

STORAGE NAME: h0093s1.rpp
DATE: January 26, 1999

**HOUSE OF REPRESENTATIVES
COMMITTEE ON
Real Property and Probate
BILL ANALYSIS & ECONOMIC IMPACT STATEMENT**

BILL #: CS/HB 93
RELATING TO: Title Insurance Reserve
SPONSOR(S): Representative Bob Starks
COMPANION BILL(S):

ORIGINATING COMMITTEE(S)/COMMITTEE(S) OF REFERENCE:

- (1) Real Property and Probate YEAS 5 NAYS 0
- (2) Insurance
- (3) Judiciary
- (4)
- (5)

I. SUMMARY:

Current law requires a title insurer ["insurer"] to establish a guaranty fund or unearned premium reserve in addition to their reserve for outstanding losses. The unearned premium reserve cannot be used by the insurer for general purposes; must be held in trust in favor of the holders of title guarantees and policies; and, is to be held available for reinsurance of the title guarantees and policies in the event the insurer becomes insolvent. The insurer may invest the reserves, and the income from such investment must be included in the general income which the insurer may use for any lawful purpose.

Current law also provides that the unearned premium reserve shall consist of not less than: (a) the amount of the unearned premium reserve in existence on June 30, 1992; and (b) a sum equal to 30 cents for each \$1,000 of net retained liability under each title insurance policy on a single risk written on or after July 1, 1992. The adequacy of the reserve existing on December 31, 1992, must be determined in accordance with the reserve requirements existing on July 1, 1992. CS/HB 93 changes the year from 1992 to 1999 with regard to the previously listed dates.

CS/HB 93 also provides that unearned premium reserves be released over a period of 20 years, instead of the existing requirement that reserves be released in 12 equal annual installments. Reserves with respect to unearned premiums for policies written or title liability assumed in reinsurance before July 1, 1999, and the total amount of net retained liability after July 1, 1999, are to be released pursuant to the variable schedule as set forth in this bill.

CS/HB 93 further provides that if the amount of the reserve stated in the actuarial opinion is greater than the sum of the known claim reserve and the unearned premium reserve, then the insurer must deposit the difference into the unearned premium reserve.

The Department of Insurance has determined that this bill has no fiscal impact on the department, state agencies or on local government.

See "Comments" section for concerns regarding several of this bill's provisions.

II. SUBSTANTIVE ANALYSIS:

A. PRESENT SITUATION:

Statutory Law

Under current statutory law, a title insurer ["insurer"] must maintain two types of reserves:

1. An insurer must retain adequate **loss reserves** sufficient to cover its unpaid losses, claims and expenses for which the insurer may be liable and for which the insurer has received notice by or on behalf of the insured.¹ See Fla. Stat. §§ 625.101; 625.111.²
2. In addition to the reserves required above, an insurer shall establish, segregate and maintain a guaranty fund or **unearned premium reserve** to be used for reinsurance in the event the insurer becomes insolvent. Fla. Stat. § 625.111.

Section 625.111, F.S., states in pertinent part that the **unearned premium reserve** must consist of not less than an amount computed as follows:

- (a) The amount of the unearned premium reserve on June 30, 1992; and
- (b) A sum equal to 30 cents for each \$1,000 of net retained liability under each title insurance policy on a single risk written on or after July 1, 1992.³

Accordingly, the amount in reserves for each insurer throughout the state is different depending upon the number of policies the company writes.

Section 625.111, F.S., further provides that the adequacy of the unearned premium reserve existing on December 31, 1992, must be determined in accordance with the unearned premium reserve requirements existing on July 1, 1992, and the reserves must be released in 12 equal annual installments (or approximately 8.34 percent) beginning

¹The purpose of the reserve is to "cover all unpaid losses, claims and allocated loss adjustment expenses arising under title insurance policies, guaranteed certificates of title, guaranteed searches and guaranteed abstracts of title, and all unpaid losses, claims and allocated loss adjustment expenses for which the title insurer may be liable and for which the insurer has received notice by or on behalf of the insured, holder of a guarantee or escrow or security depositor." Section 10, Title Insurers Model Act, April 1996.

