

SENATE STAFF ANALYSIS AND ECONOMIC IMPACT STATEMENT

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

Prepared By: Banking and Insurance Committee

BILL: PCS/SB 1488

SPONSOR: Banking and Insurance Committee and Senator Garcia

SUBJECT: Property Insurance

DATE: March 26, 2005

REVISED: _____

ANALYST	STAFF DIRECTOR	REFERENCE	ACTION
1. Deffenbaugh	Deffenbaugh	BI	Pre-meeting
2. _____	_____	JU	_____
3. _____	_____	GA	_____
4. _____	_____	WM	_____
5. _____	_____	RC	_____
6. _____	_____	_____	_____

I. Summary:

PCS/SB 1488 makes the following changes to the laws related to property insurance, primarily affecting residential property insurance:

Florida Hurricane Catastrophe Fund (FHCF) -- Lowers the “retention” or amount of residential hurricane losses that insurers must meet to be reimbursed from the FHCF, from \$4.96 billion to \$4.5 billion per hurricane, for the 2005 contract year. Reduces the retention to one-third of the full retention for the third and each additional hurricane in a year (in order of loss magnitude).

Low-interest loan program for hurricane loss mitigation -- Requires the Department of Community Affairs to establish a low-interest loan program for homeowners to retrofit their homes to reduce hurricane losses. Up to \$3 million of the \$10 million annually appropriated to DCA from the FHCF could be used for subsidizing or guarantying loans by financial institutions. Deletes the requirement that at least \$2.8 million be used for mobile home tie-downs.

Insurance Rating Law

- Authorizes the Financial Services Commission to adopt rules establishing standard rating territories for residential property insurance;
- Repeals the law that allows an insurer to submit a rate filing to an arbitration panel after it has been disapproved by the Office of Insurance Regulation (OIR);
- Requires a public hearing for property insurance rate filings exceeding 15 percent;
- Provides that hurricane loss models approved by the Florida Commission on Hurricane Loss Projection Methodology are admissible and relevant in a rate proceeding only if OIR and the insurance consumer advocate have access to all aspects of the model;

- Prohibits an insurer from recouping more than 1 year of reimbursement premium paid to the FHCF at a time.

Citizens Property Insurance Corporation ("Citizens")

- Changes appointments to the board of governors from 7 appointed by the Chief Financial Officer (CFO), to 2 members each appointed by the Governor, CFO, President of the Senate, and Speaker of the House or Representatives (8 total);
- Limits personal lines dwelling coverage to \$1 million;
- Requires that rates for Citizens shall be actuarially sound and not excessive, inadequate, or unfairly discriminatory, rather than the highest average rate in a county compared to the 20 leading insurers in the state, for those areas where OIR determines that a reasonable degree of competition does not exist;
- Repeals authority for Citizens to provide bonuses to insurers taking policies out of Citizens;
- Requires Citizens to make its best efforts to procure catastrophe reinsurance to cover its projected 100-year probable maximum loss;
- Requires the Auditor General to conduct an operational audit of Citizens.

Standard Personal Lines Residential Policies -- Requires the CFO to appoint an advisory committee to develop standard personal lines policies to submit for approval to OIR by January 1, 2006, to be offered by all insurers within 12 months after the effective date.

Disapproval of Policy Forms -- Authorizes OIR to disapprove a policy form for property and casualty insurance if it contains provisions that are unfair or inequitable, contrary to the public policy of this state, or that encourage misrepresentation.

Checklist of Coverage -- Requires that insurers provide a checklist of coverage for homeowners including whether standard policy provisions are included, limits of liability, property covered and not covered, replacement cost or actual cash value coverage, primary exclusions, etc.

Hurricane Deductibles --

- Increases the maximum allowable deductible for personal lines residential policies from 5 percent to 10 percent of the dwelling limits;
- Requires insurers to offer deductibles of 1 percent, 2 percent, 5 percent, and 10 percent of dwelling limits for personal lines residential policies, rather than just 2 percent;
- Requires that the dollar amount of a percentage deductible be specified.

Replacement Cost Coverage -- Requires that if a loss is insured for replacement cost, the insurer must pay the replacement costs without holdback of any depreciation in value, whether or not the insured replaces or repairs the dwelling or property.

Mediation Program -- Expands the mediation program administered by the Department of Financial Services for resolving claims to commercial policies, and provides a penalty for insurers failing to notify claimants of their right to mediation.

Valued Policy Law (Mierzwa) -- In response to a recent district court opinion, provides legislative intent that the valued policy law is not intended to require an insurer to pay for a loss caused by a peril other than the covered peril.

Notice of Premium Discounts for Hurricane Loss Mitigation -- Requires insurers to notify applicants and policyholders of the availability and amount of premium discounts and credits for fixtures and construction techniques that reduce the amount of loss in a windstorm.

Timely Payment of Claims -- Requires property insurers to pay, deny, or request additional information on claims within 30 days, subject to a 10 percent annual interest penalty.

Additional Staffing for Insurance Consumer Advocate -- Appropriates \$350,000 from the Insurance Regulatory Trust Fund and 4 positions to the Office of the Consumer Advocate appointed by the CFO.

This bill substantially amends the following sections of the Florida Statutes: 215.555, 215.559, 627.062, 627.0628, 627.0629, 627.351, 627.411, 627.4143, 627.701, 627.7011, and 627.7015.

The bill creates the following sections of the Florida Statutes: 627.06291, 627.40951, 627.711, and 627.712.

The bill repeals the following section of the Florida Statutes: 627.3511.

II. Present Situation:

The 2004 Hurricane Season

Hurricanes Charlie, Frances, Ivan, and Jeanne struck Florida within a 45-day period between August 13 and September 26, 2004, causing extensive damage throughout the state. The Governor issued orders declaring a state of emergency during this period and the President of the United States declared most of Florida a federal disaster area.

As of March 10, 2005, insurance companies have reported to OIR that 1.6 million property insurance claims have been filed for the four hurricanes and that insurers have paid \$15.3 billion in total claims payments. The companies estimate that the total expected gross property loss will reach \$22.8 billion. This figure includes residential, commercial (business), and auto losses, but not National Flood Insurance Program losses. But, this amount also includes the amount of losses below the deductible (not paid by the insurer), estimated at \$3.1 billion for residential deductibles alone, plus an unreported amount of deductibles for non-residential policies.

Joint Select Committee on Hurricane Insurance

On January 5, 2005, the Senate President and House Speaker appointed the Joint Select Committee on Hurricane Insurance and directed it to study all aspects of the property insurance market that promote the availability and affordability of coverage, but to focus on particular issues related to hurricane deductibles, the Florida Hurricane Catastrophe Fund (FHCF), and

Citizens Property Insurance Corporation (Citizens). The Joint Select Committee issued its final report and recommendations on February 25, 2005.¹ The recommendations were as follows:

Hurricane Deductibles and Consumer Disclosures

- 1) Retain the mandatory annual hurricane deductible for homeowners policies and other personal lines residential policies, rather than making the annual deductible an option for such policies.
- 2) Require insurers to offer both an annual hurricane deductible and a per event deductible to condominium associations and other commercial residential policies.
- 3) Petition Congress to allow for hurricane savings accounts so that residential policyholders can save money, tax-free, to cover deductible expenses, repair costs, or to strengthen their home, recognizing that implementation may be long-term.
- 4) The Legislature should consider requiring insurers to offer hurricane deductibles of 1, 3, 5, 7, and 10 percent of policy limits, in addition to the 2 percent deductible that must currently be offered. Recognizing that requiring insurers to offer lower deductibles may have a negative impact on the financial capacity of insurers to write policies, the Legislature should consider linking this requirement to other means for increasing the capacity of insurers to write policies, such as lowering the retention for insurers to be reimbursed by the Florida Hurricane Catastrophe Fund (addressed below).
- 5) Require insurers to compute and prominently display the actual dollar value of percentage hurricane deductibles on the declarations page of the insurance policy and on the premium renewal notice.
- 6) Require residential property insurers to provide a standard disclosure form to be signed by applicants and policyholders, adopted by rule by the Financial Services Commission, that explains in easily understood terms what is covered and what is not covered, principal limitations on coverage, the method for determining the value of damage or loss, and options available for different types or amounts of coverage.

