FINAL BILL ANALYSIS

BILL #: CS/CS/CS/SB 408

FINAL HOUSE FLOOR ACTION:
85 Y's 33 N's

SPONSOR: Sen. Richter (Rep. Wood)

GOVERNOR'S ACTION: Approved

COMPANION BILLS: CS/CS/HB 803

SUMMARY ANALYSIS

CS/CS/CS/SB 408 passed the House on May 4, 2011. The bill was approved by the Governor on May 17, 2011, chapter 2011-39, Laws of Florida, and took effect on May 17, 2011. This bill makes numerous changes to the laws related to property and casualty insurance, primarily residential property insurance. The bill addresses the following major issues:

- Types of losses, amounts, and expenses reimbursable by the Florida Hurricane Catastrophe Fund.
- Increased surplus requirements for property insurance companies to obtain and maintain a certificate of authority to transact insurance.
- Public adjuster fees, advertisement, solicitation, and other conduct.
- Time period for filing a notice of a property insurance claim.
- Statute of limitations for filing suit on a property insurance policy.
- Rate increases and timing of an expedited rate filing.
- Prohibition on use of a "use and file" rate filing for property insurance.
- Payment of acquisition costs by insurance companies.
- Certification of additional or supplemental information provided to a property insurance rate filing at the request of the Office of Insurance Regulation (OIR).
- Reduced policyholder notice of nonrenewal for nonrenewals due to an insurance company's problematic financial condition, if a policyholder has been insured with the insurer for five years, or if the policyholder has a combination property and automobile policy.
- Insurer verification of mitigation discount forms submitted by policyholders or insurance agents.
- Change of policy terms of property and casualty insurance by insurers at policy renewal under specified conditions.
- Procedure and payment timing related to payment of replacement costs to policyholders for partial dwelling losses and personal property losses.
- Renegotiation of surplus notes issued to insurers under the Insurance Capital Build-Up Incentive Program.
- Fees charged for use of the public hurricane model.
- Citizens Property Insurance Corporation (Citizens), specifically addressing rates and coverage for sinkhole losses; a study on outsourcing claims functions; the timing, payment, and notification of assessments; and voting of board members.
- Numerous revisions to the laws governing sinkholes claims, including adding definitions, changing the adjusting of claims and the payment of testing and reporting, changing repair requirements, and modifying the neutral evaluation process.
- Repeal of the sinkhole database.
- Payment of sinkhole claims by the Florida Insurance Guaranty Association.

The bill has no fiscal impact on local government. The Criminal Justice Impact Conference has not met to determine the prison bed impact of this bill. However, because the bill creates a new third degree felony relating to insurance fraud for rebating in sinkhole claims, there may be a prison bed impact on the Department of Corrections. Some of the provisions in the bill have fiscal impacts on consumers and the insurance industry. Some of the provisions restrict insurance coverage and some may impact rates and premiums. (See Fiscal Analysis Section of the staff analysis.)

This document does not reflect the intent or official position of the bill sponsor or House of Representatives.

I. SUBSTANTIVE INFORMATION

A. EFFECT OF CHANGES:

This bill makes numerous changes for property and casualty insurance, primarily property insurance.

Florida Hurricane Catastrophe Fund

The Florida Hurricane Catastrophe Fund (FHCF) is a tax-exempt trust fund created after Hurricane Andrew as a form of reinsurance for residential property insurers.[1] The purpose of the FHCF is to protect and advance the state's interest in maintaining insurance capacity in Florida by providing reimbursements to insurers for a portion of their catastrophic hurricane losses.

Each insurance company writing insurance policies covering residential property or any policy covering a residential structure or its contents must participate in the FHCF. (s. 215.555(4)(a), F.S. and s. 215.555(2)(c), F.S.). Residential property is defined in s. 627.4025(1), F.S. to include personal lines and commercial lines residential coverage. This coverage entails the following insurance policies: homeowner's, mobile homeowner's, dwelling, tenant's, condominium unit owner's, condominium association, cooperative association, and apartment building.

The FHCF is administered by the State Board of Administration and is a tax-exempt source of reimbursement to property insurers for a selected percentage (45, 75, or 90 percent) of hurricane losses to residential property above the insurer's retention (deductible).[2] A reimbursement contract between the FHCF and the property insurer governs an insurer's participation in the FHCF and the percentage of the insurer's reimbursement. Reimbursement contracts run from June 1st – May 30th.

Current law only specifies losses for fair rental value, rental income, or business interruption losses are not reimbursable by the FHCF. The bill adds the following additional losses, amounts, and expenses that are not reimbursable by the FHCF:

- Liability coverage losses.
- Property losses that are not proximately caused by a hurricane.
- Amounts paid because the insurer voluntarily expanded coverage, such as the waiver of a deductible.
- Reimbursement to the policyholder for an assessment levied by a condominium association or homeowners' association.
- Bad faith awards, punitive damage awards, and court-imposed fines, sanctions, or penalties.
- Amounts paid in excess of the insurance policy coverage limit.
- Allocated and unallocated loss adjustment expenses.

