

## HOUSE OF REPRESENTATIVES STAFF ANALYSIS

**BILL #:** CS/HB 129 Sinkhole Coverage  
**SPONSOR(S):** Regulatory Affairs Committee; Raburn  
**TIED BILLS:** **IDEN./SIM. BILLS:** CS/SB 416

REFERENCE	ACTION	ANALYST	STAFF DIRECTOR or BUDGET/POLICY CHIEF
1) Insurance & Banking Subcommittee	13 Y, 0 N	Callaway	Cooper
2) Regulatory Affairs Committee	12 Y, 4 N, As CS	Callaway	Hamon

### SUMMARY ANALYSIS

A sinkhole is defined in law as a landform created by subsidence of soil, sediment, or rock as underlying strata are dissolved by groundwater. Catastrophic ground cover collapse is also defined in the law and is more severe than sinkhole loss. Florida law requires property insurers to cover only catastrophic ground cover collapse, rather than all sinkhole loss, in the base property insurance policy. But, insurers must also offer policyholders, for an appropriate additional premium, sinkhole loss coverage.

If a covered building suffers a sinkhole loss, the policyholder must repair the damage using the repair method recommended by the insurer's professional engineer. But, if repairs cannot be completed within policy limits, the insurer can pay to complete the repairs or tender policy limits without a reduction for any repair expenses incurred. A sinkhole repair contract must be entered into within 90 days after the policyholder is notified that the insurer confirms a sinkhole loss and the repairs must be completed within 12 months, with limited exceptions. Although current law requires the homeowner to repair property affected by a verified sinkhole, oftentimes the sinkhole claim is settled before repair work is started. Homeowners that settle sinkhole claims are not required to use claim settlements to repair or remediate the home and land.

Citizens Property Insurance Corporation (Citizens) has proposed a voluntary sinkhole managed repair program to ensure property insured by the corporation and damaged by a sinkhole is repaired. The program is not yet operational. If a policyholder participates in the program, once it is determined sinkhole stabilization services are needed, the policyholder chooses a vendor in the program to provide the services. Vendors in the program are experienced, credentialed and meet minimum qualifications determined by Citizens. Vendors give a five year warranty on repair work done. Citizens periodically remits payment for work completed to the vendor directly and the policyholder does not directly receive any payment for the sinkhole claim. The bill creates a Citizens Sinkhole Repair Program to be operational by March 31, 2015 to ensure sinkhole repairs are done by approved repair contractors. The repair program created by the bill is substantially similar to the proposed voluntary program. The primary difference between the sinkhole repair programs is that participation in the program created by the bill is mandatory, whereas participation in the current program is voluntary.

The bill requires Citizens to submit a biannual report on the number of residential sinkhole policies requested, issued, declined, and the reasons for a policy being declined. No report on sinkhole coverage is required in current law for Citizens or other property insurers. The bill also requires Citizens to offer sinkhole deductible amounts of 2%, 5% and 10% of the policy dwelling limits. Current law allows all property insurers, including Citizens, to offer these deductibles, but does not require all three deductible options to be offered, and Citizens, like other insurers, has chosen to only offer a 10% sinkhole deductible.

The bill has no fiscal impact on state or local government. In most cases, Citizens' policyholders will no longer receive a direct monetary sinkhole claim payment, but will get their property repaired, maintaining the property value and thus, maintaining the local tax base. If sinkhole loss costs are reduced by the mandatory repair program implemented by the bill, premium increases for sinkhole insurance from Citizens may be reduced.

The bill is effective July 1, 2014.

# FULL ANALYSIS

## I. SUBSTANTIVE ANALYSIS

### A. EFFECT OF PROPOSED CHANGES:

#### **Background on Sinkhole Insurance**

A sinkhole is defined in Florida law as a landform created by subsidence of soil, sediment, or rock as underlying strata are dissolved by groundwater.<sup>1</sup> Sinkholes occur in certain parts of Florida due to the unique geological structure of the land. Sinkholes are geographic features formed by movement of rock or sediment into voids created by the dissolution of water-soluble rock. This type of subsidence formation may be aggravated and accelerated by urbanization and suburbanization, by water usage and changes in weather patterns.