Florida Hurricane Catastrophe Fund

- 7) Lower the retention in the FHCF, primarily to address multiple hurricanes within the same year.
- 8) Further study the premium structure for the FHCF to determine whether additional premiums should be charged to reduce the likelihood of bonding.

Citizens Property Insurance Corporation

- 9) The Legislature should begin a complete reexamination and study of the statutory requirements and operation of Citizens Property Insurance Corporation and give specific consideration to the following issues:
 - a. Whether appointments to the Board of Governors of Citizens, who are all currently appointed by the Chief Financial Officer, should be divided among additional state officers and whether the criteria for board membership should be revised.
 - b. Whether the bonuses paid by Citizens to carriers taking policies out of Citizens provide a cost-effective means of reducing Citizens' potential liability.

¹ The final report is available at: <http://www.flsenate.gov/data/committees/joint/jshi/finalreport.pdf>

- c. Whether the “Consumer Choice” law should be repealed or amended to assure that Citizens serves as the insurer of last resort, so that a policyholder would not be eligible for coverage from Citizens if an offer of coverage is made by an authorized insurer at approved rates, regardless of whether the current agent of record is willing or able to be appointed by the insurer.
- d. Whether the rates for Citizens should be based on actuarial soundness rather than compared to rates for other insurers, in areas where a reasonable level of competition does not exist.
- e. Whether coverage should be limited to \$1 million for personal lines, windstorm-only policies in the High Risk Account, as currently limited for multiperil personal lines policies in the Personal Lines Account.
- f. Whether Citizens has hired an adequate level of permanent claims and adjusting staff in addition to outsourcing its claims adjusting to independent adjusting firms.
- g. Consider any legislative recommendations made by the Task Force on Policyholder Services and Relations for Citizens Property Insurance Corporation.
- h. Require the Office of the Auditor General to conduct an Operational Audit of Citizens regarding its customer service, claims handling, accessibility of policyholder information to the agent of record, takeout programs, and financing arrangements. The audit should contain policy alternatives for legislative consideration.
- i. Whether Citizens should be required to implement specific programs to address problems of communication and service to agents and policyholders, such as establishing an independent advisory committee and providing web-based access to policyholder information.

Hurricane Loss Mitigation

- 10) Require insurers to clearly notify homeowners about the availability and amount of premium discounts for hurricane loss mitigation along with an explanation of what a homeowner must do to qualify for these discounts.
- 11) Appropriate mitigation funds from the Florida Hurricane Catastrophe Fund to subsidize low-interest loans to consumers to retrofit structures to mitigate hurricane damage, for structures built before the new building codes took effect.
- 12) Improve methods of reducing the amount of damage caused by hurricanes. This will include evaluating whether the building code should be strengthened and/or have the geographic boundaries of the high speed wind zone expanded. There should also be evaluations of other methods of strengthening new and existing structures, including but not limited to, possible tax incentives and additional insurance discounts.

Hurricane Loss Models

- 13) Amend s. 627.0628(3), F.S., to provide that the Office of Insurance Regulation and the Insurance Consumer Advocate must have access to all of the assumptions and components used in developing a hurricane loss model found to be acceptable by the Florida Commission on Hurricane Loss Projection Methodology, in order for the findings and factors of the model to be admissible and relevant in consideration of an insurer’s rate filing. Provide an exemption from the Public Records law and Public Meetings law for any trade secret information related to a proprietary hurricane loss model.

- 14) Require residential property insurers and licensed rating and advisory organizations that compile loss data to timely report residential hurricane loss data to the Office of Insurance Regulation for transmission to the type I center at a state university under contract with the OIR for the development and updating of the Public Hurricane Model, subject to administrative fines for non-compliance. Provide that company specific data submitted is a trade secret and is exempt from the public records law and that the OIR is responsible for maintaining the confidentiality of such information.
- 15) The Legislature should appropriate adequate funds for the annual maintenance and updating of the Public Hurricane Model.

Other Issues

- 16) Non-renewals of damaged homes -- Codify the emergency rule approved by the Financial Services Commission to prohibit insurers from canceling or non-renewing a homeowner's policy until 60 days after repairs to damages caused by a hurricane are completed.
- 17) Construction Fee Schedule -- Statutorily require that a schedule of reasonable ranges of construction costs be adopted by rule in the event of a natural disaster for guidance to insurers, contractors, and policyholders for repair of damaged property, including temporary mitigation measures.
- 18) Staffing and Funding for Insurance Consumer Advocate -- The Legislature should evaluate the staffing, powers, and funding of the Office of the Insurance Consumer Advocate to determine if increases or strengthening is needed.
- 19) Loyalty Provision -- The Legislature should consider and study the impact of restricting an insurer's right to cancel or non-renew a policyholder who has been insured for at least 5 years without any claims.
- 20) Valued Policy Law (*Mierzwa*) -- The Legislature should consider amending the valued policy law (s. 627.702, F.S.) to clarify that a property insurer is responsible to pay only for that portion of damage to a structure which is caused by a peril insured under the property insurance policy and is not required to pay for damage caused by excluded perils; thereby clarifying that the Fourth DCA opinion in *Mierzwa v. Florida Windstorm Underwriting Association* was incorrect.
- 21) Sinkhole Coverage -- The Legislature should continue to study the sinkhole liability exposure issue and consider any recommendations made by the sinkhole study to be submitted by Florida State University.

Florida Hurricane Catastrophe Fund

Overview -- The Florida Hurricane Catastrophe Fund (FHCF or Fund) was created in 1993 after Hurricane Andrew as a form of mandatory reinsurance for residential property insurers.² All insurers who write residential property insurance in Florida are required to buy coverage from the FHCF to reimburse them for a portion of their residential hurricane losses. The Fund is a tax-exempt state fund administered by the State Board of Administration (SBA) that provides an additional source of reinsurance to insurers that is much less expensive than private reinsurance. This generally enables insurers to write more residential coverage in Florida than could otherwise be written and acts to lower premiums for consumers.

² Section 215,555, F.S.

Retention -- Each insurer must have hurricane losses that exceed its “retention” or deductible, before it is reimbursed from the Fund. The law, as amended in 2004, establishes a \$4.5 billion retention for all insurers combined for each hurricane, beginning with the June 1, 2004 contract year, subject to an annual growth factor equal to the percentage increase in the Fund’s exposure. Separate retentions are calculated for each insurer based on the insurer’s percentage share of total premiums paid to the Fund.

Coverage Limits -- The FHCF reimburses insurers above their retention for 90 percent, 75 percent, or 45 percent of their residential losses, as selected by the insurer. The maximum amount the FHCF is required to pay is \$15 billion for 2004, subject to the same annual growth factor as the retention, except that the limit cannot increase more than the dollar growth in the Fund’s cash balance. Each insurer’s recovery in any year is limited to its percentage share of the total \$15 billion (or greater) limit, equal to the insurer’s percentage of total Fund premiums. However, if capacity remains after all insurers have been fully reimbursed, the Fund must reimburse Citizens Property Insurance Corporation, the state insurer of last resort, for its reimbursable losses exceeding its share of the \$15 billion limit.

Premiums -- Each insurer pays a reimbursement premium approved by the SBA, which must be the “actuarially indicated” premium for the coverage provided, based on hurricane loss projection models found acceptable by the Florida Commission on Hurricane Loss Projection Methodology, and a premium formula developed by an independent consultant hired by the SBA. Each insurer’s reimbursement premium is based on the insured value of its residential policies, their location, construction type, deductible amounts, and other factors. For 2004, FHCF premiums paid by insurers totaled \$616 million.

Funding; Assessments -- If the cash balance of the FHCF is insufficient to meet its obligations, the SBA is authorized to issue revenue bonds funded by emergency assessments levied as surcharges against all property and casualty insurance premiums paid by policyholders, other than for workers’ compensation and, until June 1, 2007, medical malpractice, and including surplus lines policyholders. Annual assessments (never yet levied) are capped at 6 percent of premium for losses from any 1 year and 10 percent of premium for losses from multiple years.

