HOUSE OF REPRESENTATIVES STAFF ANALYSIS

BILL #: HB 1983 (PCB IN 04-04) Florida Hurricane Catastrophe Fund
SPONSOR(S): Insurance
TIED BILLS: None **IDEN./SIM. BILLS:** CS/CS/CS/SB 2488

REFERENCE	ACTION	ANALYST	STAFF DIRECTOR
1) Insurance	19 Y, 0 N	Cheek	Cooper
2)			
3)			
4)			
5)			

SUMMARY ANALYSIS

The Florida Hurricane Catastrophe Fund (CAT Fund) was created after Hurricane Andrew as a form of mandatory reinsurance for residential property insurers. The CAT Fund is a source of reimbursement to property insurers for excess losses due to hurricanes. The CAT Fund derives its revenue from actuarially determined "reimbursement premiums" paid by insurers. It has the ability to levy assessments against all property-and-casualty insurance premiums (other than workers' compensation) when reimbursement premiums and other fund resources are insufficient to cover the fund's obligations. Assessments are capped at 4 percent of premium with respect to losses from any one-storm season and an absolute maximum of 6 percent of premium. Payouts are capped at $11 billion for losses from any one-storm season, with provision for a higher cap after the fund is capable of paying $22 billion to cover losses from two storm seasons. The bill also adds several administrative and clarifying provisions. More specifically, the bill:

Expands the Capacity of the CAT Fund by increasing the capacity to $15 billion and adjusting both the initial and subsequent season coverage limits to grow with CAT Fund exposure growth. The bill also funds the extra capacity by increasing the amount of emergency assessments from 4 percent for any one year and 6 percent for all years (of the prior year's gross direct written premium for all property-and-casualty lines, excluding workers' compensation) to 6 percent and 10 percent, respectively.

Modifies the way emergency assessments are recouped by insurers by allowing insurers to collect the assessments from policyholders and then remit the funds as directed. Current law requires insurers to pay the annual assessment amount up front and then make a deemed approved rate filing to recover the assessments from policyholders.

Includes surplus lines in the CAT Fund Assessment Base by extending the assessment base to include surplus lines. The assessments would be made on surplus lines policyholders and collected by the Florida Surplus Lines Service Office to be remitted as directed by the CAT Fund.

Resets the insurance industry retention level to $4 billion as of 2005 and allows it to grow with exposure growth (values of insured property) in the future. This type of adjustment is made under current law, and the insurance industry retention has grown to $4.397 billion as of the CAT Fund's 2003 contract year. In the current law, the insurance industry retention is set at $3 billion as of 1998 and is adjusted for exposure growth each year. Resetting the retention would adjust the retention downward by about $1 billion and increase capacity below the current CAT Fund layer since the aggregate insurance industry retention is expected to exceed $5 billion in 2005.

This bill does not appear to have a fiscal impact but has a potential impact on the private sector.

FULL ANALYSIS

I. SUBSTANTIVE ANALYSIS

A. DOES THE BILL:

1. Reduce government?	Yes[]	No[]	N/A[x]
2. Lower taxes?	Yes[]	No[]	N/A[x]
3. Expand individual freedom?	Yes[]	No[]	N/A[x]
4. Increase personal responsibility?	Yes[]	No[]	N/A[x]
5. Empower families?	Yes[]	No[]	N/A[x]

For any principle that received a "no" above, please explain:

B. EFFECT OF PROPOSED CHANGES:

BACKGROUND

The Florida Hurricane Catastrophe Fund (CAT Fund) was created after Hurricane Andrew as a form of mandatory reinsurance for residential property insurers. The CAT Fund is administered by the State Board of Administration (SBA) and is a tax-exempt source of reimbursement to property insurers for excess losses due to hurricanes. The CAT Fund derives its revenue from actuarially determined "reimbursement premiums" paid by insurers. It has the ability to levy assessments against all property-and-casualty insurance premiums (other than workers' compensation) when reimbursement premiums and other fund resources are insufficient to cover the fund's obligations. Assessments are capped at 4 percent of premium with respect to losses from any one storm season and an absolute maximum of 6 percent of premium. Payouts are capped at $11 billion with respect to losses from any one storm season, with provision for a higher cap after the fund is capable of paying $22 billion to cover losses from two storm seasons.

