way to identify the size and age of the market.

The Task Force determined that the following issues were of such significance that they should be addressed in terms of the Florida insurance market as a whole, in addition to Citizens and recommends:

- Conducting an analysis based on the evidence from multiple sources, regarding mobile home construction, installation, and age, to determine whether mobile homes with attached additions (carports and other attached structures) are insurable risks and whether or not they should be insured by the admitted market.
- Conducting an analysis to determine whether other attached or free-standing structures such as pool cages for which risk cannot be reduced, should be insured.
- Amending Citizens' enabling statute to provide that eligibility for coverage with Citizens is limited to those properties with a structural value of less than \$1 million (increased annually for CPI) for Coverage A for HO-3 and Coverages A+C for HO-6 including provisions that permit flexibility by Citizens' to address contractions in the property market and permit Citizens to use a manual rate that is actuarially derived for properties valued over \$1 million.

Since maintaining and expanding competitive conditions in the Florida private sector property insurance market is critical to the economic viability of the state, the Task Force recommends:

- Expanding the Office's monitoring and analysis of market conditions.
- In order to reduce the frictional cost of regulation and to encourage capital in the market, the Legislature should authorize the Office of Insurance Regulation to establish a streamlined rate filing process, publish a reasonable competitive rate of return model for investors, and publish trend factors to be used in rate filings.
- A streamlined rate filing process should be implemented that permits insurers to use a manual rate that is actuarially derived for properties valued over \$1 million to permit competition with the surplus lines market.
- Ensuring, through the Office's leadership position within the NAIC, that any arbitrary, artificial barriers to competition in the reinsurance market are removed without jeopardizing solvency. State leadership should develop closer working relationships with the global reinsurers.
- The Office continuing to work closely with Citizens and the private market to encourage investment in Florida's property insurance market.

- Not amending the Florida Statutes to require insurers to write specific lines of business. Linking whether companies are able to write one line of business to being able to write other lines of business may be detrimental to market expansion and create an artificial barrier to capital entering the Florida insurance market.
- Amending Section 631.57(1)(a)2, Florida Statutes regarding FIGA to increase the cap for homeowners' dwelling claims to \$500,000.
- Determining whether or not hurricanes and sinkholes represent risks insurable in the private market is a critical determination that needs to be made as consideration is given to public policy concerning the Florida property insurance market.

Regarding the FHCF, the Task Force recommends:

- Determining the ability of the FHCF to continue to fulfill its mission or improve the market given its current structure and design as well as to determine if changes to trigger levels and/or exhaustion points are needed. This analysis should include a determination of better ways to address multiple event years that would better fulfill the FHCF's mission.
- Building a rapid cash build-up into the FHCF's rate structure in order to replenish the cash depleted in 2004 and 2005, which may offset the need for post-storm assessments, albeit after an increase in rates initially.
- Amending the Florida Constitution to help protect the capital of the FHCF so that it is used specifically to pay hurricane claims and related expenses including mitigation funding, which is a statutory requirement (Section 215.555(7)(c), Florida Statutes, that requires the legislature to annually appropriate at least \$10 million, not to exceed 35% of the FHCF's investment income, for mitigation projects).
- Exploring other methods for enhancing cash buildup of the FHCF.
- Considering a public policy determination as to whether some of the increased sales tax revenues realized from post-storm recovery should be earmarked for the FHCF, mitigation activities, and public infrastructure.

Regarding Citizens, the Task Force recommends:

- Amending Citizens' enabling statute to provide that eligibility for coverage with Citizens is limited to those properties with a structural value of less than \$1 million (increased annually for CPI) for Coverage A for HO-3 and Coverages A+C for HO-6 including provisions that permit flexibility by Citizens' to address contractions in the property market and permit Citizens to use a manual rate that is actuarially derived for properties valued over \$1 million.

- Continuing to levy a seasonal occupancy surcharge of 5% for the HRA and 10% for PLA policies (for personal residential policies), until such time as Citizens is able to gather sufficient data to actuarially determine the surcharge amounts.
- Citizens continuing to limit coverage offered on mobile homes built prior to 1994 to Actual Cash Value.
- Citizens determining the feasibility of making available other policies with more restrictive coverage to allow more choices for insurance consumers placed into Citizens.
- Clarifying the statutory language governing Citizens' ratemaking process to clearly delineate that Citizens use the higher of the "Top 20" requirement and the "actuarially sound" requirement.
- Amending Section 627.351, F.S., to codify in law the ethics and conflict of interest provisions that were added to the Citizens' Plan of Operations and approved by the Office of Insurance Regulation.
- Requiring that the rates charged by Citizens include a capital accumulation component so that Citizens will develop a capital base similar to that required of insurers in the voluntary market. This will, over time, reduce the need for and frequency of assessments.
- Implementing a pilot project to reduce the risk of loss for Citizens' policyholders with second homes or with structures valued over \$500,000 in the wind borne debris area to make them more marketable in the voluntary market by limiting to a period of three years the amount of time an insured property may remain in Citizens without an additional surcharge if the property could be insured in the private market with additional investment in retrofitting those structures using mitigation hardening techniques. This pilot project should be coordinated with the Department of Community Affairs mitigation programs to access available grant and low-cost loan funding sources as appropriate.
- Requiring Citizens to report twice a year on the effectiveness of the recently implemented revision to its take-out program. The report should document the number of policies taken out of Citizens' portfolio, the net reduction in exposure resulting from the take-out, the expected net cost to Citizens of the policies taken out, and the expected net reduction in reinsurance or other risk transfer resulting from the policies taken out.
- Citizens continuing to aggressively market its bonus program to encourage depopulation activities in conjunction with the Office.



- Obtaining statutory clarification to provide clarity in the law that Citizens is authorized to offer a myriad of bonuses approved by the Citizens' Board and the Office.
- Citizens developing and implementing a keep-out program designed to help market risks to the private insurance market before being bound in Citizens.
- Enacting a statutory provision such that the agent and agency shall have no E & O (errors and omissions) exposure for "take-out" and "keep-out" policies so long as the risk is placed with an admitted insurer that is covered by the Florida Insurance Guarantee Association (FIGA).
- Earmarking the increased sales tax revenues realized from post-storm recovery for Citizens to decrease the likelihood of an assessment.
- The Office establishing an ongoing reporting structure highlighting claims-handling performance using metrics similar to those used in the Office's disaster reporting framework, e.g., number of claims filed in a period, number of days to adjust, and settle a claim, using recent audits such as the Auditor General's report, Citizens' internal audit, and the processes of the Office's Market Investigations Unit to establish the framework for reports.
- Using the information contained in the Auditor General's report, as well as the Citizens' Board recommendations, to maintain a feasible plan of operation that can be objectively monitored and results measured, including provisions that would ensure competent customer service.
- Establishing a meaningful set of uniform performance metrics to be reported by Citizens to the Office. These metrics would be the same as those available to the Office for measuring similar performance in the voluntary market.
- Establishing other performance methods that would permit consumers to compare companies as is done in the private market.

Regarding the designation of the Windpool area, the Task force recommends:

- Designing a systematic methodology for establishing Windpool areas.
- Suspending 2004 statutory changes to the arbitrary Windpool line and not permitting the line to be moved by operation of law.

There is industry opposition to shrinking the Windpool. Some parts of the industry advocate expansion of the Windpool to statewide. However, removing all other perils from the residual market, it may become very difficult for Citizens to purchase reinsurance and to pay claims.

# **Florida's Hurricane Insurance Market – Background, Findings, and Recommendations**

## ***Creation of the Task Force on Long-Term Solutions for Florida's Hurricane Insurance Market***

Recognizing that the continued availability of property insurance, especially after the 2004 Florida hurricane season, is critical to the state's economic survival, the Florida Legislature created the Task Force on Long-Term Solutions for Florida's Hurricane Insurance Market (the Task Force) in 2005. The express purpose of the Task Force is to make recommendations to Florida's legislative and executive branches to ensure that there remains sufficient capacity in the private and public sectors to ensure that all Floridians can obtain appropriate insurance coverage for hurricane losses. The specific language creating the Task Force, its membership, and its charges and responsibilities are referenced in Appendix One.

The Task Force was created prior to the 2005 hurricane season, which further accentuated the critical role of property insurance in the Florida economy. In fact, the inaugural meeting of the Task Force was on August 24, 2005, the day Tropical Storm Katrina (later to become Hurricane Katrina) developed off Florida's east coast. From August, 2005 through February 2006, the Task Force met eight times at various locations around the state to receive informational testimony from experts in the fields of insurance, reinsurance, construction and insurance regulation, and especially to receive public testimony on these important issues. The meeting dates and locations were:

August 24, 2005 – Tallahassee  
September 28, 2005 – Tallahassee  
November 14, 2005 – Tampa  
November 30, 2005 – Tallahassee  
December 14, 2005 – Pensacola  
January 18/19, 2006 – Miami  
January 30/31, 2006 – Orlando  
February 27/28 – Tallahassee.

The agenda and minutes for each meeting are also referenced in Appendix One. The facts, issues, and public testimony were thoroughly debated and this report serves to convey the Task Force's final recommendations.

The Task Force members included representatives from the insurance industry, the lending industry, the academic community, the construction industry, an expert in hurricane mitigation, the Insurance Commissioner of the State of Florida and the Insurance Consumer Advocate of the State of Florida. The members of the Task Force were:

Kevin M. McCarty, Commissioner, Office of Insurance Regulation, Chair  
Leslie Chapman-Henderson, President/CEO, Federal Alliance for Safe Homes,  
Vice-Chair

Steve Burgess, Insurance Consumer Advocate, State of Florida  
Richard Cain, Vice President, State Farm Insurance Company  
Dave Cobb, Former insurance agent  
Randy Dumm, Ph.D., Associate Professor of Risk Management and Insurance,  
Florida State University  
Dan Gilmore, President, Florida Homebuilders' Association  
Blair Glenn, Senior Vice President, Wachovia Mortgage Corporation  
George Grawe, Counsel, Allstate Floridian Insurance Company  
Tony Grippa, Executive Vice President, Brown & Brown Insurance Company  
Robert P. Hartwig, Ph.D., CPCU, Senior Vice President & Chief Economist,  
Insurance Information Institute  
Harold Humphrey, Vice Chairman, InSource, Inc.  
James Wurdeman, President/CEO, Poe Financial Group

The remainder of this report is organized as follows. The economic impact of the 2004 and 2005 hurricane seasons on the Florida insurance market are reviewed in order to provide a framework and perspective for looking forward. The next section provides information and estimates regarding the future demand for property insurance in Florida, along with the attendant capital required to satisfy the expected demand. The report then reviews the financial economic and regulatory aspects of the private property insurance market, with a particular focus on Florida's unique situation.

Following this discussion, the report reviews the status of Florida's public sector hurricane risk mechanisms, Citizens and the FHCF. Attention is given not only to the performance of these entities during the 2004 and 2005 seasons, but also to their current economic and financial situations, and what changes to their structure might be warranted.

Based on the information presented and reviewed, the report then offers specific recommendations for consideration by the legislative and executive branches of Florida. These recommendations include not only those specifically mandated in the legislative charge of the Task Force, but other long-term solutions as well.

### ***The 2004 and 2005 Hurricane Seasons***

Any recommendations or plans for the long-term hurricane insurance market need to be made within the context of the remarkable hurricane seasons of 2004 and 2005. These two seasons have had a dramatic impact on how hurricane risk is viewed, modeled and priced. As a result, the suppliers of capital to the Florida market are forced to re-evaluate the risk/return possibilities as they decide how much new capital to put at risk in the state.

The 2004 season saw four significant hurricanes (Charley, Frances, Ivan and Jeanne) together create 1.66 million claims resulting in \$20.9 billion dollars of insured losses in the Florida market, based on data reported to the Office's disaster reporting data system. This loss of premium income and capital was distributed among the insurers (\$11.3 billion – of that amount, \$1.8 billion related to Citizens), the reinsurance market (\$5.75 billion) and the FHCF (\$3.85 billion).

The insurance and reinsurance industry, after consideration of the risk implications provided by this unusual season of hurricane frequency, did recapitalize. That is, the capital lost by primary insurers and reinsurers was replenished, and actually came into the market relatively quickly. The FHCF was able to pay its share of the losses out of cash reserves

As the state was still recovering, recapitalizing and rebuilding from the hurricanes of 2004, the 2005 season began early with Hurricane Dennis. Then Hurricane Katrina moved across the southern portion of the state, Hurricane Rita moved from the Atlantic into the Gulf of Mexico, also across the southern part of the state, and then Hurricane Wilma came from the Gulf of Mexico across the state and then out into the Atlantic.

Claim and loss statistics are still in development and being reported, but as of this writing these four storms are estimated to have generated a combined 1.17 million claims and at least a combined \$9.3 billion in insured losses in Florida:

<b>Date</b>	<b>Storm</b>	<b>Florida Insured Loss*</b>	<b>Saffir-Simpson Category at FL Landfall</b>
July 10, 2005	Dennis	\$1.2 Billion	3
August 25, 2005	Katrina	\$597.4 Million	1
September 20, 2005	Rita	\$11.4 Million	2
October 24, 2005	Wilma	\$7.4 Billion	3

\*Losses are estimated maximum loss for Dennis and Wilma, and losses paid to date for Katrina and Rita, Loss Data from Office Disaster Reporting, and Multi-State Reporting

While firm numbers on how these Florida only losses are distributed among primary insurers and the reinsurance market are still being developed, losses from both Dennis and Wilma have already triggered payments from the FHCF, which estimates total 2005 season loss payments at \$2.58 billion as of January, 2006, but probably does not reflect the actual final cost.

Insurers and reinsurers have been evaluating their appetite for investing in the Florida market following the hurricanes of 2005, which immediately followed the four hurricanes of 2004. These losses, combined with expectations that the increase in hurricane activity will continue for the foreseeable future, have caused both insurers and reinsurers to reevaluate their tolerance for risk as well as the related amount of additional capital they are willing to put into Florida. Some insurers have added new underwriting restrictions to reflect changes in their exposure tolerance.

The reinsurance market has partly recapitalized, but not yet fully replenished their investment capital, according to the Reinsurance Association of America. While Florida is unique in the reinsurance market, with the majority of renewals coming in June to coincide with the FHCF contract term, the January reinsurance market for the rest of the

property risk in the United States shows some signs that reinsurers are reconsidering the risk/return relationships available when compared with other investment opportunities.

According to published reports, the January market was much slower in closing transactions than in the past, including 2005. As well, while overall rates appear not to have increased dramatically, wind reinsurance along the Gulf States is reported to have risen substantially. More common were narrowing in reinsurance treaty terms and conditions and increases in retention levels for private insurers looking to lay off risk to the reinsurers (e.g., a previous \$3 million retention may have moved to a \$5 million retention). Compounding the pricing and availability in 2006 will be new, higher capital requirements established by the rating agencies (Standard and Poor's, Moody's and Fitch) in order for a reinsurer to maintain their rating. It should be noted that higher capital requirements has had a similar impact on the primary insurance market.

