

HOUSE OF REPRESENTATIVES STAFF ANALYSIS

BILL #: HB 983 Windstorm Insurance Coverage
SPONSOR(S): Ross
TIED BILLS: **IDEN./SIM. BILLS:** SB 2784

REFERENCE	ACTION	ANALYST	STAFF DIRECTOR
1) <u>Committee on Insurance</u>	<u>14 Y, 0 N</u>	<u>Callaway/Topp</u>	<u>Overton</u>
2) <u>Jobs & Entrepreneurship Council</u>	<u></u>	<u>Callaway/Topp</u>	<u>Thorn</u>
3) <u>Policy & Budget Council</u>	<u></u>	<u></u>	<u></u>
4) <u></u>	<u></u>	<u></u>	<u></u>
5) <u></u>	<u></u>	<u></u>	<u></u>

SUMMARY ANALYSIS

This bill creates a new program for windstorm insurance coverage. The new program, the Florida Windstorm Insurance Program (Program or Windstorm Program), is created within the Florida Hurricane Catastrophe Fund (FHCF) to provide windstorm coverage for non-commercial residential property (e.g. homes, mobile homes, tenants, condominium unit owners, but not condominium associations or apartments). The creation of this Program does not preclude private insurers from providing windstorm coverage for non-commercial residential property as they do under current law. The FHCF will continue to provide reinsurance coverage for commercial residential property (e.g. condominium associations, cooperative associations) with private insurers providing direct windstorm coverage for these properties.

Insurers writing windstorm coverage on non-commercial residential property are given a choice as to whether to participate in the Program. Citizens Property Insurance Corporation (Citizens) must participate in the Program. If an insurer chooses to participate in the Windstorm Program, the Program will cover the windstorm risk on the policies. The participating insurer will cover the non-windstorm risk on the policies.

The premium rate the Program charges for windstorm coverage will be set annually by unanimous vote of the State Board of Administration (SBA). The Program rates must be as close as possible to the actuarially indicated rate for each participating insurer's exposure to windstorm, but also must take into account the state's need to restore or maintain affordability for consumers, the cost of reinsurance, and financial alternatives to reinsurance. The bill limits coverage under the Program to the first \$2 million of structural loss. In addition, any residential property insured by the windstorm program which sustains a total loss at least three times in any 10 year period is no longer eligible for coverage under the Program.

If the FHCF or the Program incurs a deficit, the FHCF is authorized to levy emergency assessments to defray the deficit. Under the bill, starting June 1, 2010, the assessments are levied only on all personal lines and commercial lines policies providing property insurance coverage, including policies issued by the Program. However, property insurers not participating in the Program cannot be assessed for FHCF or Program deficits.

Effective June 1, 2009, Citizens cannot issue or renew personal lines residential windstorm-only policies. Instead, the Windstorm Program will issue the windstorm policy on the property.

The bill lowers the maximum amount the FHCF reimburses for losses from \$15 billion to \$3 billion. It also lowers the retention/deductible of the FHCF from \$4.5 billion to \$1 billion.

The bill is effective "upon becoming a law."

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

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FULL ANALYSIS

I. SUBSTANTIVE ANALYSIS

A. HOUSE PRINCIPLES ANALYSIS:

Provide limited government: The bill creates a new program within the Florida Hurricane Catastrophe Fund to insure windstorm risks in Florida.

Safeguard individual liberty: The bill allows private insurance companies to choose to participate in the Windstorm Program. Those companies who choose to participate in the Program will be responsible for only the non-windstorm related risks on their property insurance policies.

Promote personal responsibility: The bill allows private insurance companies to choose to participate in the Windstorm Program. Those companies who choose to participate in the Program will be responsible for only the non-windstorm related risks on their property insurance policies.

B. EFFECT OF PROPOSED CHANGES:

This bill creates a new program for windstorm insurance coverage. The new program, the Florida Windstorm Insurance Program (Program or Windstorm Program), is created within the Florida Hurricane Catastrophe Fund (FHCF). The purpose of the Program is to provide windstorm coverage for non-commercial residential property (e.g. homes, mobile homes, tenants, condominium unit owners, but not condominium associations or apartments). The creation of this Program does not preclude private insurers from providing windstorm coverage for non-commercial residential property as they do under current law. The FHCF will continue to provide reinsurance coverage for commercial residential property (e.g. condominium associations, cooperative associations) with private insurers providing direct windstorm coverage for these properties.