During the 2003 Legislative Session, the CAT Fund proposed legislation, which was sponsored by Representative Waters in the House and by Senator Posey in the Senate. Although the legislation passed out of the House and made it on the Senate calendar, it failed to make it to the floor of the Senate on the final day of the session due to time constraints. Unsuccessful attempts were made to get the legislation heard during several of the special legislative sessions over the summer. For the 2004 Legislative Session, the proposed legislation is similar to what was proposed during 2003 with the exception that it increases CAT Fund capacity more aggressively and addresses several new (but noncontroversial) administrative issues.

A concern has been expressed that the CAT Fund capacity needs to "catch up" for some of the ground lost during the last several years. This entails increasing the capacity of the CAT Fund to $15 billion and requires that additional emergency assessments be authorized. In addition, the idea of lowering the insurance industry's retention to $4 billion is included in an effort to lower costs to policyholders. These concepts are discussed in more detail below.

MAJOR CHANGES TO CURRENT LAW

The bill increases the capacity and enhances the structure of the CAT Fund, as well as addresses several administrative issues. The capacity of the CAT Fund has been limited to $11 billion since 1999. However, reported exposure to the CAT Fund has increased over 50 percent during this time. As a result, participating insurer coverage has declined by over 10 percent and their CAT Fund retention (deductible) has increased by over 35 percent during the last 5 years. The main reason this has occurred is because "subsequent season capacity" has been building up while "initial season capacity" has been required to hold steady at $11 billion. Subsequent season capacity is defined as the CAT

Fund capacity that is available the year following a hurricane loss that triggers CAT Fund coverage. Subsequent season capacity results in the CAT Fund being able to recharge its capacity following a major event that depletes the CAT Fund's resources. The inability to recharge the CAT Fund following a major hurricane event could result in a severe market disruption as insurers may be required to replace inexpensive CAT Fund coverage with more expensive private reinsurance at perhaps three to four times the cost.

The CAT Fund's capacity is composed of its cash balance, which is built up from premiums and investment income, and its ability to issue bonds that are financed by emergency assessments on all property-and-casualty lines of business, except workers' compensation. According to the SBA, as of May 2003, the CAT Fund had enough capacity to provide $11 billion for an initial season loss and to fully recharge with $11 billion for a subsequent season loss. Since 1999, the "gap" between initial season and subsequent season capacity has been closing. The CAT Fund has now reached the "break even" point, and the gap will now begin to widen in the other direction as initial season capacity should begin to grow and subsequent season capacity will remain constant at $11 billion. Under current law, subsequent season capacity will remain at $11 billion for some time into the future, but the initial season capacity will begin to grow depending on the growth in the CAT Fund's assessment base and the level of interest rates. This will create a bigger and bigger potential problem each year in that the current law does not provide for the full recharging of capacity after a major event. Also, the manner in which capacity grows is not directly related to the growth of insured values in the state, but is influenced in large part by changes in the interest rate environment. This results in the future capacity of the CAT Fund being uncertain, which causes difficulties as insurers plan for their private reinsurance purchases each year.

Changes to the law are being proposed that correct this problem and allow the capacity of the CAT Fund to grow with exposure growth (insured value growth) in the state. The SBA contends that this is a more rational approach and will allow insurers to better plan their reinsurance programs. Additionally, a "catch up" adjustment is being added to make up for the lack of growth in the CAT Fund's capacity since 1998. By increasing the CAT Fund's capacity from $11 billion to $15 billion, an additional $4 billion of capacity will be created that should help insurers write more business and depopulate the residual market (Citizens Property Insurance Corporation [Citizens]). The number of Citizens policyholders has grown significantly over the last several years and pays the largest premium to the CAT Fund. There is a provision that limits the growth of capacity to the dollar growth in the cash balance each year.

The State of Florida has been growing at the rate of about 3 million people every ten years. Land falling hurricanes are infrequent events, but occur on average about once every other year. Severe hurricanes (Category 3 or higher with wind speeds exceeding 110 miles per hour) tend to make landfall in Florida on average once every four years. The combination of exposure growth and hurricane frequency results in an average cost of $2.2 billion a year. Thus, over the next 30 years, the state can expect over $60 billion of insured losses. Insurers, private reinsurers, and the CAT Fund will share in financing the cost of these losses.

