

## HOUSE OF REPRESENTATIVES STAFF ANALYSIS

**BILL #:** HB 1127 Citizens Property Insurance Corporation

**SPONSOR(S):** Albritton

**TIED BILLS:** **IDEN./SIM. BILLS:** SB 1346

| REFERENCE   | ACTION | ANALYST  | STAFF DIRECTOR or<br>BUDGET/POLICY CHIEF |
|---|--------|----------|--|
| 1) Insurance & Banking Subcommittee                     |        | Callaway | Cooper                                   |
| 2) Government Operations Appropriations<br>Subcommittee |        |          |  |
| 3) Economic Affairs Committee                           |        |          |  |

### SUMMARY ANALYSIS

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 November 30, 2011, Citizens is the largest property insurer in Florida with almost 1.5 million policies extending over \$515 billion of property coverage to Floridians. Citizens writes various types of property insurance coverage for its policyholders. The types of coverage are divided into three separate accounts within the corporation: the Personal Lines Account, the Commercial Lines Account, and the Coastal Account.

In the event Citizens incurs a deficit, the corporation can levy assessments on most of Florida's property and casualty insurance policyholders in the following sequence set by statute:

1. Citizens Policyholder Assessments: Citizens assess its policyholders of up to 15% of premium per account in deficit, for a maximum total of 45%.
2. Regular Assessments: Upon the exhaustion of the Citizens Policyholder Assessment for a particular account, Citizens levies a regular assessment of up to 6% of premium or 6% of the deficit per account, for a maximum total of 18%. The regular assessment is levied on virtually all property and casualty policies in the state, but is not levied on Citizens' policies.
3. Emergency Assessments: Upon the exhaustion of the Citizens Policyholder Assessment and regular assessment for a particular account, Citizens levies an emergency assessment of up to 10% of premium or 10% of the deficit per account, for a maximum total of 30%. 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.

The bill eliminates the regular assessment for the Personal Lines Account and the Commercial Lines Account and reduces the assessment amount for the Coastal Account from 6% to 2%. The bill does not change the amount of or collection process for the Citizens Policyholder Surcharge. The bill also does not change the amount of or collection process for the emergency assessment, but specifies the Office of Insurance Regulation (OIR) cannot order policyholders to pay this assessment sooner than 90 days after Citizens levies the assessment. The bill also extends the time period limited apportionment companies have to pay a regular assessment to Citizens from 12 months to 15 months. Generally, limited apportionment companies are property insurers with less than \$25 million in surplus.

The bill has no fiscal impact on state or local governments, but does impact the private sector. For example, the bill increases the amount of assessments paid by Citizens' policyholders. It prevents a drain on the surplus of property insurers in the private market caused by the insurers having to prepay a Citizens' regular assessment and recoup it from policyholders over the following year. Citizens may issue more pre-event and post-event bonds than it does currently to ensure the corporation has sufficient cash to pay claims as the corporation will no longer receive the quick influx of cash the regular assessment levy provides. A more detailed fiscal impact on the private sector is provided in the Fiscal Analysis.

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: h1127.INBS

DATE: 1/22/2012

# FULL ANALYSIS

## I. SUBSTANTIVE ANALYSIS

### A. EFFECT OF PROPOSED CHANGES:

#### **Background**

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 November 30, 2011, Citizens is the largest property insurer in Florida with almost 1.5 million policies extending over \$515 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.

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.

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.

In the event Citizens incurs a deficit (i.e., its obligations to pay claims exceeds its capital plus reinsurance recoveries), it can levy assessments on most of Florida's property and casualty insurance policyholders in a specific sequence set by statute.<sup>4</sup> The three Citizens' accounts calculate deficits and resulting assessment needs independently, so assessments can be levied when any one or more of the three Citizens' accounts has a deficit.

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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.