² If an insurer's loss reserves are inadequate, the Department of Insurance must require the insurer to maintain a **supplemental loss reserve** in the needed additional amount. Fla. Stat. § 625.101.

³ In 1992, the Legislature changed the basis for determining the amount to be deposited into the unearned premium reserve to a percentage of the liability on the face of the policy instead of a percentage of the premiums collected during a calendar year. ch. 34, § 1(b), 1992 Fla. Laws, 389-390. This remains the law today. Fla. Stat. § 625.111(1)(a)(b).

STORAGE NAME: h0093s1.rpp

DATE: January 26, 1999

PAGE 3

with the calendar year 1993.⁴ Fla. Stat. § 625.111(2)(a). With regard to amounts reserved on or after January 1, 1993, the insurer must release amounts reserved during a particular calendar year in 12 equal annual installments, beginning in the subsequent calendar year.

Title Insurer's Model Act: Reserving Funds

The National Association of Insurance Commissioners (NAIC) drafted the Title Insurers Model Act in 1983 (revised April 1996). The NAIC suggest that when establishing an unearned premium reserve, one should keep in mind that there can be a wide difference among insurers as to the correct reserve requirement. NAIC Title Insurers Model Act, s. 10, B, ftnt 2. Reserve requirements may change over time according to the insurer's varying exposure to risk. *Id.* Therefore, the reserve requirements are best determined by each state.⁵

The NAIC's Title Insurers Model Act does, however, provide in pertinent part, the following:

- (a) The amount of the statutory or unearned premium or reinsurance reserve on the effective date of this Act, which balance shall be released in accordance with the law in effect at the time such sums were added to the reserve; and
- (b) Out of total charges for policies of title insurance written or assumed commencing with the effective date of this Act, and until December 31, 1997, a title insurer shall add to and set aside in this reserve an amount equal to [insert amount] of the sum of the following items set forth in the title insurer's most recent annual statement on file with the commissioner:
 - i) Direct premiums written;
 - ii) Escrow and settlement service fees;
 - iii) Other title fees and service charges including fees for closing protection letters; and
 - iv) Premiums for reinsurance assumed less premiums for reinsurance ceded (transferred) during year.
- (c) Additions to the reserve after January 1, 1998, shall be made out of the total charges for title insurance policies and guarantees written, equal to the sum of the following items, as set forth in the title insurer's most recent annual statement on file with the commissioner:
 - i) For each title insurance policy on a single risk written or assumed after January 1, 1998, [\$500,000 an insert amount] per \$1,000 of net retained liability for policies

⁴ Prior to 1992, the unearned premium reserves were to be released at a rate of 5 percent of the original amount of such reserve for 20 years. Fla. Stat. § 625.111 (1991). In 1992, s. 625.111, F.S., was amended authorizing release of the reserves in 12 equal annual installments. ch. 34, § 1(b), 1992 Fla. Laws, 389-390.

⁵ For example, other states set aside the following reserves on a \$100,000 policy: MO \$15 (\$.015 per \$1,000 liability); PA \$11(\$1 per policy + \$.10 per \$1000 liability); TX \$25 (\$0.25 per \$1000 liability); CA \$23 (4.5% of revenue); VA \$14 (\$1.50 per policy + \$.0125 per \$1000 liability); MN \$23 (10% of total premiums); and LA \$0. American Pioneer Title Insurance Company's Comparison of Statutory Premium Reserve (SPR) for a \$100,000 Policy, Florida Calculation vs. Calculation of Domiciliary State (12/31/98).

STORAGE NAME: h0093s1.rpp

DATE: January 26, 1999

PAGE 4

under d [insert amount] per \$1,000 of net retained liability for policies of \$500,000 or greater; and

ii) [insert amount] of escrow, settlement and closing fees collected in contemplation of the issuance of title insurance policies or guarantees.