The proposed CAT Fund's legislation is designed to increase the CAT Fund's capacity to $15 billion (a "catch-up" provision) and then to adjust the capacity of the CAT Fund with the growth of insured values (exposure) in the state. It also allows for the "full" recharging of the CAT Fund's capacity following a large event. The CAT Fund's role is not only to reimburse insurers for their covered losses after a hurricane event, but also to help maintain capacity in the residential property insurance marketplace following an event. If there is a large reduction in CAT Fund capacity following a major hurricane loss, insurers will need to replace CAT Fund coverage at a cost of three to four times the cost of CAT Fund coverage (if coverage is obtainable in the private reinsurance market).

In order to accomplish growth in the CAT Fund's capacity, an increase in the CAT Fund's assessment authority is needed. Under current law, the emergency assessment authority is limited to 4 percent per year and 6 percent in the aggregate for all years. The proposed change would be to increase these limits to 6 percent maximum per year and 10 percent aggregate assessments for all years.

Another aspect of the legislation includes surplus lines in the CAT Fund's assessment base. This would expand the CAT Fund's assessment base by about 10 percent. The current assessment base is about $22 billion in premiums and includes all property-and-casualty lines with the exception of workers' compensation. The comparable lines for surplus lines represents about $2.8 billion in premiums. Surplus lines is included in Citizens Property Insurance Corporation's (Citizens) assessment base, and the proposed CAT Funds legislation is designed to operate similarly to Citizens in that the assessments would be collected by the Florida Surplus Lines Service Office from the surplus lines agent and remitted by the various surplus lines policyholders. The benefit of including surplus lines in the CAT Fund's assessment base will be to spread the potential cost of bonding over a broader assessment base and lower assessments to other policyholders by about 14 basis points.

Another structural aspect addressed by the proposed legislation is to lower participating insurers' retentions (or deductibles). Insurer retention has been designed to increase each year as exposure grows. Since 1999, an individual insurer's retention (the amount of loss they are required to absorb prior to being eligible for CAT Fund reimbursement) has increased by 35 percent. The major reason for this has been the rapid exposure growth, which has occurred since 1998. A legislative change in 2001 added coverage to the CAT Fund for additional living expenses (ALE). The result has been to abruptly increase insurer retentions. The proposed legislation resets the retention by adjusting the insurance industry retention level down from $4.397 billion, where it was for contract year 2003/2004, to $4 billion. Since private reinsurance is more expensive below the CAT Fund coverage layer, it is thought that less expensive CAT Fund coverage will help lower consumer costs. Without resetting the retention, the aggregate insurance industry retention is expected to exceed $5 billion for 2005. There is a provision that limits the growth of the retention to the percentage growth in the capacity each year.

The administrative issues addressed in the bill are as follows: 1) clarifies "prior fiscal year" for mitigation funding; 2) allows higher exposure amounts for insurers who are eligible to opt out of the CAT Fund; 3) provides greater flexibility to purchase reinsurance, if it is needed; 4) allows for interest to be charged on delinquent assessments; 5) excludes excess policies and deductible buy-back policies by rule; 6) clarifies excess recoveries to Citizens; 7) clarifies and expand coverage for additional living expenses; 8) adds a definition for "corporation"; 9) clarifies the publication of borrowing capacity estimates and notification to insurers; 10) deletes language requiring that recoveries from reinsurance and the CAT Fund shall not exceed 100 percent of the insurer's losses; 11) adds language to clarify that emergency assessments can be used for debt service coverage; 12) changes language related to auditing to establish by rule standards that are more appropriate for validating the accuracy of exposures and losses; and 13) clarifies that assessments can be used to pay off debt that has been refinanced.

EFFECTIVE DATES

As indicated below, the bill has two effective dates. The changes in Section 1 are meant to become effective upon becoming law. These include all of the administrative issues listed below with the exception of the last two (emergency assessments used for debt service and clarifying that emergency assessment can be used to pay off refinanced debt). The changes in Section 2 have an effective date of June 1, 2005, and include the controversial issues listed below and the last two administrative issues. Section 3 provides that "Except as otherwise provided herein, this act shall take effect upon becoming law."