Since 1981, insurers offering property coverage in Florida have been required by law to provide coverage for property damage from sinkholes.<sup>2</sup> In 2007, Florida law was amended to require insurers in Florida to cover only catastrophic ground cover collapse, rather than all sinkhole loss, in the base property insurance policy.<sup>3</sup> Catastrophic ground cover collapse is also defined in the law and is more severe than sinkhole loss. Insurers must also offer policyholders, for an appropriate additional premium, sinkhole loss coverage covering any structure, including personal property contents.<sup>4</sup> At a minimum, sinkhole loss coverage includes repairing the covered building, repairing the foundation, and stabilizing the underlying land. By law, sinkhole loss coverage by Citizens Property Insurance Corporation (Citizens)<sup>5</sup> does not cover sinkhole losses to appurtenant structures, driveways, sidewalks, decks, or patios. All property insurers can restrict catastrophic ground cover collapse and sinkhole loss coverage to the property's principal building. Furthermore, insurers can require an inspection of the property before providing sinkhole loss coverage.

For sinkhole loss coverage in residential property insurance, current law allows insurers to include a deductible that applies only to sinkhole loss in the following amounts: 1% of policy dwelling limits, 2% of policy dwelling limits, 5% of policy dwelling limits, or 10% of policy dwelling limits. The insurer has the option to choose which sinkhole loss deductible is offered to policyholders and currently, most insurers, including Citizens, offer policyholders only a 10% sinkhole loss deductible.

Notice of all sinkhole claims, including initial, reopened, or supplemental claims must be given to the insurer in accordance with policy terms within two years of the policyholder knowing about the sinkhole loss or within two years from when the policyholder reasonably should have known about the sinkhole loss.

Substantial changes to Florida's sinkhole law occurred in 2005, 2006, and 2011.<sup>6</sup> In 2011, the Legislature reviewed the sinkhole law and enacted comprehensive reforms addressing all areas of the law. Data collected by the Office of Insurance Regulation (OIR) in 2010, before the reforms were enacted, showed a significant increase in the number and cost of sinkhole claims from 2006 to 2010.<sup>7</sup> These increases impacted the financial stability of property insurers in Florida, including Citizens, and were used by insurers to justify property insurance rate increases.

The sinkhole reforms enacted in 2011 were in response to the increasing number and cost of sinkhole claims. The goal of the reforms was to keep sinkhole loss insurance available to homeowners while providing more certainty in sinkhole claims for homeowners and insurers in terms of coverage, costs, repairs, and exposure.

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<sup>1</sup> s. 627.706(2)(b), F.S.

<sup>2</sup> Ch. 1981-280, L.O.F.

<sup>3</sup> Section 30, Ch. 2007-1, L.O.F.

<sup>4</sup> s. 627.706, F.S.

<sup>5</sup> Citizens Property Insurance 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.

<sup>6</sup> Ch. 2005-111, L.O.F.; Ch. 2006-12, L.O.F.; Ch. 2011-39, L.O.F.

<sup>7</sup> Report on Review of the 2010 Sinkhole Data Call by the Office of Insurance Regulation, dated November 8, 2010, [link available at http://www.flor.com/Office/DataReports.aspx](http://www.flor.com/Office/DataReports.aspx) (last viewed December 23, 2013).

The first complete year the reforms were in effect was 2012.<sup>8</sup> No data has been collected on an industry-wide basis on the number of claims, claim severity, or claim costs since the reforms were enacted, so their impact on sinkhole claims and costs on an industry-wide basis is unknown. However, Citizens performed a sinkhole study in 2012 to compute the impact of the 2011 reforms on their policies.<sup>9</sup> This study looked at actual sinkhole claim files from Citizens and readjusted the losses and expenses associated with the claims as if the 2011 reforms had been in effect. The actuarial analysis which accompanied the study projected the 2011 reforms would reduce Citizens' expected incurred sinkhole losses for 2013 by almost 55 percent. In Citizens' rate filing for 2014,<sup>10</sup> their actuary projected Citizens' sinkhole losses will decrease by over 52 percent relative to what they would have been without the 2011 reforms. The actuary further noted, however, that even with the projected reduction in sinkhole losses, Citizens still has a significant rate deficiency in the sinkhole area. In fact, in 2012, Citizens earned almost \$57 million in sinkhole premium but paid almost \$227 million in sinkhole losses and expenses.

According to data from Citizens,<sup>11</sup> in 2013, new sinkhole claim volume is down 61% from 2012. Also, Citizens has 54% fewer pending sinkhole claims in 2013 than 2012. Paid indemnity, outstanding indemnity reserves, and loss adjustment expenses paid to date for sinkhole claims filed against Citizens have also decreased in 2013 when compared to 2012.

