

## HOUSE OF REPRESENTATIVES STAFF ANALYSIS

**BILL #:** HB 245 Depopulation Programs of Citizens Property Insurance Corporation

**SPONSOR(S):** Boyd

**TIED BILLS:** **IDEN./SIM. BILLS:** SB 578

REFERENCE	ACTION	ANALYST	STAFF DIRECTOR or BUDGET/POLICY CHIEF
1) Insurance & Banking Subcommittee		Callaway	Cooper
2) Economic Affairs Committee			

### SUMMARY ANALYSIS

Citizens Property Insurance Corporation (Citizens) is a state-created, not-for-profit, tax-exempt governmental entity whose public purpose is to provide property insurance coverage to those unable to find affordable coverage in the voluntary admitted market. Under current law, Citizens is authorized to develop and maintain a depopulation program to reduce the number of its insured properties and to decrease its financial exposure. The depopulation program encourages insurance companies licensed in Florida to assume policies currently covered by Citizens.

Surplus lines insurance is a category of insurance for which there is no market available through licensed insurance companies. Surplus lines insurers are not authorized insurers and thus do not obtain a certificate of authority from the Office of Insurance Regulation to transact insurance in Florida. Rather, surplus lines insurers are eligible to transact surplus lines insurance.

Under current law, surplus lines insurers are not allowed to participate in the Citizens' depopulation program because the program is limited to insurers licensed in Florida and surplus lines insurers are not licensed in Florida. The bill changes current law to allow surplus lines insurers meeting specified financial criteria to take policies out of Citizens through depopulation. The bill does not require a Citizens' policyholder offered insurance by a surplus lines insurer to accept the insurance offered; the policyholder can remain in Citizens.

The bill requires a surplus lines insurer removing policies from Citizens to provide prominent notice to the Citizens' policyholder, before the insurer assumes the policy, that the surplus lines policy is not covered by the Florida Insurance Guaranty Association. Also, the surplus lines insurer must offer the Citizens' policyholder similar coverage as his or her Citizens' policy and must notify the Citizens' policyholder of the differences in coverage offered by the insurer and Citizens. If the Citizens' policyholder receives an offer for insurance from both a Florida licensed insurer and a surplus lines insurer, then the offer from the Florida licensed insurer has priority.

Surplus lines insurers assuming policies from Citizens must deposit a specified amount of premium from the assumed policies with the Bureau of Collateral Management in the Department of Financial Services. The premium deposit can be used to pay claims of Citizens' policyholders assumed by the insurer if the surplus lines insurer becomes insolvent.

Lastly, the bill allows additional types of insurers and insurance entities considering depopulating Citizens to receive Citizens' underwriting and confidential claims files, but maintains current law requiring release of the files only if the receiving insurer or entity agrees in writing to maintain the confidentiality of the files.

The bill has no fiscal impact on state or local government. Because insurance written by surplus lines insurers is often more expensive than insurance written by licensed insurers and by Citizens, Citizens' policyholders who choose to be taken out of Citizens to obtain insurance from a surplus lines insurer could pay more for insurance.

The bill is effective July 1, 2012.

This document does not reflect the intent or official position of the bill sponsor or House of Representatives.

**STORAGE NAME:** h0245.INBS

**DATE:** 10/28/2011

## FULL ANALYSIS

### I. SUBSTANTIVE ANALYSIS

#### A. EFFECT OF PROPOSED CHANGES:

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

Citizens Property Insurance Corporation (Citizens or corporation) is a state-created, not-for-profit, tax-exempt governmental entity whose public purpose is to provide property insurance coverage to those unable to find affordable coverage in the voluntary admitted market. It is not a private insurance company. As of September 30, 2011, Citizens is the largest property insurer in Florida with over 1.4 million policies extending over \$508 billion of property coverage to Floridians.<sup>1</sup>

Citizens was created by the Legislature in 2002 by the merger of two existing property insurance associations that provided property insurance to those homeowners and businesses who could not find coverage in the private market.

##### *Coverage*

Citizens writes various types of property insurance coverage for its policyholders. The types of coverage are divided into three separate accounts within the corporation:

1. Personal Lines Account (PLA) – Multi-peril Policies<sup>2</sup>  
Consists of homeowners, mobile homeowners, dwelling fire, tenants, condominium unit owners and similar policies;
2. Commercial Lines Account (CLA) – Multi-peril Policies  
Consists of condominium association, apartment building, homeowner's association policies, and commercial non-residential multi-peril policies on property located outside the Coastal Account area; and
3. Coastal Account – Wind-only<sup>3</sup> and Multi-peril Policies  
Consists of wind-only and multi-peril policies for personal residential, commercial residential, and commercial non-residential issued in limited eligible coastal areas.

