

HOUSE OF REPRESENTATIVES STAFF ANALYSIS

BILL #: CS/HB 557 Florida Insurance Guaranty Association

SPONSOR(S): Insurance & Banking Subcommittee and Raburn

TIED BILLS: **IDEN./SIM. BILLS:** SB 836

REFERENCE	ACTION	ANALYST	STAFF DIRECTOR or BUDGET/POLICY CHIEF
1) Insurance & Banking Subcommittee	12 Y, 0 N, As CS	Peterson	Cooper
2) Finance & Tax Committee			
3) Regulatory Affairs Committee			

SUMMARY ANALYSIS

The bill revises the process for insurers to pay and recoup Florida Insurance Guaranty Association (FIGA) assessments. FIGA is the guaranty association for property and casualty insurance. If FIGA lacks adequate funds to pay claims of an insolvent insurer, it can levy an assessment on other member insurers. Under current law, insurers must pay regular assessments within 30 days of the levy, although FIGA, at its discretion, may authorize emergency assessments to be paid in monthly installments. Once the assessment is paid to FIGA, the insurance company may begin to recoup the payment from policyholders at policy issuance or renewal. The amount of an insurance company's assessment is determined based on its premiums written in the calendar year preceding the assessment, regardless of the value of premiums in effect at the time recoupment occurs. Thus, if an insurance company's book of business decreases during that period, it may need to apply and collect the recoupment factor for more than 12 months to recoup the full amount of an assessment paid. Insurance companies that did not write the type of insurance affected by the assessment in the prior year are not subject to the assessment.

The bill revises the assessment and collection procedure to:

- Create a uniform assessment percentage to be collected from all policyholders.
- Authorize FIGA to require payment of assessments by advance payment, prior to an insurer's recoupment of payment from a policyholder; monthly installment; or a combination of both.
- Require insurers who did not write the affected line of insurance in the preceding year to pay an assessment based on an estimate of premiums it will write in the assessment year.
- Require insurers to submit a reconciliation report that reflects actual collections as compared to the initial payment.
- Provide for payment of excess collections to FIGA.
- Provide for credits to insurers against future assessments for collections that are less than an insurer's payment.

The bill allows insurers to recognize FIGA assessments that are subject to recoupment as an admissible asset, thereby codifying current practice of the Office of Insurance Regulation.

The bill has no impact on local government and may have a fiscal impact on state government because it exempts FIGA regular assessments from the insurance premium tax. The amount of lost revenue is unknown until the Revenue Estimating Conference renders its opinion.

The bill has a July 1, 2015 effective date.

FULL ANALYSIS

I. SUBSTANTIVE ANALYSIS

A. EFFECT OF PROPOSED CHANGES:

Florida Insurance Guaranty Association (FIGA)

Part II of chapter 631, F.S., governs the operations of the Florida Insurance Guaranty Association (FIGA). FIGA is a nonprofit corporation that was created to pay covered claims,¹ including unearned premiums,² to policyholders of insolvent property and casualty insurers. Current law requires property and casualty insurance companies doing business in Florida to be a member of FIGA as a condition of their authority to transact insurance.³ When a property and casualty insurance company becomes insolvent, FIGA assumes the claims of the insurer and pays the claims of its policyholders, which include claims on residential and commercial property insurance, automobile insurance, and liability insurance, among others. This ensures that policyholders who have paid premiums for insurance are not left with valid, yet unpaid claims. Generally, the maximum claim amount FIGA will cover is \$300,000, but certain special limits may apply.⁴

In order to pay claims and to maintain the operations of an insolvent insurer, FIGA has several potential funding sources. FIGA's primary funding source is from the liquidation of assets of insolvent insurance companies domiciled in Florida.⁵ In addition, FIGA obtains funds from the liquidation of assets of insolvent insurers domiciled in other states, but having claims in Florida.