### **Investigation of Sinkhole Claims**

The 2011 legislative sinkhole reforms substantially revised the statutory process for investigating sinkhole claims in s. 627.707, F.S.<sup>12</sup> The process requires the insurer to determine whether the building has incurred structural damage that has been caused by sinkhole activity.<sup>13</sup> Coverage for sinkhole loss is not available if structural damage is not present or sinkhole activity is not the cause of structural damage. The investigation process is as follows:

*Initial Inspection & Structural Damage Determination:* Upon receipt of a claim for sinkhole loss, the insurer must inspect the policyholder's premises to determine if there has been structural damage which may be the result of sinkhole activity.<sup>14</sup> This inspection will often require the insurer to retain a professional engineer to evaluate whether the insured building has incurred structural damage as defined by statute.

*Notice to the Policyholder:* The insurer must provide written notice to the policyholder detailing what the insurer has determined to be the cause of damage (if the determination has been made) and a statement of the circumstances under which the insurer must conduct sinkhole testing.<sup>15</sup> The policyholder must also be notified of his or her right to demand sinkhole testing and the circumstances under which the policyholder may incur costs associated with testing.<sup>16</sup>

*Sinkhole Testing:* The insurer is required to engage a professional engineer or professional geologist to conduct sinkhole testing pursuant to s. 627.7072, F.S., if the insurer confirms that structural damage exists and is either unable to identify a valid cause of the structural damage or discovers that the structural damage is consistent with sinkhole loss.<sup>17</sup> If coverage is excluded under the policy even if sinkhole loss is confirmed, then the insurer is not required to conduct sinkhole testing.<sup>18</sup> The engineer or geologist must issue a report on his or her findings (the report is discussed below).

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<sup>8</sup> The reforms were effective on May 17, 2011 when the bill (CS/CS/CS/SB 408) was signed by the Governor.

<sup>9</sup> Citizens Property Insurance Corporation Senate Bill 408 Sinkhole Analysis, prepared by Insurance Services Office, dated July 19, 2012, and presented at Citizens' Board of Governors Meeting on July 27, 2012, link available at [https://www.citizensfla.com/about/mDetails\\_boardmtgs.cfm?event=419&when=Past](https://www.citizensfla.com/about/mDetails_boardmtgs.cfm?event=419&when=Past) (last viewed December 23, 2013).

<sup>10</sup> Information on Citizens' 2014 rate filing is available at <https://www.citizensfla.com/about/mediareources.cfm> (last viewed December 20, 2013).

<sup>11</sup> Data is as of the end of September 2013 and is available in meeting materials from the Citizens' Claims Committee meeting on November 14, 2013, available at [https://www.citizensfla.com/about/mDetails\\_boardmtgs.cfm?event=531&when=Past](https://www.citizensfla.com/about/mDetails_boardmtgs.cfm?event=531&when=Past) (last viewed December 20, 2013).

<sup>12</sup> Ch. 2001-39, L.O.F.

<sup>13</sup> s. 627.707(1), F.S.

<sup>14</sup> s. 627.707(1), F.S.

<sup>15</sup> s. 627.707(3), F.S.

<sup>16</sup> s. 627.707(3), F.S.

<sup>17</sup> s. 627.707(2), F.S.

<sup>18</sup> s. 627.707(2), F.S.

Testing standards for sinkholes are established in s. 627.7072, F.S. The professional geologist or engineer must perform whatever tests are sufficient to determine the presence or absence of sinkhole loss or cause of damage within reasonable professional probability and to allow the engineer to make recommendations regarding any necessary building stabilization and foundation repair. Typically, the testing procedures used are shallow boring, ground penetrating radar, and deep boring.

*Sinkhole Report:* Once testing is complete, the engineer or geologist performing the testing issues a report and certification to the insurance company and policyholder.<sup>19</sup> The requirements of the sinkhole report and certification are found in s. 627.7073(1), F.S. and are based upon sinkhole testing. If sinkhole loss is verified in the sinkhole report and certification, in addition to the other statements required by law, the report and certification must state structural damage to the covered building has been identified within a reasonable professional probability. In addition to other statements required by current law, if there is no structural damage or if sinkhole activity is eliminated as the cause of damage to a covered building, the report and certification must state there is no structural damage or the cause of structural damage found is not sinkhole activity within a reasonable professional probability. Florida law gives a presumption of correctness to specified information contained in the report.<sup>20</sup>

*Authorization to Deny Sinkhole Claim:* Insurers deny the claim upon a determination that there is no sinkhole loss.<sup>21</sup>

