

# SENATE STAFF ANALYSIS AND ECONOMIC IMPACT STATEMENT

(This document is based only on the provisions contained in the legislation as of the latest date listed below.)

BILL: CS/SB 1886

SPONSOR: Banking and Insurance Committee and Senator Geller

SUBJECT: Windstorm Insurance Risk Apportionment

DATE: April 20, 1999 REVISED: \_\_\_\_\_

	ANALYST	STAFF DIRECTOR	REFERENCE	ACTION
1.	<u>Deffenbaugh</u>	<u>Deffenbaugh</u>	<u>BI</u>	<u>Favorable/CS</u>
2.	_____	_____	<u>FP</u>	_____
3.	_____	_____	_____	_____
4.	_____	_____	_____	_____
5.	_____	_____	_____	_____

## I. Summary:

Committee Substitute for Senate Bill 1886 revises the provisions of current law that state that if the Florida Windstorm Underwriting Association (FWUA) obtains an offer of coverage from an authorized insurer to insure a homeowner or other risk at its approved rates under either a standard or basic policy including wind coverage, the risk is no longer eligible for coverage through the FWUA. The bill authorizes the FWUA to establish depopulation procedures, subject to the approval of the Department of Insurance. The bill deletes provisions that require the FWUA to send written notice to a policyholder and agent of record stating that the policy must be canceled as of 60 days after the date of notice because of the offer of coverage from an authorized insurer. The bill also adds an insurance agent to the board of the FWUA.

The bill revises the definition of "hurricane coverage" for purposes of residential property insurance policies, which affects whether the hurricane deductible and other coverage limitations for hurricane losses apply or not. The current definition somewhat vaguely refers to damage "caused by the peril of windstorm during a hurricane." As amended by the bill, the definition would further require that the damage occur in a county in which the Division of Emergency Management of the Department of Community Affairs, based upon official forecasting information from the National Weather Service, declares within 24 hours after the storm system enters a county that an area in the county sustained winds that were part of the storm system.

The FWUA sells policies covering only windstorm and hail losses in the coastal areas of 29 of Florida's 35 coastal counties. A purchaser of a windstorm policy from the FWUA must obtain a separate "ex-wind" or "non-wind" policy from another insurer that covers other perils. The FWUA currently has 493,352 policies in force, insuring \$90.17 billion in property value (exposure), and an estimated probable maximum loss for a 100-year storm of \$5.6 billion. In addition to premiums, the FWUA depends upon debt financing supported by assessments against all Florida property insurers and their policyholders to fund losses in the event of a deficit.

The FWUA has received offers from insurers to take policies out of the FWUA. However, the board of the FWUA has determined that despite the statutory language, the board would not move forward with any insurer's offer to take a policy out of the FWUA until a "depopulation rule" has been approved by the department, which the FWUA has filed and revised, but has not yet been approved by the department.

This bill substantially amends sections 627.351 and 627.4025 of the Florida Statutes.

## **II. Present Situation:**

### **The Florida Windstorm Underwriting Association (FWUA) and the Florida Residential Property and Casualty Joint Underwriting Association (RPCJUA); Background**

The Florida Windstorm Underwriting Association (FWUA) was formed in 1970 to sell policies covering only windstorm and hail losses, and only in those areas of the state where the Department of Insurance determined that such coverage was not generally available and that certain other conditions existed. The FWUA was formed in 1970 to cover the Florida Keys and the coastal areas of 8 counties. Today, the coastal areas of 29 of Florida's 35 coastal counties are eligible for FWUA coverage, including the area east of Interstate 95 in Dade, Broward, and Palm Beach Counties. Legislation in 1998 prohibited further expansion of the geographical boundaries of the FWUA. The FWUA sells both commercial and personal lines policies that cover both residential and non-residential risks. A purchaser of a windstorm policy from the FWUA must obtain a separate "ex-wind" or "non-wind" policy from another insurer that covers other perils such as fire, theft, and liability.