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

The Citizens' assessment scheme is as follows:

1. 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> This surcharge is collected over twelve months and is collected at the time a new Citizens' policy is written or an existing Citizens' policy is renewed.
2. Regular Assessments: Upon the exhaustion of the Citizens Policyholder Assessment for a particular account, Citizens levies 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. Mechanically, property casualty insurers with policies subject to the regular assessment "front" the assessment to Citizens and recover it from their policyholders at the issuance of a new policy or at renewal of existing policies. Thus, Citizens will collect funds raised by a regular assessment quickly after the assessment is levied, usually within 30 days after levy.
3. Emergency Assessments: Upon the exhaustion of the Citizens Policyholder Assessment and regular assessment for a particular account, Citizens levies 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. Mechanically, property and casualty insurers with policies subject to the emergency assessment collect the assessment from policyholders at the issuance of a new policy or at renewal of existing policies and then remit the assessments periodically to Citizens. Thus, Citizens will not collect funds raised by an emergency assessment immediately after the assessment is levied but will collect funds intermittently throughout the collection period as policies are renewed and new policies written.

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 \$6.5 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 \$12.775 billion.<sup>9</sup>

As of November 30, 2011, Citizens' total exposure is over \$515 billion. Citizens estimates the 1-in-100 year hurricane would cost over \$23.2 billion.<sup>10</sup> The \$10.4 billion difference between Citizens' resources to pay claims (\$12.775 billion) and its 1-in-100 year exposure (\$23.2 billion) would be covered by assessments levied by Citizens on its own policyholders and on policyholders of most property and casualty insurance. Specifically, Citizens is able to assess the following maximum amounts with their current assessment authority:

1. Citizens Policyholder Surcharge – approximately \$1.172 billion (\$391 million for the Coastal Account and \$781 million for the PLA/CLA).
2. Regular Assessment – approximately \$5.580 billion (\$1.860 billion for the Coastal Account and \$3.720 billion for the PLA/CLA).

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<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>Data as of July 13, 2011. Information on file with the Insurance & Banking Subcommittee.

<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 \$16.5 billion to pay claims during the 2011 hurricane season.

<sup>10</sup> A 1-in-100 year hurricane has a 1% probability of occurring. Information obtained from Citizens' presentation to the Financial Services Commission dated November 1, 2011.

3. Emergency Assessment –Unlimited maximum assessment in the aggregate because the length of the assessment is not limited. However, yearly assessments are limited to 10% of premium or 10% of the deficit per account.

### **Effect of Proposed Changes**

The bill eliminates the regular assessment for the PLA and CLA and reduces the assessment amount for the Coastal Account from 6% to 2%. The bill does not change the amount of or collection process for the Citizens Policyholder Surcharge. The bill also does not change the amount of or collection process for the emergency assessment, but specifies the Office of Insurance Regulation (OIR) cannot order policyholders to pay this assessment sooner than 90 days after Citizens levies the assessment. No time frame is given in current law for the OIR to order payment of emergency assessments. Nevertheless, for the emergency assessment levied by Citizens in 2007 due to losses from the 2005 hurricanes, Citizens requested, and OIR approved, a start date for the levy of emergency assessments over six months after the date the levy was requested and approved.<sup>11</sup>

The bill also makes revisions designed to assist Citizens in the promulgation and collection of assessments. The bill authorizes Citizens' Board of Governors to levy Citizens Policyholder Surcharges and regular and emergency assessments upon their projection that a Citizens' account will incur a deficit. Current law requires the Citizens' account to actually incur a deficit prior to the levy of the Citizens Policyholder Surcharge or assessments.

Under current law, a limited apportionment property insurance company<sup>12</sup> must pay the regular assessment to Citizens within 12 months after Citizens levies the assessment. Generally, limited apportionment companies are property insurers with less than \$25 million in surplus. All other types of insurers subject to the regular assessment pay the assessment amount to Citizens within 30 days after Citizens levies the assessment. The bill extends the time period limited apportionment companies have to pay a regular assessment to Citizens from 12 months to 15 months. Because regular assessments for the PLA and CLA are eliminated by the bill, the 15 month payment timeframe would apply to only regular assessments for the Coastal Account.

### **B. SECTION DIRECTORY:**

**Section 1:** Amends s. 627.351, F.S., relating to Citizens Property Insurance Corporation.

**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.

#### **2. Expenditures:**

None.