Current Financial Status; Impact of 2004 Hurricanes -- For the 2004 contract year, the FHCF had a year-end balance of \$6.12 billion, before losses. As a result of the hurricanes, the Fund is expected to reimburse insurers approximately \$3 billion, or about one-half of its \$6.12 billion cash balance; therefore, bonding will not be necessary. However, the loss estimates for the FHCF are still preliminary and have continued to increase from earlier estimates. A total of 186 insurers reported losses to the Fund, but only 133 are expected to have losses in excess of their retention for at least one hurricane and trigger FHCF coverage. Of these, 55 companies are expected to exhaust their limits of FHCF recovery.

For the 2005 contract year, the FHCF will have a year-end cash balance of approximately \$3.5 to \$3.8 billion, assuming no hurricane losses or further changes to the law. This includes amounts estimated for 2005 premium revenue, investment income, appropriations for the multiple deductible reimbursement program and hurricane mitigation, and additional reserves for 2004 losses. Since the cash balance is less than the prior year, the maximum reimbursement remains at \$15 billion for 2005. This exposes the FHCF to potential bonding and assessment liability of

about \$11.2 to \$11.5 billion beyond its cash balance. The total industry retention will increase from \$4.5 billion to \$4.96 billion per hurricane for 2005, due to the increase in the Fund's exposure, which is primarily a function of total insured value of residential property.

Citizens Property Insurance Corporation

Overview -- In 2002, the Florida Legislature created Citizens Property Insurance Corporation (Citizens) which combined the then existing Florida Residential Property and Casualty Joint Underwriting Association (RPCJUA) and the Florida Windstorm Underwriting Association (FWUA).³ Citizens is the state's "insurer of last resort" and a property is eligible for coverage with Citizens only if there is no other offer from an authorized insurer.

Board of Governors -- Citizens operates under the direction of a 7-member Board of Governors, all appointed by the Chief Financial Officer (CFO) for 3-year terms, representing geographically diverse regions of the state. The CFO also appoints a technical advisory board to provide information and advice to the Board of Governors.

Types of Coverage -- Citizens offers three types of insurance in three separate accounts: 1) Personal Lines Account (PLA) which provides coverage statewide for homeowners, mobile homeowners, dwelling fire, tenants, condominium unit owners and similar policies; 2) Commercial Lines Account (CLA) covering condominium associations, apartment buildings and homeowners associations statewide; and 3) High-Risk Account (HRA) which provides windstorm-only policies for residential and non-residential (commercial) risks in designated areas near the coast which met prior statutory criteria. In these HRA "wind only" territories, private insurers are allowed to sell property insurance policies that exclude windstorm coverage. This HRA territorial boundaries cannot be expanded, but they must be reduced on February 1, 2007, in order to reduce the HRA's probable maximum loss or PML for a 100-year storm to 25 percent below its "benchmark" 100-year PML of February 1, 2001.

Policy Count and Exposure -- As of February 28, 2005, Citizens provided coverage to 805,198 policyholders, making Citizens the second largest insurer in Florida. The numbers of policyholders in the three accounts are: PLA -- 345,774; CLA -- 3,641; and HRA -- 455,783. The buildings and contents insured by these policies combine for about \$197 billion in insured value. Citizens projections for the 2005 hurricane season are that the HRA is exposed to a \$7.6 billion probable maximum loss (PML) for a 100-year storm, and the combined PLA/CLA faces an additional \$2 billion 100-year PML.

Limits of Coverage -- Although not specified by statute, Citizens currently has a maximum policy limit of \$1 million for homeowner policies issued in its Personal Lines Account. This account also limits coverage to \$100,000 for mobile homes, \$200,000 for condominium units, and \$100,00 for tenants policies. However, there is no upper limit for residential (wind-only) policies issued the High Risk Account (HRA). At year end 2004, of the 453,765 policies in the HRA, 5,705 had policy limits at \$1 million or above. These policies had a total insured value of about \$13 billion, or about 10.8 percent of the insured value for the HRA. Citizens estimates that its probable maximum loss in 2004 in the HRA was \$6.7 billion, which would have been reduced

³ Section 627.351(6), F.S.

by \$700 million, or 10.4 percent, if personal residential policies risks above \$1 million were excluded.

Premiums -- In order to assure that Citizens rates are not competitive with the voluntary market, the current law requires that rates for its Personal Lines Account be actuarially sound and that its average rates for each county must be no lower than the average rates charged by the insurer that had the highest average rate in that county among the 20 insurers (5 insurers for mobile home coverage) with the greatest direct written premium in the state for that line of business. For its High Risk Account (wind-only policies), the law more generally requires that Citizens rates be actuarially sound and not be competitive with approved rates charged by authorized insurers. Citizens and OIR were required to jointly develop a wind-only ratemaking methodology to meet this purpose, for rates effective on or after July 1, 2004. The wind-only rate methodology that was developed uses a variation of the "Top 20" approach mandated for personal residential multi-peril policies.

Additional Funding; Deficit Assessments -- Generally, if Citizens does not have adequate funds to pay claims in any of its three accounts, it may levy regular assessments for each such account against property insurers, including surplus lines insurers, up to 10 percent of each insurer's net written premium from the prior year for subject lines of business. Insurers are then permitted to recoup this assessment in future rate filings. This assessment base has about \$7.5 billion in premium, so a one-time regular assessment would generate about \$750 million for each account. If that is not sufficient, Citizens may issue revenue bonds funded by multi-year emergency assessments collected by insurers as premium surcharges on all property insurance policyholders in the state, generally limited to 10 percent of premium, or 10 percent of the deficit, whichever is greater.

Citizens must purchase reinsurance from the Florida Hurricane Catastrophe Fund and must use its "best efforts to procure catastrophe reinsurance at reasonable rates as determined by the board of governors." Citizens has never purchased reinsurance other than its FHCF coverage.

Impact of 2004 Hurricanes; Current Financial Status -- For the 2004 storms, Citizens losses are currently estimated at about \$2.4 billion, primarily impacting the High Risk Account. Pending final audit results for 2004, Citizens had a surplus of about \$1.3 billion in its HRA and its losses are estimated at \$1.8 billion, resulting in an estimated deficit of \$525 million. This may require about a 7 percent, one-time regular assessment on property insurers to fund this deficit, which the insurer may then recoup from its policyholders. For example, this would be about a \$70 surcharge for a policy with a \$1,000 annual premium. Even though Citizens purchased reinsurance from the Florida Hurricane Catastrophe Fund, its residential losses for each hurricane were below the \$950 million per-storm retention for the HRA, so Citizens was not reimbursed by the Fund.

For its other two accounts, the PLA/CLA combined had an estimated \$602 million in losses in 2004, which can be paid out of its 2004 surplus of about \$700 million, so assessments do not appear to be necessary for these accounts. All of these estimates are still preliminary as losses continue to develop and final audits are completed.

Citizens reports that about 118,000 claims have been filed for the four hurricanes, of which about 95 percent have been settled. However, many claims payments were delayed due primarily to problems Citizens encountered in securing an adequate number of claims adjusters. In response to consumer complaints in this regard, the CFO has appointed the Task Force on Policyholder Services and Relations to Citizens Property Insurance Corporation (Task Force) to make recommendations to Citizens for improving customer service and returning policies to the private insurance market. The Joint Select Committee on Hurricane Insurance also heard testimony regarding problems with communication and customer service to insurance agents and policyholders by Citizens.

Depopulation of Citizens; Take-Out Bonuses -- The current law expresses legislative intent to provide a variety of financial incentives to encourage the replacement of policies written in Citizens with policies written by authorized insurers at approved rates. There is specific authority for Citizens, as there was for the RPCJUA, to pay a “take-out bonus” to insurers of up to \$100 for each policy removed from Citizens, under certain conditions.⁴ However, Citizens, like the RPCJUA before it, has implemented greater bonuses under conditions approved by its board and the OIR, based on a broader grant of authority to adopt programs and incentives for the reduction of both new and renewal writings.⁵ Most recently, Citizens has provided a take-out bonus ranging from 12.5 to 25 percent of the premium for policies removed, subject to requirements for taking out a specified minimum number of policies and a specified minimum percentage in Miami-Dade, Broward, or Palm Beach counties. Insurers are required to insure a take-out policy for three years as a condition of receiving the bonus, which is held in an escrow account until that time.