CONTROVERSIAL ISSUES

It is anticipated that any controversy surrounding the proposed CAT Fund legislation will arise from four areas: 1) increasing the CAT Fund's capacity; 2) modifying the way emergency assessments are recouped by insurers; 3) the inclusion of surplus lines in the assessment base; and 4) resetting the retention.

Increasing the CAT Fund's Capacity – The question arises as to how much should capacity be increased. The proposal to increase the capacity to $15 billion may be controversial since it requires much greater bonding ($8-9 billion) and higher assessment authority (6 percent per year and 10 percent in the aggregate). If the emergency assessment authority is not increased, there could be a large "gap" between initial and subsequent season capacity. In such a case, the CAT Fund may not be able to stabilize the residential property insurance market after the next large hurricane event, especially if interest rates are high at the time. Recent figures for the state's total debt indicate that the state currently has $20.4 billion in outstanding debt. A CAT Fund $9-billion bond issue would be large after a major hurricane (the probability of occurring would be once every 50 years or so), and if back-to-back hurricanes hit, the total CAT Fund debt could approach $23 billion, although the likelihood of this occurring is extremely remote.

Modifying the way emergency assessments are recouped by insurers – The bill modifies the way emergency assessments are recouped by insurers by allowing insurers to collect the assessments from policyholders and then to remit the funds. This language is designed to solve the controversial issue of how assessments are recouped, which is that insurers have to pay the assessments up front before collecting the funds from their policyholders.

The inclusion of surplus lines in the assessment base – The issue of including surplus lines in the CAT Fund assessment base was a very controversial issue during the 2003 legislative session and the special sessions that followed. The surplus lines insurers opposed this provision. Emergency assessments are levied on all property-and-casualty lines except workers' compensation. Only $4.7 billion of the $22 billion assessment base represents residential property insurance premiums, the remaining premiums are from other lines of business, which do not participate in the CAT Fund. The surplus lines insurers have argued that they should not be included in the emergency assessment base since they do not participate in the CAT Fund. If this argument was considered a valid argument, the CAT Fund could not exist as a tax-exempt trust fund since a requirement of the Internal Revenue Service in granting tax-exempt status to the CAT Fund is that a broad base of insurance lines which do not benefit from and are not covered by the CAT Fund support the bonding needs. The inclusion of surplus lines will increase the emergency assessment base by over 10 percent.

Resetting of the retention – It is anticipated that the reinsurers represented by the Reinsurance Association of America (RAA) will oppose resetting the insurance industry retention level to $4 billion. The RAA has argued for years to raise the retention. Their concern is for the private reinsurance market to write a larger and larger share of the reinsurance business in the state. They argue that the CAT Fund's capacity should only be used for large catastrophes and preserved for the "mega" type events as opposed to reimbursing the smaller events (which they argue can be handled by the private reinsurance market).

The lowering of the retention to $4 billion will have an impact on CAT Fund reimbursement premiums charged to insurers. Such premiums are expected to increase by +25 percent. Although the increase may be offset by reductions in the price of private reinsurance below the CAT Fund, not all insurers have private reinsurance below the CAT Fund. Also, some insurers with national catastrophe reinsurance programs do not get credit for CAT Fund coverage in Florida since they write a small portion of their business in the state. Regardless of these situations, the lowering of the retention will benefit some insurers and may provide benefits to the overall insurance system in Florida.

An additional concern regarding lowering the retention is that the CAT Fund will be triggered more frequently, which will have a tendency to exhaust the build up of cash quicker than otherwise. The other side of the argument is that a lower retention means larger CAT Fund premiums, which builds cash quicker.

ADMINISTRATIVE PROVISIONS

Clarifying "prior fiscal year"
Each year the Legislature appropriates $10 million from the investment income of the CAT Fund and may appropriate up to a maximum of 35 percent of the CAT Fund's investment income. There is lack of clarity under the current statute in that the term "prior fiscal year" could be interpreted in one of two ways – either the past fiscal year-end or the upcoming fiscal year-end. The problem of using an interpretation based on the upcoming fiscal year-end is that the amount of investment income would need to be estimated prior to the end of the legislative session. The proposed change defines "prior fiscal year" to mean the most recently concluded fiscal year for which audited financial statements are available. This would solve the problem of not knowing exactly how much is available each year.

