

## HOUSE OF REPRESENTATIVES STAFF ANALYSIS

**BILL #:** HB 1267                      Citizens Property Insurance Corporation  
**SPONSOR(S):** Robaina and others  
**TIED BILLS:**                              **IDEN./SIM. BILLS:** SB 2498

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REFERENCE	ACTION	ANALYST	STAFF DIRECTOR
1) <u>Committee on Insurance</u>	<u>(ref. removed)</u>	<u></u>	<u></u>
2) <u>Jobs &amp; Entrepreneurship Council</u>	<u></u>	<u>Callaway</u>	<u>Thorn</u>
3) <u>Policy &amp; Budget Council</u>	<u></u>	<u></u>	<u></u>
4) <u></u>	<u></u>	<u></u>	<u></u>
5) <u></u>	<u></u>	<u></u>	<u></u>

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### SUMMARY ANALYSIS

This bill makes changes to the Citizens Property Insurance Corporation ("Citizens") law, prohibits the formation of Florida domestic residential property insurance subsidiaries ("pup companies"), provides for the expiration of such insurance subsidiaries and requires rate filings for insurance subsidiaries to include parent company profit information. Specifically, the bill:

- Revises Citizens' legislative intent language emphasizing the need for affordable property insurance to be provided by Citizens;
- Authorizes Citizens to offer multi-peril and wind-only coverages, or both types of coverages, for risks located in areas eligible for coverage in its high-risk account (HRA) beginning July 1, 2007;
- Provides that applicants for coverage from Citizens are *not ineligible* for coverage based on the availability of coverage from an authorized insurer or surplus lines insurer;
- Provides that when Citizens applies its underwriting criteria for determining eligibility as to applicants for coverage, it must consider whether such applicants have taken actions to mitigate the risk of windstorm loss;
- Provides that effective January 1, 2008:
  - A new certificate of authority (COA) may not be issued to a Florida domestic residential property insurer that is a wholly owned subsidiary of an insurer authorized to conduct business in another state (pup company);
  - An existing COA of a Florida domestic residential property insurer that is a wholly owned subsidiary of an insurer authorized to conduct business in another state (pup company) shall expire at the end of its period of validation and may not be renewed or reissued by the Office of Insurance Regulation or the Financial Services Commission; and,
  - The rate filings of any Florida domestic insurer that is a wholly owned subsidiary of an insurer authorized to do business in another state (pup company) shall include information relating to the profits of the parent company of the Florida domestic insurer.

This bill may be susceptible to an adequate title challenge under Article III, Section 6 of the Florida Constitution.

This bill has no fiscal impact on state or local governments and is effective upon becoming a law unless otherwise expressly provided in the bill.

## FULL ANALYSIS

### I. SUBSTANTIVE ANALYSIS

#### A. HOUSE PRINCIPLES ANALYSIS:

**Provide Limited Government, Safeguard Individual Liberty:** The bill provides new regulations for insurance companies including the prohibition on new pup companies, the elimination of existing pup companies, and the consideration of parent insurer profits in a pup company's rate filing. The bill removes the restrictions in current law relating to eligibility for property insurance in Citizens Property Insurance Corporation (Citizens) and allows Citizens to offer more types of property insurance coverage (i.e. multi-peril coverage in the High Risk Account).

#### B. EFFECT OF PROPOSED CHANGES:

##### **Citizens Property Insurance Corporation ("Citizens")**

In 2002, the Florida Legislature created Citizens by combining the state's two insurers of last resort, the Florida Residential Property and Casualty Joint Underwriting Association (RPCJUA) and the Florida Windstorm Underwriting Association (FWUA).<sup>1</sup> The merger allowed Citizens to become exempt from federal income taxes, resulting in millions of dollars in annual savings, as well as additional administrative and economic efficiencies.

Since that time, Citizens has become the largest property insurer in the State. As of February 28, 2007, Citizens provided coverage to over 1.3 million policyholders with \$432 billion in exposure and a market share of approximately 22 percent based on the number of policies in force.