[1] s. 215.555, F.S.

[2] Retention is defined to mean the amount of losses below which an insurer is not entitled to reimbursement from the fund. A retention is calculated for each insurer based on its proportionate share of fund premiums.

The FHCF has not historically reimbursed insurers for these losses, amounts, and expenses. The bill specifies the exceptions to the FHCF definition of "losses" first apply to the reimbursement contracts between the FHCF and the insurer that takes effect on June 1, 2011.

The bill also defines "losses" as all incurred losses and specifies amounts paid as fees on behalf of or inuring to the benefit of a policyholder are included in the definition of "losses" and thus reimbursable by the FHCF.

Insurer Surplus Requirements

Florida law specifies certain minimum surplus and capital requirements for property and casualty insurers to transact insurance in the state. Surplus is the reserves an insurer has available to pay claims and is a critical component in measuring the financial strength of a company.[3] The current surplus and capital requirements for property and casualty insurers have not been changed since 1993.[4]

Surplus Needed To Obtain A Certificate of Authority

With limited exceptions, a certificate of authority from the Office of Insurance Regulation (OIR) is needed to act as an insurer and transact insurance.[5] Generally, a new property and casualty company that is not a pup company must have the greater of $5 million in surplus or ten percent of the insurer's liabilities to obtain a certificate of authority.[6]

Under the bill, an insurance company that is formed under Florida law, that is licensed after the bill takes effect to write residential property insurance, and that is not a pup company of an existing insurer must have $15 million in surplus to obtain a certificate of authority, rather than the greater of $5 million or ten percent of the insurer's liabilities.

Surplus Needed To Maintain A Certificate of Authority

Once a property and casualty insurer is licensed in Florida, the minimum surplus required to keep a certificate of authority is the greater of $4 million or ten percent of the insurer's liabilities.[7] In addition, generally, a property and casualty insurer's written premium to surplus ratio must not exceed 4 to 1 for net written premiums or 10 to 1 for gross written premiums.[8]

Under the bill, an insurance company formed under Florida law and licensed after July 1, 2011, to write residential property insurance must have the greater of ten percent of the insurer's liabilities or $15 million, rather than $4 million, in surplus to keep a certificate of authority.

However, residential property insurance companies licensed before July 1, 2011, must keep the greater of ten percent of the insurer's liabilities or:

- $5 million, rather than $4 million, in surplus until June 30, 2016;
- $10 million, rather than $4 million, in surplus until June 30, 2021; and
- $15 million, rather than $4 million, in surplus after June 30, 2021.

[3] An insurer's surplus is the remainder after a company's liabilities are subtracted from its assets.
[4] Ch. 1993-410, L.O.F.
[5] s. 624.401(1), F.S.
[6] ss. 624.407(1)(a) and (d), F.S. The $5 million surplus requirement is increased to $50 million for pup companies writing residential property insurance in Florida. Pup companies are wholly owned Florida subsidiaries of an insurer domiciled in another state.
[7] s. 624.408(1)(a), F.S.
[8] s. 624.4095(1), F.S. Net Premiums = Gross Premiums minus reinsurance premiums ceded

Thus, companies writing residential property insurance and licensed before July 1, 2011, must incrementally meet increased surplus requirements, whereas, companies licensed after July 1, 2011, must immediately meet increased surplus requirements.

The OIR can reduce the required surplus under three circumstances:

- the insurer is not writing new business;
- the insurer has residential property insurance premiums less than $1 million per year; or
- the insurer is a mutual insurance company[9].

The bill does not increase surplus requirements for property insurers writing nonresidential property insurance. These companies have to have $4 million or 10 percent of the insurer's liabilities in surplus in order to keep a certificate of authority.

Public Adjusters

Background

Chapter 626, F.S., regulates insurance field representatives and operations. Part VI of the chapter governs insurance adjusters. The law recognizes various types of adjusters, including public adjusters, independent adjusters, company employee adjusters, and catastrophe or emergency adjusters. Adjusters can be further classified as resident or nonresident. Resident adjusters are those who reside in Florida and are licensed in Florida, whereas, nonresident adjusters reside outside of Florida and are licensed by their home state.

The Department of Financial Services (DFS) regulates all types of adjusters. The DFS reports that as of January 31, 2011, Florida licenses almost 32,500 resident adjusters and almost 45,000 non-resident adjusters.[10] Of these, 2,086 are resident public adjusters and 380 are non-resident public adjusters.[11]

A public adjuster is hired and paid by the policyholder to act on his or her behalf in a claim the policyholder files against an insurance company. Public adjusters can represent a policyholder in any type of insurance claim, not just property insurance claims. Public adjusters, unlike company employee adjusters, operate independently and are not affiliated with any insurance company. Independent and company employee adjusters work for insurance companies.