Increasing the exposure limit for de minimis exposure
Six participating insurers currently qualify as writing de minimis exposure for the 2003/2004 contract year of the CAT Fund. The aggregate CAT Fund premium is $1,040. Current law allows the SBA to provide for an exemption if insurers write business on covered policies with less than $500,000 in exposure. The proposed change is to increase the limit to $10 million in exposure. Such a change would add another 21 insurers who would be eligible for an exemption, bringing the total to 27 insurers, and representing an aggregate CAT Fund premium of about $19,323. The largest individual insurer's premium would be around $4,640. Allowing an exemption for these insurers would not adversely impact the actuarial soundness of the CAT Fund and would facilitate the administration of the CAT Fund. It would also relieve insurers that write small amounts of residential insurance from participation and reporting requirements (at their option). Often, an insurer will write only a few residential policies on its books as "accommodation business" when its primary business is business commercial lines.

Broadening the selection of reinsurers
The proposed legislation broadens the selection of reinsurers from which the CAT Fund may purchase reinsurance by allowing for the purchase of reinsurance from reinsurers acceptable to OIR rather than being limited to the purchase of reinsurance from a reinsurer approved under s. 624.610 F.S.

Although the CAT Fund is not presently considering the purchase of reinsurance, flexibility may be needed in the future if circumstances change and reinsurance becomes a feasible option. During 1999, the CAT Fund considered, but rejected, the purchase of a reinsurance product that would have insured against a bonding shortfall. Reinsurers who are capable of designing and offering products specific to the CAT Fund's needs may not have been previously approved under s. 624.610, F.S. Reinsures may be required to enter into "fronting company" arrangements to offer a specific product. This was the case in 1999. Such arrangements can add to the cost of purchasing reinsurance. By removing the requirement to procure reinsurance only from a reinsurer approved under s. 624.610 F.S. and allowing the CAT Fund to procure reinsurance from reinsurers "acceptable" to OIR, the CAT Fund would have access to a broader reinsurance market. This could include other U.S. reinsurers as well as European and Bermudan reinsurers.

Providing rulemaking authority to allow for the charging of interest on late remittances
It has been recognized there is a need to allow specifically for the charging of interest on late remittances. Remittances would include reimbursement premiums, emergency assessments, and any other situation where funds are due the CAT Fund. The proposed provisions that deal with adding surplus lines to the CAT Fund's assessment base are impacted by this provision by allowing the CAT Fund to specify interest charges on delinquent funds due from surplus lines agents after collecting emergency assessments from policyholders.

Providing specific rulemaking authority to address the need to exclude certain covered policies where rating is difficult or impractical

Certain situations often arise where insurers have difficulty reporting exposure values. Problems may arise due to the way a policy is written or how it is combined with other coverages. For example, residential commercial exposure may be covered in the same policy that covers business commercial exposure. It may be difficult or impossible for an insurer to split out the business exposure from the residential exposure in these situations. Policies written on a multiple-state basis and those using either blanket limits or blanket deductibles could present similar problems. There are also situations that have been recently recognized where an insurer may write a deductible buy-back policy. Since such policies may be for less than the full insured value of the risk, there can be rating inequities associated with insuring an exposure where the probabilities of loss are greater per given dollar of value for one reported exposure than another. Individual ratemaking is often required in these situations, and can be expensive. If an insurer writes a small amount of business, the cost of rating the business may exceed the calculated CAT Fund premium. What the proposed statutory language will do is give the SBA the authority to adopt rules to exclude by type or category policies that require individual ratemaking.

Clarifying excess recoveries for Citizens

The law provided for excess recoveries to benefit Citizens. Excess recoveries are those CAT Fund funds that are available after all other insurers have received their pro rata share (based on CAT Fund premiums) of the CAT Fund's capacity. Citizens has two contracts with the CAT Fund. The creation of Citizens from the combination of the Florida Windstorm Underwriting Association and the Florida Residential Property and Casualty Joint Underwriting Association creates a need to clarify the best way for excess recoveries to be handled. Clarifications in the statutory language are made such that each account within Citizens receives a pro rata share of excess recoveries based on losses rather than premiums. This will add greater certainty to debt holders of Citizens' bonds, as well as banks advancing lines of credit to Citizens.

