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 1980

INTRODUCER: Banking and Insurance Committee and Senator Garcia

SUBJECT: Property Insurance

DATE: April 2, 2006 REVISED: 04/06/05

	ANALYST	STAFF DIRECTOR	REFERENCE	ACTION
1.	BI Committee Staff	Deffenbaugh	BI	**Pre-meeting**
2.			JU	**Withdrawn**
3.			WM	
4.				
5.				
6.				

I. Summary:

PCS/SB 1980 makes the following major changes:

Citizens Property Insurance Corporation ("Citizens")

Depopulation and reducing the potential for deficit assessments:

- Makes ineligible for coverage homes and other specified residential property valued at $1 million or more, effective January 1, 2007, with certain exceptions.
- Requires rates for nonhomestead property to include a 25 percent surcharge. If Citizens incurs a deficit, nonhomestead property owned by a nonresident of Florida would be subject to an additional 25 percent policy surcharge. "Homestead property" is defined to include certain properties in addition to those that qualify for a homestead tax exemption.
- Requires that deficit assessments against insurers (and recouped from their policyholders) be reduced by amounts to be collected from surcharges on Citizens' policyholders.
- Requires applications for coverage to have a 10-day waiting period (with exceptions), and be made available for review by agents and insurers. If an authorized insurer offers coverage during this period, the applicant is not eligible for coverage in Citizens, whether or not the insurer appoints the agent who submitted the application.

Oversight and Internal Controls

- Requires the Financial Services Commission (Governor and Cabinet), rather than the Office of Insurance Regulation (OIR), to approve Citizens' plan of operation.
- Requires Senate confirmation of the Executive Director of Citizens.
- Requires Citizens to have an internal auditor who must submit an annual report to the board, the Financial Services Commission, and the Legislature.
- Requires OIR to do a market conduct examination of Citizens every two years.
- Requires the Auditor General to conduct an operational audit of Citizens every three years.

- Requires competitive bidding of contracts, with exceptions, and board approval of contracts of $100,000 or more.
- Requires OIR background checks of applicants for senior management positions.

Standards of Conduct

- Subjects board members and senior managers to the code of ethics and financial disclosure requirements applicable to public officials and specified state employees.
- Prohibits board members and employees from accepting any gifts from any person or entity under contract with Citizens or under consideration for a contract.
- Prohibits Citizens from retaining lobbyists, but allows employees to register as lobbyists.
- Prohibits senior managers from representing any person or entity before Citizens for two years following termination of employment from Citizens.

Other Changes to Citizens

- Requires insurers writing the non-wind coverage to contract with Citizens to provide claims adjusting services for the wind coverage provided by Citizens in the high-risk account.
- Requires Citizens to offer quarterly and semiannual premium payment plans.
- Extends for two years (until Feb. 1, 2009) the requirement that the board reduce the boundaries of the high risk area eligible for wind-only coverage.
- Requires that any take-out bonus paid to an insurer by Citizens must be conditioned on the insurer keeping the policy for five years. Also, requires Citizens to monitor whether such policies are later insured by Citizens.
- Requires Citizens to report to the Legislature its recommendations regarding consolidation of its three existing accounts and the actions taken to minimize the cost of carrying debt.

Florida Hurricane Catastrophe Fund

- Requires that the premiums paid by insurers for coverage from the fund be increased by 25 percent in order to provide for more rapid cash buildup in the fund.

Hurricane Loss Mitigation

- Requires the Department of Community Affairs (DCA) to establish the Home Retrofit Hardening Program, as a competitive grant program administered by local governments or non-profit agencies, to fund improvements to homes to make them less vulnerable to hurricane damage. Specifies priorities for eligible homes and maximum funding limits. The bill makes an unspecified appropriation from General Revenue for this purpose.
- Requires DCA to provide wind certification and hurricane mitigation inspections to homeowners at no cost, pursuant to a request for proposals from providers who must meet specified criteria of prior experience or specialized training. The bill makes an unspecified appropriation from General Revenue for this purpose.
- Exempts specified mitigation improvements from the assessed value of the home.

Rating Law

- Prohibits OIR from disapproving a rate as excessive for personal lines residential coverage with insured value at $1 million or more.
- Requires OIR to approve a rating factor that provides an insurer a reasonable rate of return commensurate with the risk of exposing its capital and surplus to the risk of hurricane losses.
- Allows an insurer to recoup its costs of reinsurance in its rates, unless OIR establishes that the costs are in excess of amounts consistent with prudent business practices and sound actuarial principles.

Sinkhole Claims

- Requires the Department of Financial Services to certify engineers and geologists to serve as "neutral evaluators" of sinkhole claims disputes between insurers and policyholders. This process would be optional and nonbinding and the costs must be paid by the insurer. However, if an insurer requests this process and the policyholder either declines to participate or declines to resolve the matter in accordance with the recommendation of the neutral evaluator, the insurer would not be liable for attorney's fees or other extra-contractual damages related to a claim.
- Allows the insurer to make payment directly to the persons selected by the policyholder to make the repairs, if approved by the policyholder and lienholder.
- Deletes the requirement that testing by a geologist be conducted in compliance with the Florida Geological Survey.

Florida Insurance Guaranty Association (FIGA)

- Authorizes FIGA to impose annual emergency assessments on insurers of up to 2 percent of written premium for specified lines of property and casualty insurance to fund revenue bonds issued by a municipality or county to pay claims of an insurer rendered insolvent due to a hurricane.
- Increases the maximum amount of FIGA's liability for a covered homeowners insurance claim against an insolvent insurer from $300,000 to $500,000.
- Provides that FIGA covers claims of a corporation or business (as a policyholder or claimant of an insolvent insurer) if the business has its principal place of business in Florida, rather than incorporated in Florida.
- Allows FIGA to pay claims of unearned premium refunds, without requiring the policyholder to file a proof of claim form, under certain conditions.

Direct Payment to Policyholder for Dual-Interest Property

- Requires property insurers to issue separate checks payable to the primary policyholder only, to pay claims for contents, living expenses, and the lesser of $20,000 or the first 20 percent of the estimated total covered claim amount for the replacement or repair of dual interest (mortgaged) property.

Emergency Orders; Rules

- Authorizes the Commissioner of Insurance Regulation to issue orders to temporarily modify or suspend provisions of the Insurance Code to expedite recovery of communities affected by a disaster, when the Governor declares a state of emergency.
- Requires the Financial Services Commission to adopt rules standardizing requirements that may be applied to insurers after a hurricane, addressing claims reporting requirements, grace periods for payment of premiums, and temporary postponement of cancellations and nonrenewals.

Other Provisions

- Allows insurers to make electronic payment of insurance claims without written authorization, under certain conditions.
- Permits alien surplus lines insurers to use letters of credit meeting certain criteria to fund the required minimum $5.4 million trust fund.
- Clarifies that if a property insurer does not obtain a written rejection from the policyholder for law and ordinance coverage, the policy is deemed to include the law and ordinance coverage limited to 25 percent of the dwelling limit (and not the alternative 50 percent limit that must also be offered).

This bill substantially amends the following sections of the Florida Statutes: 193.555; 215.555, 626.918, 627.062, 627.351, 627.3511, 627.3517, 627.4035, 627.7011, 627.7019, 627.707, 627.7072. 627.7073, 627.727, 631.54, 631.55, and 631.57, The bill creates the following sections of the Florida Statutes: 215.5586, 252.63, 627.6121, 627.7074, and 631.695.