##### *Financial Resources*

Citizens' financial resources to pay property insurance claims include both resources typically available to private insurance companies and resources uniquely available to Citizens as a governmental entity with the statutory authority to levy assessments in the event of a deficit in Citizens' financial resources. Like typical private insurance companies, Citizens' financial resources include:

- Insurance premiums;
- Investment income;
- Accumulated surplus;
- Reimbursements from the Florida Hurricane Catastrophe Fund due to Citizens' purchase of reinsurance from the Florida Hurricane Catastrophe Fund; and
- Reimbursements from private reinsurance companies if Citizens purchases private reinsurance.

Financial resources unique to Citizens include: Citizens Policyholder Surcharges, regular assessments, and emergency assessments.

##### *Assessments*

In the event Citizens incurs a deficit (i.e., its obligations to pay claims exceeds its capital plus reinsurance recoveries), it may levy assessments on most of Florida's property and casualty insurance

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<sup>1</sup> <https://www.citizensfla.com/>

<sup>2</sup> A multi-peril policy is defined as a package policy, such as a homeowners or business insurance policy that provides coverage against several different perils. It also refers to the combination of property and liability coverage in one policy. (<http://www2.iii.org/glossary/>) Multi-peril property insurance policies include coverage for damage from windstorm and from other perils, such as fire, theft, and liability.

<sup>3</sup> A wind-only policy is a property insurance policy that provides coverage against windstorm damage only. Coverage against non-windstorm events such as fire, theft, and liability are available in a separate policy.

policyholders in a specific sequence set by statute.<sup>4</sup> The three Citizens' accounts calculate deficits and resulting assessment needs independently.

Citizens Policyholder Assessments: If Citizens incurs a deficit, Citizens will first levy surcharges on its policyholders of up to 15% of premium per account in deficit, for a maximum total of 45%.<sup>5</sup>

Regular Assessments: Upon the exhaustion of the Citizens Policyholder Assessment for a particular account, Citizens may levy a regular assessment of up to 6% of premium or 6% of the deficit per account, for a maximum total of 18%.<sup>6</sup> The regular assessment is levied on virtually all property and casualty policies in the state, but is not levied on Citizens' policies. The assessment is also not levied on workers' compensation, medical malpractice, accident and health, crop or federal flood insurance policies.

Emergency Assessments: Upon the exhaustion of the Citizens Policyholder Assessment and regular assessment for a particular account, Citizens may levy an emergency assessment of up to 10% of premium or 10% of the deficit per account, for a maximum total of 30%.<sup>7</sup> This assessment can be collected for as many years as is necessary to cure a deficit. Emergency assessments are levied on virtually all property and casualty policies in the state, including Citizens' own policies. However, this assessment is not levied on workers' compensation, medical malpractice, accident and health, crop or federal flood insurance policies.

#### *Claims Paying Capacity*

Citizens projects the corporation will have over \$5.7 billion in surplus to pay claims during the 2011 hurricane season.<sup>8</sup> In addition, Citizens could be reimbursed another \$6.6 billion for claims paid by the Florida Hurricane Catastrophe Fund. Citizens purchased private reinsurance for the Coastal Account that would reimburse the corporation up to \$575 million for claims paid in this Account. Thus, the maximum amount Citizens has to pay claims in all accounts for the 2011 hurricane season is approximately \$12.9 billion.<sup>9</sup>

As of September 30, 2011, Citizens' total exposure is over \$508 billion. Citizens estimates the 1-in-100 year hurricane would cost over \$22.3 billion.<sup>10</sup> The \$9.4 billion difference between Citizens' resources to pay claims (\$12.9 billion) and its 1-in-100 year exposure (\$22.3 billion) would be covered by assessments levied by Citizens on its own policyholders and on policyholders of most property and casualty insurance.

#### *Depopulation*

Under current law, Citizens is authorized to develop and maintain a depopulation program to reduce the number of its insured properties and to decrease its financial exposure.<sup>11</sup> The depopulation program encourages insurance companies licensed in Florida to assume policies currently covered by Citizens, thus reducing Citizens' policy count and exposure. However, current law allows a Citizens policyholder to choose to remain in Citizens even though the policyholder receives an offer of coverage (assumption) from an insurance company in the private market. Furthermore, a Citizens' policyholder cannot be removed from Citizens by a private insurer licensed in Florida if the policyholder's insurance agent is not appointed by the insurer removing the policy from Citizens.<sup>12</sup>

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<sup>4</sup> s. 627.351(6)(b)3.a., d., and i., F.S.