Generally, public adjusters are paid a percentage of the claim payment. The fee percentage is usually negotiated between the public adjuster and the policyholder, except in residential property and condominium association property claims. For these claims, public adjuster fees are limited by law to a specified percentage which varies depending on whether the claim is hurricane or non-hurricane related and if the claim is hurricane-related, depending on how soon after the hurricane the claim is filed. In addition with supplemental claims for residential property or condominium associations, the public adjuster fee cannot be based on the amount paid to the policyholder on the previous claim. Independent and company employee adjusters do not charge policyholders a fee for adjusting the claim.

[9] A mutual insurance company is defined in s. 628.031, F.S.
[10] Information obtained from the DFS dated 2/25/11, on file with staff of the Insurance & Banking Subcommittee.
[11] According to DFS, there are 15,010 licensed resident independent adjusters (13,847 non-resident independent adjusters); 15,399 licensed resident company employee adjusters (30,675) non-resident company employee adjusters).

Public adjusters are licensed by the DFS if they meet the statutory qualifications for licensure found in s. 626.865, F.S. Qualifications include age, residency, testing, experience, and trustworthiness.[12] Public adjusters must also present a $50,000 bond to DFS in order to be licensed.[13] No bond is required of company employee or independent adjusters.

Administrative rules relating to public adjusters, in part, address public adjuster contract cancellation, public adjuster actions relating to business referrals, and public adjuster actions relating to the hiring of other professionals to help with the claim.[14] Administrative rules also govern the solicitation of business and advertising by public adjusters and the contract used by public adjusters.[15] Public adjusters must also abide by general ethical rules applicable to all types of adjusters.[16]

2008 Legislation Relating to Public Adjusters

In 2008, the Legislature enacted legislation imposing restrictions and regulations on public adjusters in residential property and condominium association property insurance cases.[17] The legislation restricted public adjuster fees to: 20 percent on non-hurricane claims, 10 percent on hurricane claims filed during the year after the hurricane, and 20 percent on hurricane claims filed later than a year after a hurricane. The 2008 legislation also prohibited a public adjuster from including the amount paid to a policyholder in a previous claim in the fee calculation on a supplemental claim.

The legislation in 2008 made numerous changes relating to public adjuster client solicitation and business practices. The legislation prohibited public adjusters from soliciting directly or indirectly between the hours of 8:00 pm and 8:00 am Monday through Saturday and all day on Sunday. Public adjusters were also prohibited from directly or indirectly contacting any policyholder until 48 hours after an event that triggered a claim, unless contacted by the policyholder. However, this provision was recently struck down by the First District Court of Appeal which ruled the restriction on soliciting customers within 48 hours of a disaster or other insurance claims event violated commercial speech protected by the state Constitution.[18] The First District Court of Appeal decision was appealed to the Florida Supreme Court and is currently pending.[19]

In 2008, public adjusters were prohibited from giving or offering to give a monetary loan or advance to a client or prospective client and were prohibited from giving or offering to give anything with a value in excess of $25 for advertising or as an inducement to enter into a

[12] Similar qualifications apply to independent and company adjusters.
[13] s. 626.865(2), F.S.
[14] Rule 69B-220.201(4) and (5), F.A.C.
[15] Rule 69B-220.051, F.A.C.
[16] s. 626.878, F.S.
[17] Ch. 2008-220, L.O.F. The 2008 legislation resulted from findings of the Task Force on Citizens Property Insurance Claims Handling and Resolution created in 2007 to make recommendations to the legislative and executive branches relating to the appropriate handling, service and resolution of the open 2004/2005 hurricane claims of Citizens Property Insurance Corporation (Citizens). During review of Citizens' hurricane claims, the Task Force became aware of the impact public adjusters have on the claims process. The Task Force found that while the services of public adjusters can be beneficial to policyholders who have suffered a loss, the laws in place in 2007 did not adequately protect consumers from unscrupulous public adjusters. The Task Force heard testimony that some public adjusters were not properly trained or qualified to represent insureds. Also, these adjusters charged exorbitant fees which oftentimes were not apparent to insureds because the fees were not prominently displayed in the public adjuster contract. Stakeholders also testified that there was a need for an apprentice type program for public adjusters so that individuals would be knowledgeable and experienced when they because public adjusters. In an effort to remedy concerns expressed about abuses by some public adjusters, the Task Force proposed legislation in 2008.
[18] *Kortum v. Sink,* 2010 WL 5381934 (Fla. 1st DCA 2010)**.** In the lawsuit challenging the constitutionality of the 48 hour restriction, the plaintiff, a public adjuster, argued the first 48 hours are of vital importance because policyholders may make decisions that affect how much they could receive from an insurer during this time.
[19] *Atwater v. Kortum,* Case number SC11-133

contract with the public adjuster. In addition, the 2008 legislation enacted time periods for cancellation of a public adjuster contract without penalty. The legislation also made public adjuster circulation or dissemination of untrue, deceptive, or misleading information relating to insurance an unfair and deceptive insurance trade practice.