II. Present Situation:

The 2004 & 2005 Hurricane Season

The 2004 and 2005 hurricane seasons were particularly destructive to Florida, with four hurricanes hitting Florida each year. The four hurricanes in 2004 resulted in 1.66 million insurance claims and $20.9 billion dollars of insured losses in the Florida market.[1] Claim and loss statistics from the 2005 hurricanes are still in development and being reported, but as of March 17, 2006, the number of reported insurance claims totals 1.1 million and the gross insured losses in the state are estimated to be $12.7 billion. Just for Hurricane Wilma alone, as of March 17, 2006, insurers have already paid over $8.4 billion in insurance proceeds for claims.[2]

Citizens Property Insurance Corporation -- Background

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). 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.

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[1] The Task Force on Long Term Solutions to Florida's Hurricane Insurance Market report adopted March 6, 2006, page 11. (citing the Office of Insurance Regulation's (OIR) disaster reporting data system)

[2] Information received from the OIR on March 22, 2006.

Citizens operates under the direction of an 8-member Board of Governors, two each appointed by the Governor, Chief Financial Officer, the Senate President, and the Speaker of the House of Representatives for 3-year terms. The Chief Financial Officer also appoints a technical advisory board to provide information and advice to the Board of Governors. Citizens offers three types of property and casualty insurance in three separate accounts:

1. Personal Lines Account (PLA) which covers 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; and
3. High-Risk Account (HRA) which covers personal lines windstorm-only policies, commercial residential wind-only polices and commercial non-residential wind-only policies.

As of February 28, 2006, Citizens provided coverage to 815,482 policyholders, making Citizens the second largest insurer in Florida. The numbers of policyholders in the three accounts are: PLA - 445,513, CLA - 3,167, and HRA - 366,802.[3] Currently, Citizens is averaging 30,000 new applications for coverage per month. At this rate, it is soon likely to become the largest insurer in Florida.

The High-Risk Account provides windstorm only coverage. Citizens provides coverage in specially designated areas which have been determined to be particularly vulnerable to severe hurricane damage. In these "wind only" zones, private insurers may offer other peril insurance, but are not required to provide windstorm coverage. For the HRA policies in effect on February 28, 2006, Citizens reports approximately $767 million generated in premiums, representing an exposure of approximately $135 billion.[4] The premiums generated by the HRA policies account for approximately 55 percent of all premiums generated and represents 64 percent of Citizens' total exposure.

In 2004 and 2005, Citizens policyholders were impacted by all four hurricanes hitting Florida. Citizens reports 120,000 claims have been filed for the four 2004 hurricanes and 165,000 claims for the 2005 hurricanes. As of February 1, 2006, Citizens has paid over $2.5 billion in claims for the 2004 hurricane season and an additional $775 million in claims for the 2005 hurricane season.[5] Hurricane Wilma was especially devastating for Citizens. This hurricane accounted for over 145,216 claims. As of February 28, 2006, Citizens has paid over $1.3 billion in losses for Hurricane Wilma and estimates its total losses will be over $2.3 billion.[6]

Citizens' Deficits

Generally, if Citizens does not have adequate funds to pay claims in any of its three accounts (i.e. a deficit), 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.[7] The entire regular assessment is levied against property

[3] http://www.citizensfla.com/Exposure_Prem_Reports.asp (last viewed April 2, 2006).
[4] Id.
[5] *See* Citizens Property Insurance Corporation Board of Governor's Report to the Florida Legislature dated February 1, 2006.
[6] Data from Citizens as of March 13, 2006.
[7] Subject lines of business that are subject to Citizens' deficit assessment include insurance for: fire, industrial fire, allied lines, farm owners multiperil, homeowners multiperil, commercial multiperil, and mobile homes, and includes liability

insurers, who may recoup such amounts from their policyholders in subsequent rate filings. Citizens is then required to impose a "market equalization surcharge" on its own policyholders equal to the same percent of premium assessment that is imposed on property insurers. This is intended to keep the Citizens' rates from being non-competitive, but also acts to increase revenues to Citizens above the amount of the deficit.

An insurer must pay a regular assessment within 30 days of receipt of notification from Citizens. If the regular assessment is not sufficient to cover the deficit, 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.

However, "limited apportionment companies" (and their policyholders) are exempt from a substantial portion of a regular assessment. These are insurers with a surplus of $25 million or less, and writing 25 percent or more of thier total countrywide property insurance premiums in Florida. These insurers are exempt from regular assessments for any amount of the deficit in excess of $50 million. However, if a deficit is great enough to require multi-year emergency assessments in order to fund bonds, the policyholders of limited apportionment companies are subject to emergency assessments at the same amount as other property insurance policyholders.

Currently, Citizens' assessment base has about $8.3 billion in premium, so a one-time regular assessment would generate about $830 million.[8]

Prior to the 2004 hurricane season, Citizens had a surplus of about $1.1 billion for its High Risk Account and $700 million for the PLA/CLA combined. Citizens' claims losses related to the 2004 hurricane season amounted to more than $2.4 billion, depleting its entire surplus in the High Risk Account. Thus, Citizens incurred a $516 million deficit in the HRA. The other two accounts (PLA and CLA) did not incur deficits.

The $516 million deficit translates into statewide average 6.8 percent assessment on all non-Citizens insured homeowners in Florida. However, Citizens policyholders will also pay a 6.8 percent assessment, a "market equalization surcharge," upon renewal of their policy. Historically, joint underwriting authorities have used an assessment mechanism to fund deficits.[9] Florida's assessment mechanism for the property and casualty joint underwriting authority has been in place since the mid 1970s. The following chart outlines the assessments made by the property and casualty joint underwriting authority since 1970:

Year	Account	Principal Storm(s)	Assessment Amount
1975	HRA	Hurricane Eloise	$ 5.0 million
1985	HRA	Hurricane Elena	$ 3.2 million

coverage on all such insurance except for inland marine and certain vehicle insurance other than the insurance on mobile homes used as permanent dwellings.

[8] Personal communication with representatives from Citizens.

[9] *See* s. 617.3512, F.S. (2005); s. 627.311(5)(d), F.S. (2005) (relating to the Florida Workers' Compensation Joint Underwriting Association); s. 627.351(4)(e), F.S. (2005) (relating to the Medical Malpractice Joint Underwriting Association)

1992	HRA	Hurricane Andrew	$ 16.2 million
1993	HRA	Winter Storm	$ 3.2 million
1994	PLA	Non-hurricane	$ 17.7 million
1995	HRA	Hurricane Opal	$ 84 million
1995	PLA	Hurricane Opal	$ 22.8 million
1998	HRA	Hurricane George and Tropical Storm Mitch	$100 million

Source: Citizens Property Insurance Corporation (August 25, 2005)

Although all of the assessments outlined above were levied before the creation of Citizens, they were levied by the predecessor "insurer of last resort" for property and casualty insurance (i.e. the Florida Residential Property and Casualty Joint Underwriting Association (RPCJUA) or the Florida Windstorm Underwriting Association (FWUA)).

Citizens started the 2005 hurricane season with no surplus in the HRA.[10] Because this account sustained losses again in 2005 as a result of the 2005 hurricanes, Citizens incurred a deficit for the second year in a row. Although Citizens does not have actuarially determined amounts of its 2005 deficit, it estimates the deficit in the High Risk Account will be $1.7 billion.[11] However, this amount includes $590 million in worsening loss development for claims from 2004.

Citizens started the 2005 hurricane season with an estimated $162 million surplus in the PLA and $25.7 million surplus in the CLA.[12] For 2005, Citizens estimates a deficit of $82 million in the PLA and a deficit of $4 million in the CLA.[13]

The assessment amount needed to cover the 2005 deficit has not yet been determined.