<sup>5</sup> s. 627.351(6)(b)3.i., F.S.

<sup>6</sup> s. 627.351(6)(b)3.a. and b., F.S.

<sup>7</sup> s. 627.352(6)(b)3.d., F.S.

<sup>8</sup> Information received from Citizens on August 23, 2011.

<sup>9</sup> Although Citizens has another \$3.82 billion in pre-event bonding for the Coastal Account that would be available to pay claims, this bonding would have to be repaid through assessments, so is not included in the calculations. If this amount were included, Citizens would have \$16.7 billion to pay claims during the 2011 hurricane season.

<sup>10</sup> A 1-in-100 year hurricane has a 1% probability of occurring.

<sup>11</sup> s. 627.351(6)(q)3., F.S.

<sup>12</sup> See s. 627.3517, F.S.

The following table outlines Citizens' recent depopulation statistics:

### Depopulation of Citizens Property Insurance<sup>13</sup>

Year	Number of Policies	Exposure
2003	28,219	\$ 8,140,681,906
2004	158,416	\$ 30,663,076,480
2005	293,684	\$ 53,658,840,059
2006	67,853	\$ 15,637,589,369
2007	247,887	\$ 68,259,426,361
2008	385,084	\$ 106,870,490,165
2009	149,645	\$ 37,784,506,743
2010	59,792	\$ 13,888,913,857

### Surplus Lines Insurance

Surplus lines insurance refers to a category of insurance for which there is no market available through standard insurance carriers in the admitted market (insurance companies licensed to transact insurance in Florida). There are three basic categories of surplus lines risks:

1. Specialty risks that have unusual underwriting characteristics or underwriting characteristics that admitted insurers view as undesirable;
2. Niche risks for which admitted carriers do not have a filed policy form or rate; and
3. Capacity risks which are risks where an insured needs higher coverage limits than those that are available in the admitted market.

Surplus lines insurers are not "authorized" insurers as defined in the Florida Insurance Code and thus do not obtain a certificate of authority from the Office of Insurance Regulation (OIR) to transact insurance in Florida.<sup>14</sup> Rather, surplus lines insurers are "unauthorized" or "nonadmitted" insurers, but are eligible to transact surplus lines insurance under the surplus lines law as "eligible surplus insurers".<sup>15</sup>

The OIR determines whether a surplus lines insurer is "eligible" based on statutory guidelines.<sup>16</sup> Eligibility requirements<sup>17</sup> reviewed by the OIR for surplus lines include:

- Eligibility is requested in writing for the insurer by the Florida Surplus Lines Service Office;
- Insurer is authorized for the prior three years in the state or country of its domicile to write the kinds of insurance the insurer wants to write in Florida (with limited exceptions);
- Insurer provides the OIR with its current annual financial statement;
- Insurer meets surplus requirements (delineated below); and
- Insurer has a good reputation relating to payment of claims and policyholder service.

Generally, a surplus lines insurer must have and maintain surplus of \$15 million or more in order to obtain and maintain eligibility.<sup>18</sup> In addition, an insurer formed outside the U.S. must have and maintain in the U.S. a trust fund containing at least \$5.4 million.

The OIR has no duty or responsibility to determine the actual financial condition or claims practice of surplus lines insurers; a finding of eligibility by the OIR only means the surplus lines insurer appears to be financially sound and to have satisfactory claims practice.<sup>19</sup>

<sup>13</sup> <https://www.citizensfla.com/about/depopinfo.cfm> (last viewed October 26, 2011).

<sup>14</sup> s. 624.09(1), F.S., defines "authorized" insurer.

<sup>15</sup> s. 624.09(2), F.S. defines "unauthorized" insurer, s. 626.914(2), F.S., defines "eligible surplus lines insurer," and s. 626.918, F.S., provides eligibility for surplus lines insurers.

<sup>16</sup> s. 626.918(2), F.S.

<sup>17</sup> s. 626.918, F.S.

<sup>18</sup> s. 626.918(1)(d)1.a., F.S.

<sup>19</sup> s. 626.918(4), F.S.