Citizens reports that as of March 25, 2005, Citizens and the former RPCJUA have paid 27 different insurers a total of \$119 million to take out slightly more than 1 million policies. An additional \$67.5 million is currently held in escrow for six insurers taking out an additional 267,075 policies that have not yet been insured for three years. Citizens reports that in 2004 alone, four insurance companies removed 158,416 policies from Citizens.

One of the challenges to depopulating Citizens is the “Consumer Choice” law, enacted in 2002, when Citizens was created. The prior RPCJUA law provided that a policyholder was not eligible for coverage if an offer of coverage was made by an authorized insurer at approved rates. But, the Consumer Choice law provides that a Citizens policyholder who receives an offer of coverage may remain in Citizens if the current agent of that insured is “unable or unwilling to become appointed for the takeout insurer.” This is less disruptive to a Citizens policyholder and his agent and allows for a smoother transition to a take-out company, if the agent is appointed, but Citizens reports that the law also operates to reduce the number of policies taken out.

Hurricane Deductibles

The Legislature authorized the use of separate, percentage hurricane deductibles for residential policies in 1993 after Hurricane Andrew. Section 627.701, F.S., establishes the maximum and minimum hurricane deductibles that are allowable and mandates that insurers offer hurricane

⁴ Section 627.3511, F.S.

⁵ Section 627i.351(6)(g)3., F.S.

deductibles of specified amounts. The Legislature's expressed purpose in allowing for higher hurricane deductibles is to limit premium increases and to increase the availability of coverage.

The law generally requires insurers to offer homeowners a hurricane deductible of 2 percent of the dwelling limits, but for homes valued under \$100,000, the insurer must also offer a \$500 hurricane deductible. About 76 percent of the homes in Florida have a 2 percent hurricane deductible. For example, a home insured for \$200,000, would have a \$4,000 deductible for hurricane damage. For homes valued at \$100,000 or greater, insurers generally do not offer a homeowner a hurricane deductible lower than the 2 percent deductible that must be offered, but some insurers do so. Insurers are generally allowed to offer hurricane deductibles as high as 5 percent of policy limits, but are prohibited from offering higher amounts, except for homes valued in excess of \$500,000 for which no maximum limit applies. About 5 percent of the homes in Florida have a 5 percent deductible. The following table summarizes the current law.

Current Requirements for Residential Hurricane Deductibles
(s. 627.701, F.S.)

Dwelling Limits	Minimum Deductible Allowed	Maximum Deductible Allowed**	Specific Mandatory Offerings
0-\$24,999	\$250.00	2%	None
\$25,000-50,000	\$250.00	2%	\$500 & 2%
\$50,001-99,999	\$500.00	2%	\$500 & 2%
\$100,000-249,999	\$500.00	5%	2% (and \$500*)
\$250,000-500,000	\$500.00	5%	2%
\$500,001 and up	\$500.00	Unlimited	2%

*For houses valued between \$100,000 and \$250,000, an insurer is not required to offer the \$500 deductible if it guarantees it will not nonrenew to reduce potential loss from hurricanes for one additional renewal period. As interpreted by OIR, this guarantee had to be provided for only one renewal period, after April 1, 1996, and thereafter the insurer is no longer required to offer the \$500 deductible (s. 627.701(3)(b), F.S.; OIR interpretation provided to committee staff.)

**Commercial Residential Policies: For all values, a 5 percent maximum deductible is allowed for condominium association and cooperative association policies and a 10 percent maximum deductible is allowed for other commercial lines residential policies (e.g., apartment buildings). The insurer must offer a 3 percent deductible. (s. 627.701(8), F.S.).

“Grandfather” Exception: Notwithstanding the hurricane deductible limits summarized above:

- An insurer may require higher deductibles than shown above if a risk was covered on August 24, 1992, under a policy having a higher deductible than allowed by the above limits. (s. 627.701(3)(a), F.S.)
- An insurer is not required to offer either the \$500 or 2 percent deductible with respect to a deductible program lawfully in effect on June 14, 1995, or any similar

deductible program, that requires a minimum deductible amount of at least 2 percent of policy limits. (s. 627.701(3)(b)2, F.S.)

Mobile Homes: Hurricane deductibles for a mobile home property insurance policy:

- may not exceed 5 percent of the property value if the property is subject to any liens, and
- may not exceed 10 percent of the property value if the property is not subject to any liens.

Other Perils (non-hurricane): Policies must offer a \$500 deductible for all perils other than hurricane. (s. 627.701(6), F.S.)

Mandatory Annual Hurricane Deductibles -- Legislation enacted in the 2004 Special Session A requires that for residential property insurance policies issued or renewed on or after May 1, 2005, the hurricane deductible must be applied on an annual basis to all hurricanes that occur during the calendar year, rather than to each hurricane.⁶ However, insurers are allowed to apply the “other perils” deductible, which is typically \$500, or the remaining amount of the hurricane deductible, whichever is greater, to a loss for each subsequent hurricane that year.

The new law applies to both personal lines residential policies (homeowners, mobile homeowners, etc.) and commercial residential policies (condominium associations, apartment buildings, etc.). Although the premium impact on personal lines policies is expected to be small (about 1 to 3 percent), it is likely to be much greater for condominium association policies. Last week, the Senate passed CS/SB 1486 (in House Messages) which provides that the mandatory annual deductible would be limited to personal lines residential policies issued on or after May 1, 2005. For commercial residential policies issued or renewed on or after January 1, 2006, the insurer would be required to offer the policyholder the option of an annual hurricane deductible and a hurricane deductible that applies to each hurricane.

Property Insurance Rating Law; Hurricane Loss Models

Rate Filing Standards and Procedures --Property and casualty insurers are required to file rates for approval with OIR either 90 days before the proposed effective date (“file and use”) or 30 days after the rate filing is implemented (“use and file”).⁷ Under the file and use option, OIR must finalize its review by issuing a notice of intent to approve or disapprove within 90 days after receipt of the filing; otherwise the filing is deemed approved. Under the “use and file” option, an insurance company may be ordered by OIR to refund to the policyholder that portion of the rate found by OIR to be excessive.

The OIR may disapprove a rate filing if it determines such rates to be “excessive, inadequate, or unfairly discriminatory” as these terms are defined. The law specifies numerous factors which the OIR must consider in making this determination.

If OIR disapproves a rate filing, the insurer may request an administrative hearing under the Administrative Procedures Act (ch. 120, F.S., A.P.A.). Under the APA, a formal adversarial

⁶ Chapter 2004-480, L.O.F.

⁷ Section 627.062, F.S.

hearing is held before a State Administrative Law Judge (ALJ) of the Division of Administrative Hearings. Once the hearing is completed, the ALJ has 30 days to issue a recommended order to OIR. The recommended order contains findings of fact and conclusions of law as found by the ALJ. The OIR has 90 days to issue a final order which may reject or modify the conclusions of law contained in the recommended order. However, OIR's final order may not substitute findings of facts contained in the recommended order which were supported by competent substantial evidence. An insurer may then appeal OIR's final order to the First District Court of Appeal.

Arbitration -- In 1996, the law was amended to allow property and casualty insurers to request binding arbitration of a rate filing as an alternative to an administrative hearing.⁸ After OIR issues a notice of intent to disapprove a rate filing, the insurer may request arbitration before a panel of three arbitrators. One arbitrator is selected by the insurer, one by OIR, and the third is chosen by the two other arbitrators. An arbitrator must be certified by the American Arbitration Association and may not be the employee of any insurance company or insurance regulator. The procedures of the Arbitration Code (chapter 682, F.S.) apply, and the costs of arbitration are paid by the insurer. The decision of the panel, which must be made within 90 days, constitutes the final approval of a rate filing.