Citizens' Operations

Chapter 2005-111, L.O.F., directed the Auditor General to conduct an audit of Citizens. On December 7, 2005, the Auditor General released an operational audit (report number 2006-096) of Citizens, which included findings in the areas of administration, policy eligibility determination and depopulation, customer service, claims handling, actuarial soundness of rates, and financing options. The report included the following recommendations related to the administration of Citizens:

- No documentation was available to show that Citizens had conducted an enterprise-wide evaluation of the effectiveness of operational and financial controls.
- The statutes governing Citizens do not require the OIR to conduct background investigations of Citizens' management and officers, which are required for voluntary insurers.
- Additional steps should be taken to strengthen the standards of conduct.
- Citizens had not implemented a comprehensive written procurement of policies and procedures.

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[10] Personal communication from a representative of Citizens.
[11] *Id.*
[12] *Id.*
[13] *Id.*

In response to concerns expressed by the Auditor General, the Legislature, and the Office of Insurance Regulation, the board of governors of Citizens approved the following amendments to the plan of operation to strengthen standards of conduct on October 20, 2005, which were subsequently approved by the OIR on November 30, 2005:

- A requirement that senior management be subject to the background investigation provisions of ss. 624.404(3) and 628.261, F.S.
- A requirement that the Division of Insurance Fraud of the Department of Financial Services will be notified within 48 hours of any suspected fraud or compromise of public trust by a quasi-governmental employee.
- A code of ethics that includes detailed provisions regarding conflicts of interest, dual-employment and post-employment restrictions. Gifts of more than $100 are prohibited. Financial and other interest that conflict with the interests of Citizens are prohibited. Senior management is required to file a financial disclosures form substantially similar to the form required for state employees under s. 112.3145, F.S., with the OIR and the internal auditor of Citizens. Senior management is prohibited from doing business before the board of Citizens for a period of 2 years following termination from Citizens.
- Prior to the entering into a procurement relationship, employees involved in the procurement process and vendors are required to disclose any conflict of interest. Generally, purchases estimated to cost $25,000 or more are subject to the competitive bid process. Employees engaged in the purchasing process are prohibited from accepting any gifts, other than advertising novelties of nominal value.

Code of Ethics and Financial Disclosure; Procurement of Goods and Services
Part III of ch. 112, establishes the code of ethics for public officers and employees, which mandates that employees comply with financial disclosure and reporting requirements. Each year, public officers and specified employees are required to submit a financial disclosure to the Commission on Ethics. Noncompliance with these provisions may result in civil penalties and forfeiture of public retirement benefits. [s. 112.317, F.S.] In addition, any contract that has been executed in violation with this part is voidable by any party to the contract, the Commission on Ethics, the Attorney General, and any citizen materially affected by the contract that resides in the jurisdiction of the agency entering into such contract. [s. 112.3175, F.S.]

In December 2005, the Legislature revised the laws governing the acceptance of gifts by members and employees of the Legislature and agency officials, to prohibit any gifts or expenditures, regardless of the value. [ch. 2005-359, L.O.F.]

The provisions of part I of ch. 287, F.S. governs the procurement of goods and services by agencies of the state. Under current law, state agencies are generally required to procure goods and services valued over $25,000 through competitive selection process. Exceptions to this process are authorized for exempted services (legal and auditing, etc.), sole sourcing and emergency purchases. Section 287.059, F.S. provides guidelines and criteria for determining whether staff attorneys or outside attorneys should be used and factors to be used in selecting outside firms.

Pursuant to s. 11.062, F.S. an agency of the executive branch is prohibited from using state funds to retain a lobbyist to represent it before the executive or legislative branch. However, full-time

employees of the agency may register as lobbyists and represent that employer before the executive or legislative branch.

Florida Hurricane Catastrophe Fund

The Florida Hurricane Catastrophe Fund (FHCF or "fund") is a tax-exempt trust fund created after Hurricane Andrew as a form of mandatory reinsurance for residential property insurers.[14] All insurers that write residential property insurance in Florida are required to buy reimbursement coverage (reinsurance) on their residential property exposure through the FHCF. The FHCF is administered by the State Board of Administration (SBA) and is a tax-exempt source of reimbursement to property insurers for a selected percentage (45, 75, or 90 percent) of hurricane losses above the insurer's retention/deductible.

Because the FHCF provides insurers an additional source of reinsurance to what is available in the private market, insurers are generally able to write more residential property insurance in the state than would otherwise be written. Because reinsurance purchased through the FHCF is significantly less expensive than private reinsurance, the FHCF also acts to lower residential property insurance premiums for consumers.

The FHCF must charge insurers 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. Each insurer's "reimbursement premium" is different, based on the insured value of the residential property it insures, their location, construction type, deductible amounts, and other factors.

Under current law, the maximum amount the FHCF must pay in any 1 year is $15 billion, adjusted annually based on the percentage growth in fund exposure, but not to exceed the dollar growth in the cash balance of the fund.[15] The total industry retention is $4.5 billion per hurricane, also adjusted annually based on the FHCF's exposure (regardless of any change in the FHCF's cash balance).[16]

The FHCF generally operates on a "contract year." The contract year runs from June 1st to May 31st of the next calendar year. The start of hurricane season coincides with the start of the fund's contract year.

For the current 2005-06 contract year (June 1, 2005 – May 31, 2006), the insurance industry as a whole has an aggregate retention of $4.5 billion, meaning the total of all individual insurer retentions/deductibles will hypothetically total to $4.5 billion per event, assuming all participating insurers reached their retention. Although the insurance industry's aggregate deductible/retention totals $4.5 billion, loss recovery from the FHCF is based on an individual insurer meeting its own retention prior to losses being reimbursed. The industry aggregate retention is expected to grow to $5.3 billion for the 2006-2007 contract year.

[14] s. 215.555, F.S. (2005).
[15] s. 215.555((4)(c)1., F.S. (2005).
[16] s. 215.555(1)(e)1., F.S. (2005).

Each insurer must meet a retention/deductible before FHCF monies are available to pay claims. The retention level for each insurer is different because the retention level is based on the amount of premium the insurer pays to the FHCF. Insurers with a high FHCF premium will absorb more as a retention/deductible than an insurer with a low FHCF premium. The insurer must meet its retention level for each storm in a hurricane season before the FHCF will step in to pay its claims. For insurers who experience losses due to multiple storms in a year, the insurer's full retention is applied to the two storms causing its two largest losses and its retention for the other storms causing loss is one-third of the full retention.[17]

As with the FHCF retention/deductible levels, every insurer participating in the FHCF has coverage based on its FHCF reimbursement premium. Each insurer has a maximum amount of coverage the FHCF will pay for claims each year. The maximum amount of coverage is different for each insurer because it is linked directly to the amount of premiums the insurer pays to the FHCF. Thus, insurers that pay higher premiums to the FHCF have more coverage than those that pay lower premiums. For the current contract year (2005-2006), the insurance industry as a whole is covered for up to $15 billion, meaning $15 billion is the most the FHCF will pay to the insurance industry on claims for a hurricane season. The coverage limit for the fund for the 2006-2007 contract year will remain at $15 billion because the fund's capacity may not grow more than the growth in the fund's cash balance.

Additionally, insurers also choose a percentage level of reimbursement by the FHCF. By statute, insurers can select 45, 75, or 90 percent coverage reimbursement for losses that exceed its deductible/retention for each hurricane.[18] Most insurers choose the 90 percent reimbursement percentage.[19] This means once an insurer triggers FHCF coverage, 90 percent of its losses will be covered by the FHCF, up to the insurer's limit of coverage. Insurers may purchase additional reinsurance in the private market to cover their hurricane losses for amounts below the retention, amounts above their reimbursement limit, or for the coinsurance amount (e.g., 10 percent) that is the insurer's responsibility for the layer of coverage provided by the FHCF.