The year 2005 was a record year for catastrophe losses in the United States according to several different industry sources, driven primarily by the impact of Hurricane Katrina in the Gulf States. For Florida specifically, it is useful to put the 2004/2005 seasons into some economic historical context. The table below lists the 10 most expensive (in terms of insured loss) catastrophes in the United States:

Top 10 Most Expensive U.S. Catastrophes				
Insured Loss (in \$ millions)				
Rank	Date	Peril	Dollars When Incurred	In 2005 Dollars
1	Aug. 2005	Hurricane Katrina	\$38,111	\$38,111
2	Aug. 1992	Hurricane Andrew	15,500	21,579
3	Sep. 2001	World Trade Center, Pentagon terrorist attacks <sup>(1)</sup>	18,800	20,716
4	Jan. 1994	Northridge, CA earthquake	12,500	16,475
5	Oct. 2005	Hurricane Wilma	8,418	8,418
6	Aug. 2004	Hurricane Charley	7,475	7,729
7	Sep. 2004	Hurricane Ivan	7,110	7,352
8	Sep. 1989	Hurricane Hugo	4,195	6,608
9	Sep. 2005	Hurricane Rita	4,976	4,976
10	Sep. 2004	Hurricane Frances	4,751	4,751

(1) Property coverage only; As of February 2006.

Source: ISO; Insurance Information Institute.

As the highlighted rows in the Table show, in the last two years Florida has been exposed, either solely or along with other states, to six of the most expensive catastrophes in history.

### ***Lessons and Actions from the 2004-2005 Seasons***

Just as Andrew was a wake-up call and learning experience for the Florida market in 1992 (see *The Property Insurance Market in Florida 2004: The Difference a Decade Makes* published by the Office at: <http://www.floir.com/pdf/TheDifferenceADecadeMakes.pdf> ) the hurricanes of 2004 and 2005 offered important lessons and insights to its citizens, legislators, insurers, reinsurers and insurance regulators. Following the meltdown of the insurance market following Hurricane Andrew, a number of initiatives and changes to the market were implemented that were tested in 2004 and again in 2005.

Deductibles for hurricane damage were changed from a flat dollar deductible to either 2% or 5% of the insured value for many homes valued at over \$100,000. This type of deductible is no longer unusual for loss due to catastrophic risk; indeed some 16 or 17 states have the same policy provisions for damage due to hurricanes and earthquakes.

A statewide Building Code was adopted to require both site-built and mobile homes to be able to more readily withstand major hurricane wind levels. Programs to retrofit site-built homes were implemented by state and local agencies. Initiatives to provide mitigation tools to mobile homes were begun.

The Florida Residential Property Casualty Joint Underwriting Authority (FRPCJUA) was created to provide a public/private response to the deterioration of insurance availability in the private market following Hurricane Andrew. As well, the Florida Windstorm Underwriting Association (Windpool), established in 1972, offered wind-only coverage in limited coastal areas to those who could not acquire it in the private market. By year-end 1995, the FRPCJUA had about 850,000 policies in force. By year-end 1999, the Windpool had roughly 500,000 policies in force with a combined exposure of almost \$86.5 billion. In 2002, these two entities were merged to create Citizens.

The FHCF was created in November 1993 during a special legislative session. Designed to provide a form of protection similar to reinsurance in an effort to maintain insurance capacity, the FHCF provides reimbursements to insurers, paid for by policyholders, for some level of catastrophic losses resulting from hurricanes. Insurers writing in Florida are required to participate in the FHCF, but are given some choice in their level of participation.

Much of what was implemented in Florida following Hurricane Andrew was structurally and operationally designed to deal with the return of another Category 5 hurricane like Andrew (or worse). Instead, 2004 and 2005 brought a different hurricane peril, multiple storms. Rather than one devastating Category 5 storm, 2004 brought four somewhat more moderate storms and 2005 another four even less powerful storms as measured by the Saffir-Simpson Hurricane Index.

	Hurricane	Saffir-Simpson Category at Florida Landfall
2004		
	Charley	4
	Frances	2
	Ivan	3
	Jeanne	3
2005		
	Dennis	3
	Katrina	1
	Rita	2
	Wilma	3

The financial losses mentioned earlier served to reinforce that wind speed is not the only measure of a hurricane’s potential damage as Wilma, Charley, Ivan and Frances have joined Andrew on the list of most expensive catastrophes to impact the United States. These storms offered other lessons as well.

It has been reported that the 2004 hurricanes caused damage to an estimated one in every five homes in Florida. The paths of these storms also indicated that indeed no place in Florida is immune from hurricane risk; three of the 2004 hurricanes passed through Central Florida, causing substantial damage well away from either coast.

The evidence left behind by these eight hurricanes also emphasized how effective the enacted Building Code can be. Storm after storm revealed that both site built and mobile homes that were built in compliance with the Florida Building Code fared demonstrably better than those that did not. Further, data are being collected that are showing that even those homes not built to the current code, but that were “hardened” via effective mitigation techniques fared much better than those not retro-fitted. The evidence also showed that some structures, such as pool cages, storage sheds and other out-buildings did not fare well and that there may be little that can be done to make them more wind-resistant.

Financially, the hurricanes of 2004 and 2005 showed that Citizens and the FHCF, for the most part, served the purpose for which they were designed. While Citizens’ claims handling processes did not work well during 2004, changes made showed in 2005 as consumer complaints fell dramatically. Financially, Citizens incurred \$1.8 billion in losses as a result of the 2004 season and had to assess \$516 million. A further assessment is expected following the 2005 season. While the assessments are not generally popular, they were the funding mechanism created by statute.

As a shock absorber to minimize disruptions in the market that could occur after these events as private market insurers re-evaluated their risk exposures, Citizens worked as intended. Policies being non-renewed by private insurers flowed into Citizens so

coverage was still available. It is also true that even during these two seasons, hurricane-exposed policies were taken out of Citizens and placed back into the private market.

The FHCF provided the reinsurance protection it was designed to offer. Losses from the 2004 and 2005 hurricanes were paid from cash resources held by the FHCF and to date, no bonding or assessment has been required. In the aftermath of the 2004 season, however, it became clear that the nature of the reinsurance mechanism that is the FHCF needed modification. Originally designed in response to the concerns of another single major hurricane, the triggering mechanism designed into the FHCF contract relied on a deductible retention level held by insurers on a separate per-event basis.

Following the 2004 season the Florida Legislature convened a Joint Select Committee on Hurricane Insurance in order to study the state of the Florida market after the 2004 storms and to determine what legislative changes needed to be made. One of the crucial determinations was that the per-event insurer deductible embedded in the FHCF contract needed to be re-engineered to allow the Fund more flexibility in responding to hurricane losses by creating a deductible system, described later, that would reflect the economic devastation that can be brought on by multiple storms.

Following the 2004 season and heading in to the 2005 season a number of actions were taken at the state level and as well at the national level.

### ***Senate Bill 1486***

In the regular session of 2005, the Legislature passed Senate Bill 1486 (SB 1486), which prescribed a number of changes to the property insurance market in Florida. The Task force heard from both the Office and the Department of Financial Services (DFS) on the status of the implementation of the bill. The Task Force also heard testimony from insurance industry trade groups about the implementation of SB 1486. This testimony is referenced in Appendix 8.

### **Implementation of SB 1486 by the Office**

The Office reported that it is proceeding with its implementation of the requirements of SB 1486, and has met the statutory requirements. The legislative requirements can be divided into four broad categories:

- New Insurance Guidelines
- Insurance Company Filings
- Committee and Task Force Issues
- Informational Reports

### ***New Insurance Guidelines***

The Office drafted hurricane loss mitigation premium discount guidelines, which were adopted by the Financial Services Commission during the January 11, 2006 meeting. The development of the Standard Rating Territory Plan and the outline of insurance coverage checklists have both been completed, and have been posted to the Office's website (<http://www.fl.com>).



During August 2005, the Office issued a data call to the industry to obtain detailed information about property exposure, and has begun collecting this information in rate filings on a going forward basis. Subsequently, the Office created a comprehensive list of data elements necessary for hurricane modeling, and issued *Notices of Intent to Disapprove* to insurers not following these guidelines in their rate filings.

### ***Insurance Company Filings***

Beginning in January 2006, insurers are required to submit additional deductible options (\$500, 2%, 5% and 10%), and these dollar amounts need to be prominently displayed on their policy forms. These filing requirements are being monitored by the Office's Property and Casualty Product Review Business Unit as new rate filings are received.

### ***Committee and Task Force Issues***

The SB 1486 Property Legislation established the Standard Personal Lines Residential Insurance Policies Advisory Committee, as well as this Task Force. These entities have been formed, are meeting, and are progressing with their work. The new membership requirements for the Citizens' Board outlined in the new law also have been effectuated.

### ***Informational Reports***

The legislation required the Office to issue a report pertaining to "Law and Ordinance" coverage. The report has been completed, and has been posted to the Office's website ([http://www.floir.com/pdf/OIRLaw\\_Ordinance\\_Cov\\_Study\\_13006.pdf](http://www.floir.com/pdf/OIRLaw_Ordinance_Cov_Study_13006.pdf)). The legislation also initiated a pilot program to encourage competitive insurance rates in Monroe County. The project is ongoing and the report was delivered to the Florida Legislature on March 1, 2006 and is posted to the OIR website at:

<http://www.floir.com/pdf/MonroeCountyPilotProjectReport.pdf>

### **DFS Implementation of SB 1486 by DFS**

SB 1486 required the Chief Financial Officer of the State of Florida to appoint a Standard Personal Lines Residential Insurance Policies Advisory Committee (Committee). The Committee was charged with developing standard personal lines residential policies and a checklist to be used for homeowners, mobile homeowners, condominium unit-owners and dwellings. The goal was for all authorized insurers offering that coverage to offer the standard policies and checklists. The Committee heard presentations and testimony from the insurance industry, consumer representatives and the Insurance Services Office, Inc. (ISO). Additionally, the Committee reviewed and compared policy forms and coverage options currently offered in at least 60 percent of the personal lines residential property market in Florida.

The Committee concluded that simplified policy language would be beneficial for consumers; however, adopting untested policy language could result in unintended legal consequences. Therefore, the Committee recommended that the Legislature appoint a task force with extensive knowledge regarding the legalities of the insurance contract along with actuarial support so they could review the impact of the 2004 consumer protection legislation and study the impact that offering a standard policy would have on the insurance market and premiums.

The Committee developed simplified language Consumer's Quick Check Guides for Homeowners, Mobile Homeowners, Condominium Unit-Owners and Dwellings which are modeled, in part, after ISO's latest policy forms. These guides are intended to provide consumers with a quick and easy-to-read guide to the various policy forms which highlight certain limits or exclusions that have been the source of concern for consumers.

The Committee was also charged with drafting a Checklist of Coverage for all personal lines residential policies. The Committee reviewed the Office's draft Checklist of Coverage which was being developed pursuant to Section 627.4143, Florida Statutes which requires the insurers to provide a Checklist when a personal lines policy is issued or delivered in Florida. The Committee concluded that the Checklist would provide consumers a greater opportunity to learn and understand the benefits and limitations if it were used by insurance agents and/or company representatives when a personal lines policy is purchased. Therefore, the Committee modified the Office's draft Checklist to address consumer concerns that were identified during the 2004 and 2005 hurricane seasons and recommended this legislative change.

The Committee's documentation and presentations as well as the Guides may be viewed on the DFS website at: <http://www.fldfs.com/standardpersonallinesadvisorycommittee>.

### ***Coastal High Hazard Study Committee***

On September 7, 2005, the Governor issued an executive order establishing the Coastal High Hazard Study Committee (Committee) to formulate recommendations for managing growth in areas of Florida affected by hurricanes. The Committee issued a report on February 1, 2006 which included recommendations on nine main issues, as well as recognizing areas meriting additional evaluation and assessment.

The Committee recognized that although hurricane evacuation is a local issue, data should be collected and standardized on a statewide basis. Several of the recommendations included making the data, and who is in charge of administering the collection of the data, more uniform. The Committee recommended consistent standards for modeling the impact of hurricanes by using the storm surge model utilized by the National Hurricane Center.

The Committee recommended centralizing the Hurricane Evacuation Studies (HESs) with the Division of Emergency Management. The report also encouraged better defined evacuation zones, and improving communications to homebuyers who purchase homes in these areas. The Committee also discussed building standards, specifically, making a recommendation to improve building standards for homes located seaward of the Coastal Construction Control Line (CCCL), as well as updating the CCCL, especially in the Florida Panhandle.

The report focused on dune protection pre and post- hurricane including the post-storm emergency coastal armoring and its effect on the environment. The committee recommended that the Department of Environmental Protection (DEP) review this issue and develop a recommendation by June 1, 2006 – the beginning of the next hurricane

season. Finally, the Committee noted that the Department of Health (DOH) has no statute or rule addressing the CCCL. The Committee recommended making statutory changes to allow coordination between the DOH and DEP on permitting issues.

### ***Mitigation Programs***

Any meaningful, long-term solution to the Florida hurricane insurance market must recognize the critical link between structures' wind-resistance and survivability. Increasing wind-resistance of buildings on the front end at the time of construction or retroactively through retrofitting will deliver a return on investment by reducing damage and therefore insurance losses. Fundamental approaches to increasing structures' survivability include adoption and enforcement of strong model building codes, increased public awareness of hurricane mitigation (action taken to reduce or eliminate the long-term risk to people and property from hazards and their effects) and implementation of mitigation consumer assistance programs.

In general, mitigation is the ongoing effort to lessen the impact disasters have on people's lives and property through education and damage prevention. Within this context, hurricane mitigation is defined as "a construction activity that fortifies or hardens the envelope of residential structures by using a variety of techniques." Techniques may include reinforcing roof-to-wall connections, reinforcing roof systems, use of superior roof material attachment methods, placement of secondary water barrier on roof decking and protection of all openings (window, doors, garage doors and gable vents, etc.) by either installing shutter systems or using wind and impact-resistant window and/or door systems.

Public Awareness - Barriers to widespread public awareness and understanding of hurricane mitigation include lack of understanding of wind-resistant construction by consumers and contractors, perception that mitigation is cost-prohibitive and lack of awareness of mitigation cost benefits.

The evidence clearly demonstrates that safe homes can be built without prohibitive cost increases, especially when cost is calculated in the context of loss of quality of life post-hurricane, the payment of insurance deductibles and general societal costs. Because of the age of Florida housing stock, particular emphasis on meaningful mitigation retrofits to existing homes is critical in order to make people safer in their homes, to allow them to shelter in place, and to reduce their risk of loss. By reducing their risk of loss, policyholders make it less likely that they will need to incur the additional cost of their deductible or suffer the inconvenience and cost associated with temporary housing.