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<sup>11</sup>Due to the 2005 hurricanes, Citizens sustained a deficit of almost \$1.8 billion. In the 2006 Legislative Session, the Legislature appropriated \$715 million to defray the Citizens' deficit associated with the 2005 hurricanes, making the deficit amount passed on to property owners in Florida over \$887 million. To cover the deficit, in addition to a one-time regular assessment of 2.04%, Citizens levied an emergency assessment 1.4% for 10 years. Citizens requested the emergency assessment levy on December 7, 2006 and the OIR approved the levy on January 1, 2007. The start date of the levy, as stated in the request and approved by the OIR, was July 1, 2007. On July 1, 2011 the 1.4% assessment amount was reduced to 1% due to an increase in the assessment premium base.

(see <http://www.flor.com/sections/pandc/CitizensEmergencyAssessment.aspx>; OIR 11-03M (Informational Memorandum issued by OIR April 4, 2011 available at <http://www.flor.com/Office/Memoranda/index.aspx>)).

<sup>12</sup>Generally, a limited apportionment insurance company is an insurer with a surplus of \$25 million or less writing 25% or more of its total countrywide property insurance premiums in Florida. (see s. 627.351(6)(c)13., F.S.)

## B. FISCAL IMPACT ON LOCAL GOVERNMENTS:

### 1. Revenues:

None.

### 2. Expenditures:

None.

## C. DIRECT ECONOMIC IMPACT ON PRIVATE SECTOR:

The elimination of regular assessments for the PLA and CLA and the reduction of these assessments for the Coastal Account impacts Citizens' policyholders because they could pay more in assessments under than bill than under current law. Because regular assessments are eliminated for the PLA and CLA and reduced for the Coastal Account and the Citizens Policyholder Surcharge is unchanged, if a deficit occurs, amounts that would be collected by regular assessments to offset the deficit will no longer be collected (or will be reduced for Coastal Account deficits). Thus, the deficit amount that must be collected with emergency assessments is potentially greater than it would be under current law, leading to a larger emergency assessment or a longer assessment levy. Citizens' policyholders pay only the Citizens Policyholder Surcharge and the emergency assessment. Consequently, if there is a larger emergency assessment, then Citizens' policyholders could pay more in emergency assessments or could pay emergency assessments for a longer period under the bill than they would under current law. However, if all three Citizens' accounts levied assessments in the first year after a storm, under the bill, a Citizens' policyholder would pay less in assessments for that year due to the bill's reduction of the regular assessment in the Coastal Account and elimination of the regular assessment in the PLA and CLA, which are paid for one year only. But, in this scenario, the Citizens' policyholder would likely pay assessments over a longer period of time under the bill than under current law because the amount of deficit to be cured with emergency assessments would be larger and the time period emergency assessments can be levied is not limited.

The timing of payment of Citizens' assessments by non-Citizens' policyholders will change under the bill. Non-Citizens' property and casualty policyholders have assessments spread out over multiple years under the bill because the amount they would pay in regular assessments under current law, which is paid in one year, is transferred to emergency assessments, which are paid over multiple years. However, the total assessment amount to be paid by non-Citizens' policyholders should not change under the bill, just the timing of the payment changes.

The bill allows limited apportionment property insurance companies three additional months to pay regular assessments, from 12 months after the assessment is levied, to 15 months.

Because the bill eliminates regular assessments in the PLA and CLA, property insurers would not have to prepay these assessments up front to Citizens and recover the amount prepaid from their policyholders. Similarly, because the bill reduces the maximum regular assessment percentage in the Coastal Account, the amount prepaid by insurers for this assessment is lower than under current law. Accordingly, the drain on insurer surplus from having to prepay regular assessments up front and collecting the assessments over a year from policyholders is avoided for the PLA and CLA and reduced for the Coastal Account.

In addition, a 2011 change to statutory accounting principles relating to how regular assessments are treated on an insurer's financial statement now negatively impacts some insurer's net worth.<sup>13</sup> The bill reduces that impact. Most insurers produce financial statements using both statutory and generally accepted accounting principles. Insurer financial information prepared in accordance with Generally Accepted Accounting Principles (GAAP) are typically used by investors, whereas, insurer financial information prepared in accordance with statutory accounting is used by the OIR. Citizens' levy of regular assessments reduces an insurer's net worth under both statutory and GAAP accounting. Under

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<sup>13</sup> The changes to the statutory accounting principles that negatively impact insurer net worth paying regular assessments to Citizens were effective January 1, 2011.