If the cash balance of the fund is not sufficient to cover losses, the law allows the issuance of revenue bonds, which are funded by emergency assessments on property and casualty policyholders.[20]

The FHCF is authorized to levy emergency assessments against all property and casualty insurance premiums paid by policyholders (other than workers' compensation and, until June 1, 2007, medical malpractice), including surplus lines policyholders, when reimbursement premiums and other fund resources are insufficient to cover the fund's obligations.[21] Annual assessments (which have never been levied) are capped at 6 percent of premium with respect to losses from any 1 year and a maximum of 10 percent of premium to fund hurricane losses from multiple years.[22]

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[17] s. 215.555(1)(e)4., F.S. (2005).
[18] s. 215.555(1)(e)2., F.S. (2005).
[19] Florida Hurricane Catastrophe Fund, Fiscal Year 2003-2004 Annual Report 23.
[20] s. 215.555(6)(a)1., F.S. (2005); s. 215.555(6)(b)1., F.S. (2005).
[21] s. 215.555(6)(b)1., F.S. (2005); s. 215.555(6)(b)(10), F.S. (2005).
[22] s. 215.555(6)(b)2., F.S. (2005).

The FHCF is expected to pay out $3.8 billion to insurers as a result of the 2004 hurricanes; to date, the fund has already paid $3.5 billion to insurers. Because the amount paid in 2004 was less than the FHCF's cash balance, bonding was not necessary. However, the loss estimates for the FHCF are estimates and as losses develop, the actual payments may exceed the current estimates.

For the current 2005-2006 contract year, the fund's $15 billion capacity consists of $3 billion in cash (before losses) and $12 billion in bonding capacity. The FHCF is expected to pay out $3.3 billion to insurers as a result of the 2005 hurricane season; approximately $2.2 billion has actually been paid by the fund to insurers. The remainder will be paid out as insurers request reimbursement and provide proof of losses.

Based on the latest data, the FHCF believes it may have a cash shortfall and will have to bond in order to pay claims from the 2005 hurricane season. The fund had previously estimated a cash shortfall of $264 million.[23] However, these loss estimates for the FHCF were preliminary and as losses have developed, the estimated cash shortfall has grown significantly. On April 5, 2006, representative of the Fund have stated that the latest loss estimates will result in a deficit of $1.35 billion. This is based on both reported losses and an estimate of incurred but not reported losses, but also includes an estimated $200 million in revenue from the 25 percent "rapid cash build up" factor that the SBA recently approved for the 2006 premium formula.

Because the FHCF is not likely to have cash to carry over to fund claims resulting from the 2006 hurricane season, it will have to rely solely on premiums collected in 2006 to reimburse insurers for losses. This makes bonding more likely if the fund has to pay claims as a result of 2006 hurricanes. The fund's anticipated premium revenue for 2006 is $800 million.[24] However, premiums to the FHCF are paid by insurers in three installments on June 1, August 1, and December 1, 2006. Thus, should an early season hurricane occur, it may be necessary for the FHCF to borrow money to cover losses. For low amounts of losses, this could be done with a simple loan. For large amounts of loss, revenue bonds would need to be issued.

In summary, from the inception of the fund in 1993 until the 2004 hurricane season, the fund paid insurers for claims for only two hurricanes, Hurricanes Erin and Opal in 1995. Until 2004, the amount the FHCF paid to insurers totaled approximately $13 million. Thus, going into the 2004 hurricane season the FHCF had accumulated over $6 billion in cash. As a result of the 2004 hurricanes, the fund has spent or expects to spend almost $3.8 billion of its cash reimbursing insurers for hurricane losses. Going into the 2005 hurricane season, the fund's cash had decreased to $3 billion. With reimbursement to insurers for 2005 hurricane losses expected to be $3.3 billion, the fund anticipates it may have to bond to pay claims and will start the 2006 hurricane season with no cash. Thus, it is important to note that the $6 billion it took the FHCF to accumulate over ten years was depleted in just two years.

Hurricane Loss Mitigation Funding

Section 215.559, F.S. directs the Legislature to annually appropriate at least $10 million from the FHCF, but no more than 35 percent of the investment income from the prior fiscal year for

[23] Memorandum regarding FHCF Losses Update & Activity Report to the State Board of Administration from Coleman Stipanovich dated March 21, 2006.

[24] Florida Hurricane Catastrophe Fund 2006 Ratemaking Formula Report to the State Board of Administration (March 27, 2006).

hurricane loss mitigation programs.[25] Actual annual legislative appropriations have ranged from the minimum $10 million to $30 million.

The Hurricane Loss Mitigation Program (Mitigation Program) 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.[26] Three ($3) million from the Mitigation Program 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.

Sinkhole Claims

Nationwide, property insurance policies typically exclude coverage for "earth movement." But, in Florida, every authorized insurer must make available coverage for insurable sinkhole losses on any structure and the personal property contained within it.[27] Even though the coverage must be "made available", insurers include sinkhole coverage within their policies, apparently because it would lead to adverse selection if offered as an option, i.e., only those in sinkhole prone areas would elect the coverage.

In some areas of the state, sinkhole costs have grown at an exponential rate in recent years. This has caused policy cancellations due to paying policy limits on sinkhole claims, and insurers refusing to issue new policies in sinkhole prone areas. Citizens Property Insurance Corporation has had a significant increase in policies from the Tampa Bay area (Hernando, Hillsborough, Pasco, and Pinellas counties), increasing from 1,012 policies at the end of 2001, to 140,171 policies, or an increase of 13,751 percent.[28] This is believed to primarily be due to private insurance companies refusing or limiting coverage in this area due to the sinkhole exposure. By way of comparison, the growth in Dade, Broward, and Palm Beach counties during the same period was 104 percent. Not only do more homeowners have to seek coverage from Citizens, but such policyholders are being hit with exploding premium costs. The average Citizens premium in Pasco County more than doubled from $1,006 on March 1, 2003, to $2,368 on April 1, 2006. If a

[25] s. 215.555(7), F.S. (2005).
[26] s. 215.559, F.S. (2005).
[27] Section 627.706, F.S.
[28] Task Force on Long-Term Solutions for Florida's Hurricane Insurance Market-Final Report, pg. 41 (March 6, 2006).

pending Citizens actuarial rate filing for such homes is approved, the average premium will rise to $3,605 as of August 1, 2006.

In 2004, the Legislature commissioned a study by Florida State University, under the direction of OIR, of the feasibility and cost-benefit of a Florida Sinkhole Insurance Facility and other matters related to affordability and availability of sinkhole insurance. The report was submitted on April 1, 2005, as required. The study found that the number of paid sinkhole claims increased from 348 in 1999 to 1,108 in 2003 while total claims payments for sinkholes increased from $22.4 million in 1999 to $65 million in 2003. For this five-year period (which had no hurricane claims), there were a total of 2,509 paid sinkhole claims, representing 1 percent of all claims paid by insurers, but the $219.2 million paid for sinkhole claims accounted for 16.2 percent of total claims payments.