In the event the insolvent insurer's assets are insufficient to pay all claims, FIGA can issue two types of post-insolvency assessments against property and casualty insurance companies to raise funds to pay claims. FIGA is divided into two accounts: the auto liability and auto physical damage account; and the account for all other included insurance lines (the all-other account).⁶ FIGA may levy an assessment for either of its two accounts of up to 2% of an insurer's net direct written premium⁷ in Florida, in the preceding calendar year, for insurance within the account.⁸ This assessment is known as the "regular assessment." The second type of assessment is an emergency assessment, which may only be used to pay covered claims of an insurer that is rendered insolvent due to a hurricane. The emergency assessment is also capped at 2% of an insurer's net direct written premium in Florida in the preceding calendar year.⁹ The Office of Insurance Regulation (OIR) may exempt an insurer from an assessment if the assessment would cause the insurer's financial statement to reflect an amount of capital or surplus that is less than the minimum required to transact business.¹⁰

FIGA last levied a regular assessment in November 2012 with payment due from insurers by December 31, 2012. This assessment amount was 0.9% of an insurer's net direct written premiums for 2011 for

¹ Section 631.54(3), F.S., provides, in relevant part: "Covered claim" means an unpaid claim, including one of unearned premiums, which arises out of, and is within the coverage, and not in excess of, the applicable limits of an insurance policy to which this part applies, issued by an insurer, if such insurer becomes an insolvent insurer and the claimant is a resident of this state at the time of the insured event or the property from which the claim arises is permanently located in this state....

² The portion of a premium already received by the insurer under which protection has not yet been provided. The entire premium is not earned until the policy period expires, even though premiums are typically paid in advance. INSURANCE INFORMATION INSTITUTE, *Glossary*, <http://www.iii.org/services/glossary/u/> (last visited Feb. 17, 2015).

³ s. 631.55(1), F.S.

⁴ s. 631.57(1)(a), F.S. For damages to structure and contents in homeowners' claims, FIGA covers an additional \$200,000, for a total of \$500,000. For condominium and homeowners' association claims, FIGA covers the lesser of policy limits or \$100,000 multiplied by the number of units in the association.

⁵ Typically, insurers are placed into liquidation when the company is insolvent. The goal of liquidation is to dissolve the insurance company. See s. 631.061, F.S., for the grounds for liquidation.

⁶ s. 631.55(2), F.S.

⁷ "Net direct written premiums" means direct gross premiums written in this state on insurance policies to which this part applies, less return premiums thereon and dividends paid or credited to policyholders on such direct business. "Net direct written premiums" does not include premiums on contracts between insurers or reinsurers. s. 631.54(8), F.S.

⁸ s. 631.57(3)(a), F.S.

⁹ s. 631.57(3)(e), F.S.

¹⁰ s. 631.57(4), F.S.

insurance written in the all-other account. The last emergency assessment FIGA levied was in 2006 and was for the full 2%.¹¹

FIGA Assessment Procedure

The procedure used by FIGA to levy an assessment and the procedure used by insurers to recoup the assessment are generally the same for both regular and emergency assessments, as follows:¹²

- FIGA's board determines an assessment is needed to pay claims or administration costs, or to pay bonds issued by FIGA.
- FIGA certifies the need for an assessment levy to the OIR.
- The OIR reviews the certification and, if it is sufficient, issues an order to all insurance companies subject to the assessment instructing the companies to pay their assessment to FIGA.
- Regular assessments must be paid by the insurance company within 30 days of the levy. Emergency assessments may be paid either in one payment or in 12 monthly installments, at the option of FIGA, with the first payment due at the end of the month after the assessment is levied.
- If an insurer intends to recoup the assessment from policyholders, it must make a rate filing with the OIR. The filing reflects the rate factor the insurer determines will recoup the assessment when applied over the next 12 months, unless the insurer opts to recoup the assessment over a longer period, as policies are issued or renewed.¹³ If an insurer's book of business declines during the recoupment period, the assessment factor may be insufficient to recoup the total amount of assessment paid to FIGA. In those circumstances, the insurance company may continue to collect the assessment from policyholders beyond 12 months, until the assessment is recouped in full.
- If the insurer collects more than the assessment it paid, the insurer either remits the excess to FIGA (if the excess amount is 15 percent or less than the total assessment paid by the insurer) or refunds it to policyholders (if the excess amount exceeds 15 percent of the total assessment paid).