Title Insurer's Model Act: Releasing The Unearned Premium Reserve

The NAIC's Title Insurers Model Act provides the following schedule with regard to the release of the unearned premium reserves to the net profit of the insurer:

thirty-five percent (35%) of the aggregate sum on July 1 of the year next succeeding the year of addition; fifteen percent (15%) of the aggregate sum on July 1 of each of the succeeding two (2) years; ten percent (10%) of the aggregate sum of July 1 of the next succeeding year; three percent (3%) of the aggregate sum on July 1 of each of the next three (3) succeeding years; two percent (2%) of the aggregate sum on July 1 of each of the next three (3) succeeding years; and one percent (1%) of the aggregate sum on July 1 of each of the next succeeding ten (10) years. Title Insurers Model Act, § 10 (B)(d), April 1996.

Title Insurer's Model Act: Supplemental Reserves

The NAIC's Title Insurers Model Act addresses supplemental reserves as follows:

A supplemental reserve shall be established consisting of any other reserves necessary, when taken in combination with the reserves required by Subsections A and B of this section, to cover the company's liabilities with respect to all losses, claims and loss adjusted expenses. Title Insurers Model Act, § 10 (C), April 1996. (Subsection A, NAIC Title Insurers Model Act, references the statutory reserve and subsection B references a percentage of premiums.)

B. EFFECT OF PROPOSED CHANGES:

CS/HB 93 changes the amount of the unearned premium reserves which are to be released to the insurer. Reserves established before July 1, 1999, are to be released as follows:

- 30 percent of the initial aggregate sum released on March 31, 1999; June 30, 1999; September 30, 1999; and December 31, 1999. (March and June releases are to be retroactive and reflected on the September 30, 1999, financial statement.);
- 15 percent of the initial aggregate sum on March 31, 2000; June 30, 2000; September 30, 2000; and December 31, 2000;
- 10 percent of the initial aggregate sum on March 31, June 30, September 30, and December 31 during each of the years 2001 and 2002;

STORAGE NAME: h0093s1.rpp

DATE: January 26, 1999

PAGE 5

- 5 percent of the initial aggregate sum on March 31, June 30, September 30, and December 31 during each of the years 2003 and 2004;
- 3 percent of the initial aggregate sum on March 31, June 30, September 30, and December 31 during each of the years 2005 and 2006;
- 2 percent of the initial aggregate sum on March 31, June 30, September 30, and December 31 during each of the years 2007, 2008, 2009, 2010, 2011, 2012 and 2013; and
- 1 percent of the initial aggregate sum on March 31, June 30, September 30, and December 31 during each of the years 2014, 2015, 2016, 2017 and 2018.

The unearned premium reserve accumulated on or after July 1, 1999, are to be released on March 31, June 30, September 30, and December 31 during each succeeding year, over a twenty year period, according to the following schedule:⁶

- 30 percent of the initial aggregate sum during the year next succeeding the year the premium was written;
- 15 percent of the initial aggregate sum during the next succeeding two years;
- 5 percent of the initial aggregate sum during the next succeeding three years;
- 3 percent of the initial aggregate sum during the next succeeding two years;
- 2 percent of the initial aggregate sum during the next succeeding seven years; and
- 1 percent of the initial aggregate sum during the next succeeding five years.

This release schedule is slightly less aggressive than the schedule provided in the current NAIC Title Insurers Model Act.

CS/HB 93 also requires that all domestic title insurers obtain a Statement of Actuarial Opinion from a Fellow in good standing of the Casualty Actuarial Society regarding the insurer's loss and loss adjustment expense reserves, including: reserves for known claims; adverse development on known claims; incurred but not reported claims and unallocated loss adjustment expenses. If the amount of the recommended reserve level stated in the actuarial opinion is greater than the sum of both the known claim reserve and the unearned premium reserve, then the insurer must add the difference to the unearned premium reserve. The additional actuarial reserves are to be released according to the schedule quoted immediately above.