The Legislature in 2005 substantially amended the laws on sinkhole claims, as follows:

- Specified that sinkhole coverage includes the costs to stabilize the land and building and to repair the foundation.
- Allowed an insurer to deny a sinkhole claim if the insurer determines there is no sinkhole loss, but the insurer must provide written notice to the policyholder of their right to demand testing.
- If the policyholder demands testing, the insurer must engage an engineer or a geologist to conduct testing.
- Testing must be conducted in compliance with specified standards and a report must be issued as to the cause of the loss, with recommendations for stabilization and repair.
- The findings and recommendations of the engineer and geologist are presumed correct and the insurer must pay the costs of stabilization and repair in accordance with the recommendations.
- The insurer may limit its payment to the actual cash value of the sinkhole loss until such time as expenses related to land and building stabilization and foundation repairs are incurred, including underpinning and grouting. But, the insurer cannot require the policyholder to advance payments. The insurer must pay the expenses after a policyholder enters into a contract for stabilization or foundation repairs, and pay amounts necessary to begin and perform repairs as the work is conducted.
- If repair has begun and the engineer selected or approved by the insurer determines that the repair cannot be completed within the policy limits, the insurer must either complete the engineer's recommended repair or tender the policy limits to the policyholder without a reduction for the repair expenses incurred.
- If an insurer pays a sinkhole claim, it must file a copy of the professional report with the county property appraiser.
- Established a sinkhole database to track sinkhole insurance claims.
- Required the seller of real property to disclose to the buyer that a sinkhole claim has been paid and whether or not the insurance proceeds were used to repair the sinkhole damage.

Other Present Law issues affected by this bill are discussed in Effects of Proposed Changes, below.

III. Effect of Proposed Changes:

Section 1 amends s. 215.555, F.S., related to the Florida Hurricane Catastrophe Fund ("Fund"). The major change is to require that the Fund add a charge of 25 percent of the actuarially indicated premium to provide a more rapid cash buildup factor. It is currently estimated that the Fund premiums for 2006 will be $800 million, without any changes to the current law. The 25 percent rapid cash build up factor would add $200 million to the premium, totaling $1 billion. Representatives of the State Board of Administration have stated that the current bonding documents prohibit the Fund from utilizing premium income from the actuarially indicated premium for 2006 to pay for claims incurred in 2005. However, the portion attributable to the rapid cash buildup factor can be used to pay claims associated with the 2005 hurricane season; and, therefore, reduce the cash shortfall for the 2005 season.

The bill also deletes language that appears to be obsolete requiring a preference in reimbursement to limited apportionment companies when the cash balance is below $2 billion. This language was in the law when the Fund was designed to make payments at year end, due to each insurer's maximum share not being known until that time. Changes in 1995 established recovery limits for each insurer, which has enabled the Fund to reimburse insurers almost immediately (2 to 7 days). The current language could bring into question whether the Fund should reserve cash for limited apportionment companies, even if other insurers have claims owing, which could result in delaying payment or earlier or unnecessary bonding.

The bill clarifies:

- that the reference to "cash balance" for purposes of determining the annual growth factor for the Fund's $15 billion limit, refers to the Fund balance as of December 31, as defined by rule;
- that the Fund does not reimburse insurers for claims for loss of rent or rental income, rather than "loss of use," to further clarify that the Fund does reimburse insurers for claims for additional living expenses paid under their policies; and
- that any annual assessments that are necessary to fund bonding obligations continue "for as long as" (rather than "until") the revenue bonds are outstanding.

Section 2 creates s. 215.558, F.S., to require the Department of Community Affairs to establish the Home Retrofit Hardening Program as a competitive grant program administered by local governments, regional planning councils, or private nonprofit agencies, to fund improvements to homes to make them less vulnerable to hurricane damage. The order of priority would be: 1) low-income homeowners who live in wind-borne debris regions as defined in the Florida Building Code, who are eligible for up to 100 percent funding; 2) homestead dwellings insured at $500,000 or less and located in high-risk areas of Citizens, with priority for homes insured by Citizens, eligible for up to 50 percent funding; and 3) all other homestead dwellings insured at $500,000 or less, eligible for up to 25 percent funding. The maximum grant for an individual home is $10,000. The program must include an inspection to determine mitigation measures, a means for verifying that the improvements have been demonstrated to reduce hurricane damage and that the proceeds were spent on such improvements. (Section 27 of the bill appropriates an unspecified amount from General Revenue for this program.)

Section 3 creates s. 215.5586, F.S., to provide wind certification and hurricane mitigation inspections to homeowners at no cost, pursuant to a request for proposals from providers who must meet specified criteria of prior experience or specialized training. The bill makes an unspecified appropriation from General Revenue for this purpose.

Section 4 amends s. 193.155, F.S. to provide that specified mitigation improvements are not to be included or otherwise increase the assessed value of a home for tax purposes.

Section 5 creates s. 252.63, F.S., to authorizes the Commissioner of Insurance Regulation to issue orders to temporarily modify or suspend provisions of the Insurance Code to expedite recovery of communities affected by a disaster, when the Governor declares a state of emergency. This provision is modeled on s. 252.62, F.S., which provides similar powers to the Director of the Office of Financial Regulation relative to the laws for financial institutions.

Section 6 amends s. 626.918, F.S., to allow alien surplus lines insurers to fund trust funds with letters of credit meeting certain criteria issued or confirmed by a qualified United States financial institution, as defined. Alien surplus lines insurers (i.e., formed under the laws of another country) must maintain in the United States, a trust fund for the protection of U.S. policyholders of at least $5.4 million, in addition to the minimum $15 million minimum surplus requirement.

Section 7 amends s. 627.062, F.S., to revise the rate standards for property and casualty insurance rates, as follows:

The bill prohibits OIR from disapproving a rate as excessive for personal lines residential coverage with a dwelling replacement cost of $1 million or more, or for a condominium unit with a combined dwelling and contents replacement cost of $1 million or more. These are the same properties that would no longer be eligible for coverage with Citizens, pursuant to Section 8 of the bill. The law would still require that the insurer file the proposed rates for approval with OIR, subject to the current procedures for doing so, but the grounds for disapproval of the rate would be limited to a determination by OIR that the rates are inadequate or unfairly discriminatory. Also, the bill would not exempt such coverage from any policy or form requirements, or any required offers of coverage that apply under the current law, which would still apply.

The bill also revises the current law that allows an insurer writing residential property insurance to recoup in its rates the premiums paid to the Florida Hurricane Catastrophe Fund, together with "reasonable" costs of other reinsurance. The bill changes this standard to, instead, allow an insurer to recoup its costs of other reinsurance "consistent with prudent business practices and sound actuarial principles", but the burden would be on OIR to establish that such costs are in excess of this standard. Currently, when an insurer makes a rate filing, it has the burden to prove by a preponderance of the evidence to show that a rate is not excessive, inadequate, or unfairly discriminatory (s. 627.062(1)(g), F.S.). The bill's provision would shift this burden to the OIR only with regard to whether the costs of reinsurance the insurer is attempting to recoup exceed the statutory standard, as revised.

For that portion of a rate covering the hurricane risk for which the insurer has not purchased reinsurance and has exposed its capital and surplus to covering this risk, the bill places an

affirmative duty on the OIR to approve a rating factor that provides an insurer a reasonable rate of return that is commensurate with such risk. Current law requires OIR to consider various factors in reviewing a rate filing, including "a reasonable margin for underwriting profit and contingencies." The risk of hurricane loss is unlike other non-catastrophic risks that insurance covers, in that it exposes the insurer's capital to being depleted by a single hurricane or multiple hurricanes in a single season, to the extent that reinsurance has not been purchased by the insurer to cover that risk. Even if an insurer generally has confidence in the use of loss projection models that estimate the average expected loss, those same models will also project a probable maximum loss for a single year over a 100-year period. Insurers must be prepared to cover this loss if it happens the next year. Investors who contribute to the capital of the insurer and face the risk of experiencing that loss, expect a higher rate of return for this risk than for other more predictable risks, such as the fire, theft, and liability losses, which generally do not deviate significantly from the average annual expected loss. If the expected rate of return is not higher than for more predictable and less variable risks, investors and insurers will commit their capital to writing such risk, rather than writing coverage for hurricanes.