Changes Proposed by the Bill

The bill revises the process for insurers to remit regular and emergency assessments to FIGA, as follows.

The bill requires the OIR to specify in the order levying the assessment the percentage to be collected uniformly from all assessable policyholders and the start of the assessment year. The bill defines "assessment year" as a 12-month period that may start on the first day of a calendar quarter. The initial collection start date must be at least 90 days after the FIGA board certifies the need for an assessment.

An insurer that wrote insurance in the preceding calendar year must submit an initial payment to FIGA based on the insurer's net direct written premiums of the prior year multiplied by the uniform percentage. An insurer that did not write in the prior calendar year must submit an initial payment based on a good faith estimate of premiums it will write during the assessment year multiplied by the uniform percentage. In both cases, the initial payment is due from the insurer before the beginning of the assessment year on or before the date specified in the order.

The bill eliminates the informational filing with the OIR currently required to recoup the FIGA assessment from policyholders. Instead, the bill requires that within 45 days after the end of the assessment year, an insurer must submit a reconciliation report that reflects actual collections as compared to the initial payment. If an insurer collects more than its initial payment to FIGA, the insurer remits the excess amount to FIGA. If an insurer collects less than its initial payment to FIGA, FIGA credits the amount to the insurer against future assessments. Consumers will pay a uniform percentage of premium, however, the amount will vary depending on the premium charged.

¹¹ FLORIDA INSURANCE GUARANTY ASSOCIATION, *Assessments*, <http://www.figafacts.com/assessments> (last visited Feb. 17, 2015).

¹² s. 631.57(3), F.S.

¹³ See also OFFICE OF INSURANCE REGULATION, *Frequently Asked Questions for FIGA Recoupment Filings*, available at <http://www.figafacts.com/media/files/FAQs%20OIR-FIGA%20Assessment.pdf> (last visited Feb. 17, 2015).

If FIGA's cash flow is sufficient—adequate to pay claims for the next 6 months—FIGA may authorize insurers to collect an assessment monthly. Like the monthly payment option for emergency assessments in statute today, this option would not require an insurer to advance funds to FIGA. Instead, an insurer would only pay FIGA the insurer's actual collections from policyholders, which would be the uniform percentage multiplied by the net direct written premiums during the assessment year. FIGA may also utilize the monthly installment method in combination with the method requiring insurers to make an initial payment to FIGA and subsequently recoup that payment from policyholders.

The bill expands current law that defines when the OIR may exempt an insurer from an assessment. Today, an insurer may be exempted if the assessment would result in the insurer's financial statement reflecting an amount of capital or surplus less than the sum required by any jurisdiction in which the insurer is authorized to transact insurance.¹⁴ The bill broadens this authority to allow the OIR not just to exempt, but also to temporarily defer an assessment, and expands the basis for either a deferral or an exemption to include a finding that the insurer is impaired or insolvent.

The bill requires charges or recoupments for FIGA assessments to be delineated separately from premium in the policyholder's insurance bill and does not allow insurers to include FIGA assessments in rates.