The Program will be a direct insurer of windstorm, meaning it will pay windstorm claims covered under the Program directly to policyholders. Under current law the Florida Hurricane Catastrophe Fund acts as a reinsurer for insurers covering windstorm risks on residential property, meaning it reimburses insurers who pay windstorm claims up to a set level after the insurer incurs a deductible.

Insurers writing windstorm coverage on non-commercial residential property are given a choice as to whether to participate in the Program. Citizens Property Insurance Corporation (Citizens) must participate in the Program. If the insurer chooses to participate in the Program their entire book of business must participate; the insurer cannot pick and choose which properties they want covered for windstorm under the Program.

If an insurer chooses to participate in the Windstorm Program, the Program will cover the windstorm risk on the policies. This means the program will pay claims resulting from wind, wind gusts, hail, rain, tornadoes, cyclones, tropical storms, or hurricanes, but not flood, storm surge, or rising water. Losses to the insured structure, contents, additional living expenses, emergency debris removal, and temporary repairs after loss are paid under the Program. The participating insurer will cover the non-windstorm risk on the policies, such as fire, theft, and liability. Thus, if there is a claim resulting from a windstorm event, the Program, rather than the insurer, will pay the claim. If there is a claim resulting from fire, theft, liability, or any other non-windstorm event, the insurer will pay the claim.

Insurers that participate in the Program must collect premiums for the windstorm coverage written by the Program, administer the Program windstorm policy, and process the windstorm claims. The Windstorm Program pays the windstorm claims directly to the homeowner and reimburses the private insurer for administrative and claims costs attributable to the Program, such as loss adjustment expenses, acquisition costs, litigation costs, and judgments.

The premium rate the Program charges for windstorm coverage will be set annually by unanimous vote of the State Board of Administration (SBA), after reviewing recommendations from an independent consultant. A public hearing is required before the SBA can adopt a rate plan. The Program rates must be as close as possible to the actuarially indicated rate for each participating insurer's exposure to windstorm, but also must take into account the state's need to restore or maintain affordability for consumers, the cost of reinsurance, and financial alternatives to reinsurance. Program rates are subject to the general requirement of section 627.062 prohibiting excessive, inadequate, or unfairly discriminatory rates, and are also subject to the residential property insurance rate standards of section 627.0629 (e.g. mitigation discounts). In addition to these standards, the Program's rate plan is required, at a minimum, to produce annual premium revenue equal to the modeled statewide average annual insured windstorm loss, plus expenses.

If the balance in the Florida Hurricane Catastrophe Fund is ever below \$1 billion, the SBA may include a rapid cash buildup factor in the Program rates. This factor cannot be more than 25 percent.

The rate plan adopted by the SBA is not subject to regulatory review or approval by the Office of Insurance Regulation (OIR), but is considered final agency action of the SBA and thus subject to judicial review under section 120.68 in the same manner as other final agency actions, except that judicial review must be sought in the First District Court of Appeal, regardless of where any party resides.

Personal lines residential windstorm rates of insurers that do not participate in the Windstorm Program remain subject to regulation by the OIR, but can be disapproved only if they are inadequate or unfairly discriminatory. They cannot be disapproved if they are excessive, which current law allows.

The State Board of Administration, by rule, must establish Program policy forms and Program deductibles; Program discounts, including mitigation discounts; Program agent compensation; Program surcharges; and Program credits. The bill limits coverage under the Program to the first \$2 million of structural loss, meaning this is the policy limit on the policy. Coverage limits for contents, additional living expenses, emergency debris removal, and temporary repairs after loss must be set by the SBA. By law, any residential property insured by the Windstorm Program which sustains a total loss at least three times in any 10 year period is no longer eligible for coverage under the Program.

Once an insurer decides to participate in the Windstorm Program, the insurer enters into a 5 year contract with the Program. Under the contract, the insurer agrees:

1. To collect premiums for windstorm coverage as established by the Program, and to apply deductibles, discounts, surcharges, credits, and limits as established by the Program.
2. To administer the windstorm coverage under a separate windstorm policy issued by the Windstorm Program, and to provide the Windstorm Program policy to each of the insurer's personal lines residential property policyholders.
3. To comply with Program rules as to underwriting determinations; cancellation and nonrenewal; and agent compensation.
4. To provide application processing, premium processing claims processing, and adjusting services in accordance with Program rules.