Section 8 amends s. 627.651(6), related to Citizens Property Insurance Corporation

Residential Structures Valued at $1 million or More Ineligible for Coverage

The bill provides that effective January 1, 2007, a personal lines residential structure with a dwelling replacement cost of $1 million or more, or condominium unit with combined dwelling and content replacement cost of $1 million or more is not eligible for coverage, with certain exceptions. This will affect the wind-only coverage currently offered by Citizens in the high-risk account (HRA), since Citizens currently excludes coverage for these policies in the personal lines account.

The bill allows for "grandfathering in" certain homes. Property insured by Citizens on December 31, 2006 may continue to be insured until the end of the policy term for a renewal effective on or before December 31, 2007 (meaning a home renewed on that date could remain until December 31, 2008). In other words, beginning in 2007, a home insured with Citizens could renew for one more year. The bill also allows for new construction of homes valued over $1 million to be insured with Citizens for a limited period. If the building permit has been issued by January 1, 2007, the home may be insured with Citizens if the certificate of occupancy has been issued by December 31, 2007, and coverage may be provided until the end of that policy term (i.e., for one year).

Citizens has reported that its estimated 100-year probable maximum loss (PML) for the HRA would be reduced by approximately $800 million if it did not insure residential properties with values greater than $1 million. Citizens had also reported in February of this year that the 100-year PML for the HRA was $7.8 billion as of December 31, 2005. However, Citizens reported new PML estimates in March, that the 100-year PML of the HRA is now $10.3 billion.

In the February estimates, Citizens reported that it had 6,431 residential policies in force that were insured for values greater than $1 million, with a total insured value of $16.7 billion with a total premium of $64.3 million. In response to staff's inquiry for updated information, a representative of Citizens reported that as of December 12, 2005, it had 5,280 HRA residential

policies with dwelling coverage in excess of $1million and that the total inforce premium was $64,238,090, resulting in an average premium of $12,166.

Rate Surcharge for Non-Homestead Property

The bill requires that for policies issued or renewed on or after January 1, 2007, Citizens must impose a 25 percent rate surcharge on "nonhomestead property." This reflects a legislative policy that there should be less reliance on assessments on non-Citizens policyholders to fund deficits for losses to nonhomestead property than for homestead property. The bill also requires that if Citizens does experience a deficit, that there must be an additional 25 percent surcharge imposed on nonhomestead property, but this provision would be limited to nonhomestead property owned by a nonresident of Florida.

However, the definition of "homestead property" that is not subject to these surcharges is broader than the use of this term for tax purposes. The definition in the bill would include the following (who would not be subject to the 25 percent surcharges):

- property granted a homestead exemption under chapter 196, F.S.
- property for which the owner has a current, written lease with a renter for a term of at least 6 months;
- an owner-occupied mobile home or manufactured home as defined in s. 320.01, permanently affixed to real property (i.e., whether or not the owner also owns the land and has been granted a homestead exemption);
- tenants coverage (i.e., the coverage purchased by a renter to cover the contents)
- commercial lines coverage, including both residential and nonresidential (i.e., condominium associations, apartment buildings, commercial businesses; however, a condominium unit owner would not meet the definition of homestead unless he or she had a homestead exemption or has a current 6-month lease with a renter.)

Calculation of Deficit Assessments

The bill requires that in determining the amount of the regular assessment to be levied on insurers (and recouped from their policyholders), the amount must be reduced by amounts that are estimated to be collected from surcharges on Citizens' policyholders. There are two such surcharges under the bill. One is the current "market equalization surcharge" that the bill re-names the "Citizens policyholder surcharge." Currently, this surcharge must be imposed by Citizens on their own policyholders after an assessment has been levied, as an equal percentage of the premium that was, on average, paid by the voluntary market policyholders after being recouped by insurers. However, the current law requires the entire deficit to be funded by the regular assessment (if it is at or below 10 percent of premium), so that by imposing the market equalization surcharge, Citizens actually collects more than the estimated deficit amount. Under the bill, the amount to be collected from this surcharge on Citizens policyholders must be deducted from the regular assessment. But, in computing the Citizens policyholder assessment, the calculation requires that the total amount of the regular assessment must be determined without deducting the estimated Citizens policyholder surcharge.

The bill also requires that in calculating the amount of the regular assessment, that there must also be a reduction for the estimated amount that will be collected from the new 25 percent "deficit surcharge" that the bill requires to be imposed on premiums for nonhomestead property owned by a non-resident of Florida.

Ten-Day Waiting Period; Limited Exception to "Consumer Choice"

The bill requires that effective July 1, 2007, applications for new coverage to Citizens are subject to a 10-day waiting period, and must be made available for review by agents and insurers. However, the board is authorized to approve exceptions that allow for coverage to be effective during this time for coverage issued in conjunction with a real estate closing or other situations the board determines are necessary to prevent lapses in coverage.

Due to the change in Section 11 of the bill, below, if an authorized insurer offers coverage during this 10-day period, the applicant would not be eligible for coverage in Citizens, whether or not the insurer appoints the agent who submitted the application. This is due to the provision in current law (s. 627.651(c)5., F.S.), which provides, "Subject to the provisions of s. 627.3517, with respect to personal lines residential risks, if the risk is offered coverage from an authorized insurer at the insurer's approved rate . . . the risk is not eligible for any policy issued by the corporation." The reference to "Subject to the provisions of s. 627.3517" is a reference to the "Consumer Choice" statute that provides, "If the [Citizens] policyholder's current agent is unable or unwilling to be appointed with the insurer making the take-out or keep out offer, the policyholder shall not be disqualified from participation in [Citizens]…" However, Section 10 of the bill provides that this provision would not apply during the first 10 days after a new application for coverage has been submitted to Citizens, whether or not coverage is bound during this period. But, if the policy is taken out during this 10-day period, the bill would still apply the current law that requires the take-out insurer to provide compensation to the agent pursuant to s. 626.361(6)(c)5.a.(I), F.S., which requires paying the producing agent, for the first year, an amount that is the greater of the insurer's commission or Citizen's commission.

Oversight and Internal Controls

- Requires the Financial Services Commission (Governor and Cabinet), rather than the Office of Insurance Regulation (OIR), to approve Citizens' plan of operation.
- Requires Senate confirmation of the Executive Director of Citizens.
- Requires Citizens to have an internal auditor who must submit an annual report to the board, the Financial Services Commission, and the Legislature. Citizens' internal auditor was engaged in December 2004 and has issued reports on the following areas investments function, premiums and cash Receipts, and cat claims. Another audit on agency administration and compliance, which was part of the internal auditor's work plan, was conducted by external auditors.
- Requires OIR to do a market conduct examination of Citizens every two years.
- Requires the Auditor General to conduct an operational audit of Citizens every three years.
- Requires competitive bidding of contracts, with exceptions, and board approval of contracts of $100,000 or more. These requirements are similar to requirements that have been adopted by Citizens.

- Requires OIR background checks of applicants for senior management positions. The OIR is responsible for conducting these background checks pursuant to ss. 624.404(3), and 628.261, F.S. Currently, prospective officers and senior management of insurers in the voluntary market are subject to the same requirements. The background check includes a national fingerprint check. Effective, October 20, 2005, Citizens instituted background checks pursuant to these statutory provisions.

Standards of Conduct

- Subjects board members and senior managers to the code of ethics and financial disclosure requirements applicable to public officials and specified state employees. In October 2005, the board adopted financial disclosures similar to the forms required of senior management of state agencies. However, these forms are required to be submitted to the OIR and the Internal Auditor rather than the Commission of Ethics, as the bill requires.
- Prohibits board members and employees from accepting any gifts from any person or entity under contract with Citizens or under consideration for a contract. Currently, Citizens prohibit employees and board members of the corporation from accepting gifts valued over $100.
- Prohibits Citizens from retaining lobbyists, but allows employees to register as lobbyists.
- Prohibits senior managers from representing any person or entity before Citizens for two years following termination of employment from Citizens.