Citizens' offers three types of property and casualty insurance in three separate accounts:

- Personal Lines Account (PLA) which offers multi-peril policies covering homeowners, mobile homeowners, dwelling fire, tenants, condominium unit owners and similar policies;
- Commercial Lines Account (CLA) which offers multi-peril policies covering commercial residential (condominium associations, apartment buildings, homeowners associations) and commercial nonresidential (business); and
- High-Risk Account (HRA) which covers multi-peril policies or wind-only policies, or both, for personal residential and commercial (residential and non-residential) policyholders.<sup>2</sup>

The number of policyholders in the three accounts are: PLA = 805,327; CLA = 10,255, and HRA = 407,681.<sup>3</sup>

##### **Multi-peril Coverage in High-Risk-Account of Citizens**

During the January 2007 Special Session, legislation was enacted (Committee Substitute for House Bill 1A (HB 1A))<sup>4</sup> authorizing Citizens to offer multi-peril coverage and wind-only coverage, or both, for risks located in areas eligible for coverage in the HRA.<sup>5</sup> Specifically, the law mandated Citizens to submit for approval by the Financial Services Commission (FSC) and the Legislative Budget Commission (LBC), a business plan for issuing such policies, including the impact on Citizen's financial resources, its tax-exempt status, its customer service and claims procedures, its agents, its policyholders, and its rates and premiums. The expressed goal was to reduce average premiums by 10 percent or more for a Citizens' wind-only policyholder who obtains a multi-peril policy from Citizens.

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<sup>1</sup> Chapter 2002-240, L.O.F.

<sup>2</sup> Legislation enacted during the 2007 Special Session (ch. 2007-1, L.O.F.) authorized Citizens to offer multi-peril coverage in its HRA.

<sup>3</sup> <http://www.citizensfla.com/> (last viewed April 10, 2007).

<sup>4</sup> Chapter 2007-1, L.O.F.

<sup>5</sup> Prior to the passage of HB 1A, Citizens could issue just wind-only coverage in the HRA.

Officials with Citizens state that both the FSC and the LBC approved its business plan in March and that Citizens will begin offering multi-peril coverage and wind-only coverage, or both, for risks in the HRA in June or July of this year. These officials assert that since approximately 118,000 of its 400,000 HRA policyholders now have two policies with Citizens, operational efficiencies and improved claims processing is expected through the issuance of one policy instead of two. Also, consumers in the HRA would be provided with more choices including potential rate savings in excess of 10 percent and simplified dealings with their insurance policies, according to these officials.

### **Expanded Eligibility for Residential Coverage from Citizens**

House Bill 1A expanded eligibility for coverage in Citizens by placing Citizens in more direct competition with the voluntary market by substantially revising the law that made a property ineligible for coverage from Citizens if an offer of coverage was made by an authorized insurer at the authorized insurers' approved rates. Under HB 1A, if a *new applicant* to Citizens is offered coverage from an insurer at its approved rate, the applicant is *not eligible* for a Citizens' policy, unless the insurer's premium is more than 25 percent greater than the premium for comparable coverage from Citizens. However, a *policyholder* of Citizens remains eligible for coverage regardless of any offer of coverage from a private market insurer. This allows a policyholder to choose to stay in Citizens and to reject any "take-out" offers from the voluntary market. But, the voluntary market may continue to "keep out" policies from Citizens, provided the premium is no more than 25 percent greater than Citizens' premium. As a result of this change and the rating law provisions related to Citizens contained in HB 1-A, Citizens is now in a more competitive role with the private market, with increasing numbers of policyholders potentially eligible for coverage with Citizens. These changes make it likely to increase its policy growth at an even greater pace, at least for the near future.

### **Effect of Proposed Changes**

The bill amends s. 627.351, F.S., relating to the Citizens Property Insurance Corporation ("Citizens") law. The bill modifies the original Legislative "intent" language in the law which authorized the creation of Citizens in 2002.<sup>6</sup> The bill makes Legislative findings which emphasize the lack of affordable property insurance in the state; that private insurers are unwilling or unable to provide such affordable coverage which threatens the public health, safety and welfare and the economic health of Florida; that there is a compelling public interest that property be insured at affordable rates to facilitate rehabilitation of damaged or destroyed property; that Citizens provide such affordable property insurance because it is not devoted to private profit making pursuits and is organized to achieve efficiencies and economies, while servicing policyholders, which equals or exceeds the quality provided in the voluntary market; that Citizens serve to increase the availability of affordable property insurance and offer the lowest rates possible consistent with sound business practices. The bill retains the current intent language which provides that it is essential for Citizens to have financial resources to pay claims and that it is the Legislature's intent that Citizens' income be exempt from federal income taxation.