There is no appeal of the arbitration panel's decision to a higher court. However, either party may apply to the circuit court to vacate or modify the panel's decision under limited conditions. In general, grounds for vacating include corruption or fraud, evident partiality by a neutral arbitrator, and action beyond the arbitrators' powers or jurisdiction. Grounds for modification include miscalculations, errors as to form, and actions on matters not submitted for arbitration. Upon initiation of arbitration, the insurer waives all rights to challenge the action of OIR under the APA or any other law; however, these rights are restored to the insurer if the arbitrators fail to act within 90 days after initiation of arbitration.

According to OIR, as of October, 2004, 103 rate filings have been disapproved since the inception of arbitration in 1996. Of these 103 disapprovals, 11 had an arbitration hearing and decision. OIR states that it prevailed in only one case. In four cases, the insurer's requested rate change was approved by the arbitration panel. In the remaining six cases the panel's decision was an amount between those of the two parties. According to OIR, during this same period, very few insurers have litigated their rate filings under the APA. The vast majority of those insurers either settle their rate disputes with OIR or withdraw their filing.

Rating Territories -- Property and casualty insurers establish rating territories for which a territorial rating factor will apply to increase, decrease, or leave unchanged, the base rate charged by the insurer. The insurer must demonstrate to the OIR that the application of the territorial rating factors will not result in a rate that is unfairly discriminatory, so that the factor bears a reasonable relationship to the expected loss and expense experience amount the various risk within that territory. Each insurer is permitted to establish its own territories, based on these

⁸ The arbitration option is not available for private passenger motor vehicle insurance rate filings, which are subject to a different rating law in s. 627.0651, F.S. Also, the medical malpractice legislation enacted in 2003 provided that medical malpractice insurers were no longer permitted to use the arbitration process (ch. 2003-416, L.O.F.).

standards. Generally, OIR does not require an insurer to justify its territorial rating factors in each rate filing, but will periodically require an insurer to do so.

Public Hearings -- The current law provides that OIR must hold a public hearing on a residential property insurance rate filing that exceeds 25 percent, if the filing is based on data from a computer model.

Hurricane Loss Models -- In 1995 the Legislature established the Florida Commission (Commission) on Hurricane Loss Projection Methodology to serve as an independent body within the State Board of Administration.⁹ The Commission's role is to adopt findings relating to the accuracy or reliability of the methods, standards, principles, models and other means used to project hurricane losses. The membership of the Commission is designed to equip it with expertise in fulfilling its mission. The members include experts in insurance finance, statistics, computer system design, and meteorology appointed by the CFO who are full-time faculty members in the State University System, an actuary member from the FHCF Advisory Council, an actuary employed with a property and casualty insurer appointed by the CFO, an actuary employed by OIR, the Executive Director of Citizens, the senior employee responsible for FHCF operations, the Insurance Consumer Advocate, and the Director of Emergency Management of DCA. The Commission sets standards for loss projection methodology and examines the methods employed in proprietary hurricane loss models used by private insurers in setting rates to determine whether they meet the Commission standards.

Since the law does not provide any exemption from the Public Records Law or Public Meetings Law, the entire Commission is not able to examine, have possession of, or specifically discuss all of the various assumptions and components used in developing the various private industry models. Private modeling companies consider certain information a trade secret that could be subject to disclosure to competitors if provided to the Commission. Instead, the Commission uses a staff of five experts made up of a meteorologist, an engineer, an actuary, a statistician, and a computer scientist known as the "Professional Team" to conduct on-site reviews of proprietary models and to report back to the Commission as to their conclusions. Representatives from OIR have also been provided access to different proprietary models, but are not permitted to disclose the proprietary aspects of the models. There are currently four private hurricane loss models that have been determined by the Commission to meet its standards and found acceptable.

The law provides that an insurer may use in its rate filing hurricane loss models found by the commission to be accurate or reliable and that such findings are admissible and relevant in consideration of the rate filing by OIR or on any arbitration or administrative or judicial review.

Public Hurricane Loss Model -- The state authorized and initially funded the development of a public hurricane loss projection model, pursuant to the 2000 General Appropriations Act.¹⁰ The model is required to be designed in accordance with the standards set by the Florida Commission on Hurricane Loss Projection Methodology. The Department of Insurance was appropriated \$2.5 million to contract with the State University System, which contract was entered with the International Hurricane Research Center at Florida International University. Subsequent annual

⁹ Section 627i.0628, F.S.

¹⁰ Section 2226 of ch. 2000-166, L.O.F.

appropriations of about \$300,000 per year have been made to further the development of the public model. The process of developing and testing the public model has reportedly been slowed by the failure of some insurance companies to timely provide insurance policy and claims data. The model has been developed, is currently being tested and externally reviewed, and is expected to be completed and released by May 2005. However, the model will continue to require updating and maintenance as required for private models, particularly if it must continue to meet the standards of the Commission, which are also subject to revision, and to gather data from the 2004 storms.

Consumer Advocate -- Current law requires the CFO to appoint a consumer advocate to represent the general public before DFS and OIR.¹¹ The consumer advocate reports directly to the CFO, but is not otherwise under the authority of the department. The powers of the consumer advocate include recommending to the DFS or OIR the commencement of any proceeding or action; appearing in any proceeding or action before the DFS or OIR, or before the Division of Administrative Hearings relating to subject matter under the jurisdiction of the department or office. The powers also include examination of rate and form filings submitted to the office, hiring consultants as necessary to aid in the review process, and recommending to DFS or OIR any position the consumer advocate deems to be in the public interest. The consumer advocate must prepare an annual budget for presentation to the Legislature by the DFS, which must be adequate to carry out the duties of the office.

The current consumer advocate, who has been in his current position for approximately 1 year, has intervened in the workers' compensation rate filing made on behalf of all carriers, but has not otherwise intervened in another rate filing. In addition to the consumer advocate, the office is staffed with one attorney, two analysts, and an administrative assistant.

Hurricane Loss Mitigation

Hurricane Mitigation Premium Credits -- Since 2003, insurers have been required to provide premium credits or discounts for residential property insurance for properties on which construction techniques had been installed which reduce the amount of loss in a windstorm.¹² These construction techniques include roof strength, roof covering performance, roof-to-wall strength, wall-to-floor-to-foundation strength, opening protection, and window, door, and skylight strength, etc. Individual credits generally range from 3 to 25 percent and a fully mitigated home can qualify for total credits ranging from 20 to 42 percent off its wind insurance premium. Typically, policyholders are responsible for substantiating to their insurers the existence of loss mitigation features in order to qualify, often requiring some sort of certification or inspection. Insurers may allow homeowners to self-certify some features such as roof shape or number of stories, but require an engineer, building inspector, architect, or licensed building contractor to certify the more technical features such as roof deck attachment. Current Florida law does not require insurers to notify their insureds about credits or discounts for making wind mitigation improvements to their homes.

Hurricane Loss Mitigation Programs -- The law directs the Legislature to annually appropriate at least \$10 million from the FHCF, but no more than 35 percent of the investment income from

¹¹ Section 627.0613, F.S.

¹² Section 627.0629(1), F.S.

the prior fiscal year for hurricane loss mitigation programs.¹³ Actual annual legislative appropriations have ranged from the minimum \$10 million to \$30 million. The Hurricane Loss Mitigation Program (HLMP) within the Department of Community Affairs (DCA) was created in 1999, with an annual appropriation of \$10 million from the FHCF, to fund programs for improving the wind resistance of residences and mobile homes to prevent or reduce losses or reduce the costs of rebuilding after a disaster.¹⁴ Three (\$3) million from the HLMP is statutorily directed to retrofitting public facilities to be used as hurricane shelters while the remaining \$7 million, is appropriated for the Residential Construction Mitigation Program (RCMP) administered by DCA and statutorily allocated as follows:

- 40 percent (\$2.8 million) is used to inspect and improve tie-downs for mobile homes;
- 10 percent (\$700,000) is directed to the Type I Center of the State University System dedicated to hurricane research, e.g., Florida International University; and
- The remainder (50 percent or \$3.5 million) is generally directed to programs developed by the DCA with advice from an Advisory Council to help prevent or reduce losses to residences and mobile homes or to reduce the cost of rebuilding after a disaster.