Other Changes to Citizens

- Requires insurers writing the non-wind coverage to contract with Citizens to provide claims adjusting services for the wind coverage provided by Citizens in the high-risk account.
- Requires Citizens to offer quarterly and semiannual premium payment plans.
- Extends for two years (until Feb. 1, 2009) the requirement that the board reduce the boundaries of the high risk area eligible for wind-only coverage.
- Requires that any take-out bonus paid to an insurer by Citizens must be conditioned on the insurer keeping the policy for five years. Also, requires Citizens to monitor whether such policies are later insured by Citizens.
- Requires Citizens to report to the Legislature its recommendations regarding consolidation of its three existing accounts and the actions taken to minimize the cost of carrying debt.

Section 9 specifies that the changes in Section 8 regarding the method for calculation and determining the assessments and surcharges that must be levied to fund deficits in Citizens apply to a deficit incurred in 2006 and thereafter.

Section 10 amends s. 627.3511, F.S., to conform to the changes made in Section 8 regarding take-out bonuses paid by Citizens, to require that any bonus be conditioned on the property being insured for at least 5 years. This section currently provides for a maximum $100 per policy take-out bonus, under specified conditions, but this section has been effectively moot, due to the

broader authority in the Citizens statute that allows Citizens to adopt programs for the reduction of writings subject to the approval of OIR, (s. 627.351(6)(g)3., F.S.) provide that any take-out bonus paid to an insurer.

Section 11 amends s. 627.3517, F.S., related to Consumer Choice. This law currently provides that no provision in the Citizens statute or any other joint underwriting association or risk apportionment plan shall be construed to impair the right of any policyholder to retain his or her current agent, upon receipt of any keep out or take-out offer. The current law provides that a policyholder shall not be disqualified from being insured in Citizens or any other plan because of an offer of coverage in the voluntary market if the policyholder's current agent is unable or unwilling to be appointed by the insurer making the take-out or keep out offer. The bill provides an exception to this law, so that it would not apply during the first 10 days after a new application for coverage has been submitted to Citizens, whether or not coverage is bound during this period. As described in Section 8, above, the bill requires that applications for new coverage to Citizens are subject to a 10-day waiting period, and must be made available for review by agents and insurers.

Section 12 amends s. 627.4035, F.S., to provide an exception to the requirement that the recipient's written authorization must be provided to an insurer in order for the insurer to pay claims electronically. The bill waives this requirement if the insurer verifies the identity of the insured or recipient, does not charge a fee for the transaction, and remains liable if the funds are misdirected.

Section 13 creates s. 627.6121, F.S., to require property insurers to issue separate checks payable to the primary policyholder only, to pay claims for contents, living expenses, and the lesser of $20,000 or the first 20 percent of the estimated total covered claim amount for the replacement or repair of dual interest (mortgaged) property.

Section 14 amends s. 627.7011, F.S., to clarify that if a property insurer does not obtain a written rejection from the policyholder for law and ordinance coverage, the policy is deemed to include the law and ordinance coverage limited to 25 percent of the dwelling limit (and not the alternative 50 percent limit that must also be offered).

Section 15 creates s. 627.7019, F.S. to require the Financial Services Commission to adopt rules standardizing requirements that may be applied to insurers after a hurricane, addressing claims reporting requirements, grace periods for payment of premiums, and temporary postponement of cancellations and nonrenewals.

Section 16 amends s. 627.707, F.S, relating to standards for investigation of sinkhole claims. The bill allows the insurer to make payment directly to the persons selected by the policyholder to make the repairs, if approved by the policyholder and lienholder.

The bill also provides that provisions of subsection (5) of this statute do not apply when two or more buildings, structures, mobile homes or manufactured buildings are insured under a blanket form for a single amount of insurance. This exception would apply to all of the provisions of subsection (5), which include requirements for the insurer to pay to stabilize the land and building and repair the foundation in accordance with the recommendations of the engineer; to

limit its payment to the actual cash value of the loss, not including underpinning or grouting until the policyholder enters into a contract for repairs; requiring payment of amounts necessary to begin and make repairs as the work is performed; and requiring that if repair cannot be completed within the policy limits after the work has begun, that the insurer must either complete the engineer's recommended repair or tender the policy limits. It would also exempt such multi-building policies from the bill's new provision allowing the insurer to make payments directly to the contractor, if approved by the policyholder and lienholder.

Section 17 amends s. 627.7073, F.S., to delete the requirement that testing by a geologist be conducted in compliance with the Florida Geological Survey.

Section 18 amends s. 627.7073, F.S., to provide that the report that must be issued by the engineer or geologist that completes the required testing of a sinkhole claim must provide his or her findings as to the "cause of damage" rather than "verification or elimination of a sinkhole loss."

Section 19 creates s. 627.7074, F.S. to require the Department of Financial Services to certify engineers and geologists to serve as "neutral evaluators" of sinkhole claims disputes between insurers and policyholders. This process would be optional and nonbinding and the costs must be paid by the insurer. However, if an insurer requests this process and the policyholder either declines to participate or declines to resolve the matter in accordance with the recommendation of the neutral evaluator, the insurer would not be liable for attorney's fees or other extra-contractual damages related to a claim.

Section 20 amends s. 627.727, F.S., to make a technical change to conform to a cross-reference.

Section 21 amends s. 631.181, F.S., related to insurance guaranty associations. The bill allows FIGA and other guaranty associations to pay claims of unearned premium refunds, without requiring the policyholder to file a proof of claim form, if adequate claims file documentation exists within the records of the insolvent insurer, or if the receiver certifies to the guaranty fund that the records of the insolvent insurer are sufficient to determine the amount of unearned premium owed to each policyholder. This should result in returning unearned premiums to policyholders much more quickly.

Claimants are required to file "proof of claim" forms with the receiver (department) for any unpaid claims against an insurer in receivership, which must include certain information and be filed within the time limits specified in the receiver's notice. This applies not only to claims covered under the policy, but also to policyholder claims for the return of unearned premium, which is covered by each of the guaranty funds, subject to a $100 deductible in FIGA. This process is time consuming and often results in insureds not receiving a return of their unearned premium for months or even a year after an insolvency.

Section 22 amends s. 631.54, F.S., to revise the definition of "covered claim" to specify that for an entity other than a person, i.e., a business or other legal entity, the residence of the entity is the state where the entity's principal place of business is located. This would change the current interpretation applied by FIGA that the state of incorporation is the state of residency of a corporation.

According to representatives from FIGA, this will conform the Florida law to the majority of jurisdictions that use the principal place of business test for determining residency of a corporation for purposes of guaranty fund coverage. So, corporations and business entities with their principal place of business in Florida will be covered by FIGA if their insurer is rendered insolvent. Corporations incorporated in Florida but which have their principal place of business in another state will be required to seek reimbursement from the other state's guaranty association.

The bill adds a definition of "homeowners insurance" that is relevant to the following section of the bill which increases the maximum amount of FIGA's liability for a covered homeowners insurance claim against an insolvent insurer from $300,000 to $500,000.

Section 23 amends s. 631.55, F.S., to make a technical change to a cross-reference.

Section 24 amends s. 631.57, F.S., to authorize FIGA to impose annual emergency assessments on insurers of up to 2 percent of written premium for specified lines of property and casualty insurance to fund revenue bonds issued by a municipality or county to pay claims of an insurer rendered insolvent due to a hurricane. The bill authorizes FIGA to contract with a city or county to issue tax-exempt revenue bonds for this purpose. The provision is similar to the law enacted by the 1992 Legislature to enable FIGA to pay the hurricane-related claims of insurers who became insolvent following Hurricane Andrew, except that the bill would provide continuing authority in this regard for any hurricane-caused insolvencies.