Programs to educate consumers and contractors regarding true cost/benefits of mitigation and availability of insurance incentive programs provide important and useful information for home buyers regarding the value of wind-resistant attributes and are driving a growing market for hurricane mitigation as evidenced by demand for shutters and opening protection technologies. Additional means to spread this information include the use of real estate sellers' disclosure forms.

Mitigation Consumer Assistance Programs including retrofit loans with interest rate buy-downs, retrofit grants for low-income families and free inspections can help propel homeowners to engage in mitigation behavior.

According to the report issued in 2005 by the Multihazard Mitigation Council of the National Institute of Building Sciences, “*Natural Hazard Mitigation Saves: An Independent Study to Assess the Future Savings from Mitigation Activities*”, each dollar spent on mitigation, saves society an average of four (4) dollars. The study found that the “natural hazard mitigation activities funded by the three FEMA grant programs between 1993 and 2003 were cost-effective and reduced future losses from earthquake, wind, and flood events; resulted in significant net benefits to society as a whole (individuals, states, and communities) in terms of future reduced losses; and represented significant potential savings to the federal treasury in terms of future increased tax revenues and reduced hazard-related expenditures.”

### **Proposed Mitigation Funding**

Following the 2005 season, on February 1, 2006 Governor Bush released the Bush/Jennings Executive Budget Recommendations for Fiscal Year 2006-2007 for the state of Florida. An important part of this budget includes funding for hurricane related programs and investments in an amount of \$565 million. In addition to the \$123 million budgeted for the Back-To-School and Hurricane Preparedness Tax Holiday, the recommended budget includes:

- \$69.8 million to build County Emergency Operations Centers that can survive at least a Category 3 storm.
- \$50 million to retrofit older homes to make them more resistant to the damage caused by hurricanes.
- \$29 million to improve evacuation plans and \$6.5 million to improve logistics operations.
- \$30 million to permanently install generators in every one of Florida's special needs shelters that care for our frail, sick and elderly during a storm.
- \$12 million to add capacity for 100,000 people in general population shelters throughout the state. By this hurricane season, Florida will be able to shelter 816,000 people statewide - more than seven times the capacity available before 1999. Additionally, \$4.7 million is being recommended for a pilot project for communities to establish regional shelters.
- \$5.3 million for a public information campaign to help build a "Culture of Preparedness" throughout Florida.
- \$302 million for affordable housing in communities impacted hardest by the hurricane seasons of 2004 and 2005, including:
  - \$177 million to leverage federal funds and private capital to build, rebuild and repair rental housing.
  - \$98 million to meet the unique housing needs of a community, with an emphasis on home ownership

- \$25 million to address housing for farm workers, frail elders, people with disabilities and homeless families.
- \$2 million to repair and rehabilitate homes in communities severely impacted by the 2004 and 2005 hurricanes.

Regarding mitigation, the Task Force recommends:

- Establishing Mitigation Public Awareness/Education as a major public priority which continues enhanced promotional campaigns to educate Floridians about the effectiveness of retrofitting and incentive opportunities to stimulate demand for safe homes.
- Considering creation of a Mitigation Consumer Advocate to report annually to the Executive and Legislative branches on the state of mitigation funding and program performance.
- Encouraging local government to provide property tax credits or rebates if homeowners perform mitigation.
- Continuing and expand emphasis on the importance of professional education and training of contractors, the construction workforce and design professionals on mitigation issues, retrofitting, and technologies.
- Establishing Mitigation Consumer Assistance Programs including (1) free consumer mitigation retrofit inspections by trained and qualified inspectors, (2) provision of retrofit grants for low-income families and (3) provision of low- or no-interest loan programs for established, effective mitigation techniques (openings and roofs) should be made available, at least initially in the most high-risk areas of the state. A pilot program to establish individual residential building sturdiness index scoring should be developed using the data from the free inspections.
- Enhancing the Building Code Effectiveness Grading System (BCEGS) to provide greater incentives with appropriate discounts and surcharges.
- Implementing a pilot project to require that licensed Florida certified contractors or other Florida licensed inspectors provide written documentation in the form of a checklist so that real estate transactions include disclosure by the seller on the existence or absence of mitigation features in a property at the time of sale.
- Developing a uniform Hurricane Resistance Grading Schedule that would assign a grade to structures (houses or condominiums) based on the existence of windstorm loss mitigation features/construction techniques. This schedule, including reasonable discounts, could probably be either determined by or in conjunction with the Department of Community Affairs (DCA) or the Florida Building Code Commission. The DCA should probably also be responsible for determining the appropriate credentials necessary for licensed inspectors to perform the inspections used to determine grades.

### ***Windpool Designated Areas***

The Florida Windstorm Underwriting Association (Windpool) was created in 1970, pursuant to Chapter 70-234, Laws of Florida, to cover residential policyholders unable to secure windstorm coverage in the voluntary market. Eligibility was limited to structures in eligible areas found by the Department of Insurance, after public hearing, to meet three criteria: the lack of windstorm coverage in the area was deterring development, causing mortgages to be in default, and causing financial institutions to deny loans; the area was subject to the requirements of the Southern Standard Building Code or its equivalent; and that extending windstorm coverage to the area was consistent with the policies and objectives of environmental and growth management. In 2002, the Florida Residential Property Casualty Joint Underwriting Association merged with the Windpool to create Citizens Property Insurance Corporation. Consensus could not be reached between Task Force Members on what the Windpool area should be, but alternative positions were presented to expand the Windpool statewide.

Regarding the designation of the Windpool area, the Task Force recommends:

- Designing a systematic methodology for establishing Windpool areas.
- Suspending 2004 statutory changes to the arbitrary Windpool line and not permitting the line to be moved by operation of law.

There is industry opposition to shrinking the Windpool. Some parts of the industry advocate expansion of the Windpool to statewide. However, removing all other perils from the residual market, it may become very difficult for Citizens to purchase reinsurance and to pay claims.

### ***Building Codes***

The following is excerpted from analysis provided by the Collins Center for Public Policy, dated January 24, 2006.

The Florida Building Code (FBC) uses building standards established by the American Society of Civil Engineers (ASCE) and the International Family of Building Codes as guidance and frequently cites the ASCE standards. ASCE's Standard 7 is the national standard of engineering practice for designing buildings for all types of structural loads and risks. It is updated and maintained by the engineering society based on advances in the understanding of wind characteristics within hurricanes and advancements in building science with new editions published every three years.<sup>1</sup>

The Florida Building Commission constantly monitors the FBC and finds refinements that can add strength. It then proposes amendments to the Governor and Legislature.

Three relevant Building Code issues are before the 2006 Legislature:

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<sup>1</sup> 2005 Report of Florida Building Commission to Florida Legislature.  
[http://www.dca.state.fl.us/fbc/publications/2005\\_Leg\\_Rpt\\_ALL.pdf](http://www.dca.state.fl.us/fbc/publications/2005_Leg_Rpt_ALL.pdf). See pages 17-20.

1. Eliminate designation of the wind-borne debris region for the panhandle of Florida from Chapter 200-141, Laws of Florida, and allow the wind-borne debris region for that area of the state to be determined by the Florida Building Commission.

The FBC establishes “wind-borne debris regions” throughout the state to define coastal areas that may be subject to wind-borne debris damage during storms and consequently require more building protection than other regions of the state. Standards and definitions are found in American Society of Civil Engineers (ASCE) 7, a standard that designates types of geographic areas where buildings must be designed for wind speeds of 120 mph or more and where special window and door protection or other building strengthening is required.

For instance, all of the land in Monroe, Miami-Dade, Broward, Lee and Pinellas counties, whether directly on the coast or not, is included in the “wind-borne debris region” for those counties. The panhandle is an exception with its “wind-borne debris region” established by statute. Only one mile inland from the coast is included in the definition of “wind-borne debris region” for counties in the Florida panhandle. A few other places in the state (such as Citrus and Hernando counties) have “wind-borne debris regions” that are only one mile inland, but their status has been determined by ASCE standards rather than by special statute.

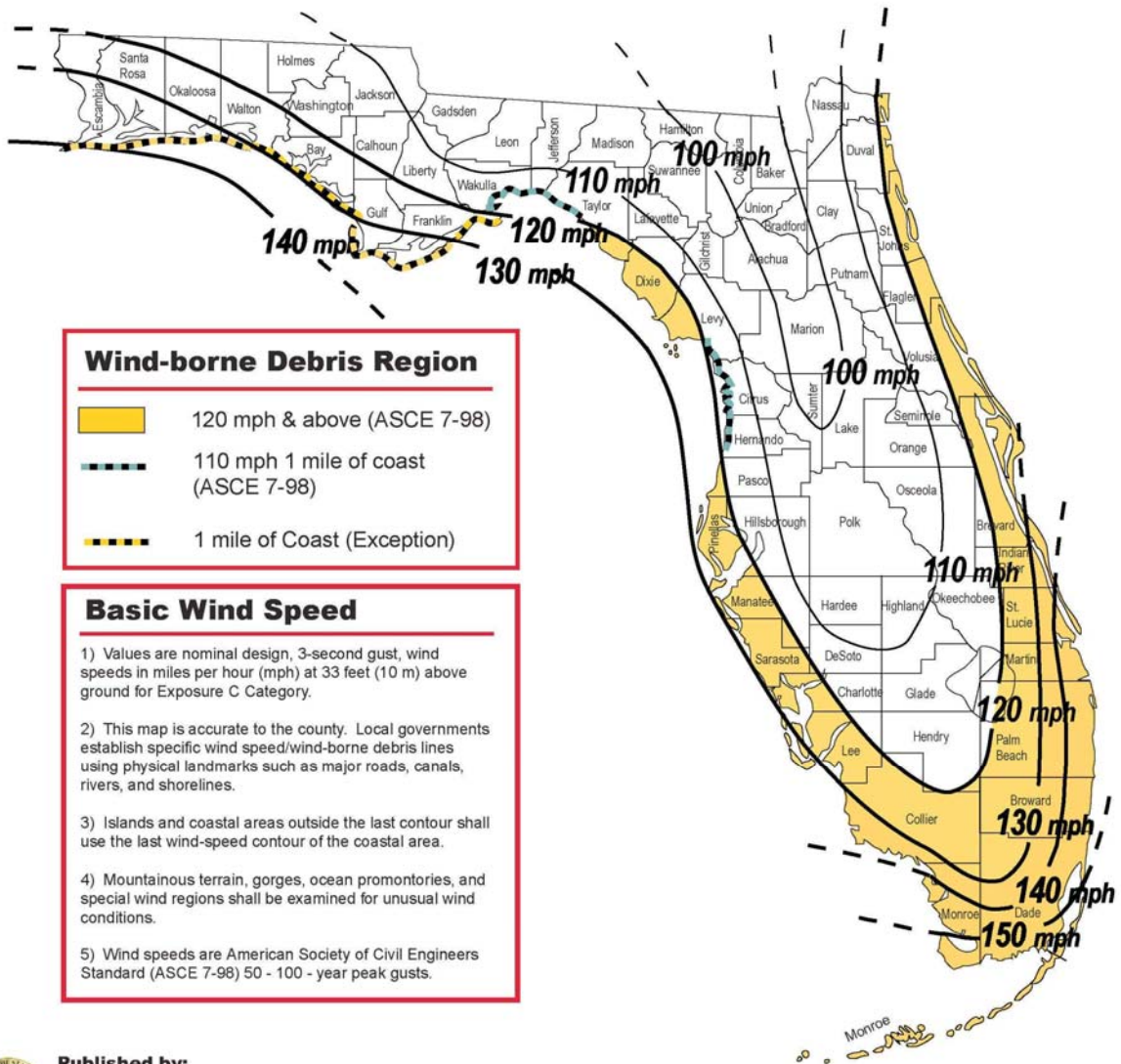
In 2000, the Legislature modified the designation of the “wind-borne debris region” for the panhandle from Appalachee Bay to the Alabama border. The modification, codified in law, designates only the area within one mile of the coast as the “wind-borne debris region” for that area of the state.

The Florida Building Commission believes that “strong tight storms”, such as Hurricanes Charley and Andrew, maintain their strength and speeds much further inland than one mile. In both 2005 and 2006, the Commission recommended that the Legislature defer to scientists in determining appropriate “wind-borne debris regions” for all areas of the state and include those designations in the FBC. This change could result in an extension of the “wind-borne debris region” in some areas in the panhandle for 5-to-20 miles inland.



# State of Florida

## Wind-Borne Debris Region



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This proposal has generated substantial controversy in the panhandle region. Most local building officials from the region do not think that the one-mile region needs to be increased and argue that damage in the panhandle is more related to surge than to



windborne debris. Some argue that some areas now included in the one-mile “wind-borne debris region” of the panhandle are not exposed to the same damage as other areas and should be even smaller than one-mile. Many agree that additional study would be useful to determine how damage has historically been caused in the panhandle region. A study is underway with a report due in March 2006.

Others, including some members of the general public, disagree. A survey by the Institute for Business and Home Safety in 2005 found that 74% of panhandle residents thought the panhandle region should have the same code as other Florida regions with the same requirements for hurricane shutters or impact-resistant windows and other protections. Many were surprised that standard “wind-borne debris region” definitions and protections did not apply in the panhandle.

The 2005 Legislature debated the issue, determined that more study was warranted, and directed citizens and interest groups to develop recommendations for action in 2006.

2. Eliminate the definition of wind exposure class C from Section 553.73 Florida Statutes, and allow the definition of ASCE-7 as adopted by the FBC to be used instead.

The effects of wind speeds on buildings can be changed dramatically by factors such as open terrain, shielding by substantial landscaping, and shielding by other buildings. Open terrain and shields of various kinds affect the strength of winds when they actually hit buildings. ASCE 7 has several classes for describing exposure to different types of winds based on whether shields are present or not.

- Exposure A is characterized by large cities with large expanses of tall buildings.
- Exposure B is characterized by suburban areas with large expanses of short and medium height buildings and some wooded areas.
- Exposure C is characterized by areas exposed to expanses of open terrain or open water.

Florida has a number of Exposure C areas: a long coastline and many lakes, bays and other bodies of water with much area exposed to wind without disruption by structures, trees or buildings. The force of winds in such areas can be 20-to-30% greater than the force of winds in areas with disruptions and shields.

Florida law now defines Exposure C areas as those that extend 1500 feet landward of the coast. The Florida Building Commission argues that this omits many other areas of the state where wind forces are considerably higher, exposing homes and residents in such areas to great risk without the building code protections that exist in legally-defined Exposure C areas.