One of the programs funded by the \$3.5 million allocation directs grants targeting homes in the Governor's designated Front Porch communities to provide hazard mitigation upgrades to low-to-moderate income homes. Currently, the RCMP does not have any low-interest loan programs.

Valued Policy Law (*Mierzwa*)

Florida's valued policy law provides that "[i]n the event of the total loss of any building...located in this state and insured by any insurer as to a covered peril...the insurer's liability, if any, under the policy for such total loss shall be in the amount of money for which such property was so insured as specified in the policy."¹⁵ In *Mierzwa v. Florida Windstorm Underwriting Association*¹⁶, a home damaged by both wind and flood damage was declared a total loss by application of a local ordinance. The FWUA policy insured only the wind risk and not the flood risk, which was insured under a separate policy. But, the court ruled that if an insurer has any liability at all for damages for a structure that is a total loss, under the valued policy law that insurer must pay policy limits. This applied in a situation where the application of a local ordinance that causes the structure to be deemed a total loss. Additionally, any attempt by the insurer to use an insurance clause that would require the apportionment of damages between insurance carriers is not permissible according to the court because such a clause would be contrary to the valued policy law.

III. Effect of Proposed Changes:

Section 1. Florida Hurricane Catastrophe Fund (FHCF) -- Amends s. 215.555, F.S., to provide that the "retention" or amount of residential hurricane losses that insurers must meet to be reimbursed from the FHCF, would be set at \$4.5 billion for all insurers combined, beginning with the 2005 contract year. This is the retention that the current law provides for the 2004

¹³ Section 215.555(7), F.S.

¹⁴ Section 215.559, F.S.

¹⁵ Section 627.702, F.S.

¹⁶ 877 So.2d 774 (Fla. 4th DCA 2004)

contract year, which increases to \$4.96 billion for 2005 under the current law, due to the annual adjustment for the percentage growth in the Fund's exposure for covered policies (primarily due to the increased value of property insured). Therefore, the bill, in effect, eliminates the growth factor for 2005 and reduces the retention from \$4.96 billion to \$4.5 billion for 2005. For subsequent years, the same growth factor would continue to apply.

The bill also provides that for insurers that have losses from multiple hurricanes in a contract year, the full retention would apply to each of the two hurricanes resulting in the largest losses for that insurer, and would be reduced to one-third of the full retention for all other hurricanes.

Section 2. Hurricane Loss Mitigation Program (Low-interest Loan Program) -- Amends s. 215.559, F.S., to require the Department of Community Affairs (DCA) to establish a low-interest loan program for homeowners and mobile homeowners to retrofit their homes to reduce hurricane losses. Up to \$3 million of the \$107 million that is currently annually appropriated to DCA from the Florida Hurricane Catastrophe Fund could be used for subsidizing or guarantying loans made by state or federal financial institutions. The amendment deletes the provision of current law that requires that at least 40 percent of the \$7 million appropriation (i.e., \$2.8 million) be used to inspect and improve tie-downs for mobile homes.

The DCA may begin the program as a pilot project in one or more counties, may adopt rules, and shall establish the qualifications and limitations for such loans and approve terms and conditions of the loan agreements in consultation with the Department of Financial Services and the Office of Insurance Regulation.

Section 3. Property and Casualty Insurance Rating Law -- Amends s. 627.062, F.S., to make the following changes to the rating law for property and casualty insurers:

- 1) Authorizes the Financial Services Commission to adopt rules establishing standard rating territories to be used by all insurers for residential property insurance, in order to enhance the ability of consumers to compare premiums and to increase the accuracy and usefulness of rate-comparison information provided by the Office of Insurance Regulation. The Commission must adopt these rules by January 1, 2006 and may specify such future date or dates when insurers must use the standard rating territories in their rate filings.
- 2) Repeals the provisions that allow an insurer to submit a rate filing to an arbitration panel for final disposition after the filing has been disapproved by OIR. The insurer would still be permitted to demand an administrative hearing under s. 120.57, F.S.
- 3) Prohibits a residential property insurer from recouping more than 1 year of reimbursement premium paid to the Florida Hurricane Catastrophe Fund at a time.

Section 4. Florida Commission on Hurricane Loss Projection Methodology -- Amends s. 627.0628, F.S., relating to hurricane loss projection models that are found to be accurate or reliable by the Florida Commission on Hurricane Loss Projection Methodology. Currently, insurers may use in rate filings those models found to be accurate or reliable by the commission and such findings are "admissible and relevant" in consideration of the rate filing by the OIR or

in any rate proceeding. Under the bill, the findings would be admissible and relevant only if OIR and the consumer advocate appointed by the Department of Financial Services have access to all of the assumptions and factors that were used in developing the model and are not precluded from disclosing such information in a rate proceeding.

Section 5. Public Hearings for Rate Filings -- Amends s. 627.0629, F.S., to require a public hearing for any residential property insurance rate filing that exceeds 15 percent, rather than 25 percent as currently required, if the filing is based on a computer model.

Section 6. Reports of Hurricane Data for Public Model -- Creates s. 627.06291, F.S., to require residential property insurers and licensed rating and advisory organizations that compile loss data to report residential hurricane loss and exposure data to OIR or to the state university under contract with OIR (Florida International University) for the purpose of developing, maintaining, and updating a public hurricane model for hurricane loss projections.

Section 7. Citizens Property Insurance Corporation (“Citizens”) -- Amends s. 627.351, F.S., to make the following changes related to Citizens:

- 1) Revises appointments to the board of governors of Citizens to delete the requirement that the Chief Financial Officer (CFO) appoint all 7 members and, instead, to require that the Governor, CFO, President of the Senate, and Speaker of the House or Representatives each appoint 2 members to the board (8 total), effective August 1, 2005. The executive director and senior managers would be hired by the board, as recommend by the CFO, rather than by the CFO directly, and would serve at the pleasure of the board, rather than the CFO. The executive director would employ other staff subject to approval by both the board and the CFO, rather than the CFO alone.
- 2) Provides that dwelling limits for any personal lines policy may not exceed \$1 million and that a residential structure valued in excess of \$1 million is not eligible for coverage. This would primarily affect personal lines residential structures insured in the High Risk Account (wind-only) of Citizens, for which there is no maximum policy limit. The current plan of operation of Citizens currently has a \$1 million limit for homeowners insured in the Personal Lines Account (multiperil coverage).
- 3) Provides an exception to the current requirement that the rates for Citizens for personal lines policies not be competitive with the private market. For the Personal Lines Account, the current requirement that Citizens charge the highest average rates in the county compared to the 20 insurers with the greatest written premium in the state would no longer apply in any county for which OIR determines that a reasonable degree of competition does not exist for personal lines policies. Similarly, the current requirement that Citizens ensure that its rates for personal lines policies in the High-Risk Account (windstorm only) are not competitive with the private market would not apply in any county for which OIR determines that a reasonable degree of competition does not exist for personal lines residential policies in the area of that county eligible for wind-only coverage. In such counties, for both accounts, Citizens would be required to charge rates that are actuarially sound and not excessive, inadequate, or unfairly discriminatory and be subject to the rating law (s. 627.062, F.S.) that applies to all property and casualty

insurers. The Financial Services Commission may adopt rules establishing criteria for determining whether a reasonable degree of competition exists for personal lines residential policies. Beginning October 1, 2005, and each 6 months thereafter, OIR must determine and identify those counties for which a reasonable degree of competition does not exist.

- 4) Deletes the authority for Citizens to provide take-out bonuses or payments to insurance companies taking policies out of Citizens. The board would still have authority to provide a credit against assessment liability and other programs to provide an incentive for insurers to take risks out of Citizens. (Also see Section 18, below).
- 5) Currently, Citizens must “make its best efforts to procure catastrophe reinsurance at reasonable rates.” The bill specifies that such reinsurance is the amount that would cover its projected 100-year probable maximum loss. This is the level of financial resources that insurance rating agencies generally require in order for an insurer to obtain an acceptable rating.