*Policyholder Demand for Sinkhole Testing:* The policyholder may demand sinkhole testing in writing within 60 days after receiving a claim denial if the insurer denies the claim without performing sinkhole testing and coverage would be available if a sinkhole loss is confirmed (i.e. the claim denial was not issued due to policy conditions or exclusions of coverage and instead was based on the failure of the loss to meet the definition of sinkhole loss).<sup>22</sup> However, if the policyholder requests such testing, it must pay the insurer 50 percent of the sinkhole testing costs up to \$2,500.<sup>23</sup> If the requested testing confirms a sinkhole loss the insurer must reimburse the testing costs to the policyholder.<sup>24</sup>

### **Payment of Sinkhole Claims**

If a covered building suffers a sinkhole loss or catastrophic ground cover collapse, the insured must repair such damage in accordance with the insurer's professional engineer's recommended repairs.<sup>25</sup> However, if repairs cannot be completed within policy limits, the insurer has the option to either pay to complete the recommended repairs or tender policy limits without a reduction for any repair expenses already incurred.<sup>26</sup>

The insurer may limit the sinkhole claim payment to the actual cash value of the sinkhole loss not including below-ground repair techniques until the policyholder enters into a contract for the performance of building stabilization repairs.<sup>27</sup> Once the contract is entered into, the insurer pays the amount needed to begin repair work. The insurer continues to pay for repair work as the work is completed and repair costs incurred. The policyholder cannot be required to advance money for the repairs. The insurer must obtain approval of the property lienholder, and not the policyholder, in order to pay repair costs directly to the repair contractor.

The two most commonly recommended stabilization techniques are grouting and underpinning.<sup>28</sup> Under the grouting procedure, a grout mixture (either cement-based or a chemical resin that expands

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<sup>19</sup> s. 627.7073(1), F.S.

<sup>20</sup> s. 627.7073(1)(c), F.S. See Universal Insurance Company of North America v. Warfel, 82 So.3d 47 (Fla. 2012) for a discussion of the presumption of correctness in sinkhole cases.

<sup>21</sup> s. 627.707(4)(a), F.S.

<sup>22</sup> s. 627.707(4)(b), F.S.

<sup>23</sup> s. 627.707(4)(b)2., F.S.

<sup>24</sup> s. 627.707(4)(b)3., F.S.

<sup>25</sup> s. 627.707(5), F.S.

<sup>26</sup> s. 627.707(5), F.S. In this case, insurers pay over policy limits on a sinkhole claim.

<sup>27</sup> s. 627.707(5)(a), F.S.

<sup>28</sup> Citizens Property Insurance Corporation, Sinkhole Repairs: Underpinning and Grouting, (Oct. 30, 2012).

<https://www.citizensfla.com/shared/sinkhole/documents/GroutVersusUnderpinning.pdf> (last viewed on January 30, 2014).

into foam) is injected into the ground to stabilize the subsurface soils to minimize further subsidence damage by increasing the density of the soils beneath the building as well as sealing the top of the limestone surface to minimize future raveling.<sup>29</sup> Underpinning consists of steel piers drilled or pushed into the ground to stabilize the building's foundation.<sup>30</sup> One end of the steel pipe connects to the foundation of the structure with the other end resting on solid limestone. Underpinning repairs, when performed, are usually combined with grouting.

The contract for below-ground repairs must be made in accordance with the recommendations set forth in the insurer's sinkhole report issued pursuant to s. 627.7073, F.S., and must be entered into within 90 days after the policyholder receives notice that the insurer has confirmed coverage for sinkhole loss.<sup>31</sup> The time period is tolled if either party invokes neutral evaluation.

Stabilization and all other repairs to the structure and contents must be completed within 12 months after the policyholder enters into the contract for repairs unless the insurer and policyholder mutually agree otherwise, the claim is in litigation, or the claim is in neutral evaluation, appraisal or mediation.<sup>32</sup>

Although current law requires the homeowner to repair the property affected by a verified sinkhole, oftentimes the insurer and homeowner settle the sinkhole claim before repair work is started.<sup>33</sup> Homeowners that settle sinkhole claims are not required to use claim settlements to repair or remediate the home and land. Thus, arguably, homeowners are incentivized to file sinkhole claims, reach a settlement with the insurer, and use the settlement proceeds for something other than repair and replacement of the sinkhole and resulting damage.

Insurers are not allowed to nonrenew a property insurance policy because a sinkhole claim is filed if the sinkhole claim payment equals or is less than policy limits or if the property was repaired. But, insurers can nonrenew a property insurance policy if policy limits or more are paid.