The Commission recommended in 2005 that the current statutory definition of Exposure C areas (1500 feet landward of the coast) be repealed. This would permit the more flexible ASCE-7 definition to be used by the FBC. The ASCE-7 standard does not use arbitrary distances, but instead considers actual circumstances that exist in each exposed area,

circumstances that can change over time with new construction, deforestation and other developments.

### 3. Authorize the Florida Building Commission to make determinations related to designing buildings for internal pressures.

The original FBC included an ASCE-7 standard that permitted buildings in “wind-borne debris areas” to be constructed with window and glass door protection or to be designed to withstand additional interior pressurization if a window or door were blown out. Since that time, model codes (including the International Family of Building Codes that Florida usually follows) require window and door protection for all residential buildings; they do not now provide for the option of designing to withstand internal pressures instead of providing window and door protection. Except for Miami-Dade and Broward counties, Florida law currently prohibits local governments from eliminating this option.

The Commission recommended in 2005 that the legal requirement for an option be repealed so that the FBC can determine what structures should have window and door protection, what structures may be better served by designing to withstand internal pressures, and what structures need both. The result probably would be a requirement in the FBC that all residential buildings have window and door protection and be designed for internal pressurization rather than simply requiring one or the other as an option.

Testimony before the Task Force discussed the rationale for this change. A decade ago, the emphasis in building codes was to strengthen the basic building structure either by protecting openings (such as windows and doors) or by designing the structure to withstand internal pressures even if openings were not protected. The more modern emphasis is to recognize the need of homeowners to shelter in place as well as live in a structure after a disaster and therefore the need to protect the interior of the home by protecting openings as well as having a strong basic structure that can resist strong winds. Current scientific thinking about **residential** buildings is that there no longer should be an option; opening protection **and** strong design to withstand internal pressures are both needed.

Regarding Building Code issues the Task Force recommends:

- Eliminating the designation of the wind-borne debris region for the panhandle of Florida from Chapter 200-141, Laws of Florida, subject to final determination by the Florida Building Commission, and allow the wind-borne debris region for that area of the state to be determined by the Florida Building Commission.
- Supporting the Florida Building Commission adoption of the 2006 International Residential code that will lead to removal of the option to design buildings as partially enclosed.
- Removing the Exposure Category C definition from law, thereby authorizing the Commission to develop and adopt a new definition within the code by administrative rule.

## ***Mobile Home Insurance Market***

One segment of the Florida housing stock that does not seem to be returning to the private markets from Citizens is the mobile home market. After the 2004 season, particularly after hurricane Charley, many insurers in the private market decided to reduce their mobile home exposure, particularly for those built prior to 1994.

In particular, the mobile home stock presents a unique problem for the Florida market. According to the *Third Party Analysis of Manufactured Home Retrofit Tie-Downs* completed in June 2005, the 2000 Census indicated 829,553 mobile homes in Florida. It further indicated that the State of Florida did not implement their updated tie down standards of Florida Administrative Code 15C-1 until 1999, which would have left approximately 847,000 mobile homes with lower anchoring standards and roughly 98 percent of those mobile homes would not meet 1994 wind design standards. The report acknowledged that not all homes counted in the census are still in service. There is no way to determine how many mobile homes became uninhabited as a result of the 2004 and 2005 storm seasons.

According to the *Final Report on Hurricane Loss Reduction for Housing in Florida* (dated July 30, 2003), completed by the International Hurricane Research Center at Florida International University, 85.5% of the mobile homes in Florida were built before 1994. The study also reported that there were 338,000 mobile home units in Florida that were constructed prior to 1976 and 643,000 constructed between 1976 and 1994. This same report indicated that the 2000 Census data reflected more than 267,000 pre-1974 units in Florida, with more than 60% of them located in the most vulnerable coastal counties.

Citizens' Mobile Home policies in force for the PLA account increased from 12,028 in October, 2003 to 62,029 in October, 2005.) Using 2000 census data, it has been estimated that mobile homes make up 12% of Florida's housing units and that 10% of Florida's population lives in mobile homes. As a first step, appropriate state agencies and other institutions should be called into a group to determine a systematic way to identify the size and age of the market.

However, there is no single entity that tracks mobile homes in current service in the state of Florida. Mobile home owners must register annually with the Department of Highway Safety and Motor Vehicles (HSMV) unless the mobile home is claimed as real property with the county property appraiser. The home may be claimed as real property if the homeowner also owns the land on which the mobile home is located. In that case they only have to register once with HSMV when they title the mobile home at purchase. This registration is the methodology used to collect the annual property tax registration (which is passed on to the taxing district) if the homeowner does not pay his/her taxes through the local property appraiser's office.

Once a mobile home is claimed as real property, the only way to determine whether the home still exists or is located on that land is by researching it through the specific county property appraiser's office.

HSMV collects data on mobile home by unit; that is a single-wide is classified as one unit; a double-wide is classified as two units and so on. Their database can only total the number of units which is not the same as the number of unique homes. The following data was provided by HSMV as of 2/2/06:

Statewide	Prior to 1976	1976 thru 1993	1994 or Newer	Totals
Mobile Home Registrations (units)	107,305	216,823	108,888	433,016
Mobile homes claimed as Real Property (units)	140,081	297,708	167,856	605,645
Totals	247,386	514,531	276,744	1,038,661

Further, other than by selling a mobile home, the only way to avoid payment of registration fees and/or property tax on the home is to obtain a Certificate of Destruction (which is needed to legally destroy a mobile home) from HSMV. It is noteworthy that of the 10,221 Certificates of Destruction issued in FY 04-05, 1103 were in Pinellas County, 1022 were in St. Lucie County, 1363 were in Desoto County, and 1636 were in Charlotte County. Historically, less than 600 certificates were issued in any year between FY 00-01 and FY 03-04.

The insurability of mobile homes has become a pressure point in the Florida market beginning in the aftermath of the 2004 hurricane season, particularly after hurricane Charley. A number of insurers historically writing in this market have revised their underwriting guidelines to exclude older mobile homes. Other companies are exiting this market entirely. The Task Force received information and testimony suggesting that effective mitigation measures for pre-1994 mobile homes, carports and other attached structures may not exist. The result is that a dramatically increasing number of these policies are being moved into Citizens' portfolio or are not obtaining insurance at all, as shown below:

Citizens' Mobile Home Policies

	<u>10/03</u>	<u>10/04</u>	<u>10/05</u>
Personal Lines Account	12,028	22,102	62,029
	<u>11/03</u>	<u>10/04</u>	<u>10/05</u>
High Risk Account (Wind-Only)	12,552	12,556	14,056

It should be noted that according to data from the Office, non-Citizens mobile home policies written in the admitted market went from 499,761 in January, 2000 to 481,114 policies in March, 2005, whereas wind-only policies in the non-Citizens admitted market remained relatively stable from 14,139 in January, 2000 to 13,849 in March, 2005.

However, the number of insured mobile homes is significantly less than the estimated number of mobile homes in Florida.

Regarding the mobile home insurance industry, the Task Force recommends:

- Conducting a more rigorous study of the mobile home market. As a first step, appropriate state agencies and other institutions should be called into a group to determine a systematic way to identify the size and age of this market.
- Conducting an analysis based on the evidence from multiple sources, regarding mobile home construction, installation, and age, to determine whether mobile homes with attached additions (carports and other attached structures) are insurable risks and whether or not they should be insured by the admitted market.

### ***The Office's Business Development and Market Research Unit***

In January 2005, the Office created a new Business Development and Market Research Unit (BDMR). The first of its kind among state insurance departments around the country, the BDMR unit is directly responsible for attracting new capital investment and insurers to the Florida market. In addition, BDMR is charged with providing regulators, legislators, consumers, and the industry with current economic analysis of market conditions and developments.

### ***National Activity***

Following the 2004 season, in February 2005, the NAIC Catastrophe Working Group, chaired by Florida, convened a meeting in Orlando to develop a comprehensive national plan for coping with the insurance consequences of natural disasters. Working with the National Conference of Insurance Legislators, who have published their own resolution in support of a national plan, the Working Group is proceeding through the development process and will present a proposal to the NAIC at the Spring 2006 meeting.

Further, in November of 2005 the Florida Commissioner of Insurance, along with the California Insurance Commissioner, the Illinois Director of Insurance, and the New York Superintendent of Insurance, convened a two-day Summit in San Francisco that had been planned well in advance of the 2005 hurricane season. The purpose of the meeting was to gather information regarding the economic consequences of plausible catastrophes, listen to national experts on the subject and develop a comprehensive plan. The NAIC draft plan and the expert testimony of Dr. Robert Litan of the Brookings Institution were presented to the Task Force. In addition, Mr. James Lee Witt of ProtectingAmerica.org provided testimony on the need for a national catastrophe plan. The Task Force also received additional information further documenting the need for a national plan from Dr. Howard Kunreuther of the Wharton School at the University of Pennsylvania. While some of the details of the various plans differ at this point, they share many principles in common, including:

- A national program should promote personal responsibility among policyholders;
- A national program should support reasonable building codes, development plans, and other mitigation tools;

- A national program should maximize the risk-bearing capacity of the private markets, and;
- A national plan should provide quantifiable risk management to the federal government.

The current draft plans envision a three-layered approach:

- The first layer builds upon a base of rational land use and building code, to minimize as much as possible the risk of loss for a catastrophic event, allows insurers to establish reserves against likely future catastrophic losses on a tax-deferred basis and promotes the maximum use of the private insurance and reinsurance markets
- The second layer uses state or regional catastrophe mechanisms, currently envisioned along the lines of the FHCF, to provide an additional layer of reinsurance capacity, at risk-appropriate rates to the private market, and
- The third layer establishes a national reinsurance facility, led by an independent Commission, to provide reinsurance for higher levels of loss, again at risk-appropriate rates to the state funds or possibly directly to insurers.

The current NAIC draft plan, Dr. Litan’s presentation to the Task Force, information from ProtectingAmerica.org and material from Dr. Kunreuther is referenced in Appendix Three.

Finally, in the aftermath of hurricane Katrina, with the growing debate on “wind vs. water” damage and the provision of flood insurance, The U.S. House of Representatives and the U.S. Senate are holding hearings to determine how best to modify the National Flood Insurance Program moving forward.

As the Florida economy recovers and the private insurance industry recapitalizes, the Task Force’s charge is to ensure that over the long-term, adequate capital is available to provide Floridians with the needed hurricane risk insurance. In order to fulfill this charge, the Task Force considered future demands for insurance, estimates of future hurricane activity, the nature and operation of the private insurance and reinsurance markets including the necessity of adequate rates of return on capital invested in the Florida market, and the functions of the public mechanisms.

In addition the Task Force considered information on how to enhance the personal safety of Floridians and to minimize the cost of insured losses in the future, that is, how the risk exposure can be shaped given that hurricanes will continue to be a fact of life in Florida.

### ***Future Demand for Property Insurance in Florida***

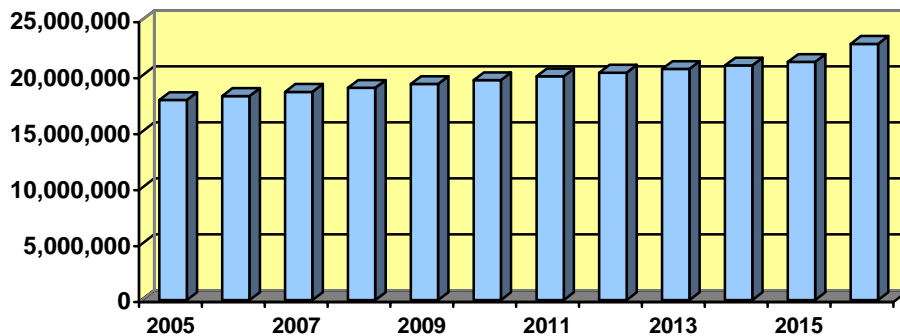
#### **Population Growth and Insurance Demand**

According to US Census data, Florida’s population grew at the rate of 8.8% from 4/1/2000 to 7/1/2004 compared to a nationwide population growth of 4.3% over the same period. The total net migration into Florida during 2004 was 351,701 which equates to an average of 964 people per day after taking into account people leaving the state. US

Census projections indicate that the population of the state of Florida will grow by more than 79% from 15.9 million 2000 to 26.7 million by 2030.

The Task Force was also presented with forward looking population estimates from the Florida Demographic Estimating Conference (FDEC), shown in the chart below, that show the population continuing to grow albeit at a slower rate. Florida's population is expected to grow from 17.87 million in 2005 to 22.89 million in 2020 for an average growth rate of 1.56%.

## Population



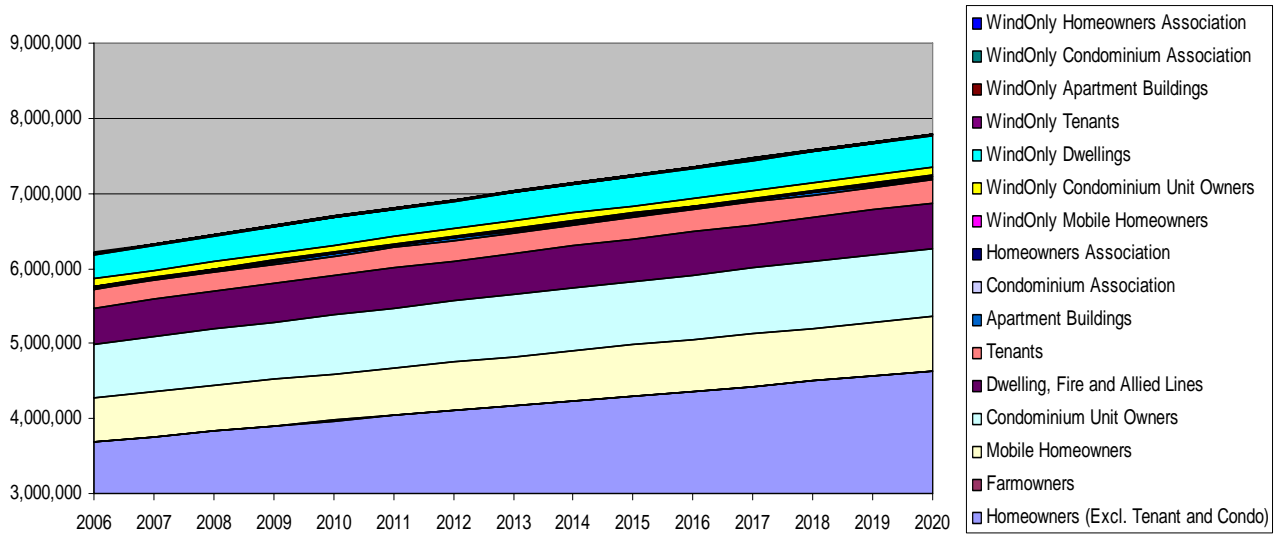
This population growth is not expected to be uniform across all areas. Appendix Four references the county level detail of the historical and forecast growth given by the FDEC. The Appendix references include the data to estimate the population growth rates across two different historical periods as well as from 2005 to 2020. The data suggest that the growth rate (not the absolute numbers) has already begun to slow as evidenced by the difference between the rates estimated from 1970-1990 and 1980-2004. Further, the growth rates are slowing and are estimated to do so until 2020. As well, the tremendous growth rates in population observed in the coastal counties is estimated to slow moving forward (again, the growth rates, not the absolute numbers).