The FWUA is the association that administers the plan approved by the Department of Insurance pursuant to s. 627.351(2), F.S. The FWUA operates pursuant to a plan of operation approved by the department and is governed by a 15-member board of directors that includes 12 representatives of its member insurance companies and trade associations and 3 representatives of consumers, including the department's Insurance Consumer Advocate. The FWUA employs its own staff (in Jacksonville) to administer the operations of the FWUA.

A second residual market insurer, the Residential Property and Casualty Joint Underwriting Association (RPCJUA), was created in 1993 after Hurricane Andrew, to sell residential property insurance in all areas of the state, insuring all perils covered under a standard or basic policy. However, in areas eligible for coverage from the FWUA, the RPCJUA policies exclude coverage for windstorm and hail.

### **Current Exposure of the FWUA and RPCJUA**

As of March 31, 1999, the FWUA has 493,352 policies in force, insuring \$90.17 billion in property value (exposure), and an estimated probable maximum loss for a 100-year storm of \$5.6 billion. In the three counties of Dade, Broward, and Palm Beach, alone, the FWUA has 289,836 policies in force, insuring \$54.23 billion in property value. In comparison, the RPCJUA, which previously insured more than 937,000 policies in 1996, now insures about 199,000 policies (\$32 billion in exposure), due to successful take-out efforts by the RPCJUA and the department and legislatively authorized financial incentives for insurers writing such policies.

### **Funding Losses in the FWUA; Premiums and Assessments**

Premiums paid by FWUA policyholders provide the first source of funding for losses paid by the FWUA. Generally, FWUA premiums are subject to the same rate filing and approval requirements that apply to other insurers and may not be excessive, inadequate, or unfairly discriminatory. The law also requires that all surplus be retained by the FWUA for the payment of future losses and prohibits the distribution of any surplus to member insurers. Unlike the RPCJUA, the rates of the FWUA are *not* required to be set at the highest rates of the top 20 insurers in the state, but the law provides legislative intent that FWUA rates not be competitive with voluntary market rates and requires the FWUA plan of operation to provide, no later than January 1, 1999, a means of assuring that FWUA's rates are reflective of department-approved hurricane rates in the voluntary market. In 1996, the FWUA had its first rate increase in 13 years, averaging 31% statewide. In 1998, the FWUA obtained an average statewide increase of 12%. A new rate filing has recently been filed by the FWUA with the department. The FWUA prepared a rate comparison with voluntary market insurers which showed that the FWUA needs a 42-66% rate increase to match the average of the top 20 companies and a 172-198% rate increase to match the highest rates charged by the top 20 companies. The department has responded that the rate comparison is inaccurate in various respects.

In addition to premiums, the FWUA (and the RPCJUA) depend upon debt financing supported by assessments against all Florida property insurers and their policyholders to fund losses in the event of a deficit. If necessary to fund a deficit, "regular" assessments may be imposed against all authorized property insurers, up to 10% of the FWUA's *deficit*, or 10% of property insurance premiums in the state, whichever is *greater*. Such assessments may be recouped by insurers from their policyholders. If the deficit in any year exceeds the maximum regular assessment, all new and renewal property insurance policies in the state are subject to "emergency" assessments, limited to the greater of 10% of the deficit, or 10% of the prior year's statewide premium for property insurance. Emergency assessments may be pledged by the board in order to secure debt financing. The FWUA (and RPCJUA) must also buy reinsurance from the Florida Hurricane Catastrophe Fund to cover a portion of their hurricane losses for residential policies, which generally provides funding above the funding provided by regular assessments, but below the funding provided by debt financing and emergency assessments.

### **Offers of Coverage to FWUA Policyholders from Insurers in the Voluntary Market**

In 1996, legislation was enacted to provide that if the FWUA obtains an offer from an authorized insurer to cover a risk (e.g., a homeowner's policy) at its approved rates under either a standard policy including wind coverage or, if consistent with the insurer's underwriting rules as filed with the department, a basic policy including wind coverage, the risk is no longer eligible for coverage through the FWUA. Upon termination of eligibility, the FWUA must provide written notice to the policyholder and agent of record stating that the FWUA policy must be canceled 60 days after the date of the notice because of the offer of coverage from an authorized insurer.