The bill provides that beginning July 1, 2007, Citizens may offer multi-peril and wind-only coverage, or both coverages, for risks located in areas eligible for coverage in its high-risk account (HRA) and that Citizens may use approved policy forms and rates for its personal lines account (PLA) through December 1, 2007. The proposal provides Legislative intent language which specifies that the offer of multi-peril coverage in the HRA be implemented in a manner that does not adversely affect the creditworthiness of its current outstanding financing obligations in its three accounts.

The above provision duplicates language enacted in HB 1A authorizing Citizens to offer multi-peril policies. That bill mandated Citizens to submit for approval by the Financial Services Commission (FSC) and the Legislative Budget Commission (LBC) a business plan for issuing multi-peril policies in its HRA. As noted above, both the FSC and the LBC subsequently approved the business plan in March and Citizens will begin offering such policies in June or July of this year.

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<sup>6</sup> Chapter 2002-240, L.O.F.

The bill changes current law by providing that a new applicant to Citizens is *not ineligible* for Citizens' coverage based on the availability of coverage from an authorized insurer or a surplus lines insurer.<sup>7</sup> Further, applicants or policyholders may choose to be insured by Citizens even if the applicant or policyholder has another offer of coverage if the risk meets Citizens underwriting guidelines. The bill provides conforming changes to comply with this provision.

The above provision has the effect of allowing Citizens to be a competitor with insurers in the voluntary market because it allows *new applicants* to choose Citizens coverage regardless of the offer of coverage from an authorized insurer. Under current law enacted in HB 1A, if a new applicant to Citizens is offered coverage from an insurer at its approved rate, the applicant is not eligible for a Citizens' policy, unless the insurer's premium is more than 25 percent greater than the premium for comparable coverage from Citizens. As to *current policyholders* of Citizens, the law is not changed under this bill. Such policyholders can remain eligible for Citizens coverage regardless of any offer of coverage from a private market insurer.

The provision allowing applicants to select Citizens' coverage regardless of an offer of coverage from an authorized insurer raises the issue of its federal tax exempt status.<sup>8</sup> This provision places Citizens more into the role of a private insurer competing for insurance business in the voluntary market and less of a government controlled insurer of last resort that serves to augment the private insurance market.

The bill provides that Citizens provide objective criteria and procedures to be uniformly applied for all applicants in determining whether an individual risk is "eligible for coverage" and removes language that a risk is "so hazardous as to be uninsurable." The bill also provides that when Citizens applies its underwriting criteria for determining eligibility for a Citizens policy as to new applicants for coverage, it must consider whether the applicant has taken actions reasonably necessary to reduce the risk of loss. Under current law, all residential property insurers (including Citizens) are mandated to provide windstorm mitigation premium discounts to homeowners who utilize fixtures or construction techniques to reduce the risk of windstorm loss.<sup>9</sup>

The bill makes conforming changes by removing a requirement that Citizens policies must provide that if Citizens or the Market Assistance Plan (MAP) obtains an offer from an authorized insurer to cover the risk at its approved rates, the risk is no longer eligible for renewal with Citizens. The bill also removes a notice provision that Citizens policies could be replaced with policies issued by authorized insurers that are not identical as to coverage provisions.

### **Certificate of Authority/"Pup" Companies**

Insurance companies transacting insurance in Florida or from offices located in Florida are, with limited exceptions, required to have a certificate of authority (COA) issued by the Office of Insurance Regulation (OIR).<sup>10</sup> To qualify for a COA, a prospective insurer<sup>11</sup> must meet specified financial criteria including maintaining reserves<sup>12</sup> applicable to the kind of insurance transacted by the insurer, as well as

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<sup>7</sup> This provision applies to personal lines residential coverage in the PLA and HRA and commercial lines residential coverage in the CLA.