The OIR must withdraw the eligibility of a surplus lines insurer if the OIR has reason to believe the insurer is insolvent or in unsound financial condition, does not make reasonable prompt payment of claims, or does not meet the statutory guidelines for eligibility (including maintenance of \$15 million in surplus). The OIR may withdraw the eligibility of a surplus lines insurer if the insurer willfully violates a statute or rule.<sup>20</sup>

### **Effect of Proposed Changes**

The bill allows surplus lines insurers meeting specified criteria to take policies out of Citizens through depopulation. Under current law, surplus lines insurers are not allowed to participate in the Citizens' depopulation program because the program is limited to insurers licensed in Florida and surplus lines insurers are not licensed in Florida, but are "eligible" to transact insurance in Florida.<sup>21</sup> Under the bill, a Citizens' policyholder offered coverage by a surplus lines insurer does not have to accept the insurance offered by the surplus lines insurer and can remain in Citizens.

Only surplus lines insurers meeting three financial criteria are allowed to take policies out of Citizens. The criteria are designed to ensure financially sound surplus lines insurers participate in the Citizens' depopulation program. The OIR determines if the surplus lines insurer meets the specified financial criteria for participation in the Citizens' depopulation program and approves the insurer's depopulation plan.

First, the bill requires the surplus lines insurer wanting to participate in Citizens' depopulation to maintain \$50 million in surplus. Current law requires surplus lines insurers to maintain surplus of only \$15 million in order to be eligible to write insurance in Florida. Thus, the bill provides increased surplus requirements for those surplus lines insurers that take policies out of Citizens. The increased surplus will protect against insolvency of the insurer and make it more likely policyholder claims can be paid if an insolvency occurs.

Second, the insurer must also maintain an A.M. Best Financial Strength Rating of A- or better in order to take policies out of Citizens. Surplus lines insurers are not required in current law to maintain a certain A.M. Best Rating in order to be eligible to write insurance in Florida.

Third, the bill requires a surplus lines insurer wanting to participate in Citizens' depopulation to have financial resources to cover the insurer's 100-year probable maximum loss at least twice in a hurricane season. Historically, the OIR has required authorized insurers to have financial resources to cover the insurer's 100-year probable maximum loss at least once in a hurricane season. However, instead of implementing a 100-year reinsurance requirement for all authorized insurers, recently the OIR implemented reinsurance requirements based on a review of an insurer's financial picture and exposure. Thus, reinsurance requirements can vary among authorized insurers.

Under the bill, a surplus lines insurer removing policies from Citizens must provide prominent notice to the Citizens' policyholder, before the insurer assumes the policy, that the surplus lines policy is not covered by the Florida Insurance Guaranty Association (FIGA). Generally, FIGA pays claims of policyholders insured by licensed Florida insurers if the insurer becomes insolvent. Because insurance written by surplus lines insurers is not covered by FIGA, if the insurer becomes insolvent, claims will be paid solely from the assets of the insurer and claim payment, in full or in part, is not guaranteed.

A surplus lines insurer wanting to take a policy from Citizens must offer the Citizens' policyholder a policy with similar coverage as his or her Citizens' policy and must notify the Citizens' policyholder of the differences in coverage offered by the insurer and Citizens. In addition, the insurer must comply with the requirements in current law for licensed insurers that take policies out of Citizens.<sup>22</sup> If the

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<sup>20</sup> s. 626.919, F.S.

<sup>21</sup> Surplus lines insurers are not "authorized" insurers, meaning they are not licensed by the OIR to transact insurance in Florida. Rather, surplus lines insurers are "unauthorized" insurers, but are eligible to transact surplus lines insurance under the surplus lines law as "eligible surplus insurers." Claims against insurance policies issued by surplus lines insurers cannot be paid by the Florida Insurance Guaranty Association if the surplus lines insurer becomes insolvent.

<sup>22</sup> s. 627.351(6)(q)3., F.S.; s. 627.3511, F.S.; s. 627.3517, F.S.

Citizens' policyholder receives an offer for insurance from both a Florida licensed insurer and a surplus lines insurer, then the offer from the Florida licensed insurer has priority.

The bill expands the provision in current law allowing release of Citizens' underwriting and confidential claims files to certain insurers. Current law allows insurers wanting to take policies out of Citizens to obtain underwriting and claims information on policies in Citizens. This is allowed so the insurer can decide which Citizens' policies to assume based on the insurer's exposure, financial picture, and business plan. The information can be released by Citizens only if the insurer agrees in writing to maintain the confidentiality of the files.

The bill allows additional types of insurers and insurance related entities considering depopulating Citizens to receive Citizens' underwriting and confidential claims files. Under the bill, reinsurance intermediaries, eligible surplus lines insurers, and entities created to seek authority to write property insurance are allowed to receive Citizens' files. The bill maintains current law requiring release of the files only if the receiving insurer or entity agrees in writing to maintain the confidentiality of the files.