(Ch. 97-55, Laws of Florida.)

The above provision was modeled on a provision that applies to the RPCJUA [s. 627.351(6)(c)5., F.S.]. However, the situation is somewhat different as applied to the FWUA, because forcing a FWUA policyholder to accept a policy from a take-out insurer forces a policyholder to lose not

only their FWUA policy, but also their ex-wind policy, assuming that the policyholder desires to have windstorm coverage or is required to do so under the terms of his or her mortgage. This has a detrimental impact on the ex-wind insurer, as well, which loses the business.

The FWUA has received offers from insurers to take policies out of the FWUA. However, the board of the FWUA has determined that despite the statutory language, the board would not move forward with any insurer's offer to take a policy out of the FWUA until a "depopulation rule" has been approved by the department. Such "rules" are written requirements and procedures adopted by the board of the FWUA and submitted to the department for approval. The FWUA and the department have been engaged in discussions and debate over the board's proposed depopulation rule for over a year. The FWUA has filed and revised their proposed rule, which has not yet been approved by the department. The issues have included financial standards for take-out companies, adequate notice to the policyholder, the agent of record, and the ex-wind insurer, requiring that policies only be taken out upon renewal, the rates and benefits for the take-out insurer's replacement policy, and other issues.

The FWUA has also made a filing with the department to revise its policy benefits and coverages, based on the board's recommendation to reduce policyholder surcharge subsidies through greater property owner cost sharing, such as increased windstorm deductibles and essential coverage only policies. The department has not yet formally responded to this filing or to the rate filing discussed above.

### **Definition of "Hurricane Coverage" and related terms for all Residential Coverage**

Section 627.4025, F.S., defines *hurricane coverage*, *windstorm*, and *hurricane* as these terms are used in policies providing *residential coverage*, also defined. These definitions are important primarily for determining whether the hurricane deductible of a residential policy applies, and other coverage limitations that apply in the event of a hurricane loss.

"Residential coverage" is defined in this section to include both personal lines residential coverage provided by homeowner's, mobile home owner's, dwelling, tenant's, condominium unit owner's, cooperative unit owner's, and similar policies, and commercial lines residential coverage provided by condominium association, cooperative association, apartment building, and similar policies.

"Hurricane coverage" is defined (in part) as coverage for loss or damage caused by the peril of windstorm during a hurricane. "Windstorm" for purposes of this definition, means wind, wind gusts, hail, rain, tornadoes, or cyclones *caused by or resulting from a hurricane* which results in direct physical loss or damage to property. "Hurricane" means a storm system that has been declared to be a hurricane by the National Hurricane Center of the National Weather Service. The duration of the hurricane includes the time period, in Florida, beginning at the time a hurricane watch or hurricane warning is issued for any part of Florida, continuing for the time during which hurricane conditions exist anywhere in Florida, and ending 72 hours following the termination of the last hurricane watch or hurricane warning issued for any part of Florida.

These definitions are important primarily for determining whether the hurricane deductible of a residential policy applies or not, or other coverage limitations that apply in the event of a hurricane loss. For example, for dwellings valued at \$100,000 or more, insurers are permitted to

have hurricane deductibles as high as 5% of dwelling limits, if they also offer a 2% hurricane deductible and provide a minimum \$500 other-peril deductible, subject to certain conditions and exceptions (s. 627.701, F.S.) Other hurricane coverage limitations (not addressed by statute) have been approved by the department, such as restrictions on coverage for outbuildings and contents.

The current law definition is somewhat vague in basing the determination of “hurricane coverage” on whether the winds were “caused by or resulting from a hurricane.” On a case by case basis it may be difficult to determine whether a windstorm loss in a particular county or area of the state was caused by or resulting from a hurricane, particularly if the wind speed is below that of hurricane force winds (which is very difficult to determine) and is geographically distant from the center of the storm system.