<sup>8</sup> On February 20, 2002, the Internal Revenue Service (IRS) in a private letter ruling to the Department of Insurance and after reviewing the provisions of the act creating Citizens determined that Citizens would be exempt from federal taxes. This allowed Citizens to collect revenues tax-free and issue tax-free bonds. (IRS Index Number: PLR-163640-01.)

<sup>9</sup> Rule 69O-170.017, F.A.C.

<sup>10</sup> Section 624.401, F.S.

<sup>11</sup> Insurers are divided into three categories under the Insurance Code: *domestic insurers* are formed under the laws of Florida; *foreign insurers* are formed under the laws of any state, district, or territory or commonwealth of the United States, other than Florida; and *alien insurers* are defined as insurers other than domestic or foreign insurers. Foreign and alien insurers must also meet certain capital, surplus, and operational requirements.

<sup>12</sup> Part I of ch. 625, F.S.

maintaining specified assets, deposits, capital, and surplus. Insurers must provide the OIR with specified background information and meet trustworthiness, fitness, and criminal history requirements.

A COA may continue in force as long as the insurer meets the statutory requirements<sup>13</sup> of paying its annual license tax,<sup>14</sup> filing its annual statement,<sup>15</sup> and paying applicable taxes under the Insurance Code. The law does allow OIR to suspend or revoke an insurer's COA based on numerous criteria including being in unsound financial condition, committing practices which render its insurance transactions hazardous or injurious to its policyholders and violating lawful orders or rules of the OIR or FSC.

Current law does not forbid the formation of Florida domestic subsidiaries of national insurance companies ("pup companies"). According to the OIR, there may be as many as 27 Florida property and casualty domestic insurers that are wholly owned subsidiaries of insurers authorized to do business in another state. One such example is State Farm Florida Insurance Company<sup>16</sup> which was formed as a wholly owned property insurance subsidiary (offering personal and commercial property insurance coverage) of State Farm Mutual Automobile Insurance Company which is domiciled in Illinois. State Farm Florida received its Florida COA in 1998 from the Department of Insurance.<sup>17</sup> The insurer currently has over one million policies and has a 20.6 percent market share in Florida. State Farm Mutual has always sold property insurance via wholly owned subsidiaries for the past fifty years, according to a State Farm representative.

Although HB 1A did not address the formation of new "pup companies" in Florida, it increased the minimum surplus requirements for residential property insurance "pup companies" from \$5 million to \$50 million.<sup>18</sup>

Also, current law does not require and the OIR does not review the profits of national parent companies of wholly owned Florida subsidiaries when considering a rate filing.

### **Effect of Proposed Changes**

The bill provides that effective January 1, 2008, and notwithstanding any other provision of law:

1. A new certificate of authority (COA) for the transaction of residential property insurance may not be issued to any insurer domiciled in Florida that is a wholly owned subsidiary of an insurer authorized to do business in any other state;
2. An existing COA for the transaction of residential property insurance held by any insurer domiciled in this state that is a wholly owned subsidiary of an insurer authorized to do business in any other state shall expire at the end of its period of validation and may not be renewed or reissued by the Office of Insurance Regulation or the Financial Services Commission;
3. The rate filings of any insurer domiciled in this state that is a wholly owned subsidiary of an insurer authorized to do business in any other state must include information relating to the profits of the partner company of the insurer domiciled in this state.

Current law does not address the formation or the termination of Florida domestic subsidiaries of national insurance companies ("pup companies"). There is no provision in law as to COAs expiring at the end of a validation period. As noted above, a COA may continue in force as long as the insurer meets the statutory requirements of paying its annual license tax, filing its annual statement, and paying applicable taxes under the Insurance Code.

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<sup>13</sup> Section 624.416, F.S.

<sup>14</sup> Section 624.501(3), F.S.

<sup>15</sup> Section 624.424, F.S.

<sup>16</sup> DOI Case Nos. 26914-98-CO and 26390-98-C.