Accounting for FIGA Assessments

Most insurers authorized to do business in the U.S. and its territories are required to prepare statutory financial statements to their state insurance regulators in accordance with statutory accounting principles (SAP),¹⁵ which differ from generally acceptable accounting principles (GAAP) in a number of ways. While GAAP provides information useful to investors and other users of financial reporting (such as banks, credit rating agencies, and the U.S. Securities & Exchange Commission), SAP is developed in accordance with the concepts of consistency, recognition and conservatism, and assists state insurance departments with the regulation of the solvency of insurance companies. The ultimate objective of solvency regulation is to ensure that policyholder, contract holder and other legal obligations are met when they come due and that companies maintain capital and surplus at all times and in such forms as required by statute to provide a margin of safety. With the objective of solvency regulation, SAP focuses on the balance sheet, rather than the income statement, and emphasizes insurers' liquidity.¹⁶

Under both GAAP and SAP, an insurer recognizes a liability when a FIGA assessment is imposed (which reduces the insurer's surplus and net worth). However, a timing difference exists between the two principles for the recognition of an asset relating to the future recoveries of policy surcharges:

- GAAP does not treat the assessments recoverable from future premium writings as an asset, and thus results in an immediate reduction in equity and earnings in the period a FIGA assessment is billed. However, the equity reduction is eliminated the following year as the assessments are recouped from policyholders.
- On the other hand, SAP allows insurers to recognize the assessment amount likely to be recovered from future premium surcharges as an asset, which in turn offsets or eliminates the negative effect on statutory surplus, subject to certain conditions. SAP does not permit an asset to be recognized if the assessment is to be recovered from future rate structures, and limits asset recognition for accrued assessment liabilities to the extent that amount to be recovered is from in-force premiums only.¹⁷

¹⁴ s. 631.57(4), F.S.

¹⁵ The OIR requires insurers to file annual SAP statements and independently audited financial reports. s. 624.424, F.S.

¹⁶ NAIC & CENTER FOR INSURANCE POLICY AND RESEARCH, *Statutory Accounting Principles*, http://www.naic.org/cipr_topics/topic_statutory_accounting_principles.htm (last visited Feb. 17, 2015). Section 625.01115, F.S., provides that "statutory accounting principles" means accounting principles as defined in the National Association of Insurance Commissioners Accounting Practices and Procedures Manual as of March 2002 and subsequent amendments thereto if the amendments remains substantially consistent.

¹⁷ Statements of Statutory Accounting Principles, No. 35R, Guaranty Fund and Other Assessments (SSAP 35R); see also Thomas Howell Ferguson, P.A., *Accounting Implications of Proposed Statutory Changes for FIGA Assessments*, Jan. 2, 2013 (on file with the House Insurance and Banking Subcommittee).

Changes Proposed by the Bill

The bill provides that a FIGA assessment that is paid by an insurer under subparagraph (f)1., which is the procedure requiring a lump-sum payment from insurers before the assessment year begins, are paid *before* policy surcharges are collected and results in a receivable for surcharges that will be collected in the future. The amount is an admissible asset¹⁸ under SAP, to the extent the receivable is likely to be realized. This codifies a practice of the OIR,¹⁹ and eliminates the negative effect guaranty fund assessments have on statutory surplus. The bill requires the insurer to establish and record the asset separately from the liability and to reduce the amount recorded if it cannot be fully recouped because of a reduction in writings or withdrawal from the market.

For assessments that are paid *after* policy surcharges are collected, pursuant to the monthly installment option created by the bill, recognition of assets is based on actual premium written offset by the obligation to FIGA.

Insurance Premium Tax

Florida requires insurance companies to pay tax on:²⁰

- Insurance premiums;
- Premiums for title insurance;
- Assessments, including membership fees, policy fees, and gross deposits received from subscribers to reciprocal or interinsurance agreements; and
- Annuity premiums or considerations.

Florida applies the premium tax to premiums written in Florida at the following rates:²¹

- Gross property and casualty premiums, less reinsurance and returned premiums; life premiums; accident and health premiums; and prepaid limited health premiums, 1.75 percent.
- Commercial self-insurance; group self-insurance; medical malpractice self-insurance; and assessable mutual insurance, 1.6 percent.
- Annuities, 1 percent.