Section 8. Standard Personal Lines Residential Policies -- Creates s. 627.40951, F.S., to require the CFO to appoint an advisory committee to develop standard personal lines policies and checklists and to submit its recommendations for approval to OIR by January 1, 2006. If approved by OIR by order, each insurer offering similar coverage shall offer the standard plan within 12 months after the effective date of the order, in addition to other products the insurer is authorized to offer.

Section 9. Grounds for Disapproval of Policy Forms -- Amends s. 627.411, F.S., to authorize OIR to disapprove a policy form for property and casualty insurance if it contains provisions that are unfair or inequitable, contrary to the public policy of this state, or that encourage misrepresentation. Currently, OIR may disapprove a health insurance policy form under these grounds.

Section 10. Checklist of Coverage -- Amends s. 627.4143, F.S., to require that insurers provide a checklist of coverage for homeowners, mobile homeowners, dwelling, and condominium unit owners policies. The checklist must contain the standard provisions typically included in these policies, whether or not they are included, limits of liability for each item, specific property that is covered, whether coverage is based on replacement costs or actual cash value, primary exclusions from coverage, and other specified information.

Section 11. Hurricane Deductibles -- Amends s. 627.701, F.S., to make the following changes related to hurricane deductibles:

- 1) Increases the maximum allowable deductible for personal lines residential policies from 5 percent to 10 percent of the dwelling limits, with certain exceptions.
- 2) Requires insurers to offer deductibles of 1 percent, 2 percent, 5 percent, and 10 percent of dwelling limits for personal lines residential policies, with certain exceptions, for policies issued or renewed on or after January 1, 2006. Currently, insurers must offer a 2 percent deductible, with certain exceptions. (The current law and the bill would also generally

- require that insurers offer a \$500 deductible for policies with limits of less than \$100,000.)
- 3) The maximum deductible and mandatory deductible offers specified above would also apply to mobile homes. (Currently, mobile homes are subject to a maximum deductible of 5 percent if there is a lien, and 10 percent if there is not a lien, and the mandatory offer of deductibles do not apply.)
 - 4) Policyholders would be required to select the deductible among the amounts offered. Disclosure requirements are added to advise the policyholder that higher deductibles result in lower premiums but will also result in higher out-of-pocket expenses. For each percentage deductible, the form must include the dollar amount of the deduction which will result.

Section 12. Replacement Cost Coverage -- Amends s. 627.7011, F.S., to require that if there is a loss for which a dwelling or personal property is insured on the basis of replacement costs, the insurer must pay the replacement costs without reservation or holdback of any depreciation in value, whether or not the insured replaces or repairs the dwelling or property. Currently, policies that provide replacement cost coverage typically provide initial payment for the depreciated value, with the remainder of the replacement cost paid after the policyholder submits receipts for the repair or replacement.

Section 13. Mediation Program for Resolving Property Insurance Disputes -- Amends s. 627.7015, F.S., which establishes a mediation program administered by DFS to help parties resolve property insurance claims for personal lines policies. The bill expands the program to commercial policies, as well as personal lines policies.

The bill also provides that if an insurer fails to comply with the current requirement to notify a first-party claimant of his or her right to participate in the mediation program, that the insured is not required to submit to a contractual loss appraisal process of property loss damage as a precondition to filing a legal action against the insurer. (This is the current penalty that applies to an insurer if the insurer requests the mediation and the results are rejected by either party.)

Section 14. Valued Policy Law (Mierzwa) -- Amends s. 627.702, F.S., to provide legislative intent regarding the valued policy law. The bill provides that the legislative intent of this law is not to require an insurer to pay for a loss caused by a peril other than the covered peril, and that when a loss was caused in part by a covered peril and in part by a noncovered period, the insurer's liability is limited to the amount of loss caused by the covered peril. (See, also, Section 19 for further legislative intent on this section.)

In effect, this would reverse the holding of the decision in *Mierzwa v. Florida Windstorm Underwriting Association*, described in Present Situation, above. This generally means that if a total loss was caused by the combination of a covered peril, such as windstorm, and a non-covered peril, such as flood, that the insurer's liability would be limited to the amount of loss caused by the covered peril. However, it may not be clear what impact this provision has with respect to application of a local building ordinance that requires a partially damaged home to be rebuilt, as further affected by any law and ordinance coverage provided in the policy.

Section 15. Notice of Premium Discounts for Hurricane Loss Mitigation -- Creates s. 627.711, F.S., to require that before issuing a personal lines residential policy and as part of each premium renewal notice, the insurer must provide written notice to the applicant and the policyholder, on a form approved by OIR, of the availability and amount of the premium discounts and credits for fixtures and construction techniques that reduce the amount of loss in a windstorm. Insurers are currently required to provide such premium credits and discounts pursuant to s. 627.0629(1), F.S.

Section 16. Timely Payment of Claims -- Creates s. 627.712, F.S., regarding timely payment of claims for property insurance policies. Currently, s. 626.9541, F.S., provides that it is an unfair or deceptive act or practice for an insurer “failing to affirm or deny full or partial coverage of claims, and as to partial coverage, the dollar amount or extent of coverage, or failing to provide a written statement that the claim is being investigated, upon the written request of the insured within 30 days after proof of loss statements have been completed.”

The bill would require that within 30 days after receipt of a claim under a property insurance policy, the insurer must pay that portion for which the policyholder has submitted all information required for payment under the policy; provide a written denial for that portion which the insurer determines is not covered, including the specific reasons; and specify the additional information that the policyholder must submit in order for any remaining amount of the claim to be paid. Within 30 days after receipt of the additional information, the insurer must either pay or deny the claim. All overdue payments would be subject to a 10 percent annual interest payment.

Section 17. Audit of Citizens by Auditor General -- Requires the Office of the Auditor General to conduct an operational audit of Citizens regarding its customer service, claims handling, accessibility of policyholder information to the agent of record, take-out programs, and financing arrangements, including legislative recommendations.

Section 18. Repeal of Take-Out Bonus for Citizens -- Repeals s. 627.3511, F.S., which provides legislative authority for Citizens to pay take-out bonuses and to provide exemptions from deficit assessments for insurers taking out a specified number of policies from Citizens.

Section 19. Additional Legislative Intent for Changes to Valued Policy Law -- Provides that the amendment to s. 627.702, F.S., in Section 14, above, is remedial in nature and intended to clarify the intent of that section. Although this does not expressly provide that the amendment is retroactive, it may have that result.

Section 20. Additional Staffing of the Office of the Consumer Advocate -- Appropriates \$350,000 from the Insurance Regulatory Trust Fund and 4 additional FTE positions in the Office of the Consumer Advocate within the Department of Financial Services.

Section 21. Effective Date -- Provides that except as otherwise expressly provided in this act, the act shall take effect upon becoming law.

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:****Florida Hurricane Catastrophe Fund**

Lowering the retention in the FHCF exposes the Fund to a greater likelihood of paying reimbursements to insurers and of expending its cash surplus and issuing revenue bonds, funded by assessments on most property and casualty insurance policyholders. But the difference is not great, since the change in the retention is modest. A rough estimate provided by the actuarial consultant to the SBA is that the probability of triggering coverage from the FHCF will drop from about once every 9.9 years to once every 9.2 years, and the probability of bonding will drop from about once every 16 years to once every 15 years.

Citizens Property Insurance Corporation

Different provisions of the bill have a mixed impact on exposing Citizens to losses and potential deficit assessments on property insurers and policyholders:

The prohibition on insuring residential dwellings valued in excess of \$1 million will reduce the exposure of Citizens. Citizens estimates that its probable maximum loss in 2004 in the High Risk Account (wind-only) was \$6.7 billion, which would have been reduced by \$700 million, or 10.4 percent, if personal residential policies above \$1 million were excluded.

Repealing Citizens authority to pay takeout bonuses to insurers may prevent some policies from being removed and compromise efforts to reduce Citizens exposure to losses. But, the payment of bonuses also reduces the surplus of Citizens and does not guaranty that a policy will end up back in Citizens after the required 3-year renewal period.