### **Disclosure of Sinkhole Loss**

Insurers who pay a claim for sinkhole loss must file a copy of the engineer or geologist report and certification with the county clerk of court. Information filed must also include:

- the legal description of the property,
- the neutral evaluation report verifying sinkhole activity as the cause of the damage to the property, if the claim has gone to neutral evaluation,
- a copy of the certification indicating sinkhole stabilization has been completed, and
- the amount paid on the sinkhole claim.

The clerk must record the report and certification. The policyholder must also file a copy of any sinkhole report prepared for the policyholder with the clerk of court before accepting payment from the insurer on a sinkhole claim. When sinkhole repairs are completed, the engineer overseeing the repairs must issue a report to the property owner specifying what repairs were done and certifying the repairs were done properly. A copy of this report must also be filed by the engineer with the clerk of court who records the report.

When property that is the subject of a paid sinkhole claim is sold, the seller who filed the sinkhole claim must disclose to the buyer that a sinkhole claim has been paid. In addition, the seller must disclose whether or not the full amount of claim payment was used to repair the sinkhole damage.

### **The Alternative Dispute Resolution Process for Sinkhole Claims**

Section 627.7074, F.S., provides an alternative dispute resolution process for sinkhole claims. The process supersedes the mediation procedures for property insurance claims contained in s. 627.7015, F.S., but does not invalidate the appraisal clause in the property insurance policy. Thus, a sinkhole

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<sup>29</sup> See *id.*

<sup>30</sup> See *id.*

<sup>31</sup> See s. 627.707(5)(b), F.S. Although a sinkhole report can be prepared by an engineer or a geologist, only an engineer can recommend sinkhole repairs. Furthermore, insurers are allowed in the law to hire professional structural engineers to recommend repairs on the damaged structure.

<sup>32</sup> See s. 627.707(5)(b), F.S. and s. 627.707(5)(d), F.S.

<sup>33</sup> The OIR noted in its report on the 2010 data call that sinkhole repairs were initiated in only 20 percent of the total claims reported.

claim can go through the neutral evaluation process and subsequently go through the appraisal process. The neutral evaluation process begins once an insurer receives the sinkhole report under s. 627.7073, F.S., or denies a sinkhole claim. When either occurs, the insurer must notify the policyholder of the right to participate in the neutral evaluation process. The insurer must also send a pamphlet on the neutral evaluation process prepared by the Department of Financial Services (DFS) to the policyholder.

Participation in the neutral evaluation process is mandatory if one party requests it, however, it is nonbinding. Either the policyholder or the insurer can request neutral evaluation of a sinkhole claim. At the conclusion of the neutral evaluation, the neutral evaluator prepares a report containing recommendations about the validity of the sinkhole claim. The specific areas the neutral evaluator must opine on in the report are set forth in s. 627.7074(12), F.S. The recommendation of the neutral evaluator is not binding on either party, thus, either party can opt to litigate the sinkhole claim in court regardless of the neutral evaluator's recommendation on the claim. If the insurer timely agrees to comply with the neutral evaluator's recommendations in writing and does so, but the policyholder declines to resolve the claim and opts to proceed to court on the claim, the insurer is not liable for extracontractual damages for issues determined by the neutral evaluator and the insurer's actions to comply with the recommendation is not a confession of judgment that can be used in the court proceeding as an admission of liability on the part of the insurer. Furthermore, in the court proceeding, the insurer is not liable for attorney's fees unless the policyholder obtains a court judgment more favorable than the neutral evaluator's recommendation.

### **Sinkhole Claims – Citizens Property Insurance Corporation**

Citizens has proposed a sinkhole managed repair program for sinkhole stabilization only and is currently in the process of getting the program operational.<sup>34</sup> Structural and building repairs due to sinkhole loss are not part of the program. Participation in the proposed sinkhole managed repair program is voluntary for Citizens' policyholders. If a policyholder participates in the voluntary managed repair program, once it is determined the policyholder needs sinkhole stabilization services as a result of sinkhole damage, the policyholder chooses a vendor in the program to provide the needed stabilization services. Vendors in the program are experienced and credentialed and meet minimum qualifications determined by Citizens. Qualifications include a performance bond for each project, a five year labor and material warranty, and an agreement to adhere to a line item price guide. Citizens periodically remits payment for work completed to the vendor directly and the policyholder does not directly receive any payment for the sinkhole claim. Citizens projects less than 100 claims per year will be eligible for the program and does not anticipate 100 percent participation for those eligible since participation in the program is voluntary.