The law authorizes numerous insurance premium tax credits and deductions that allow insurance companies to reduce their premium tax liability.²² The state distributes revenue from the insurance premium tax to the General Revenue Fund.²³

Regular assessments levied by FIGA for insolvencies occurring on or after July 1, 2010 are considered premium for premium tax purposes and thus subject to the premium tax.²⁴ Emergency assessments levied by FIGA, however, are exempt.²⁵

Changes Proposed by the Bill

The bill repeals current law subjecting FIGA regular assessments to the premium tax. Thus, regular assessments will be treated like emergency assessments and exempt from the premium tax.

B. SECTION DIRECTORY:

Section 1: Amends s. 631.54, F.S., relating to definitions.

¹⁸ NAIC Statement of Statutory Accounting Principles No. 4.

¹⁹ OFFICE OF INSURANCE REGULATION, Supplemental Memorandum to Information Memorandum OIR-06-023M (Dec. 1, 2006).
<http://www.flor.com/siteDocuments/SupplementalMemo.pdf> (last visited Feb. 18, 2015).

²⁰ s. 624.509(1), F.S.

²¹ ss. 624.46226, 624.4625, 624.475, 624.509(1), and 627.357, F.S.; *see also* FLORIDA REVENUE ESTIMATING CONFERENCE, 2014 Florida Tax Handbook, available at <http://www.edr.state.fl.us/Content/revenues/reports/tax-handbook/index.cfm> (last visited Feb. 18, 2015).

²² Credit for payments to the Municipal Firefighters' Pension Fund (s. 175.141, F.S.) and Municipal Police Officers' Retirement Fund (s. 185.12, F.S.); Corporate Income Tax Credit (s. 624.509(4), F.S.); Florida Employees' Salary Credit (s. 624.509(5), F.S.); New Markets Tax Credit (s. 288.9916, F.S.); Capital Investment Tax Credit (s. 220.191, F.S.); Community Contribution Tax Credit (s. 624.5105, F.S.); Child Care Tax Credit (s. 624.5107, F.S.); Credit for Contributions to Scholarship-Funding Organizations (s. 624.51055, F.S.); Credit for Workers' Compensation Assessments (440.51, F.S.); and Credit for Florida Life and Health Insurance Guaranty Association Assessments (s. 631.72, F.S.).

²³ s. 624.509(3), F.S.

²⁴ s. 631.57(3)(g), F.S.

²⁵ s. 631.57(3)(e)1.e., F.S.

Section 2: Amends s. 631.57, F.S., relating to powers and duties of FIGA.

Section 3: Amends s. 631.64, F.S., relating to recognition of assessments in rates.

Section 4: Amends s. 627.727, F.S., relating to motor vehicle insurance; uninsured and underinsured vehicle coverage; insolvent insurer protection, to conform a cross reference.

Section 5: Amends s. 631.55, F.S., relating to creation of the association, to conform a cross reference.

Section 6: Provides an effective date of July 1, 2015.

II. FISCAL ANALYSIS & ECONOMIC IMPACT STATEMENT

A. FISCAL IMPACT ON STATE GOVERNMENT:

1. Revenues:

Because the bill repeals current law subjecting FIGA regular assessments to the insurance premium tax, the state may lose premium tax income under the bill. The decrease may be partially offset by retaliatory taxes paid by insurers domiciled outside of Florida, but doing business in Florida, to the extent that the tax obligations of those insurers in Florida are reduced below the tax obligation in their state of residence. The specific amount of lost revenue is unknown until the Revenue Estimating Conference opines on the impact.