### III. Effect of Proposed Changes:

**Section 1.** The bill amends s. 627.351(2), F.S., to revise the provisions of current law that state that if the Florida Windstorm Underwriting Association (FWUA) obtains an offer of coverage from an authorized insurer to insure a home or other risk at its approved rates under either a standard or basic policy including wind coverage, the risk is no longer eligible for coverage through the FWUA.

The bill retains the provision that a risk is no longer eligible for FWUA coverage if an offer of coverage is made by an authorized insurer at approved rates. However, the bill authorizes the FWUA to establish depopulation procedures, subject to the approval of the Department of Insurance. The bill deletes provisions that require the FWUA to send written notice to a policyholder and agent of record stating that the policy must be canceled as of 60 days after the date of notice because of the offer of coverage from an authorized insurer.

As explained in Present Situation, above, the FWUA board has not issued any cancellation notices to policyholders in response to take-out offers from insurers and has determined not to do so until a depopulation rule has been approved by the department. The bill provides express authority for the FWUA to establish depopulation procedures, subject to approval by the department. However, the bill does not specify any standards for requirements that could be imposed on an insurer offering to take policies out of the FWUA, which would be left to the discretion of the board and the department. “Depopulation procedures” may include notice and time frame requirements, but it may be questioned whether this authorizes more substantive requirements such as premium and benefit requirements for the replacement policies being offered if they are more restrictive than for residential policies generally.

The bill also adds an insurance agent to the board of the FWUA, to be appointed by the Insurance Commissioner. The agent must be writing insurance with the FWUA at the time of appointment. This will increase from 15 to 16 the total number of FWUA board members.

**Section 2** The bill amends s. 627.4025, F.S., to revise the definition of “hurricane coverage” as such term is used in residential property insurance policies. The term would still mean coverage for loss or damage caused by the peril of windstorm during a hurricane (and “windstorm” would still mean wind *caused by or resulting from a hurricane*), but as amended “hurricane coverage” would also require that the damage occur in a county in which the Division of Emergency

Management of the Department of Community Affairs, based upon official forecasting information from the National Weather Service, declares within 24 hours after the storm system enters a county that an area in the county sustained winds that were part of the storm system.

If the division does not make such a declaration for a particular county, within the 24-time period, then windstorm losses in that county would not be subject to hurricane coverage provisions of a residential property insurance policy, such as hurricane deductible provisions.

#### **IV. Constitutional Issues:**

##### **A. Municipality/County Mandates Restrictions:**

None.

##### **B. Public Records/Open Meetings Issues:**

None.

##### **C. Trust Funds Restrictions:**

None.

#### **V. Economic Impact and Fiscal Note:**

##### **A. Tax/Fee Issues:**

None.

##### **B. Private Sector Impact:**

Section 1. The bill appears to have no direct fiscal impact because the FWUA board has determined that under current law it will not cancel coverage for current FWUA policyholders despite the receipt of an offer of coverage from an authorized insurer, until depopulation procedures have been approved by the department. By authorizing the FWUA to establish and the department to approve such procedures, the bill does not change the current factual situation. However, the bill may have the effect of legally authorizing the current factual situation and, therefore, decrease the likelihood that current FWUA policyholders will be forced to accept higher priced coverage and, conversely, increase the potential for non-FWUA policyholders to be subject to assessments to fund deficits in the FWUA.

Section 2. By providing a more specific and objective standard for determining whether hurricane provisions of residential policies apply in the event of a windstorm loss, the bill should decrease potential disputes and litigation over this issue. Otherwise, the bill does not appear to significantly effect the definition of "hurricane coverage" as it is likely to be reasonably interpreted under current law.

**C. Government Sector Impact:**

By authorizing the FWUA and the department to establish depopulation procedures, the bill may reduce the possibility that the current efforts to establish such procedures would be legally challenged and, therefore, may reduce legal and administrative expenses that might otherwise be paid.

**VI. Technical Deficiencies:**

None.

**VII. Related Issues:**

None.

**VIII. Amendments:**

None.

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This Senate staff analysis does not reflect the intent or official position of the bill's sponsor or the Florida Senate.

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