As people continue to migrate to Florida, the long-term health of the property market must include not only today's housing demands, but the demands of the future population as well.

### Estimated Demand for Insurance

The Office provided the Task Force with estimates of the demand for property insurance by lines of business out to 2020 based on the population estimates from the Florida Demographic Estimating Conference. These forecasts assume that the demand for each line of business (homeowners, condominium owners, etc.) is related to the size of the population in the same ratios as currently exist in the Florida market.

**Estimated Policy Growth**



As the chart above shows, the estimated number of homeowner’s insurance policies is expected to rise from an estimated 2006 level of 3.7 million policies to 4.62 million by 2020. Similarly condo unit owner’s policies are expected to rise from an estimated 726,020 policies to about 911,640 policies over the same period. (See discussion on mobile home policies at the Mobile Home Insurance Market section.) Changes in habitational patterns and demographics along with other factors could alter the final outcomes, but are not readily incorporated into the estimates provided. Details are referenced as well in Appendix Four.

### **Estimated Demand for New Capital**

Along with the demand for property insurance to cover the necessary new housing that will be required to support Florida’s population growth is an attendant need for additional capital to support the insurance coverage. Information provided to the Task Force from the Insurance Information Institute estimated the minimal need for additional capital to support Florida’s insurance marketplace at around \$500 million per year.

The Office provided the Task Force with estimates based on the population and demand estimates under a variety of scenarios. These estimates, although more conservative, were not inconsistent with the information supplied by the Insurance Information Institute. It is also important to note that, in either case, the numbers reported are minimums as they do not include any injections of capital necessitated by major hurricane losses such as those observed in 2004 and 2005.

The information from the Insurance Information Institute and the Office are referenced in Appendix Four.



## ***The Private Sector Market for Property Insurance***

The Florida property insurance market continues to grow. Nearly six million (5.92 million) property insurance policies (residential, commercial residential, ex-wind and wind only policies) representing \$6.08 billion in premium and \$1.26 trillion in structural exposure to wind reported at year-end 2004 grew to 5.95 million policies paying \$6.8 billion in premium on a structural exposure to wind of \$1.36 trillion by the third quarter of 2005 according to data reported to the Office. While Citizens is a large and critical part of the Florida market, the private sector has remained the driving force throughout the state.

## ***Competitive Conditions in the Florida Property Insurance Market***

In the 2005 report published by the Office, *The Property Insurance Market in Florida 2004: The Difference a Decade Makes*, information was presented that showed that Florida ranked as one of the most competitive insurance markets in the United States when measured by Top-10 market shares. Further, the report showed that prior to the 2004 hurricane season, insurers in Florida had reported loss ratios of about half of the national average for the preceding five years.

Using data from year-end 2004 from the NAIC for reporting authorized insurers, and a more robust measure of market concentration (the Herfindahl-Hirschman Index (HHI)), a comparative analysis of Florida relative to other states is provided below. For the HHI, smaller values indicate less market concentration, with values under 1,000 commonly associated with competitive markets. Florida ranks #13 when Citizens is not included in the calculation and #25 when Citizens is included; either calculation is consistent with a competitive market.

Rank	State	HH Index	Rank	State	HH Index
# 1	Massachusetts	253.8	# 25	Minnesota	669.5
# 2	Connecticut	289.0	-----	<b>Florida -- with Citizens</b>	<b>675.1</b>
# 3	New Hampshire	330.5	# 26	Arizona	712.3
# 4	Vermont	338.7	# 27	Indiana	716.6
# 5	Maine	356.4	# 28	Utah	722.4
# 6	New Jersey	361.2	# 29	California	727.3
# 7	New York	373.3	# 30	South Carolina	733.1
# 8	Rhode Island	377.0	# 31	Tennessee	736.2
# 9	South Dakota	423.0	# 32	Nevada	741.8
# 10	North Dakota	484.9	# 33	Oregon	768.9
# 11	Ohio	536.3	# 34	Maryland	784.6
# 12	Iowa	542.5	# 35	Hawaii	798.5
<b># 13</b>	<b>Florida</b>	<b>548.8</b>	# 36	Missouri	798.7
# 14	Montana	564.3	# 37	Arkansas	816.4
# 15	Pennsylvania	575.3	# 38	Oklahoma	832.9
# 16	Washington	594.1	# 39	Texas	842.8
# 17	Michigan	615.4	# 40	New Mexico	866.8
# 18	Idaho	622.6	# 41	Colorado	873.9
# 19	Virginia	626.1	# 42	West Virginia	892.2
# 20	Wisconsin	632.3	# 43	Georgia	908.1
# 21	North Carolina	635.6	# 44	Wyoming	918.6
# 22	Kentucky	648.3	# 45	Delaware	937.0
# 23	Nebraska	660.6	# 46	Mississippi	964.9
# 24	Kansas	668.6	# 47	Illinois	967.8
# 25	Minnesota	669.5	# 48	Louisiana	1,054.1
			# 49	Alabama	1,080.3
			# 50	Alaska	1,397.7

Within the state of Florida, it is clear from information provided to the Task Force that there are areas where the noted competitive aspects of the market are not present; especially in the high risk coastal areas where Citizens is the dominant insurer.

### ***Rate Regulation and Competitive Markets***

The Task Force received information on the various rate regulation mechanisms in place across the states. Anchored on one end were “prior approval processes” where filed rates could not be implemented until after approval from the state insurance regulator. This was seen as the most competitively restrictive mechanism.

Other states, including Florida, regulated insurer rates using either or both of a “file and use” or “use and file” mechanism (see Section 627.062, Florida Statutes). In a file and use mechanism the insurer files a rate plan, and after a period of time (90 days in Florida) can implement the rates unless they are found to be inadequate, excessive or unfairly discriminatory. If the insurer chooses a use and file process, the rates are immediately put into effect, the insurer must file the rates within a specific period of time (30 days in Florida) and then the insurance regulator will review the rates to ensure that they are neither inadequate, excessive or unfairly discriminatory. If a determination is made by the Office in Florida that a rate is indeed excessive, the insurer must either rebate or credit policyholders with the amount considered excessive after the insurer has exhausted all statutory avenues to dispute the finding. Some companies prefer to obtain prior approval prior to implementing a rate change.

Within the presentation of file and use or use and file rate regulation mechanisms, the concept of a flex rating was discussed. With a flex rating or rating band, rates changes within a prescribed range are filed using an expedited review process. The ascribed advantages of a flex rating band included the ability of insurers to maintain rate adequacy in a dynamic market.

At the other end of the rate regulation spectrum, the informational filing was mentioned. As an extension of the use and file concept, the informational filing mechanism requires an insurer to file a rate plan within a period of time after its effective date with the regulator. The regulator then may review the rates for adequacy, excessiveness, or unfair discrimination. Depending on the process, the resolution of any disputes varies by jurisdiction.

Data on comparative rates across the country for a standard ISO homeowner’s (HO-3) policy were presented along with premium information on defined structures from different parts of the country obtained from a survey of larger multi-state property insurers. The results did indicate that after adjusting for comparison purposes Florida’s rates were among the highest in the nation, due primarily to the risk of hurricane.

Within this context, Florida’s rate regulation mechanism, an insurer’s choice of either use and file or file and use was shown to be in the middle area of the spectrum of possible rate regulation mechanisms. The Task Force expressed some concern over the maintenance of rates sufficient to continue to attract capital moving forward. The Task

Force agreed that the support of adequate rates was a critical element in a long-term solution to the hurricane insurance market in Florida.

### ***The Importance of Reinsurance in the Florida Property Market***

More than most other states, the Florida property insurance market is heavily dependent on the global reinsurance market. The Office presented the Task Force with an overview of the global reinsurance market, with a particular emphasis on developing issues in the marketplace and the price sensitive nature of the market, that is, the degree to which large sums move in and out of the markets based on small changes in perceived potential returns to capital.

The Office provided some detailed sample information to the Task Force relating to the use of reinsurance by Florida property insurers. For a sample of 65 companies who wrote 80% or more of their business in Florida, a comparison of the direct premium they wrote in 2004 across personal residential insurance lines (fire, allied lines, and homeowners multiple peril) was compared to how much was reinsured. These companies represented \$3.78 billion in aggregate direct premium; they assumed \$405 million in premium from other insurers and reinsurers by taking additional risk, and ceded \$2.14 billion to other insurers and reinsurers reducing their total risk. Thus, the net written premium was \$2.04 billion implying 51% of their direct and assumed premium was ceded to reinsurers.

Current statutory accounting rules require that reinsurance contracts obtained from alien reinsurance companies (e.g., non-U.S. reinsurers) be fully collateralized by funds in trust or letters of credit within the United States. Critics of this statutory accounting requirement argue that it is an artificial barrier to competition that prevents the free and unfettered flow of global reinsurance capacity into the U.S. markets. Currently, the NAIC is examining this now controversial rule through its Reinsurance Task Force of the Financial Condition (E) Committee (a complete discussion of the issue is available through the NAIC publication *U.S. Reinsurance Collateral White Paper, December 6, 2005*).

### ***New Market Entrants***

The Task Force heard from the Office that since October 2004, the Florida market has expanded with sixteen (16) new Florida domestic insurers being issued their Certificate of Authority (COA) to write property business in Florida, four of which will write post-1994 mobile homes. In addition, as of January 2006:

- three (3) Florida domestic companies have received a Permit to write property coverage but not yet applied for a COA;
- four (4) Florida domestic companies have applied for a Permit to write property coverage, one of which will write post-1994 mobile homes;
- nine (9) foreign companies (insurers domiciled in a state other than Florida) have received COAs to expand their operations into the Florida property market, however, the homeowners line of business for most of these foreign insurers is not a significant amount of the projected premium;
- one (1) foreign insurer currently has an application for COA to expand into Florida to write property coverage, including post-1994 mobile homes; and

- three (3) insurers licensed in Florida have expanded their lines of business to include property coverage; all of which will add capacity to the market.
- Since October 2004, approximately \$150 million of new capital has been invested into our state by Florida domestic companies who currently have a COA. It is estimated that another \$61 million of capital may be invested into our state by Florida domestic companies who have begun the licensure process.

### **Other Overall Property Insurance Issues**

The Task Force received information and testimony suggesting that effective mitigation measures for attached structures, such as pool cages, may not exist.

Since maintaining and expanding competitive conditions in the Florida private sector property insurance market is critical to the economic viability of the state, the Task Force recommends:

- Determining whether or not hurricanes and sinkholes represent risks insurable in the private market is a critical determination that needs to be made as consideration is given to public policy concerning the Florida property insurance market.
- Expanding the Office's monitoring and analysis of market conditions.
- In order to reduce the frictional cost of regulation and to encourage capital in the market, the Legislature should authorize the Office of Insurance Regulation to establish a streamlined rate filing process, publish a reasonable competitive rate of return model for investors, and publish trend factors to be used in rate filings.
- A streamlined rate filing process should be implemented that permits insurers to use a manual rate that is actuarially derived for properties valued over \$1 million to permit competition with the surplus lines market.
- Implementing a competitive rating structure for homes with a structural value over \$1,000,000, in conjunction with a recommendation on limiting eligibility for inclusion in Citizens.
- Ensuring, through the Office's leadership position within the NAIC, that any arbitrary, artificial barriers to competition in the reinsurance market are removed without jeopardizing solvency. State leadership should develop closer working relationships with the global reinsurers.
- The Office continuing to working closely with Citizens and the private market to encourage investment in Florida's property insurance market.
- Not amending the Florida Statutes to require insurers to write specific lines of business. Linking whether companies are able to write one line of business to being able to write other lines of business may be detrimental to market expansion and

create an artificial barrier to capital entering the Florida insurance market.

- Amending Section 631.57(1)(a)2, Florida Statutes regarding FIGA to increase the cap for homeowners' dwelling claims to \$500,000.
- Conducting an analysis to determine whether attached or free-standing structures such as pool cages for which risk cannot be reduced, should be insured.

## ***Florida's Public Sector Hurricane Risk Mechanisms***

### ***The Florida Hurricane Catastrophe Fund***

The FHCF fulfilled its purpose in the face of the 2004 hurricane season, as well as the 2005 hurricane season. The stability and availability of capital in the Florida Hurricane Catastrophe Fund has served as the cornerstone for market recovery and as the catalyst for attracting new companies and additional new capital to Florida. However, the combined losses and experience of the 2004-2005 seasons have strained the cash resources of the Fund, as well as the resources of the voluntary market.

The Task Force asked FHCF for and was presented with detailed information on recent performance, future projections and possible modifications to the FHCF. The Task Force construed several key points from this information:

- The FHCF has valued the losses for the 2004 hurricane season at \$3.85 billion. This includes \$3.75 billion in reported losses and incurred but not reported losses of \$99 million.
- The four 2004 hurricanes resulted in approximately \$21 billion in insured losses from 1.67 million claims.
- Due to limitations associated with computer models, wide variation in estimating losses for individual insurers and for various hurricanes were observed during the 2004 hurricane season. The factor of demand surge (e.g., increased cost of building materials and construction labor) and four hurricanes occurring within a 45 day time period with overlapping paths contributed to the model limitations. The FHCF losses from the 2004 hurricane season rose from the initial preliminary insurer loss report estimates by over 80% (\$2.04 billion to \$3.75 billion). However, the FHCF model projections for the entire 2004 season were less than 10% different from the most recently reported insurer loss reports.
- The 2005 hurricane season was a record year in terms of the number of named storms and U.S. insured losses. In Florida, Hurricane Wilma resulted in initial loss estimates for residential property of \$7.9 billion with an expected reported loss to the FHCF of \$2.6 billion.
- If a 10% adverse loss development factor is assumed for 2005 losses, the FHCF's cash available for 2005 claims will be exhausted. Therefore, the entire cash available of \$3.1 billion will need to be reserved for 2005 losses.
- The 2006 industry aggregate retention will be \$5.3 billion.
- As a result, there will not be any cash available to be carried forward for 2006 claims payments when the 2006 hurricane season begins. If a hurricane loss triggers the

FHCF in 2006, revenue bonds will need to be issued to provide reimbursements to insurers.