Clarifying and allowing greater flexibility in covering additional living expenses

Situations have arisen where the current limitations in the law of 20 percent on a structure and 40 percent on contents works to penalize insurers who write additional living expenses (ALE) with policies other than standard homeowners policies. The clarification allows greater flexibility and more coverage where ALE is offered without unnecessarily limiting coverage for some insurers.

Adding the definition of corporation

The addition of the term "corporation" to the definitions section of the law will help distinguish between the "CAT Fund Finance Corporation" and "Citizens Property Insurance Corporation" to avoid confusion.

Clarifying the publication of borrowing capacity estimates and notification to insurers

Language is added to clarify the ambiguity that currently exists regarding reporting requirements. The statutory language will be more in line with current notification practices and provide insurers with more meaningful and timely information.

Recoveries from Reinsurance

Language is deleted requiring that recoveries from reinsurance and the CAT Fund should not exceed 100 percent of the insurer's losses. This language is no longer relevant due to how the CAT Fund payout provisions operate and due to current practices in the reinsurance industry. The CAT Fund's reimbursement provisions prior to 1999 allowed an insurer to collect more than its expected payout (share of capacity based on its CAT Fund premium). Insurers could have been reimbursed for losses to the extent that there was any unused capacity. Today, this cannot happen since the law limits an insurer's recovery to a pro rata share of the overall capacity based on its CAT Fund reimbursement premium (the sole exception is Citizens). There is not a concern of overpaying an individual participating insurer since reimbursements are limited. Insurers pay an actuarially sound premium and receive the appropriate benefit in terms of their recovery. Prior to 1999, an insurer could get a windfall if there happened to be excess capacity. In order to conserve capacity, a provision in the law required that any excess recovery above 100 percent of the insurer's losses be returned to the CAT Fund. Today, the CAT Fund is better understood by reinsurers, and reinsurance contracts coordinate very closely with CAT Fund benefits. Therefore, the possibility of a recovery in excess of 100 percent of an insurer's losses is highly unlikely. Even if it did happen, this would not be a significant detriment to the CAT Fund or other participating insurers.

Revising Language related to Auditing Requirements
The bill changes language related to auditing and the requirement of "inspect, examine, and audit" . . ."in such manner as is consistent with generally accepted auditing standards" to "examine" and "in accordance with standards established by rule for the specific purpose of validating the accuracy of exposures and losses required to be reported under the terms and conditions of the reimbursement contract." This language is more appropriate since the CAT Fund is not doing financial audits nor opining on the financial status of insurance companies.

Emergency assessments used for debt service coverage
Language is added to clarify that emergency assessments can be used for debt service coverage. This helps avoid a problem if subsequent season capacity is needed and removes a potential constraint to ensure greater bonding potential. The CAT Fund's bond documents require debt service to have a 1.5 times coverage ratio. If capacity is increased to $15 billion and bonding is needed for a large subsequent season loss, reimbursement premiums alone will not meet the 1.5 times coverage requirement. Part of the emergency assessments will be needed to meet the debt coverage provisions in the bond documents. The added language ensures this can be done and that bonding capacity is maintained for a subsequent season event.

Clarifying that emergency assessments can be used to pay off bonds used to refinance debt
Language is added to clarify that emergency assessments can be used to pay off debt that has been refinanced. Language in the current law is not clear. The change ensures that once debt is outstanding it can be refinanced as interest rates decline, thus allowing the CAT Fund to take advantage of lower cost refinancing.

C. SECTION DIRECTORY:

<u>Section 1</u>: Amends s. 215.555, F.S., relating to the *Florida Hurricane Catastrophe Fund*.

<u>Section 2</u>: Amends s. 215.555, F.S., relating to the *Florida Hurricane Catastrophe Fund*. Provides an effective date of June 1, 2005.

<u>Section 3</u>: Provides the following: "Except as otherwise provided herein, this act shall take effect upon becoming law."

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:

The bill extends the CAT Fund assessment base to include surplus lines policies. The assessments would be made on surplus lines policyholders and collected by the Florida Surplus Lines Service Office to be remitted as directed by the CAT Fund.