Surplus lines insurers assuming policies from Citizens must deposit a certain amount of premium from the assumed policies with the Bureau of Collateral Management in the Department of Financial Services. The Bureau of Collateral Management is part of the Division of Treasury. The Chief Financial Officer has fiduciary responsibility over the Division of Treasury.<sup>23</sup>

The Division of Treasury has three bureaus:

1. The Bureau of Funds Management;
2. The Bureau of Collateral Management; and
3. The Bureau of Deferred Compensation.

The Bureau of Collateral Management is a centralized deposit location for specialized handling of regulatory collateral deposits. Regulatory collateral deposits are required by state agencies as a condition of doing business or acts of guarantee. For 2010, the Bureau's asset management staff was responsible for maintaining regulatory collateral deposits for 1,885 combined accounts representing in excess of \$17 billion dollars.<sup>24</sup>

The premium deposit can be used to pay claims of Citizens' policyholders assumed by the insurer if the surplus lines insurer becomes insolvent. The surplus lines insurer must make an accounting of the premium deposit with OIR at the time of the initial deposit and quarterly thereafter. The accounting must evidence the amount of the premium on deposit is accurate. If the deposit amount is too low, then the insurer must deposit additional funds. If the deposit amount is too high, then the insurer must receive a refund of the excess funds.

#### B. SECTION DIRECTORY:

**Section 1:** Amends s. 627.351(6), relating to Citizens Property Insurance Corporation, to amend current law on Citizens' depopulation.

**Section 2:** Provides an effective date of July 1, 2012.

## II. FISCAL ANALYSIS & ECONOMIC IMPACT STATEMENT

#### A. FISCAL IMPACT ON STATE GOVERNMENT:

##### 1. Revenues:

None.

<sup>23</sup> See s. 17.52, F.S.; s. 17.54, F.S.; s. 17.55, F.S.

<sup>24</sup> Division of Treasury Annual Report 2010 available at <http://www.myfloridacfo.com/treasuryannual/2010/> (last viewed October 24, 2011).

2. Expenditures:

According to the OIR, the fiscal impact of the bill cannot be determined because it is unknown how many surplus lines insurers, if any, will participate in Citizens' depopulation. For insurers that participate in the program, the bill requires the OIR to review and approve each insurer's depopulation plan and to review the insurer's initial and quarterly accounting of the premium deposit. Thus, the OIR has an on-going oversight role, but the extent of the oversight is not quantifiable.

B. FISCAL IMPACT ON LOCAL GOVERNMENTS:

1. Revenues:

None.

2. Expenditures:

None.

C. DIRECT ECONOMIC IMPACT ON PRIVATE SECTOR:

Insurance written by surplus lines insurers is often more expensive than insurance written by licensed insurers and by Citizens. Thus, Citizens' policyholders who choose to be taken out of Citizens to obtain insurance from a surplus lines insurer could pay more for insurance. However, the bill does not force Citizens' policyholders out of Citizens when a surplus lines insurer wants to insure their property. Obtaining insurance with a surplus lines insurer instead of Citizens is completely the policyholder's choice. Thus, if the cost of insurance from the surplus lines insurer is more than the insurance from Citizens or more than the policyholder wants to pay, then the policyholder can remain in Citizens.

A Citizens' policyholder opting to move from Citizens to a surplus lines insurer would no longer incur a Citizens Policyholder Assessment if Citizens runs a deficit. However, the policyholder would still incur regular and emergency assessments as policyholders of property and casualty surplus lines insurers are assessed for Citizens' deficits.

D. FISCAL COMMENTS:

None.

### III. COMMENTS

A. CONSTITUTIONAL ISSUES:

1. Applicability of Municipality/County Mandates Provision:

Not applicable. This bill does not appear to: require counties or municipalities to spend funds or take an action requiring the expenditure of funds; reduce the authority that counties or municipalities have to raise revenues in the aggregate; or reduce the percentage of a state tax shared with counties or municipalities.

2. Other:

None.

B. RULE-MAKING AUTHORITY:

None.

C. DRAFTING ISSUES OR OTHER COMMENTS:

The bill erroneously provides the premium deposit required by a surplus lines insurer participating in Citizens' depopulation is deposited in the Bureau of Collateral *Securities*. The correct name for the

Bureau is the Bureau for Collateral *Management*. An amendment is anticipated to correct this error. Moreover, the correct name of the Bureau is used in the staff analysis.

#### **IV. AMENDMENTS/ COMMITTEE SUBSTITUTE CHANGES**