Participating Windstorm Program insurers will be audited yearly to ensure they are in compliance with the Program's requirements. The Program requires the insurer to have a fiduciary duty to the Program to fairly adjust claims and allocate losses between windstorm and non-windstorm perils. The Program can suspend an insurer's eligibility for future participation in the Program for up to five years if the insurer fails to honor its fiduciary duty or fails to substantially comply with Program requirements. The Program can also recover actual damages plus a 50 percent maximum penalty or can recover liquidated damages.

Under the Program, the SBA is required to procure reinsurance or use other financial alternatives to transfer at least 50 percent of the risk of loss between the Program's 50-year probable maximum loss (PML) and the Program's 100-year probable maximum loss. Also, the Program must cover via reinsurance or other financial risk transfer alternatives at least the first 50 percent of the losses between the 100-year PML and the 250-year PML. The requirement to purchase reinsurance may be suspended or modified by a unanimous vote of the State Board of Administration after a public hearing. The SBA is required to provide an annual report to the Legislature regarding reinsurance and financial alternatives.

If the FHCF or the Program incurs a deficit, the FHCF is authorized to levy emergency assessments to defray the deficit. Under the bill, starting June 1, 2010, the assessments are levied only on all personal lines and commercial lines policies providing property insurance coverage, including policies issued by the Program. However, property insurers not participating in the Program cannot be assessed for FHCF or Program deficits. Under current law, if the FHCF incurs a deficit, emergency assessments can be levied on all property and casualty lines of business except workers' compensation, medical malpractice, accident, health, and flood. Thus, the bill diminishes the assessment base of the FHCF as of June 1, 2010.¹

The bill changes the FHCF assessment amount. The FHCF uses emergency assessments to fund revenue bonds which are issued by the FHCF when there is a deficit in it. Under current law, FHCF annual assessments are capped at 6 percent of premium with respect to losses from any one year and a maximum of 10 percent of premium to fund hurricane losses from multiple years. Beginning June 1, 2010, the maximum yearly assessment amount to fund deficits in the Program or in the FHCF is 10 percent of gross written premium for personal and commercial lines property insurance coverage. If the 10 percent assessment is not sufficient to defray the deficit, an additional assessment can be imposed. The maximum amount of the additional assessment is 10 percent of the deficit. As with the current FHCF assessment structure, insurers would collect the assessments on behalf of the State.

Effective June 1, 2009, Citizens cannot issue or renew personal lines residential windstorm-only policies. Instead, the Windstorm Program will issue the windstorm policy on the property as the bill requires Citizens to participate in the Program.

The bill requires Citizens to package all its existing policies into balanced blocks of business and auction them off to private insurers. The winning insurer would either have an exclusive 60-day right to offer coverage to the Citizens policyholder for non-windstorm perils when the Citizens policy expires or the right to assume coverage of the property for non-windstorm perils before the Citizens policy expires. The proceeds of these auctions would become capital contributions to the Windstorm Program.

Additionally, starting June 1, 2009, Citizens is prohibited from writing or renewing a personal lines residential property policy if the policyholder receives an offer of coverage from a private insurer participating in the Windstorm Program.

By December 31, 2010, Citizens is required to transfer a portion of its surplus to the Windstorm Program. The transfer amount is based on the ratio between Citizens' total insured value as of June 1, 2010 and Citizens' total insured value as of June 1, 2009.

The transition from the current insurance system with private insurers or Citizens writing the windstorm coverage on residential properties to the new Windstorm Program would be implemented between June 1, 2009 and May 31, 2010. Beginning June 1, 2009, the issuance or renewal of a non-commercial residential property policy by a participating insurer would include windstorm coverage provided by the Windstorm Program. During this period, a participating insurer would remain eligible for FHCF reinsurance to the extent that it, rather than the Windstorm Program, is liable for windstorm losses.

¹ For example, automobile, business, and marine insurance policies are not assessable under the bill, whereas, under current law, such policies are assessable.

Non-participating insurers would remain eligible for FHCF coverage through the end of the 2009 contract year (May 31, 2010), but would not thereafter be eligible for FHCF coverage for personal lines residential exposures. In order to allow for implementation on June 1, 2009, the State Board of Administration would be required to adopt forms, standards, and rates by January 1, 2009.

Changes to the Florida Hurricane Catastrophe Fund

The bill also makes changes to the structure and operation of the Florida Hurricane Catastrophe Fund (FHCF).