Smaller title insurers may experience a higher risk of loss than larger title insurers.⁷ A higher risk of loss will probably lead to an actuarial opinion with a higher recommended reserve level. Pursuant to this bill, when a smaller title insurer's recommended reserve

⁶ Section 625.111(2)(a), F.S., currently provides that the unearned premium reserves shall be released in 12 equal annual installments, beginning with the calendar year 1993.

⁷ Conference with Steve Rumsey, Senior Vice President and Chief Financial Officer of American Pioneer Title Insurance Company, in Tallahassee, FL. (December 28, 1998).

level increases, it will owe more money into the reserve. This may create a financial concern with many of the smaller title insurance companies.

This bill further provides that an insurer, which receives a waiver from the Department of Insurance of the requirement to obtain an actuarial analysis, is exempt from this bill's actuarial provision. The implication is that there is a provision which authorizes the Department of Insurance to grant a waiver of the requirement to obtain an actuarial analysis. No such provision exists in the bill. In reviewing the statutory provisions, a waiver provision was found in s. 624.424, F.S., but it only authorizes exemptions for title insurers from an annual audit, not from obtaining an actuarial analysis.

Additionally, nothing in the statutory provisions or in the department rules would lead one to believe that the department has authority to waive the requirement that a title insurer obtain an actuarial analysis. More particularly, Rule 4-137.001, Florida Administrative Code, adopts manuals for annual and quarterly reporting requirements for insurers. Nothing in this rule addresses waiver from obtaining an actuarial analysis. Rule 4-137.001 does, however, reference two statutory provisions: s. 624.424(1), F.S., which authorizes the department to adopt the form for financial statements as approved by the NAIC; and s. 624.308(1), F.S., which authorizes the department to adopt rules to implement provisions of law. However, neither section, expressly or impliedly, establishes the authority for the department to allow title insurers to receive a waiver from obtaining an actuarial analysis. Therefore, it is unclear where the authority, if any, exists for such a waiver. This creates uncertainty as to whether any title insurer would be exempt from the actuarial provision set forth in this bill.

This bill reenacts the current definitions of "net retained liability" (total liability retained by a title insurer for a single risk, after taking into account the deduction for ceded liability, if any) and "single risk" (the insured amount of any title insurance policy and provides for an exception where two or more title insurance policies are issued simultaneously covering different estates in the same real property).

C. APPLICATION OF PRINCIPLES:

1. Less Government:

a. Does the bill create, increase or reduce, either directly or indirectly:

(1) any authority to make rules or adjudicate disputes?

No.

(2) any new responsibilities, obligations or work for other governmental or private organizations or individuals?

No.

PAGE 7

(3) any entitlement to a government service or benefit?

No.

b. If an agency or program is eliminated or reduced:

No agency or program is eliminated or reduced.

(1) what responsibilities, costs and powers are passed on to another program, agency, level of government, or private entity?

N/A

(2) what is the cost of such responsibility at the new level/agency?

N/A

(3) how is the new agency accountable to the people governed?

N/A

2. Lower Taxes:

a. Does the bill increase anyone's taxes?

No.

b. Does the bill require or authorize an increase in any fees?

No.

c. Does the bill reduce total taxes, both rates and revenues?

No.

d. Does the bill reduce total fees, both rates and revenues?

No.

e. Does the bill authorize any fee or tax increase by any local government?

No.

PAGE 8

3. Personal Responsibility:

- a. Does the bill reduce or eliminate an entitlement to government services or subsidy?

No.

- b. Do the beneficiaries of the legislation directly pay any portion of the cost of implementation and operation?

No.

4. Individual Freedom:

- a. Does the bill increase the allowable options of individuals or private organizations/associations to conduct their own affairs?

No.

- b. Does the bill prohibit, or create new government interference with, any presently lawful activity?

No.

5. Family Empowerment:

- a. If the bill purports to provide services to families or children:

This bill does not purport to provide services to families or children.

- (1) Who evaluates the family's needs?

N/A

- (2) Who makes the decisions?

N/A

- (3) Are private alternatives permitted?