both GAAP and statutory accounting, insurers incur a liability in the form of a direct charge to surplus (i.e., a loss in surplus) in the amount of the regular assessment when the company is billed for the assessment. However, GAAP and statutory accounting treat an asset to offset that liability differently. Under GAAP accounting, the full regular assessment paid by the insurer to Citizens is a direct charge to surplus (i.e. reduces surplus) and there is no an offsetting asset allowed, which immediately reduces the insurer's net worth in the amount of the assessment. Under statutory accounting, however, the full regular assessment is also a direct charge to surplus, but there is an offsetting asset that is included on the insurer's financial statement when the assessment is paid to Citizens.<sup>14</sup> Limited apportionment companies are allowed 12 months to pay a regular assessment to Citizens, so these companies can incur a direct charge to surplus with an offsetting asset incrementally booked over a 12 month period, decreasing the net worth of the insurer until the offsetting asset is booked in full.

The bill's elimination of the regular assessment for the PLA and CLA will prevent the impact on insurer net worth associated with the assessments. The reduction of the regular assessment for the Coastal Account will reduce the impact on insurer net worth. Insurers who are not limited apportionment companies pay the regular assessment within 30 days of levy, so their net worth is not impacted as much by the accounting principles. Citizens' emergency assessments are treated the same under statutory and GAAP accounting and are not a direct charge to an insurer's surplus, thus do not impact an insurer's net worth.

Representatives from Citizens state the bill will not have a negative impact on the corporation's ability to timely pay claims in the event of a hurricane that triggers emergency assessments. Because Citizens will no longer collect assessments from insurers within 30 days of a levy and instead will collect assessments as they are paid by policyholders throughout the year, in order to obtain liquidity needed to pay claims in the event of a hurricane, Citizens may issue more pre-event bonds than is currently issued. The bond proceeds would be invested by Citizens and the interest income used to pay the debt service on the bonds. However, if the interest income earned is not enough to pay the debt service, Citizens would use surplus to pay the difference. Surplus is used to pay claims, so if surplus is used for debt service, less is available to pay claims.

Because the bill eliminates the regular assessment for the PLA and CLA, Citizens no longer has a source for a quick influx of cash to pay claims (i.e., regular assessments paid by insurers within 30 days of levy) and may instead obtain cash to pay claims after a hurricane by issuing post-event bonds supported by emergency assessments paid over multiple years. If the Florida Hurricane Catastrophe Fund is also issuing post-event bonds to raise additional funds to pay their claims after a hurricane, then both entities could receive less favorable bonding terms which, in turn, results in higher assessments levied by both entities to support the debt service on the bonds.

#### D. FISCAL COMMENTS:

Insurers having to prepay regular assessments up front to Citizens could imperil the solvency of insurers that do not have sufficient funds on hand or the ability to borrow the funds to pay the regular assessment to Citizens. If an insurer becomes insolvent, it cannot pay the claims filed by its own policyholders and the Florida Insurance Guaranty Fund (FIGA) would likely take over the insurer and pay its claims. To raise funds to pay claims of insolvent insurers, FIGA can levy regular and emergency assessments against property and casualty insurers which are passed through to policyholders to raise funds to pay claims.

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<sup>14</sup> Prior to January 1, 2011, insurers were allowed to book an offsetting asset of an account receivable to the direct charge to surplus from a regular assessment when the charge was booked, rather than waiting to book the offsetting asset when the assessment is paid by the insurer.

### **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 in the bill and none repealed by the bill.

#### **C. DRAFTING ISSUES OR OTHER COMMENTS:**

Representatives from the OIR report that some non-admitted property and casualty insurers have cited the requirement that insurers prepay the regular assessment up front to Citizens as the reason they have chosen not to write residential property insurance in Florida.

Representatives from multiple Florida admitted insurance companies assert the requirement that property and casualty insurers with policies subject to the regular assessment prepay the assessment to Citizens up front and subsequently recoup it from their policyholders may delay the ability of some insurers to timely pay claims of their own policyholders.

Allowing Citizens to levy surcharges and assessments upon a projection by the Citizens Board of Governors that a deficit exists in a Citizens account will allow Citizens to begin the process of collecting those levies at an earlier time than under current law.

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