Additionally, in December 2013, to try to settle sinkhole claim disputes over the method of sinkhole repairs, Citizens began sending letters to its policyholders who are disputing the repair recommendations on their sinkhole claims.<sup>35</sup> The letters target policyholders who have a confirmed sinkhole loss where the professional engineer verifying the loss has recommended grouting repairs, but not underpinning. The letters encourage policyholders to have the repair work recommended by the engineer completed. For these policyholders, Citizens is also encouraging them to resolve the differing engineering opinions on the method of repair through the neutral evaluation process and is agreeing to abide by the neutral evaluator's decision, regardless of which side prevails. Further, Citizens is agreeing to pay for repairs that exceed policy limits and for cosmetic repairs needed due to the sinkhole

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<sup>34</sup> Citizens solicited sinkhole repair contractors who would participate in the program through two Invitations to Bid (ITB). Sixteen vendors were chosen for the program from the first ITB. However, Citizens' Board has not yet awarded the vendor contracts due to a bid protest. The second ITB recently closed, but vendors have not yet been chosen. Additional material on the managed repair program is available from meeting materials for the Citizens Claims Committee meeting on November 14, 2013, the Citizens Board of Governors meeting on December 12, 2013, available at [https://www.citizensfla.com/about/past\\_boardmtgs.cfm](https://www.citizensfla.com/about/past_boardmtgs.cfm) (last viewed February 3, 2014), ITB 13-0020 for Sinkhole Stabilization Managed Repair Program issued by Citizens dated October 30, 2013, and ITB 13-0028 for Solicitation for Additional Sinkhole Stabilization Managed Repair Program Vendors dated December 12, 2013, available at <https://www.citizensfla.com/about/purchasing/purchasing-solicitations.cfm> (last viewed February 5, 2014).

<sup>35</sup> Citizens Property Insurance Corporation, *Citizens Chairman: Settlement Proposal Benefits Consumers*, (Press Release dated December 12, 2013). <https://www.citizensfla.com/about/pressreleases.cfm> (last viewed on January 30, 2014); Citizens Property Insurance Corporation, *Citizens Chairman: No blank checks: Sinkholes will be repaired*, (Press Release dated December 24, 2013). <https://www.citizensfla.com/about/pressreleases.cfm> (last viewed on January 30, 2014).

repairs made. Citizens estimates that of its 2,100 disputed sinkhole claims, 1,329 deal with disagreements over repair methods and thus are targeted by the settlement proposal.<sup>36</sup> As of February 4, 2014, 50 policyholders have signed repair contracts offered by the letter.<sup>37</sup> In March 2014, Citizens announced a global settlement with more than 300 policyholders of litigated sinkhole claims.<sup>38</sup> Under the terms of the settlement, Citizens will pay for underground repairs due to sinkhole loss and pay for any above ground damage caused by the underground repairs.

### **Effect of Proposed Changes**

The bill makes changes to the sinkhole law, but only for sinkhole claims submitted to Citizens. The changes do not apply to sinkhole claims submitted to other property insurers. Specifically, the bill requires Citizens to submit a biannual report on the number of residential sinkhole policies requested, issued, declined, and the reasons for a policy being declined to the OIR and the Office of the Insurance Consumer Advocate. No report on sinkhole coverage is required in current law for Citizens or other property insurers.

The bill requires Citizens to offer deductible amounts of 2%, 5% and 10% of the policy dwelling limits for sinkhole loss coverage. However, for determining whether there is comparable coverage available in the private market making a policy ineligible for insurance in Citizens, a 10% sinkhole deductible is used whether or not that is the deductible chosen by the policyholder.<sup>39</sup> Current law allows all property insurers, including Citizens, to offer sinkhole deductibles of 1%, 2%, 5%, or 10% of the policy's dwelling limits, but does not require an offer of these deductibles. Citizens has chosen to only offer sinkhole policies with a 10% deductible. Similarly, other private insurers also only offer one sinkhole deductible, usually 10%, and do not offer all four deductibles allowed under current law.

The bill also establishes a Citizens Sinkhole Repair Program which must be operational by March 31, 2015. The program established by the bill utilizes approved repair contractors to ensure sinkhole repairs are completed on property insured by Citizens. The Citizens Sinkhole Repair Program established under the bill is not substantially different than the program currently proposed by Citizens. The primary difference is that participation in the program established by the bill is mandatory, whereas the current program is voluntary. The bill specifies that sinkhole repairs under the program are not an election to repair and therefore do not imply or create a new contractual relationship under the terms of the insurance policy.<sup>40</sup>

Most of the process and timeline specified in the bill that Citizens must use in contracting for sinkhole stabilization repairs and operating the repair program is consistent with Citizens' voluntary sinkhole repair program. Under the mandatory program created by the bill, stabilization repair contractors are approved by Citizens to participate in the program if they meet statutory qualifications. The pool of repair contractors approved by Citizens must be competitive and inclusive. If the pool has at least 12 contractors, it is presumed the pool is competitive and inclusive.