Starting June 1, 2009, the FHCF will no longer provide reinsurance coverage for personal lines residential policies. Although the FHCF will still be in existence after June 1, 2009, it will only reimburse losses incurred by private insurance companies for commercial lines residential property (e.g. condominium associations and apartment buildings).

The bill lowers the maximum amount the FHCF reimburses for losses. Under current law, the amount is \$15 billion adjusted annually based on the percentage growth in fund exposure, but not to exceed the dollar growth in the cash balance of the fund. Under the bill, the maximum amount the FHCF would reimburse insurers for claims is \$3 billion adjusted each year based on the exposure growth of the policies reinsured by the FHCF (commercial residential policies only).

The bill lowers the FCHF retention. Under current law, the FCHF retention is \$4.5 billion adjusted each year based on the FHCF's exposure. The bill lowers the retention to \$1 billion adjusted each year based on the exposure growth of the policies reinsured by the FHCF.

C. SECTION DIRECTORY:

Section 1: Amends s. 215.555 relating to the Florida Hurricane Catastrophe Fund.

Section 2: Creates an unnumbered section of law relating to the State Board of Administration; implementation of the Florida Windstorm Insurance Program.

Section 3: Amends s. 627.351 relating to insurance risk apportionment plans.

Section 4: Amends s. 627.712 relating to residential windstorm coverage required; availability of exclusions for windstorm or contents.

Section 5: Provides an effective date of "upon becoming a law".

II. FISCAL ANALYSIS & ECONOMIC IMPACT STATEMENT

A. FISCAL IMPACT ON STATE GOVERNMENT:

1. Revenues:

See fiscal comments.

2. Expenditures:

See fiscal comments.

B. FISCAL IMPACT ON LOCAL GOVERNMENTS:

1. Revenues:

None.

2. Expenditures:

None.

C. DIRECT ECONOMIC IMPACT ON PRIVATE SECTOR:

Since the wind premium charged by the Program is unknown, it is unknown whether individual policyholders will have higher or lower premiums than currently charged by the private market or Citizens. It is also unknown the amount of emergency assessments that may be charged to policyholders in the Program since such assessments are dependent on the extent of loss to the Program and the number of policies in the Program. Policyholders of insurers who opt out of the Program will not be subject to assessments by the Program.

D. FISCAL COMMENTS:

Since the number of insurers who will chose to participate in the Program is unknown the fiscal impact to state government of the bill is indeterminate. If a substantial number of insures participate in the program, the FHCF estimates that it could have significant costs to administer the Program.

The FHCF states that the narrowing of its assessment base by the bill could have an adverse effect on its ability to issue tax-exempt bonds.

III. COMMENTS

A. CONSTITUTIONAL ISSUES:

1. Applicability of Municipality/County Mandates Provision:

The mandates provision does not apply because this bill does not: require counties or municipalities to spend funds or to take an action requiring the expenditure of funds; reduce the authority that municipalities or counties 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:

By January 1, 2009, the State Board of Administration is required to adopt rules to implement the Florida Windstorm Insurance Program.

C. DRAFTING ISSUES OR OTHER COMMENTS:

The reduction of the FHCF's assessment base could jeopardize the tax-exempt status of the FHCF as the private ruling letter from the Internal Revenue Service granting tax-exempt status to the FHCF basing the exemption, in part, on the state's exercise of power to collect revenue by assessing non-participants in the FHCF.² Although the state will still be exercising its power to collect revenue by assessing non-participants in the FHCF, the number of non-participants to be assessed is reduced by the bill.

D. STATEMENT OF THE SPONSOR

No statement submitted.

IV. AMENDMENTS/COUNCIL SUBSTITUTE CHANGES

On March 13, 2008, the Committee on Insurance considered the bill, adopted five amendments, and reported the bill favorably. The amendments made the following changes to the bill:

- Specified that insurers not participating in the Windstorm Program are still assessable for deficits associated with the Florida Hurricane Catastrophe Fund.
- Removed the bill's provision requiring the SBA to set agent compensation amounts for Windstorm Program policies.
- Removed the bill's provision requiring the private insurers contracting with the Windstorm Program to comply with the Program rules relating to agent compensation.
- Required the Windstorm Program to pay acquisition costs of the private insurers participating in the Program at the usual and customary amount.
- Required Citizens to auction off only their personal lines residential policies, rather than all their policies.

² Private letter ruling relating to the Florida Hurricane Catastrophe Fund from the Internal Revenue Service dated November 21, 1994.