N/A

- (4) Are families required to participate in a program?

N/A.

(5) Are families penalized for not participating in a program?

N/A.

b. Does the bill directly affect the legal rights and obligations between family members?

No.

c. If the bill creates or changes a program providing services to families or children, in which of the following does the bill vest control of the program, either through direct participation or appointment authority:

This bill does not create or change a program providing services to families or children.

(1) parents and guardians?

N/A.

(2) service providers?

N/A.

(3) government employees/agencies?

N/A.

D. STATUTE(S) AFFECTED:

s. 625.111

E. SECTION-BY-SECTION ANALYSIS:

Section 1 -- Section 625.111, F.S., is amended to provide that the financial statements with evaluation dates on or after July 1, 1999, must include at least an amount equal to the reserve established on December 31, 1999; changes the date and provides that a sum equal to 30 cents for each \$1,000 of net retained liability under each title insurance policy on a single risk written on or after July 1, 1999, [instead of 1992] must be included in the reserve fund; creates an actuarial provision requiring domestic title insurers to obtain an actuarial opinion; provides that if the amount of the recommended reserve stated in the actuarial opinion is higher than the amount in both the known claim reserve and the unearned premium reserve, then the title insurer is to deposit the difference in reserve; provides that some companies may be exempt from this section if they qualify for a waiver from the Department of Insurance; requires the unearned premium reserve prior to July 1, 1999, to be released quarterly and according to a specified schedule herein; provides that the reserve accumulated after July 1, 1999, and the actuarial reserve are to be released quarterly and according to the variable schedule specified; provides that the reserves released are to be deducted from the total unearned premium

PAGE 10

reserve before the actuarial provisions are established; and reenacts the current definitions of "net retained liability" and "single risk."

Section 2 -- Provides an effective date of July 1, 1999.

III. FISCAL ANALYSIS & ECONOMIC IMPACT STATEMENT:

F. FISCAL IMPACT ON STATE AGENCIES/STATE FUNDS:

1. Non-recurring Effects:

None

2. Recurring Effects:

None

3. Long Run Effects Other Than Normal Growth:

None

4. Total Revenues and Expenditures:

None

G. FISCAL IMPACT ON LOCAL GOVERNMENTS AS A WHOLE:

1. Non-recurring Effects:

None

2. Recurring Effects:

None

3. Long Run Effects Other Than Normal Growth:

None

H. DIRECT ECONOMIC IMPACT ON PRIVATE SECTOR:

1. Direct Private Sector Costs:

None

PAGE 11

2. Direct Private Sector Benefits:

The private sector may be able to obtain title insurance at a lower premium from Florida domiciled title insurers.

3. Effects on Competition, Private Enterprise and Employment Markets:

This bill may increase competition for Florida domiciled title insurers doing out-of-state business.

I. FISCAL COMMENTS:

None.

III. CONSEQUENCES OF ARTICLE VII, SECTION 18 OF THE FLORIDA CONSTITUTION:

A. APPLICABILITY OF THE MANDATES PROVISION:

This bill does not require counties or municipalities to spend funds or to take an action requiring the expenditure of funds.

B. REDUCTION OF REVENUE RAISING AUTHORITY:

This bill does not reduce the authority that municipalities or counties have to raise revenues in the aggregate.

C. REDUCTION OF STATE TAX SHARED WITH COUNTIES AND MUNICIPALITIES:

This bill does not reduce the percentage of a state tax shared with counties or municipalities.

IV. COMMENTS:

CS/HB 93 Concerns

1. Section 1 of this bill is in artfully worded and appears to create requirements for the *financial statements*, instead of creating requirements to establish a *reserve fund*.
2. The phrase "actuarial provision" is used as a term of art. This phrase may be commonly known and/or used throughout the title insurance industry, however, its meaning is not defined within this bill nor is it clear from the context.
3. This bill requires a title insurer to obtain a Statement of Actuarial Opinion from a Fellow in good standing of the "Casualty Actuarial Society" regarding the insurer's loss and loss adjustment expense reserves. However, both s. 624.424, F.S., and the NAIC Title Insurers Model Act refer to the American Academy of Actuaries. Proponents suggest removing "Fellow in good standing of the Casualty Actuarial Society" from page 3, lines

1 and 2, and simply adding "qualified actuary." Then place the term "qualified actuary" in the definitional section to be more appropriately defined.