- Given the expected disbursements for the 2004 and 2005 seasons, it is unlikely that there will be sufficient cash available in 2006 to provide insurers with advances.
- Any expansion of the FHCF will place more of a burden on Florida policyholders to fund the added coverage.
- Any reduction in the FHCF's industry retention of \$4.5 billion will increase the probability of triggering the FHCF and therefore, the need to issue bonds. Since 2003, the FHCF has had its capacity expanded by \$4 billion which was funded by increasing the emergency assessment authority for bonding; losses in 2004 and 2005 have exhausted cash and add an additional bonding burden of \$6 billion. This \$6 billion added to the \$4 billion of additional capacity thus increasing the potential debt burden on Florida policyholders by \$10 billion since 2003.

Recognizing the economic impact of a per-event deductible amount, the FHCF statute was changed in the special session in December of 2004 to address the issue of multiple hurricanes in one year. Insurers basically absorb two full retentions for their two largest hurricane events and for the third largest and all subsequent events, the retention drops down to one-third the prior level. While this does provide some relief against multiple storms, some members of the Task Force wonder if it is enough.

Late during the last legislative session, an alternative triggering rule, referred by the Task Force as the "Beta" proposal emerged but was not enacted. The Beta concept is a hybrid approach that would use a per event retention combined with an aggregate retention. For each event, a minimum per event retention would apply, but an aggregate annual retention would have to be met as well. Once the aggregate retention (e.g., \$3.5 billion for all events) is met, for each subsequent event an insurer would be required to meet the minimum per event retention (e.g., based on \$1 billion industry retention). This approach was designed to provide a flexible framework to Florida policymakers which could address the multiple event issue and separately address the level of risk borne to Florida policyholders. Depending on the choice of aggregate limit and per event retention, the plan could increase, decrease, or have a neutral effect on the risk to Florida policyholders and both the probability of needing to issue bonds and the amount of bonds following a multiple event hurricane season.

If a hybrid approach (aggregate with minimum per occurrence per event) is implemented, policymakers may wish to consider adjusting the retention levels to much higher levels so as to transfer risk back to insurers in exchange for Florida policyholders taking the multiple hurricane per season risk. For example, the 2005 FHCF retention of \$4.5 billion could be doubled to \$9 billion if it is changed to a season aggregate. This could be seen as favorable trade off for Florida policyholders and make the insurer's risk more predictable. An approach that would be even more favorable to policyholders would be to utilize per-event retention of \$2 billion and aggregate season retention on top of that of \$6 billion. This program was not endorsed by the Task Force because the concept has not been fully developed as to its financial impact on either the insurance market or FHCF.

The Task Force also heard testimony about the use of a rapid cash buildup factor within the FHCF's rate structure. A rapid cash buildup could be implemented by establishing a factor as a percentage of FHCF premiums and adding it to the FHCF premium. The FHCF has calculated these costs each year and included them in its Premium Formula Report. For example, if the FHCF premium is \$735 million, a 10% rapid cash buildup factor would be \$73.5 million added to the \$735 million premium making the premium sum to \$808.5 million (\$735 million + \$73.5 million). This is a "rapid cash buildup factor" – not a "risk load." A risk load would include an attempt to price the cost of taking the risk. The public policy question becomes how much of a rapid cash buildup factor is appropriate.

Since the factor charge will eventually be passed through to policyholders, residential policyholders' rates would be impacted. Since the FHCF premium is about 12% of the total residential premium, a 25% rapid cash buildup factor would translate into about a 3% increase in residential premiums on average, but will vary widely by policyholder. For example, if the FHCF's premium for 2006 is \$750 million before the rapid cash buildup factor is applied, the factor would be \$187.5 million (\$750 million x .25). This would build up cash in the amount of \$187.5 million per year plus interest earnings. That means that an additional \$187.5 million plus interest earnings would be added to the cash balance and the bonding needs would drop by the same amount.

The Task Force also heard from several sources on the need to be able to reduce bonding and assessment probabilities by ensuring that the money in the FHCF is available only for the payment of claims and the mandated funding of mitigation programs. It is felt that a constitutional amendment would be needed to accomplish this goal.

Regarding the Florida Hurricane Catastrophe Fund, the Task Force recommends:

- Determining the ability of the FHCF to continue to fulfill its mission or improve the market given its current structure and design as well as to determine if changes to trigger levels and/or exhaustion points are needed. This analysis should include a determination of better ways to address multiple event years that would better fulfill the FHCF's mission.
- Building a rapid cash build-up into the FHCF's rate structure in order to replenish the cash depleted in 2004 and 2005, which may offset the need for post-storm assessments, albeit after an increase in rates initially.
- Amending the Florida Constitution to help protect the capital of the FHCF so that it is used specifically to pay hurricane claims and related expenses including mitigation funding, which is a statutory requirement (Section 215.555(7)(c), Florida Statutes, that requires the legislature to annually appropriate at least \$10 million, not to exceed 35% of the FHCF's investment income, for mitigation projects).
- Exploring other methods for enhancing cash buildup of the FHCF.

- Considering a public policy determination as to whether some of the increased sales tax revenues realized from post-storm recovery should be earmarked for the FHCF, mitigation activities, and public infrastructure.

### ***Citizens Property Insurance Corporation***

The Florida Residential Property Casualty Joint Underwriting Association (FRPCJUA) was established after hurricane Andrew to provide a public/private response to the deterioration of insurance availability in the private market. The Florida Windstorm Underwriting Association (Windpool) offered wind-only coverage to those who could not acquire it in the private market. By year-end 1995, the FRPCJUA had about 850,000 policies in force. By year-end 1999, the Windpool had roughly 500,000 policies in force with a combined exposure of almost \$86.5 billion.

In 2002, these two entities were merged to create Citizen's. Designed to offer insurance only where the private market will not provide coverage, Citizens is mandated to be the provider of last resort with a rate structure that is uncompetitive with the private market. By December 31, 2004, Citizen's ([www.citizens.fl.com](http://www.citizens.fl.com)) reported 849,243 policies in force (including high risk, personal-residential, and commercial-residential accounts), with a \$196.6 billion structural exposure to wind. By the end of the third quarter 2005, Citizens' total policy count had fallen to 796,970 with a structural exposure to wind of \$192.3 billion based on data reported to the Office.

The Task Force asked for and received detailed information regarding Citizens' financial position following the 2004 and 2005 seasons along with ideas for alternative means for funding deficits beyond assessments, the effectiveness of its depopulation efforts, changes to its operational plans following the 2004 season, and particularly its rating structure. The detailed information provided by Citizens is referenced in Appendix Seven.

As part of the discussion, Citizens was asked about the number of "builder's risk" policies they underwrite for new construction projects. Citizens has over 5,700 such policies (mostly representing single dwelling rather than commercial residential structures) with a combined exposure of \$4.29 billion. The Task Force questioned whether Citizen's should be offering builder's risk policies or if that was creating new demands for Citizens as the construction was placed into the permanent housing market.

After reviewing and discussing the information provided, the Task force found:

- There is growing evidence that the growth in Citizens is the result of the unique features of the Florida market that may be viewed as representing risks uninsurable in the voluntary market; notably the risk of hurricanes (especially for older housing stock and older mobile homes in particular) and sinkholes.
- Whether or not hurricanes and sinkholes represent risks insurable in the private market is a critical determination that needs to be made as Florida moves forward.
- As a result of Hurricane Andrew the Florida Residential Property and Casualty Joint Underwriting Authority (FRPCJUA) was created to address the uninsurable market, but prior to that storm there were uninsurable risks in Florida. A determination will



have to be made on whether there is a public policy obligation to insure all structures in the state.

- Policies in force in Citizens for the Tampa Bay area (Hernando, Hillsborough, Pasco and Pinellas counties) increased 13751% from 1012 policies on 12/31/2001 to 140,171 policies on 12/31/2004. This is compared to growth in Dade, Broward, and Palm Beach counties of 104% for the same time period. These growth patterns are believed to be the result of sinkhole claims. Citizens' sinkhole claims have increased loss costs on multi-peril policies and inadvertently increased the wind exposure for Citizens. Legislative modifications provided in SB 1486 are not sufficient to return capital markets to the west coast of Florida because of the sinkhole issue.

Regarding sinkholes, the Task Force found:

1. Citizens provided output showing that 29%-34% of the wind exposure in the PLA's PML comes from the PLA sinkhole counties- Citrus, Hernando, Hillsborough, Pasco and Pinellas. This is an indirect measure of the problem as it includes all wind (i.e., tornados) but it gives a sense of the potential wind-related exposure to Citizens stemming from the sinkhole exposure.
  2. The Sinkhole Study commissioned by the Office in April 2005 indicates that Florida has three basic options related to coverage for the peril of sinkhole: (1) keep the coverage for sinkhole losses within the homeowners' policy but allow insurers to rate for it; (2) establish a facility to which insurers would cede all sinkhole coverage; or (3) establish a facility to operate as a direct insurer for sinkhole losses.
  3. Regardless of the method by which the coverage will be provided, the state of Florida should consider: (1) changes to the definition of sinkhole loss and activity to address geologists' concerns about ambiguity; (2) working to create uniform procedures for adjustment of claims utilizing experts; and (3) establishing a data warehouse to store sinkhole claims information.
  4. Many insurers have reported a refusal to write in the sinkhole prone areas due to the vague definition of sinkhole and sinkhole activity. They have expressed a need to drive some of the frictional costs out of the system that occur as a result of cracking and settling and the ensuing litigation which makes this a tort issue that is significantly impacting capacity in the private market.
- Citizens' PLA mobile home policies have increased from 12,028 in October, 2003 to 62,029 in October 2005, an increase of 416 percent in just two years.
  - If unabated, the growth trends of Citizens could jeopardize the economic viability of the state of Florida and impact all Floridians with respect to the affordability and availability of insurance.
  - The recent depopulation trend bodes well for the return of private markets, but leaves the uninsurable markets and wind exposure in Citizens.
  - According to Citizens, the take-out program has had substantial impact in keeping PLA policies from growing more than they have and in stabilizing the number of

HRA policies. The number of PLA policies, for instance, would have been at least 30% higher if the take-out program had not existed and the number of HRA policies would have grown by more than 20%. Citizens' depopulation activities for 2003 – 2005 are summarized below:

Total Number of Policies Removed: 483,905  
 Total Exposure Reduction: \$92.5 Billion

Reduction in PLA Exposure as a Result of Depopulation

<u>Year</u>	<u>Number of Policies</u>	<u>Coverages A-D</u>
2005	218,108	\$40,174,893,046
2004	145,959	\$29,161,307,321
2003	28,219	\$8,140,681,906
Total 2003-2005	392,286	\$77,476,882,273

Reduction in HRA Exposure as a Result of Depopulation

<u>Year</u>	<u>Number of Policies</u>	<u>Coverages A-D</u>
2005	78,570	\$13,483,947,013
2004	13,049	\$1,501,769,159
2003	0	0
Total 2003-2005	91,619	\$14,985,716,172

- Since its creation in 2002 there have been times and areas where Citizens has not in fact operated as the insurer of last resort. Citizens now has the ability to provide an actuarially sound rate filing (the first one was filed in December 2005) in addition to the “Top 20” rates.
- Evidence was presented indicating that consumer choice has prevented a number of policyholders from being removed from Citizens. However, evidence was also presented to the Task Force documenting depopulation activities. Notwithstanding the effect on depopulation, several arguments were advanced that the value of consumer choice outweighed the capacity utilized in Citizens by these policies.
- Citizens has made significant progress in resolving customer service issues and addressing claims as demonstrated by complaints to the Department of Financial Services, Division of Consumer Assistance. During the 2004 hurricane season, Citizens received 120,000 claims and DFS received 6,000 requests for assistance. During the 2005 hurricane season, Citizens received 155,000 claims and DFS received just over 300 requests for assistance.
- Following the 2004 hurricane season, Citizens made a number of changes to its infrastructure including significantly expanding the Catastrophe Claims Department. During the 2005 storm season, Citizens directly managed both company employees and adjusting firms in the processing and payment of claims. Under this new system, Citizens' Catastrophe Team was able to provide more efficient claims handling and better overall customer service. Citizens is establishing a regional claims processing office in Miami-Dade County. Citizens has thus far hired two General Adjusters who are adjusting claims in the field. It has added enhanced technology and has increased

customer service staff levels for its consumer hotline. It has made a transition to a traditional insurance adjusting model, developed an administrative plan, acquired key catastrophe resources (such as a new hurricane model), improved vendor solicitation and management and installed a claims tracking system.

- Citizens' Board of Governors approved the purchase of reinsurance at their June 29, 2005 meeting. For the PLA, Citizens purchased \$175 million in season-long coverage, which is available after \$225 million in losses. Citizens also purchased reinsurance for the HRA. Under the approved plan, Citizens will obtain \$282 million in season-long coverage after \$775 million in losses, which supplements current FHCF coverage.
- Citizens is required by statute to offer policy coverage that is comparable to that offered by the voluntary market. The statute does not prevent Citizens from making available other policies with more restrictive coverage to allow insurance consumers placed into Citizens more choices.

Regarding Citizens Property Insurance Corporation, the Task Force recommends:

- Amending Citizens' enabling statute to provide that eligibility for coverage with Citizens is limited to those properties with a structural value of less than \$1 million (increased annually for CPI) for Coverage A for HO-3 and Coverages A+C for HO-6 including provisions that permit flexibility by Citizens' to address contractions in the property market and permit Citizens to use a manual rate that is actuarially derived for properties valued over \$1 million.
- Continuing to levy a seasonal occupancy surcharge of 5% for the HRA and 10% for PLA policies (for personal residential policies), until such time as Citizens is able to gather sufficient data to actuarially determine the surcharge amounts.
- Citizens continuing to limit coverage offered on mobile homes built prior to 1994 to Actual Cash Value.
- Citizens determining the feasibility of making available other policies with more restrictive coverage to allow more choices for insurance consumers placed into Citizens.
- Clarifying the statutory language governing Citizens' ratemaking process to clearly delineate that Citizens use the higher of the "Top 20" requirement and the "actuarially sound" requirement.
- Amending Section 627.351, F.S., to codify in law the ethics and conflict of interest provisions that were added to the Citizens' Plan of Operations and approved by the Office of Insurance Regulation.
- Requiring that the rates charged by Citizens include a capital accumulation component so that Citizens will develop a capital base similar to that required of insurers in the voluntary market. This will, over time, reduce the need for and

frequency of assessments.

- Implementing a pilot project to reduce the risk of loss for Citizens' policyholders with second homes or with structures valued over \$500,000 in the wind borne debris area to make them more marketable in the voluntary market by limiting to a period of three years the amount of time an insured property may remain in Citizens without an additional surcharge if the property could be insured in the private market with additional investment in retrofitting those structures using mitigation hardening techniques. This pilot project should be coordinated with the Department of Community Affairs mitigation programs to access available grant and low-cost loan funding sources as appropriate.