The private sector impact is contingent upon a series of large hurricanes occurring in successive years, triggering the fund. According to the SBA, the likelihood of this is remote. No private impact is anticipated under any circumstance over the next 2 years. The increase in emergency assessment authority from 4 percent per year and 6 percent in the aggregate to 6 percent per year and 10 percent in the aggregate will not have an immediate impact on the private sector even after a large hurricane event. This is because the cash balance of the fund is of such size (over $5 billion), it is anticipated that less than a 2-percent emergency assessment is sufficient to fund bonding needs.

D. FISCAL COMMENTS:

The bill is expected to help stabilize the property insurance market, particularly after a major hurricane, by increasing capacity and providing insurers with a relatively constant layer of reinsurance, which grows by the same amount as exposure to losses grow, and which is more likely to be maintained the year following a storm season that triggers fund losses.

The impact of resetting the aggregate industry retention to $4 billion and providing for a $15 billion limit starting in 2004 may significantly increase reimbursement premiums. However, overall reinsurance costs to the policyholder, because coverage from the fund may be significantly less expensive than private reinsurance for some insurers, may decline. The precise amount of such decline cannot yet be quantified.

Surplus lines insurance policyholders would be subject to the emergency assessments, if they are levied. See Effects of Proposed Changes, above, for the impact on increasing the assessment base.

The increase in the maximum potential assessments against property-and-casualty insurers has a very low probability of actually being needed. But the possibility of such assessments could be realized if multiple year storms require the fund to pay maximum levels of reimbursement. In such a case, insurers would be permitted to recoup such costs from their policyholders, which include all lines of property-and-casualty insurance.

The bill increases the minimum amount of exposure (insured values) an insurer can write and be exempt from the fund. According to the SBA, this allows approximately 27 additional insurers the option of not participating in the fund, and facilitates the administration of the fund where small premiums and very low coverage is involved. The total fund premium otherwise payable by these insurers would be less than $20,000, and the largest individual insurer's premium would be approximately $4,600.

III. COMMENTS

A. CONSTITUTIONAL ISSUES:

1. Applicability of Municipality/County Mandates Provision:

   None.

2. Other:

None.

B. RULE-MAKING AUTHORITY:

The bill provides specific rulemaking authority to address the need to exclude certain covered policies that require individual ratemaking. The bill also provides specific rulemaking authority to allow for the charging of interest on late remittances.

C. DRAFTING ISSUES OR OTHER COMMENTS:

Comments:

According to SBA, a summary of the benefits and ramifications of the proposed legislation are as follows:

Summary of the Benefits of the Legislation

- The bill increases CAT Fund capacity to $15 billion, thereby adding $4 billion of reinsurance to the Florida market, thus helping make residential property insurance more affordable to consumers. Extra reinsurance capacity will allow insurers to write more business and thus be able to either keep business out or take business out of the residual market (Citizens).

- The bill allows the capacity of the CAT Fund to grow with exposure (insured value) growth in Florida and thus keep pace with the rapid growth of the state.

- The bill allows for the fully recharging or replenishment of capacity after a major event to avoid or mitigate market disruptions after a large hurricane.

- The bill lowers potential assessment costs by the inclusion of surplus lines in the CAT Fund's assessment base, and thus spreads more equitably the cost of a catastrophe among a broader base of insurance lines.

- The bill improves the operations and administration of the CAT Fund by addressing several administrative issues.

- The bill helps improve the financing structure of Citizens Property Insurance Corporation.

- The bill allows insurers to recoup emergency assessments from policyholders prior to remitting the funds.

Ramifications of the Proposed Legislation

- The bill increases the potential for a larger bond issuance (currently $6 billion to $9 billion for an initial season).

- The bill increases the emergency assessment authority from 4 percent per year and 6 percent in the aggregate to 6 percent per year and 10 percent in the aggregate.

- The combination of increasing the capacity limit to $15 billion and reducing the aggregate insurance industry retention (deductible) to $4 billion from the projected $5 billion will increase CAT Fund reimbursement premiums by about +25 percent.

- The inclusion of surplus lines will be controversial and will be opposed by the surplus lines insurers.

- The expansion of the CAT Fund capacity (to $15 billion and lowering the retention to $4 billion) will be opposed by private reinsurers.

- The increase in the emergency assessment authority may be opposed by some in the insurance industry, as well as by special interest groups.

IV. AMENDMENTS/COMMITTEE SUBSTITUTE CHANGES

None.