The qualifications for contractors, in part, require them to have experience in sinkhole stabilization, have all insurance required by law, have a drug-free workplace, and to provide payment and performance bonds and a five year warranty on the work performed. Citizens must guarantee the repair work if a warranty cannot be procured within a specified cost. Citizens must also provide a warranty for up to five years if the contractor originally providing the warranty cannot honor the warranty to the policyholder. These qualifications are similar to the ones required by the voluntary Citizens sinkhole repair program.

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<sup>36</sup> *Id.*

<sup>37</sup> Information received from a representative of Citizens on February 4, 2014.

<sup>38</sup> Citizens Property Insurance Corporation, *Sinkhole Settlement to Save \$30 Mil in Legal Costs*, (Press Release dated March 12, 2014).

<https://www.citizensfla.com/about/pressreleases.cfm> (last viewed on April 3, 2013).

<sup>39</sup> Comparable coverage in the private market must also be offered at a premium 15% or less than the Citizens' premium.

<sup>40</sup> Generally, insurance policies provide language in the policy giving the insurer the right to repair the damaged property and when an insurer elects to repair, the insurer hires the contractor, the insurance policy is changed to a repair contract with no limit of liability (i.e., no policy limits), and the insurer must pay for all repairs until the damaged property is completely repaired.

The contractors in the repair program must contract with Citizens to perform the stabilization repairs outlined in the Citizens' engineer's report for line-item prices reflecting market prices for the repairs. Citizens also uses line-item prices in the voluntary sinkhole repair program.

Under the sinkhole repair program created by the bill, the policyholder has 30 days to select a repair contractor from the pool of contractors. If the policyholder does not select a contractor within the 30 day period, Citizens selects the contractor. The policyholder does not have to advance funds for repair work done under the program.

During the course of the sinkhole stabilization repairs, the Citizens' engineer monitors the repair work done by the contractor to ensure the repairs done are compliant with the engineer's recommendation. The engineer also confirms when the stabilization has been completed by the contractors and no further repair is needed to remedy the sinkhole damage.

If, after sinkhole repairs are begun under the repair program, Citizens' engineer determines that additional stabilization repairs are needed and the cost of the additional repairs is within policy limits, then the contractor must complete the additional repairs. If, after sinkhole repairs are begun under the repair program, Citizens' engineer determines that additional stabilization repairs are needed but the total cost of the additional repairs and the original repairs is more than policy limits, then Citizens must pay more than policy limits to complete the repairs or pay policy limits to the policyholder without reducing the payment to account for repair expenses already paid. If policy limits are paid, the repair work paid for by Citizens under the repair program stops. The policyholder can use the insurance proceeds to finish the sinkhole repairs begun, but is not required to do so.

The bill requires repairs in litigated sinkhole claims if a court order is entered verifying a sinkhole loss and requiring repairs that are different than the repairs recommended by the Citizens' engineer.

The bill also requires the Office of Program Policy Analysis and Government Accountability (OPPAGA) to review the Citizens sinkhole repair program and report on the program to the Governor, Chief Financial Officer, the President of the Senate, and the Speaker of the House of Representatives by January 1, 2017. The bill specifies the contents of the required report.

## B. SECTION DIRECTORY:

Section 1: Amends s. 627.351, F.S., relating to insurance risk apportionment plans.

Section 2: Amends s. 627.706, F.S., relating to sinkhole insurance; catastrophic ground cover collapse; definitions.

Section 3: Creates an unnumbered section of law requiring OPPAGA to report on the repair program created by the bill.

Section 4: Creates an unnumbered section of law providing a severability clause.

Section 5: Provides an effective date of July 1, 2014.

## II. FISCAL ANALYSIS & ECONOMIC IMPACT STATEMENT

### A. FISCAL IMPACT ON STATE GOVERNMENT:

#### 1. Revenues:

None.

#### 2. Expenditures:

None.

**B. FISCAL IMPACT ON LOCAL GOVERNMENTS:**

1. Revenues:

None.

2. Expenditures:

None.