The bill also increases the maximum amount of FIGA's liability for a covered homeowners insurance claim against an insolvent insurer from $300,000 to $500,000.

Section 25 amends s. 631.695, F.S. to authorize any city or county substantially affected by a hurricane, to issue bonds to fund an assistance program in conjunction with FIGA, to pay covered claims arising from the insolvency of an insurer determined by FIGA to have been a result of a hurricane. Such bonds would be secured by the current assessments that can be levied by FIGA, and may be for a term not to exceed 30 years. The bond proceeds may be used by FIGA to settle unpaid claims or to refund unearned premiums to citizens of the state affected by the hurricane, even if the claimant's residence is not in the city or county that issues the bonds.

The bill makes legislative findings that it is necessary for the protection of the public health, safety, and general welfare of the residents of this state, and declared to be an essential public purpose, to permit municipalities and counties to take such actions as will provide relief to claimants and policyholders having claims against insolvent insurers. Related findings are made regarding the personal hardship to persons and families who suffer losses during a hurricane and the need for claims to be settled expeditiously. The findings also recognize the success of the FIGA bonds issued in 1993 and their potential for future use. The legislative findings likely will be used as part of the supporting documents that accompany any future bond issue for hurricane recovery.

The bill authorizes several uses for bonds issued for hurricane recovery. Among the authorized uses is the payment of covered claims of an insolvent insurer; to refinance or replace previous

borrowings; to fund reserves for the bonds; to pay expenses incident to bond issuance; and other similar enumerated purposes. The bill provides that the state covenants (promises) not to take any action that could endanger the availability of funds to repay the bonds.

The bill requires FIGA to file a report annually with the Senate President, the Speaker of the House, and the Chief Financial Officer on the status of the bond proceeds.

Section 26 provides that no provision of s. 631.57, F.S. (as amended by the bill) or s. 631.695, F.S. (as created by the bill) shall be repealed until such time as the principal and interest on all bonds issued pursuant to such sections have been paid in full or adequate provision for payment has been made.

Section 27 makes an unspecified appropriation from the General Revenue Fund to the Department of Community Affairs for the purposes of the Home Retrofit Hardening Program.

Section 28 makes an unspecified appropriation from the General Revenue Fund to the Department of Community Affairs for the purposes of wind certification and hurricane mitigation inspections specified in this act.

Section 29 provides that except as otherwise expressly provided, this act takes effect upon becoming law. (Many of the sections of the bill have later effective dates.)

IV. Constitutional Issues:

A. Municipality/County Mandates Restrictions:

None.

B. Public Records/Open Meetings Issues:

None.

C. Trust Funds Restrictions:

None.

D. Other Constitutional Issues:

The bill requires Citizens to impose a 25 percent deficit surcharge on nonhomestead property (as defined) owned by a non-resident of Florida. This raises a constitutional issue regarding the "right to travel." The right is derived from Art. IV, Sect. 2 of the constitution which states that "[t]he Citizens of each State shall be entitled to all the Privileges and Immunities of Citizens in the several States." The United States Supreme Court has found a fundamental right to interstate travel within the Constitution.[29] The right has three components: (1) the right of a citizen of one state to enter and leave another state; (2) the right to be treated as a welcome visitor rather than an unfriendly

[29] *Saenz v. Roe*, 526 U.S. 489 (1999).

alien while temporarily in the state; and (3) for persons who elect to become permanent residents, the right to be treated like other citizens of that state.[30] The right to be treated as a welcome visitor while temporarily in a state, is the most likely of the three provisions to be implicated by the provisions regarding Citizens surcharges.

V. Economic Impact and Fiscal Note:

A. Tax/Fee Issues:

None.

B. Private Sector Impact:

Owners of homes valued at $1 million or more (not including the value of the land) would no longer be eligible for windstorm coverage in Citizens HRA account. Such homeowners may be more likely to find coverage from an authorized insurer due to the bill's provisions that allow authorized insurers to increase rates for such homes, without being subject to a finding by OIR that the rate is excessive. However, such policies would still be subject to other requirements of Florida law and form approval by OIR. Alternatively, such homeowners may find coverage in the surplus lines market. A representative of the surplus lines market has recently stated that a market for these homes exists, but that market conditions can change rapidly.

Owners of nonhomestead homes (as defined) insured by Citizens would be subject to a 25 percent surcharge and non-Florida residents owning such homes would be subject to an additional 25 percent surcharge if there is a deficit.

Non-Citizens policyholders will have a lower exposure to deficit assessments for deficits due to the increased rates for nonhomestead property and the requirement that the calculation of the regular assessment deduct the amount to be collected from Citizens' policyholders. The impact of providing that homes valued over $1 million are not eligible for coverage is unknown, since it is unknown where hurricanes will land and whether Citizens will have a profit or loss for such homes in the future. But, eliminating these homes reduces the 100-year probable maximum loss of Citizens by an estimated $800 million, according to Citizens.

Greater depopulation of Citizens (and lower potential for assessments) may also result from the 10-day waiting period for Citizens coverage and the exception from the Consumer Choice law during this period, meaning that a keep-out offer would make the applicant ineligible for coverage whether or not the current agent is appointed by the keep-out insurer.

Financial institutions and mortgage holders that are currently entitled to have checks issued jointly in their name and the name of the primary policyholder will no longer be entitled to this for claims payments up to the lesser of $20,000 or 20 percent of the

[30] *Saenz*, at 500.

estimated damage. This will compromise the ability of such institutions to protect their collateral for the mortgage and, potentially, the marketability of mortgages on the secondary market.

The bill requires that the premiums paid by insurers for coverage from the Florida Hurricane Catastrophe Fund be increased by 25 percent in order to provide for more rapid cash buildup in the fund. This is expected to increase property insurance premiums by about 3 percent.

The bill may facilitate the insurer's attempt to have rate filings approved by requiring OIR to approve a rating factor that provides an insurer a reasonable rate of return commensurate with the risk of exposing its capital and surplus to the risk of hurricane losses, and by allowing an insurer to recoup its costs of reinsurance in its rates, unless OIR establishes that the costs are in excess of amounts consistent with prudent business practices and sound actuarial principles.

Sinkhole claims payments may be reduced with a favorable impact on premiums due to the requirement that for the arbitration process and the prohibition on awards of attorney fees under certain circumstances.

The bill authorizes FIGA to impose annual emergency assessments on insurers of up to 2 percent of written premium for specified lines of property and casualty insurance to fund revenue bonds issued by a municipality or county to pay claims of an insurer rendered insolvent due to a hurricane.

The bill increases the maximum amount of FIGA's liability for a covered homeowners insurance claim against an insolvent insurer from $300,000 to $500,000. This favorably impacts an affected homeowner, but would add to the liability of FIGA.

C. Government Sector Impact:

The bill requires that the Florida Hurricane Catastrophe Fund add a charge of 25 percent of the actuarially indicated premium to provide a more rapid cash buildup factor. It is currently estimated that the Fund premiums for 2006 will be $800 million, without any changes to the current law. The 25 percent rapid cash build up factor would add $200 million to the premium, totaling $1 billion. Representatives of the State Board of Administration have stated that the current bonding documents prohibit the Fund from utilizing premium income from the actuarially indicated premium for 2006 to pay for claims incurred in 2005. However, the portion attributable to the rapid cash buildup factor can be used to pay claims associated with the 2005 hurricane season; and, therefore, reduce the cash shortfall for the 2005 season.

VI. Technical Deficiencies:

None.

VII. Related Issues:

None.

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