The Task Force agreed that the takeout bonus program is a cost-effective means of reducing the potential liability of Citizens and recommended:

- Requiring Citizens to report twice a year on the effectiveness of the recently implemented revision to its take-out program. The report should document the number of policies taken out of Citizens' portfolio, the net reduction in exposure resulting from the take-out, the expected net cost to Citizens of the policies taken out, and the expected net reduction in reinsurance or other risk transfer resulting from the policies taken out.
- Citizens continuing to aggressively market its bonus program to encourage depopulation activities in conjunction with the Office.
- Obtaining statutory clarification to provide clarity in the law that Citizens is authorized to offer a myriad of bonuses approved by the Citizens' Board and the Office.
- Citizens developing and implementing a keep-out program designed to help market risks to the private insurance market before being bound in Citizens.
- Enacting a statutory provision such that the agent and agency shall have no E & O (errors and omissions) exposure for "take-out" and "keep-out" policies so long as the risk is placed with an admitted insurer that is covered by the Florida Insurance Guarantee Association (FIGA).
- Earmarking the increased sales tax revenues realized from post-storm recovery for Citizens to decrease the likelihood of an assessment.
- The Office establishing an ongoing reporting structure highlighting claims-handling performance using metrics similar to those used in the Office's disaster reporting framework, e.g., number of claims filed in a period, number of days to adjust, and settle a claim, using recent audits such as the Auditor General's report, Citizens' internal audit, and the processes of the Office's Market Investigations Unit to establish the framework for reports.

- Using the information contained Auditor General’s report, as well as the Citizens’ Board recommendations, to maintain a feasible plan of operation that can be objectively monitored and results measured, including provisions that would ensure competent customer service.
- Establishing a meaningful set of uniform performance metrics to be reported by Citizens to the Office. These metrics would be the same as those available to the Office for measuring similar performance in the voluntary market.
- Establishing other performance methods that would permit consumers to compare companies as is done in the private market.

### ***Consumer Choice***

The Task Force was unable to reach consensus on whether or not to repeal Consumer Choice. Evidence was presented indicating that consumer choice has prevented a meaningful number of policyholders from being removed from Citizens. However, evidence was also presented to the Task Force documenting depopulation activities. Notwithstanding the effect on depopulation, several arguments were advanced that the value of consumer choice outweighed the capacity utilized in Citizens by these policies including: possible disruption of the long-time relationship between the consumer and agent, and the potential liability to the agent of sending a policy to an assuming “take-out company.” One of the middle ground areas discussed included a requirement for the agent to disclose to the consumer the specific premium differential between the offer from the take out company and continuing with Citizens’ coverage, but consensus was not reached on that issue.

Regarding Consumer Choice, the Task Force recommends:

- Citizens developing and implementing a keep-out program designed to help market risks to the private insurance market before being bound in Citizens.
- Enacting a statutory provision such that the agent and agency shall have no E & O (errors and omissions) exposure for “take-out” and “keep-out” policies so long as the risk is placed with an admitted insurer that is covered by the Florida Insurance Guarantee Association (FIGA).

## **Specifically Mandated Tasks (From SB 1486, Section 24)**

(5) **SPECIFIC TASKS.**--The task force shall conduct such research and hearings as it deems necessary to achieve the purposes specified in subsection (4) and shall develop information on relevant issues, including, but not limited to, the following issues:

**(a) Whether this state currently has sufficient hurricane insurance capacity to ensure the continuation of a healthy, competitive marketplace, taking into consideration both private-sector resources and public-sector resources.**

- The hurricane losses of 2004-2005 have strained the resources of both the voluntary market and the public sector mechanisms of Citizens Property Insurance and the Florida Hurricane Catastrophe Fund.
- Following the 2004 season, the voluntary market recapitalized in large part, but a number of firms re-evaluated their hurricane exposure, reducing market share in some cases. The same is true following the 2005 season, though new firms are entering the market. However, the re-trenchment by the large insurers has not been offset by the new companies. Since the 2004 hurricane season, Florida insurers have infused approximately \$1 billion of new capital into the market. However, given the 2005 hurricane season and projections for future hurricane activity in Florida, it is recognized that without sufficient rate increases and other changes that provide greater pricing certainty in the property insurance marketplace (e.g., mitigation), it is likely that the Florida marketplace will suffer severe limitations on investor resources for continued recapitalization will have future limitations.
- Attracting new capital to the Florida market will remain a critical priority for the foreseeable future, based on projections of current and future needs.

**(b) Identifying the future demands on this state's hurricane insurance capacity, taking into account population growth, coastal growth, and anticipated future hurricane activity.**

- According to U.S. Census data, Florida's population grew at the rate of 8.8% from 4/1/2000 to 7/1/2004 compared to a nationwide growth rate of 4.3%. The total net migration into Florida during 2004 was 351,701 which equates to an average of 964 people per day after taking into account people leaving the state. US Census projections indicate that the population of the state of Florida will grow by more than 79% from 15.9 million 2000 to 26.7 million by 2030.
- To satisfy this new demand, separate estimates suggest that approximately \$500 million in new capital will be needed each year (assuming no mega-catastrophe or repeat of the 04/05 hurricane season) to support the expanding demand for property insurance.

**(c) Whether the Florida Hurricane Catastrophe Fund fulfilled its purpose of creating additional insurance capacity sufficient to ameliorate the current dangers to the state's economy and to the public health, safety, and welfare in its response to the 2004 hurricane season.**

The FHCF fulfilled its purpose in the face of the 2004 hurricane season, as well as the 2005 hurricane season. The stability and availability of capital in the Florida Hurricane Catastrophe Fund has served as the cornerstone for market recovery and as the catalyst for attracting new companies and additional new capital to Florida. However, the combined losses and experience of the 2004-2005 seasons have strained the cash resources of the Fund, as well as the resources of the voluntary market.

The FHCF has valued the losses for the 2004 hurricane season at \$3.85 billion. This includes \$3.751 billion in reported losses and incurred but not reported losses of \$99 million. The four 2004 hurricanes resulted in approximately \$21 billion in insured losses from 1.67 million claims. Gross inaccuracies in computer models, coupled with demand surge evidently caused a substantial amount of adverse loss development. The FHCF losses rose from the initial preliminary reports by over 80% (\$2.043 billion to \$3.75 billion). The 2005 hurricane season was a record year in terms of the number of named storms and U.S. insured losses. In Florida, Hurricane Wilma resulted in initial loss estimates for residential property of \$7.9 billion with an expected reported loss to the FHCF of \$2.6 billion. With 10% adverse loss development, the FHCF's cash available for 2005 claims will be exhausted. Therefore, the entire cash available of \$3.1 billion will need to be reserved for 2005 losses. As a result, there will not be any cash available to be carried forward for 2006 claims payments when the 2006 hurricane season begins. If a hurricane loss triggers the FHCF in 2006, revenue bonds will need to be issued to provide reimbursements to insurers. Given the expected disbursements for the 2004 and 2005 seasons, it is unlikely that there will be sufficient cash available in 2006 to provide insurers with advances. Any expansion of the FHCF will place more of a burden on Florida policyholders (all property and casualty policyholders excluding workers compensation and medical malpractice) to fund the added coverage. Any reduction in the FHCF's industry retention of \$4.5 billion will increase the probability of triggering the FHCF and therefore, the need to issue bonds. Since 2003, the FHCF has had its capacity expanded by \$4 billion which was funded by increasing the emergency assessment authority for bonding, losses in 2004 and 2005 have exhausted cash and add an additional bonding burden of \$6 billion. This \$6 billion added to the \$4 billion of additional capacity thus increasing the potential debt burden on Florida policyholders by \$10 billion since 2003.

The FHCF statute was changed in the special session in December of 2004 to address the issue of multiple hurricanes in one year. Insurers basically absorb two full retentions for their two largest hurricane events and for the third largest and all subsequent events, the retention drops down to one third the prior level.

The Task Force recommends:

- Determining the ability of the FHCF to continue to fulfill its mission or improve the market given its current structure and design as well as to determine if changes to trigger levels and/or exhaustion points are needed. This analysis should include a determination of better ways to address multiple event years that

would better fulfill the FHCF's mission.

- Considering a public policy determination as to whether some of the increased sales tax revenues realized from post-storm recovery should be earmarked for the FHCF, mitigation activities, and public infrastructure.

**(d) The extent to which the growth in Citizens Property Insurance Corporation is attributable to insufficient insurance capacity.**

- There is growing evidence that the growth in Citizens is the result of the unique features of the Florida market that may be viewed as representing risks uninsurable in the voluntary market; notably the risk of hurricanes (especially for older housing stock and older mobile homes in particular) and sinkholes.
- Whether or not hurricanes and sinkholes represent risks insurable in the private market is a critical determination that needs to be made as Florida moves forward.
- Policies in force in Citizens for the Tampa Bay area (Hernando, Hillsborough, Pasco and Pinellas counties) increased 13751% from 1012 policies on 12/31/2001 to 140,171 policies on 12/31/2004. These growth patterns are believed to be the result of sinkhole claims. Citizens' sinkhole claims have increased loss costs on multi-peril policies and inadvertently increased the wind exposure for Citizens.
- Citizens' PLA mobile home policies have increased from 12,028 in October, 2003 to 62,029 in October 2005, an increase of 416 percent in just two years.

**(e) The extent to which the growth trends of Citizens Property Insurance Corporation create long-term problems for property owners, buyers, and sellers in this state and for other persons and businesses that depend on a viable market.**

- If unabated, the growth trends of Citizens Property Insurance Corporation could jeopardize the economic viability of the state of Florida and impact all Floridians with respect to the affordability and availability of insurance.
- The increased sales tax revenues realized from post storm recovery should be earmarked for Citizens to decrease the likelihood of an assessment.
- The recent depopulation trend bodes well for the return of private markets, but leaves the uninsurable markets and wind exposure in Citizens. According to Citizens, the take-out program has had substantial impact in keeping PLA policies from growing more than they have and in stabilizing the number of HRA policies.

**(f) The operation and role of Citizens Property Insurance Corporation, including:**

1. *How to ensure that the corporation operates as an insurer of last resort which does not compete with insurers in the voluntary market, but which charges rates that are not excessive, inadequate, or unfairly discriminatory;*



Recognizing that since its inception in 2002 there have been times and areas where Citizen's has not in fact operated as the insurer of last resort, the Task Force recommends:

- Continuing to levy a seasonal occupancy surcharge of 5% for the HRA and 10% for PLA policies (for personal residential policies), until such time as Citizens is able to gather sufficient data to actuarially determine the surcharge amounts.
  - Clarifying the statutory language governing Citizens' ratemaking process to clearly delineate that Citizens use the higher of the "Top 20" requirement and the "actuarially sound" requirement.
  - Implementing a pilot project to reduce the risk of loss for Citizens' policyholders with second homes or with structures valued over \$500,000 in the wind borne debris area to make them more marketable in the voluntary market by limiting to a period of three years the amount of time an insured property may remain in Citizens without an additional surcharge if the property could be insured in the private market with additional investment in retrofitting those structures using mitigation hardening techniques. This pilot project should be coordinated with the Department of Community Affairs mitigation programs to access available grant and low-cost loan funding sources as appropriate.
2. *Whether the bonuses paid by the corporation to carriers taking policies out of the corporation provide a cost-effective means of reducing the potential liability of the corporation;*

The Task Force agreed that the takeout bonus program is a cost-effective means of reducing the potential liability of Citizens. Citizens' Board approved a new bonus program at its board meeting in December, 2005. Citizens is required by law to design incentive programs and make every best effort to encourage licensed insurance companies to assume policies. In all incentive programs, takeout companies must remove a percentage of selected policies from Miami-Dade, Broward or Palm Beach Counties and retain policies for a minimum of three years to qualify for a bonus.

The Task Force recommends:

- Citizens continuing to aggressively market its bonus program to encourage depopulation activities in conjunction with the Office.
- Obtaining statutory clarification to provide clarity in the law that Citizens is authorized to offer a myriad of bonuses approved by the Citizens' Board and the Office.

3. *Whether the "Consumer Choice" law should be repealed or amended to ensure that the corporation serves as the insurer of last resort;*

The Task Force was unable to reach consensus on whether or not to repeal Consumer Choice. Evidence was presented indicating that consumer choice has prevented a meaningful number of policyholders from being removed from Citizens. However, evidence was also presented to the Task Force documenting depopulation activities. Notwithstanding the effect on depopulation, several arguments were advanced that the value of consumer choice outweighed the capacity utilized in Citizens by these policies including: possible disruption of the long time relationship between the consumer and agent, and the potential liability to the agent of sending a policy to an assuming "take-out company." One of the middle ground areas discussed included a requirement for the agent to disclose to the consumer the specific premium differential between the offer from the take out company and continuing with Citizens' coverage, but consensus was not reached on that issue.

The Task Force recommends:

- Requiring Citizens to report twice a year on the effectiveness of the recently implemented revision to its take-out program. The report should document the number of policies taken out of Citizens' portfolio, the net reduction in exposure resulting from the take-out, the expected net cost to Citizens of the policies taken out, and the expected net reduction in reinsurance or other risk transfer resulting from the policies taken out.
- Citizens developing and implementing a keep-out program designed to help market risks to the private insurance market before being bound in Citizens.
- Enacting a statutory provision such that the agent and agency shall have no E & O (errors and omissions) exposure for "take-out" and "keep-out" policies so long as the risk is placed with an admitted insurer that is covered by the Florida Insurance Guarantee Association (FIGA).

4. *Whether coverage amounts should be limited;*

- Citizens is required by statute to offer policy coverage that is comparable to that offered by the voluntary market. The statute does not prevent Citizens from making available other policies with more restrictive coverage to allow insurance consumers placed into Citizens more choices.

The Task Force determined that the following issues were of such significance, that they should be addressed in terms of the Florida insurance market as a whole, in addition to Citizens, and recommend:

- Citizens continuing to limit coverage offered on mobile homes built prior to 1994 to Actual Cash Value.
- Citizens determining the feasibility of making available other policies with more restrictive coverage to allow more choices for insurance consumers placed into Citizens.
- Conducting a more rigorous study of the mobile home market. As a first step, appropriate state agencies and other institutions should be called into a group to determine a systematic way to identify the size and age of the market.
- Conducting an analysis based on the evidence from multiple sources, regarding mobile home construction, installation, and age, to determine whether mobile homes with attached additions (carports and other attached structures) are insurable risks and whether or not they should be insured by the admitted market.
- Conducting an analysis to determine whether other attached or free-standing structures such as pool cages for which risk cannot be reduced, should be insured.
- Amending Citizens' enabling statute to provide that eligibility for coverage with Citizens is limited to those properties with a structural value of less than \$1 million (increased annually for CPI) for Coverage A for HO-3 and Coverages A+C for HO-6 including provisions that permit flexibility by Citizens' to address contractions in the property market and permit Citizens to use a manual rate that is actuarially derived for properties valued over \$1 million.