4. This bill provides that an insurer which receives a waiver from the Department of Insurance of the requirement to obtain an actuarial analysis, is exempt from this bill's actuarial provision. This implies that the Department of Insurance has the authority to grant a waiver to title insurers of the requirement to obtain an actuarial analysis. However, there is nothing in this bill, in the department rules, or in the Florida Statutes that would lead one to believe that the department has authority to grant such waivers. See page six of this analysis for a more detailed discussion.

Proponents' Position

Proponents of this bill which are domiciled in the State of Florida and conduct business nationwide, contend that this proposed legislation would have two primary effects on title insurers domiciled in the State of Florida doing business nationwide:⁸

1. **CS/HB 93 would release monies currently held in the unearned premium reserve on the front end of the policy.**

As a bill proponent, American Pioneer stated that it currently holds \$17 million in unearned premium reserves which, according to a study conducted by an actuarial firm pursuant to a contract with American Pioneer, is three times the actuary's recommended reserve level of \$5.5 million. *Id.* (American Pioneer has not provided staff with written data confirming these reserve levels). American Pioneer contends that a majority of this surplus should be released back to the underwriter on the front end of the policy. *Id.*

CS/HB 93 provides for the release of 30 percent of the reserves after the first year compared to the current law which authorizes the release of approximately 8.34 percent in the first year. Pursuant to this bill, in six years, a total of 60 percent of the reserves would be released compared to the current law which authorizes a release of a total of 50 percent of the reserves.

2. **CS/HB 93 would increase out of state competition.**

Proponents contend that CS/HB 93 would increase their ability to compete in out-of-state markets. *Id.*⁹ Florida insurers are bound by Florida reserve rate requirements even when writing policies in other states. *Id.* Proponents suggest that Florida has one of the highest reserve rates in the country and therefore, it is hard to compete with out-of-state insurers. *Id.* Although this bill does not affect reserve rates, proponents suggest that having a more

⁸ Conference with Steve Rumsey, Senior Vice President and Chief Financial Officer of American Pioneer Title Insurance Company, in Tallahassee, Fl. (December 28, 1998).

⁹ One such proponent, Alliance Title of America ("Alliance"), which is domiciled in Florida, supports HB 93 and contends that it puts the smaller insurers in the same position as the insurers in other states. Alliance spoke with its actuarial firm, which also supports the bill. Telephone conversation with Kevin Thomas, General Counsel, Alliance Title of America, domiciled in Florida (December 29, 1998).

STORAGE NAME: h0093s1.rpp

DATE: January 26, 1999

PAGE 13

aggressive return rate of the reserve monies will effectively reduce their overall reserve requirement.

V. AMENDMENTS OR COMMITTEE SUBSTITUTE CHANGES:

On January 20, 1998, the Committee on Real Property and Probate adopted: (1) a "remove everything" after the enacting clause amendment, and (2) an amendment to that amendment.

The "remove everything" amendment requires that where the recommended reserve level set forth in the actuarial opinion is higher than both the known claim reserve and the unearned premium reserve then the insurer is to deposit the difference into the unearned premium reserve.¹⁰ The original bill does not include this requirement. This amendment also changes the dates which establish the reserve and provides a slightly different release schedule than the original bill.

The amendment to the amendment provided that certain reserves should be released at five percent during each of the next succeeding three years, instead of two years.

VI. SIGNATURES:

COMMITTEE ON Real Property and Probate:

Prepared by:

Staff Director:

Christine Hoke, J.D.

J. Marleen Ahearn, Ph.D., J.D.

¹⁰ See discussion on page 5 herein regarding the actuarial provision requirement.