See Private Sector, below, regarding the impact of the changes in the rates for Citizens and the impact of purchasing reinsurance.

B. Private Sector Impact:**Florida Hurricane Catastrophe Fund**

By lowering the retention in the FHCF, the bill may provide additional capacity to insurers to write residential property insurance in Florida, due to substituting less expensive FHCF coverage for private reinsurance. Insurers would be provided significantly greater coverage in years with three or more hurricanes, lessening the need for insurers to financially plan for this event via private reinsurance. The SBA estimates that the reimbursement premiums for the FHCF will increase by 4.88 percent due to this provision. But, other than for multiple storm coverage, the bill does not provide insurers a greater layer of coverage from the FHCF. The layer of coverage simply “drops down” since the maximum dollar amount of recovery for an insurer remains the same (i.e., the insurer’s same share of the \$15 billion limit). But, private reinsurance is much more expensive at the low end, below the retention, than at the high end, so the net impact should be cheaper reinsurance. This will negatively impact private reinsurers.

Citizens Property Insurance Corporation

The impact on rates is unknown of requiring Citizens to charge actuarially sound rates, rather than the highest average rates in the county compared to the top 20 insurers, in those areas where OIR determines a reasonable degree of competition does not exist. Citizens reports that this will not necessarily lower rates, and could even increase rates in certain areas. By using the current top 20 rating formula, Citizens has reportedly not necessarily charged a rate as high as the actuarially indicated rate in all areas. It is also unknown which counties or areas would be determined by OIR to lack a reasonable degree of competition. But, OIR reports that as of June 30, 2004, Citizens writes 93 percent of the total policies in Monroe County that include wind coverage and writes 48 percent of the total policies in Dade County that include wind coverage. Since this includes policies being renewed, it may understate the lack of competition for new policies.

Policyholders of homes valued in excess of \$1 million will be ineligible for coverage from Citizens. If coverage is not available from an authorized insurer, a policyholder would then look to the surplus lines market. The Florida Surplus Lines Service Office (FSLSO) reported that 179,180 homeowner policies were written in the surplus lines market in 2004, including 5,690 policies with coverage limits in excess of \$1 million, of which 3,980 provided wind coverage. The FSLSO reported that there is capacity and interest in the surplus lines market in writing high-value dwellings, but windstorm deductibles are typically 5 or 10 percent and sinkhole coverage is typically excluded.

Insurers would no longer be eligible to receive take-out bonuses for taking policies out of Citizens. Such payments are often paid to start-up Florida domestic companies.

The bill does not mandate that Citizens purchase reinsurance, but directs it to use its best efforts to purchase reinsurance to cover its 100-year probable maximum loss. Citizens provided an estimate that for its High Risk Account (HRA), which has a zero surplus, this may cost a total of \$743 million to cover its estimated \$7.6 billion 100-year PML, which includes its estimated Cat Fund premium of \$135 million. This total premium is almost

the entire 2005 estimated written premium of \$754 million for Citizens' HRA. For its Personal Lines Account/Commercial Lines Account, which has a \$235 million surplus, the 100-year PML is \$2.2 billion. Citizens estimates that it would cost \$151.5 million (including a \$35 million Cat Fund premium) to purchase this level of reinsurance, as compared to its estimated \$1.1 billion estimated premium for 2005 for these accounts.

Deductibles

Requiring insurers to offer a 1 percent deductible would give consumers an option, at a higher premium, to lower their potential out-of-pocket expense after a hurricane, as compared to the 2 percent deductible. But, requiring insurers to offer lower deductibles may reduce the capacity of insurers to write policies in this state, depending on the premium charged for the lower deductible and the number of policyholders who elect it. Lower deductibles increase an insurer's "probable maximum loss" or PML, requiring additional reserves or reinsurance that may not be fully financed by the additional premium, requiring the insurer to reduce or limit the policies it writes in order to reduce its PML.

Requiring insurers to offer a 10 percent deductible, compared to the current maximum 5 percent deductible, would potentially increase the capacity of insurers to write policies depending on how many policyholders actually elected the higher deductibles. It would also give consumers an additional option to lower their premium, but would increase their potential out-of-pocket expense at the time of loss.

Insurers will be subject to the administrative costs of developing forms and rates for offering additional deductibles.

Rating Law

Requiring insurers to utilize standard rating territories established by the Financial Services Commission will enhance the ability of consumers to compare premiums among insurers. It will also simplify the preparation and increase the accuracy and usefulness of rate comparison information provided by OIR. Insurers will be subject to increased costs to re-establish their rating territories to conform to the uniform rating territories. Although the overall rate level charged by an insurer should not be affected, individual policyholders may be charged higher or lower rates, depending on the change in their territorial boundaries.

Repealing arbitration as an option to insurers for rate filings disapproved by OIR, may make it somewhat more difficult for an insurer to have a rate increase approved or otherwise provide a greater disincentive to an insurer to challenge OIR's determination. Also, requiring a public hearing on residential rate filings in excess of 15 percent may discourage rate increases above this level. This may result in lower rates, but may also discourage insurers from writing policies.

Other Provisions

Requiring insurers to notify policyholders of premium discounts for construction mitigation will better inform policyholders of premium discounts they are currently entitled to, and provide greater incentive to make retrofits to qualify. The low-interest

loan program that is required to be established by the Department of Community Affairs may further provide economic incentives for this purpose. Both of these provisions should help reduce hurricane losses and favorably impact premiums.

Insurers would be required to pay 10 percent interest on late payment of claims. This may result in more timely payment of claims to policyholders.

The amendments to the valued policy law will limit an insurer's liability for structures that are a total loss, due in part to a risk not covered under the policy. Policyholders will not receive payment of policy limits in such cases, under certain circumstances. But, these changes are expressly intended to clarify the current law. Though not expressly retroactive, it may have that effect on outstanding claims from the 2004 storms.

Requiring insurers to offer a standard policy approved by OIR will enable policyholders to make an "apples to apples" comparison of rates charged by insurers for the standard policy and may make it less likely for someone to purchase inferior coverage. Insurers may be required to provide benefits in a standard policy they would not otherwise provide, at a higher premium. The checklist of coverage should aid policyholders in understanding their policy and be better informed of other coverage options that are available.

Requiring insurers to pay the full replacement cost under replacement cost policies, without holding back depreciated value until the property is replaced or repaired, will benefit policyholders who can collect such payments and then decide whether to actually replace or repair the property. But, this will increase loss payments by insurers and could cause an increase in fraudulent claims and is likely to increase premiums. It may also result in damaged property not being repaired, which could negatively impact financial institutions that hold mortgages and the secondary mortgage market.

The broader authority for OIR to disapprove policy forms for property and casualty insurance for any provision that is unfair, inequitable, etc., may provide greater protection and greater benefits to policyholders, but it may be at a higher premium.

Commercial insurers would be subject to the costs of paying for mediation of property insurance disputes, as currently required for personal lines insurers.

C. Government Sector Impact:

The bill appropriates \$350,000 from the Insurance Regulatory Trust Fund and 4 positions to the Office of the Consumer Advocate within the Department of Financial Services. This approximately doubles the current funding and positions of this office.

The bill authorizes the Department of Community Affairs to use up to \$3 million of its current \$10 million in mitigation appropriations from the Florida Hurricane Catastrophe Fund, to establish a low-interest loan program for homeowners and mobile homeowners to retrofit their homes to prevent wind damage. It deletes the current requirement that \$2.8 million be used for a mobile home tie down program.

The Office of the Auditor General has requested that \$75,000 be appropriated for the provision requiring that it conduct an operational audit of Citizens, in order to engage a specialist related to claims adjusting and processing.

There are likely to be increased costs to OIR due to the requirement to hold a public hearing on residential rate filings exceeding 15 percent, but this has not been estimated.

The costs to the Office of Insurance Regulation are unknown regarding its role in establishing uniform rating territories, adopting standard policy forms and checklists, and approving rates and forms for additional deductible options.

VI. Technical Deficiencies:

None.

VII. Related Issues:

PCS/SB 1478 is a proposed public records exemption bill that is linked to this bill.

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

VIII. Summary of Amendments:

None.

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