5. *Whether the corporation has hired an adequate level of permanent claims and adjusting staff in addition to outsourcing its claims-adjusting functions to independent adjusting firms;*

- Citizens has made significant progress in resolving customer service issues and addressing claims as demonstrated by complaints to the Department of Financial Services, Division of Consumer Assistance:

During the 2004 hurricane season, Citizens received 120,000 claims and DFS received 6,000 requests for assistance. During the 2005 hurricane season, Citizens received 155,000 claims and DFS received just over 300 requests for assistance.

The Task Force recommends:

- The Office establishing an ongoing reporting structure highlighting claims-handling performance using metrics similar to those used in the Office's disaster reporting framework, e.g., number of claims filed in a period, number of days to adjust, and settle a claim, using recent audits such as the Auditor General's report, Citizens' internal audit, and the processes of the Office's Market Investigations Unit to

establish the framework for reports.

- Amending Section 627.351, F.S., to codify in law the ethics and conflict of interest provisions that were added to the Citizens' Plan of Operations and approved by the Office of Insurance Regulation.

6. *The effect of reducing or expanding the areas that are eligible for coverage in the high-risk, wind-only account;*

The Task Force Members could not determine what the Windpool area should be. The Task Force recommends:

- Designing a systematic methodology for establishing Windpool areas.
- Suspending 2004 statutory changes to the arbitrary Windpool line and not permitting the line to be moved by operation of law.

There is industry opposition to shrinking the Windpool. Some parts of the industry advocate expansion of the Windpool to statewide. However, removing all other perils from the residual market, it may become very difficult for Citizens to purchase reinsurance and to pay claims.

7. *Whether the corporation should purchase reinsurance or take other actions that reduce the potential for debt financing and deficit assessments;*

Section 627.351(6)(c)(9), F.S., requires that Citizens, "shall make its best efforts to procure catastrophe reinsurance at reasonable rates, to cover its projected 100-year probable maximum loss as determined by the board of governors." Citizens' Board of Governors approved the purchase of reinsurance at their June 29, 2005 meeting.

For the PLA, Citizens purchased \$175 million in season-long coverage, which is available after \$225 million in losses. The coverage is designed to supplement current coverage provided by the FHCF. The plan reduces the possibility of assessing by 21 percent if losses are due to one major storm or 41 percent if losses are due to multiple storms. Citizens also purchased reinsurance for the HRA. Under the approved plan, Citizens will obtain \$282 million in season-long coverage after \$775 million in losses, which supplements current FHCF coverage.

The Task Force recommends:

- Requiring that the rates charged by Citizens include a capital accumulation component so that Citizens will develop a capital base similar to that required of insurers in the voluntary market. This will, over time, reduce the need for and frequency of assessments.

- Earmarking the increased sales tax revenues realized from post-storm recovery for Citizens to decrease the likelihood of an assessment.

8. *An evaluation of the infrastructure and administration of the corporation and how to improve customer service, claims handling, and communication and the exchange of information with agents of policyholders of the corporation.*

Following the 2004 hurricane season, Citizens made a number of changes to its infrastructure including significantly expanding the Catastrophe Claims Department. As a result of these changes, during the 2005 storm season, Citizens directly managed both company employees and adjusting firms in the processing and payment of claims. Under this new system, Citizens' Catastrophe Team was able to provide more efficient claims handling and better overall customer service. Citizens is establishing a regional claims processing office in Miami-Dade County. Citizens has thus far hired two General Adjusters who are adjusting claims in the field.

Citizens is establishing a regional claims office in Miami-Dade County where it has a large concentration of policies and risks. It has added enhanced technology and has increased customer service staff levels for its consumer hotline. It has made a transition to a traditional insurance adjusting model, developed an administrative plan, acquired key catastrophe resources (such as a new hurricane model), improved vendor solicitation and management and installed a claims tracking system.

The Task Force recommends:

- Using the information contained Auditor General's report, as well as the Citizens' Board recommendations, to maintain a feasible plan of operation that can be objectively monitored and results measured, including provisions that would ensure competent customer service.
- Establishing a meaningful set of uniform performance metrics to be reported by Citizens to the Office. These metrics would be the same as those available to the Office for measuring similar performance in the voluntary market.
- Establishing other performance methods that would permit consumers to compare companies as is done in the private market.

(7) **ADDITIONAL ACTIVITIES.**--The task force shall monitor the implementation of hurricane insurance-related legislation enacted during the 2005 Regular Session and shall make such additional recommendations as it deems appropriate for further legislative action during the 2004-2006 legislative biennium.

Regarding Building Codes, the Task Force recommends:

- Eliminating the designation of the wind-borne debris region for the panhandle of Florida from Chapter 200-141, Laws of Florida, subject to final determination by the Florida Building Commission, and allow the wind-borne debris region for that area of

the state to be determined by the Florida Building Commission.

- Supporting the Florida Building Commission adoption of the 2006 International Residential code that will lead to removal of the option to design buildings as partially enclosed.
- Removing the Exposure Category C definition from law, thereby authorizing the Commission to develop and adopt a new definition within the code by administrative rule.

Regarding Mitigation, the Task Force recommends:

- Establishing Mitigation Public Awareness/Education as a major public priority which continues enhanced promotional campaigns to educate Floridians about the effectiveness of retrofitting and incentive opportunities to stimulate demand for safe homes.
- Considering creation of a Mitigation Consumer Advocate to report annually to the Executive and Legislative branches on the state of mitigation funding and program performance.
- Encouraging local government to provide property tax credits or rebates if homeowners perform mitigation.
- Continuing and expand emphasis on the importance of professional education and training of contractors, the construction workforce and design professionals on mitigation issues, retrofitting, and technologies.
- Establishing Mitigation Consumer Assistance Programs including (1) free consumer mitigation retrofit inspections by trained and qualified inspectors, (2) provision of retrofit grants for low-income families and (3) provision of low- or no-interest loan programs for established, effective mitigation techniques (openings and roofs) should be made available, at least initially in the most high-risk areas of the state. A pilot program to establish individual residential building sturdiness index scoring should be developed using the data from the free inspections.
- Enhancing the Building Code Effectiveness Grading System (BCEGS) to provide greater incentives with appropriate discounts and surcharges.
- Implementing a pilot project to require that licensed Florida certified contractors or other Florida licensed inspectors provide written documentation in the form of a checklist so that real estate transactions include disclosure by the seller on the existence or absence of mitigation features in a property at the time of sale. Developing a uniform Hurricane Resistance Grading Schedule that would assign a grade to structures (houses or condominiums) based on the existence of windstorm loss mitigation features/construction techniques. This schedule, including reasonable discounts, could probably be either determined by or in conjunction with the

Department of Community Affairs (DCA) or the Florida Building Code Commission. The DCA should probably also be responsible for determining the appropriate credentials necessary for licensed inspectors to perform the inspections used to determine grades.

Regarding the private insurance market, the task force recommends:

- Expanding the Office's monitoring and analysis of market conditions.
- In order to reduce the frictional cost of regulation and to encourage capital in the market, the Legislature should authorize the Office of Insurance Regulation to establish a streamlined rate filing process, publish a reasonable competitive rate of return model for investors, and publish trend factors to be used in rate filings.
- A streamlined rate filing process should be implemented that permits insurers to use a manual rate that is actuarially derived for properties valued over \$1 million to permit competition with the surplus lines market.
- Ensuring, through the Office's leadership position within the NAIC, that any arbitrary, artificial barriers to competition in the reinsurance market are removed without jeopardizing solvency. State leadership should develop closer working relationships with the global reinsurers.
- The Office continuing to working closely with Citizens and the private market to encourage investment in Florida's property insurance market.
- Not amending the Florida Statutes to require insurers to write specific lines of business. Linking whether companies are able to write one line of business to being able to write other lines of business may be detrimental to market expansion and create an artificial barrier to capital entering the Florida insurance market.
- Amending Section 631.57(1)(a)2, Florida Statutes regarding FIGA to increase the cap for homeowners' dwelling claims to \$500,000.
- Determining whether or not hurricanes and sinkholes represent risks insurable in the private market is a critical determination that needs to be made as consideration is given to public policy concerning the Florida property insurance market.

## Appendices

All of the following material can be viewed on the Task Force website at  
[www.fldfs.com/HurricaneInsuranceTaskForce/](http://www.fldfs.com/HurricaneInsuranceTaskForce/)

### **Appendix One: The Creation, Charge and Responsibilities of the Task Force, Meeting Agendas and Minutes**

Excerpt from Senate Bill 1486  
Agenda for August 24, 2005  
Minutes from August 24, 2005  
Agenda for September 28, 2005  
Minutes from September 28, 2005  
Agenda for November 14, 2005  
Minutes from November 14, 2005  
Agenda for November 30, 2005  
Minutes from November 30, 2005  
Agenda for December 14, 2005  
Minutes from December 14, 2005  
Agenda for January 18 and 29, 2006  
Minutes from January 18 and 29, 2006  
Agenda for January 30 and 31, 2006  
Minutes from January 30 and 31, 2006  
Agenda for February 27 and 28, 2006  
Agenda for March 6, 2006

### **Appendix Two: Mitigation and Building Codes**

Mitigation and Building Code Issues and Emergency Management – Thaddeus L. Cohen, Secretary, Florida Department of Community Affairs  
Wind Resistant Homes, Old and New and the State of the Florida Housing Market - Dr. Robert C. Stroh, Director of the Shimberg Center for Affordable Housing  
Introduction to Disaster Resistant Construction - Bill York, President, W.H. York Consulting  
The Cost Effectiveness of Disaster Mitigation – Brent Woodworth, Chair of the National Institute of Building Sciences Multihazard Mitigation Council;  
Report is posted at:  
[http://www.nibs.org/MMC/MitigationSavingsReport/natural\\_hazard\\_mitigation\\_saves.htm](http://www.nibs.org/MMC/MitigationSavingsReport/natural_hazard_mitigation_saves.htm)  
Garrett Walton, Co-Exec. Dir., Rebuild NW Florida; Miles Anderson, FL Div. of Emergency Man., Dir., Northwest Florida Recovery  
Assessing the Performance of Modern Building Codes & Standards in Reducing Hurricane Damage - Timothy Reinhold, VP/Engineering, Institute for Business & Home Safety



Third Party Analysis of Manufactured Home Retrofit Tie Downs – Assessment and Analysis – State of Florida Residential Construction Mitigation Retrofit Program

**Appendix Three: National Catastrophe Plan**

Natural Catastrophe Risk: Creating a Comprehensive National Plan (Draft by National Association of Insurance Commissioners)  
Resolution Regarding Natural Disaster Insurance Issues – National Conference of Insurance Legislators  
“Sharing and Reducing the Financial Risks of Future Mega-Catastrophes” - Robert E. Litan, VP/Research & Policy, Kauffman Foundation; Sr. Fellow, Economic Studies, The Brookings Institution  
Preparing for and Protecting America from Catastrophe - James Lee Witt, National Co-Chair Protecting America.org  
Has the Time Come for Comprehensive Natural Disaster Insurance? Howard Kunreuther, Cecilia Yen Koo Professor of Decision Sciences & Public Policy Co-Director Risk Management and Decision Processes Center

**Appendix Four: Population Growth, Insurance and Capacity Demands**

Florida Population and New Capital Estimates Ray Spudeck, Senior Research Economist, Office of Insurance Regulation  
Table 1: Florida Population Growth Estimates by County  
Table 2: Estimated Policy Count Growth  
Table 3: Estimated Minimum New Capital Needed for Florida residential insurance

**Appendix Five: The Private Insurance Market**

The Private Insurance Market – Ray Spudeck, Senior Research Economist, Office of Insurance Regulation  
Overview of the Florida Hurricane Risk Market– Office of Insurance Regulation  
Overview of State Rating Laws - Eric Nordman, CPCU, CIE, Director of Research  
Overview of State Rating Laws -State Rating Systems - Eric Nordman, CPCU, CIE, Director of Research, NAIC  
Overview of State Rating Laws -State Filing Methods - Eric Nordman, CPCU, CIE, Director of Research, NAIC  
Solvency and Capacity Overview - Sharon Binnun, Deputy Insurance Commissioner, Office of Insurance Regulation  
Consumer Statement on Rate Review Process - Bob Hunter, Director of Insurance, Consumer Federation of America  
Industry Perspective of Florida Hurricane Market - Steve Goldberg, Chief Actuary, Benfield Group  
Perspective and Recommendations by Florida Alliance on Hurricane Insurance - Sam Miller, VP, Florida Insurance Council & Scott Johnson, Ex. VP, Florida Association of Insurance Agents  
Hurricanes Katrina & Rita: Impacts on the P/C Insurance & Reinsurance Industries - Robert P. Hartwig, Ph.D., CPCU, Senior VP & Chief Economist, Insurance Information Institute  
Academy of Florida Trial Lawyers Perspective and Recommendations – Steve Marino, Esq.

Comparison of Admitted and Surplus Lines Property Insurance Market and Climate Survey  
Gary Pullen, Executive Director, Florida Surplus Lines Service Office  
Perspective and Recommendations by the Florida Association of Insurance Agents – Scott Johnson, Executive Vice President  
Insurance & Coastal Risk in Florida: Lessons on Availability & Affordability - Robert P. Hartwig, Ph.D., CPCU, Senior VP & Chief Economist, Insurance Information Institute

**Appendix Six: The Florida Hurricane Catastrophe Fund**

Florida Hurricane Catastrophe Fund Presentation - Jack Nicholson, Senior Florida Hurricane Catastrophe Fund Officer  
Documentation on future capacity needs & adjustments to the Fla. Hurricane Catastrophe Fund - Letter to Trustees re: Limit Adjustment - Jack Nicholson, Senior FHCF Officer

**Appendix Seven: Citizens Property Insurance Corporation**

Citizens Property Insurance Corporation Presentation - Bob Ricker, President and Executive Director, Citizens Property Insurance Corporation  
Data Responses by Citizens Property Insurance Corporation, Susanne Murphy, General Counsel  
Citizens Loss Mitigation Credits Description  
Citizens Loss Mitigation Credits Summary  
Citizens Depopulation History  
Citizens Memo on Combining Citizens' Accounts  
Impact on Citizens if Coverage Reductions Occur with Hard Caps (\$500,000)  
Impact on Citizens if Coverage Reductions Occur with Hard Caps (\$1,000,000)

**Appendix Eight: Testimony by Florida Insurance Council on Senate Bill 1486**

**Appendix Nine: Hurricane Resistance Grading(s) for Residential Property**