It is not clear how the new collection procedure may affect FIGA cash flow or its ability to project the amount of an assessment that may be necessary to meet its statutory obligations. Today, the amount of an assessment is fixed at the time it is levied and FIGA can budget based on that amount, subject to any exemptions that may be granted. The bill still provides for advance payments based on the prior year's net direct written premiums, but it creates a reconciliation process that would have insurers pay all excess amounts to FIGA and have FIGA credit insurers any shortfalls in collections against future assessments. Further, the bill extends an assessment to insurers who did not write the affected line of insurance in the preceding year, which will result in collections from policyholders which were not factored into the assessment percentage. Thus, the value of the assessment is not fixed until after collections are recouped from policyholders.

2. Expenditures:

None.

B. FISCAL IMPACT ON LOCAL GOVERNMENTS:

1. Revenues:

None.

2. Expenditures:

None.

C. DIRECT ECONOMIC IMPACT ON PRIVATE SECTOR:

Under current law, the assessment levied is based on an insurer's premiums in the calendar year preceding the assessment and the total value of the assessment is fixed at the time it is paid. The insurer recoups the amount from its policyholders by applying a separate recoupment factor, which the insurer selects based on the probability that it will recoup the amount paid. If an insurer writes less in the current year than the prior year, it will have to recoup the full amount from fewer policyholders. If an insurer collects more than it paid, the excess is either paid to FIGA or refunded to policyholders, depending on the amount of the excess. An insurer that did not write the type of insurance subject to the assessment in the prior year, but is currently writing it, is not subject to the assessment. Thus, its policyholders do not pay toward the assessment at all.

The bill establishes a uniform assessment percentage that is to be recouped from all policyholders and extends an assessment to insurers who did not write in the calendar year preceding the assessment. This means that policyholders will all pay the same percentage toward the assessment regardless of any changes in market conditions, for example, if the insurer's market share or rates increase or decrease. The insurer has no discretion to adjust the percentage. If the amount collected (paid by policyholders) is higher than the amount needed to offset the assessment, the excess would be paid to FIGA. The bill does not authorize a refund to policyholders.

D. FISCAL COMMENTS:

The bill's clarification of statutory accounting for FIGA assessments should mitigate the impact of assessments on an insurer's financial statement.

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 provided by the bill.

C. DRAFTING ISSUES OR OTHER COMMENTS:

Lines 155 – 156 refer to emergency assessments used to defease bonds issued “under this part,” which would include bonds issued for insolvencies unrelated to a hurricane. Currently, the law permits FIGA to levy emergency assessments only to address hurricane-related insolvencies. Thus, the reference to “part” should be restored to “paragraph.”

Line 205 refers to “emergency assessments” pursuant to paragraph (a) or paragraph (e). Assessments pursuant to paragraph (a) are “regular” assessments, thus “emergency” should be removed.

Lines 259 – 282 describes a monthly installment payment option that FIGA may use for collecting regular or emergency assessments. It is unclear how this relates to the monthly payment option currently in law for use, at FIGA's discretion, for payment of emergency assessments, only. The newly-created monthly installment process may only be used if FIGA has adequate cash on hand to pay six months of claims; this requirement does not apply to the current monthly installment procedure. Lines 266 – 268 authorize the FIGA board to recommend “the assessment percentage that may be collected as a monthly assessment.” It is not clear if this is a percentage that is intended to be different from the uniform percentage described earlier in the bill and on line 272.

Lines 299 – 301 creates a new paragraph (i) within subsection (3). The first sentence states that assessments “under this subsection,” which would include regular and emergency assessments, are not subject to the premium tax. The paragraph continues with additional provisions related to emergency assessments, only. To eliminate doubt regarding intent, it may be appropriate to put the language related to the premium tax and the language related to emergency assessments in separate paragraphs.

IV. AMENDMENTS/ COMMITTEE SUBSTITUTE CHANGES

On March 3, the Insurance & Banking Subcommittee adopted one amendment and reported the bill favorably as a committee substitute. The amendment removed one of two deadlines for filing the reconciliation report which conflicted with each other. The remaining deadline is 90 days after the end of the assessment year.

The staff analysis is drafted to reflect the committee substitute as passed by the Insurance & Banking Subcommittee