<sup>17</sup> In 2002, the programs, employees and trust funds of the Department of Insurance were transferred to the Department of Financial Services and the Financial Services Commission (Office of Insurance Regulation). (ch.2002-404, F.S.)

<sup>18</sup> Section 624.407, F.S.

If provision #2 above were to take effect and be interpreted to authorize the OIR to revoke Florida subsidiary COAs, as many as 27 residential property insurers would be affected. One large domestic subsidiary, State Farm Florida, has more than 1 million policyholders whose homeowners insurance coverage could be in placed in jeopardy should State Farms' certificate be revoked. The bill as drafted does not allow for a notice to policyholders informing them to obtain other coverage or allow for policies to be nonrenewed over a phased in period of time. A parent company, in order to protect the assets of its subsidiary, could choose to obtain a Florida COA (if it does not currently hold one) and insure its subsidiary's policyholders. The overall effect of provisions #1 and #2 could limit the availability of residential property insurance in Florida.

Provision # 3 could be interpreted to allow the OIR to consider the profitability of an insurer's parent company during rate reviews. However, according to the OIR, such considerations are outside the bounds of the historical rate review process in virtually every state. The profit of the parent is not relevant to the losses and expenses that support the rate filing of an insurer doing business in Florida. Normally, an insurance regulator reviews premiums, claims costs, loss adjustment expenses and other related expenses it is review of an insurer.

C. SECTION DIRECTORY:

**Section 1:** Amends s. 627.351(6), relating to Citizens Property Insurance Corporation.

**Section 2:** Creates an unnumbered section, relating to "pup companies" and inclusion of parent company profits in rate filings for "pup companies."

**Section 3:** Provides an effective date of "upon becoming a law" unless otherwise expressly provided in the bill.

## II. FISCAL ANALYSIS & ECONOMIC IMPACT STATEMENT

A. FISCAL IMPACT ON STATE GOVERNMENT:

1. Revenues:

None.

2. Expenditures:

None.

B. FISCAL IMPACT ON LOCAL GOVERNMENTS:

1. Revenues:

None.

2. Expenditures:

None.

C. DIRECT ECONOMIC IMPACT ON PRIVATE SECTOR:

Citizens' applicants should economically benefit by being able to obtain Citizens coverage regardless of whether they receive an offer of coverage from an authorized insurer. Current Florida domestic subsidiaries could be in jeopardy of losing their certificates of authority to offer residential property insurance in Florida should this bill be interpreted as authorizing OIR to revoke their COAs. As a result, a subsidiary's policyholders would be placed in jeopardy of losing their homeowners insurance.

D. FISCAL COMMENTS:

None.

**III. COMMENTS**

A. CONSTITUTIONAL ISSUES:

1. Applicability of Municipality/County Mandates Provision:

The mandates provision does not apply because this bill does not: require counties or municipalities to spend funds or to take an action requiring the expenditure of funds; reduce the authority that municipalities or counties have to raise revenues in the aggregate; or reduce the percentage of a state tax shared with counties or municipalities.

2. Other:

This bill may be susceptible to an adequate title challenge under Article III, Section 6 of the Florida Constitution which provides that “[e]very law shall embrace but one subject and matter properly connected therewith, and the subject will be briefly explained in the title.”

The title for this bill indicates that the bill relates to “Citizens Property Insurance Corporation.” Section 1 of the bill amends provisions relating to Citizens Property Insurance Corporation. This section of the bill is directly related to the subject described in the bill title’s “relating to” clause. The second section of the bill, however, addresses the formation and continuing existence of insurance pup companies and the inclusion of parent insurer profits in pup company rate filings.

B. RULE-MAKING AUTHORITY:

None provided in the bill.

C. DRAFTING ISSUES OR OTHER COMMENTS:

To avoid adequate title susceptibility, the title of the bill should be changed. The title “[a]n act relating to the Citizens Property Insurance Corporation” may be problematic as the bill also applies to the issuance of certificates of authority to specified residential property insurers. Committee on Insurance staff suggests the title is changed to “[a]n act relating to property insurance.”

D. STATEMENT OF THE SPONSOR

**IV. AMENDMENTS/COUNCIL SUBSTITUTE CHANGES**

None.