**C. DIRECT ECONOMIC IMPACT ON PRIVATE SECTOR:**

In cases where the sinkhole can be repaired within policy limits, Citizens' policyholders no longer receive a direct monetary claim payment for sinkhole stabilization. However, their property affected by the sinkhole is repaired. Ensuring homes with sinkhole claims are repaired should maintain the property value of the house which also maintains the local tax base.

If sinkhole loss costs are reduced by the program implemented by the bill, premium increases for sinkhole insurance from Citizens may be reduced.

**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 provided in the bill.

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

None.

**IV. AMENDMENTS/ COMMITTEE SUBSTITUTE CHANGES**

On April 3, 2014, the Regulatory Affairs Committee heard the bill, adopted a strike all amendment and an amendment to the strike all amendment, and reported the bill favorably with a committee substitute. The amendments adopted:

- Repealed current law authorizing Citizens to establish a pilot program to offer optional sinkhole coverage.
- Changed the legislative findings relating to Citizens' sinkhole claims and repairs.
- Removed authority for a third party administrator to manage the Citizens Sinkhole Stabilization Repair Program (program) and requires Citizens to manage the program.
- Added a definition of "sinkhole loss" for use in the program.

- Required the repair contractor pool to be competitive and inclusive and provides a presumption that the pool is competitive and inclusive if it has a minimum of 12 contractors.
- Removed the provision in the bill allowing Citizens to set the insurance amount required for the program's repair contractors and replaces it with a requirement that the contractors maintain public liability, property damage, and worker's compensation insurance in amounts required by the contractor licensing and workers' compensation law.
- Removed authority for Citizens to set requirements for repair contractors to participate in the program other than those listed in the bill.
- Added authority for Citizens to adopt requirements for the contractors that are consistent with s. 287.057, F.S, the state procurement law.
- Required approved contractors to perform repairs based on line-item prices developed by Citizens that reflect market prices, instead of on a fixed price submitted by the repair contractor.
- Made the amount of the required payment and performance bonds provided by the repair contractor to be an amount equal to the amount of the contract for each repair project, rather than the total amount of contracts awarded annually to the contractor.
- Made the 5-year warranty provided by the repair contractor to be secured by an insurer or registered retention group, instead of a third-party surety.
- Made Citizens the guarantor for the repairs done by the contractor if the contractor cannot obtain a 5-year warranty or cannot obtain the warranty for a cost equal to or less than 3% of the amount of the repair contract.
- Required Citizens to provide a 5-year warranty to the policyholder for stabilization repairs if the contractor is unable to honor its 5-year warranty to the policyholder.
- Allowed the policyholder to select a contractor from all qualified contractors that offer to perform the repair, rather than permitting Citizens to exclude contractors from the list given to the policyholder based on the contractor's quality, cost-effectiveness, and other criteria set by Citizens.
- Removed language allowing Citizens to enter a property into the contractor selection process a second time or pay policy limits on the claim, if no repair offer is made by a contractor the first time the property goes through the process or if the repair offer received the first time is over policy limits.
- Required the sinkhole repair contractor to complete additional stabilization repairs recommended by the Citizens' engineer if the additional repair work can be done within policy limits.
- Required Citizens to pay for additional repairs recommended by the Citizens' engineer, even if the cost is more than policy limits, or tender policy limits, without reducing the payment for the cost of repairs already incurred, if repairs begin and during the repair period the Citizens' engineer determines additional repairs are needed which cannot be completed within policy limits.
- Removed the provision from the bill providing specific performance as the sole remedy for disputes between Citizens and the policyholder related to the repairs done under the program.
- Required sinkhole repairs be made for litigated sinkhole claims where an order is entered verifying a sinkhole loss and requiring repairs that are not the same as the repairs recommended by the Citizens' engineer.
- Added a provision specifying the program does not alter the procedure in current law for engaging an engineer in sinkhole claims.
- Maintained the provision requiring Citizens to offer sinkhole deductibles of 2%, 5%, and 10% of dwelling limits, but adds a provision requiring a 10% sinkhole deductible to be used for evaluating if there is comparable coverage in the private market when determining whether a risk is eligible for insurance from Citizens.
- Changed the definitions of "neutral evaluator" and "engineer" in the current law that applies to sinkhole claims to be consistent with CS/CS/HB 633 passed by the House on March 27, 2014.
- Required OPPAGA to report on the repair program to the Governor, Chief Financial Officer, Senate President, and Speaker of the House by January 1, 2017 and specifies the content of the report.
- Added a severability clause.
- Changed the title from "insurance" to "sinkhole coverage."

The staff analysis was updated to reflect the committee substitute.