Changes to public adjuster licensure, the creation of a public adjuster apprenticeship program and license, and amendments to continuing education requirements for public adjusters were also enacted in 2008.

2009 Legislation Relating to Public Adjusters

In 2009, the Legislature enacted further changes related to the activity of public adjusters.[20] The 2009 legislation prohibited public adjusters or public adjuster apprentices from paying fees for referrals of business to the public adjuster. The legislation also required public adjuster apprentices to obtain a certain claims adjuster designation before applying for an apprentice license. Furthermore, the number of active apprentices employed by a public adjusting firm was limited to 12 and the number of apprentices supervised by a public adjuster limited to three.

The 2009 legislation also required the Office of Program Policy Analysis and Government Accountability (OPPAGA) to do a study on public adjusters. This report was completed in January 2010 (Report 10-06) with the following primary findings:[21]

- The number of licensed public adjusters in Florida has grown significantly in the last six years, and the incidence of complaints, regulatory actions, and allegations of fraud involving public adjusters is generally low;
- Florida's public adjusters laws are comparable to and in some cases more restrictive than those of other similar states;
- According to Citizens' claims data, cases took longer to reach a settlement but received higher payments when policyholders used public adjusters for claims filed in 2008 and 2009; and
- Public adjusters represented policyholders in 26 percent of non-catastrophe and 39 percent of catastrophe claims filed in 2008 and 2009 against Citizens.

Effect of the Bill:

The bill makes significant changes to the regulation of public adjusters in residential property and condominium unit owner property insurance claims.

Advertising or Solicitation by Public Adjusters

Section 626.854(8), F.S., makes public adjuster circulation or dissemination of advertisements, statements, or announcements that contain untrue, deceptive, or misleading assertions, representations, or statements relating to insurance an unfair and deceptive trade practice. The bill sets forth specific statements that are deceptive or misleading if the statements are contained in advertising or solicitation of public adjusters. Thus, if a public adjuster uses these statements in advertising or solicitation, the adjuster commits an unfair and deceptive trade practice. The penalty for commission of an unfair and deceptive trade practice is found in s.

[20] Ch. 2009-87, L.O.F.

[21] http://www.oppaga.state.fl.us/Summary.aspx?reportNum=10-06 (last viewed March 4, 2011).

626.9521, F.S., and is a fine no more than $5,000 for each nonwillful violation and a fine no more than $40,000 for each willful violation.[22]

The bill provides the following statements by a public adjuster are an unfair and deceptive trade practice:

- Statement inviting a policyholder to file a property insurance claim when the policyholder may not have property damage covered by an insurance policy;
- Statement inviting a policyholder to file a property insurance claim by offering monetary or other valuable inducement to a policyholder;
- Statement inviting a policyholder to file a property insurance claim by stating there is "no risk" to a policyholder to file a property insurance claim; and
- Statement or use of a logo or shield that implies or could be construed to mean the adjuster's solicitation was issued or distributed by a governmental agency or is sanctioned or endorsed by a governmental agency.

The bill also requires any written advertisements[23] by public adjusters to contain a specific disclaimer in bold print and capital letters in a specific typeface. The disclaimer identifies the advertisement as a solicitation for business.

Public Adjuster Fees
Initial Claims: The bill clarifies current law relating to public adjuster fees on initial residential and condominium association property insurance claims. Starting June 1, 2011, public adjusters can be paid a maximum of ten percent of the insurance claim payment for claims resulting from a declaration of a state of emergency (i.e., claims from a hurricane) if the initial claim is made in the year after the declaration. Public adjusters can be paid a maximum of 20 percent of the claim payment for claims from a hurricane if the claim is made anytime in the year after the declaration. The bill applies these fee caps to condominium unit owner claims, rather than condominium association claims.

Current law allowing public adjusters to be paid a maximum of 20 percent of a claim payment for claims not resulting from hurricanes is not changed by the bill. However, the bill applies the current law relating to fee caps on non-hurricane related claims to condominium unit owner claims, rather than condominium association claims, starting June 1, 2011.

Reopened or Supplemental Claims: The only restriction in current law relating to public adjuster fees on reopened or supplemental claims against residential and condominium association property insurance policies is in s. 626.854(11)(a), F.S. This statute allows a public adjuster to be paid a fee only on the amount paid on the reopened or supplemental claim. Thus, the claim payment amount on the initial claim is not included in the public adjuster fee on a reopened or supplemental claim. There is no cap in current law, however, on the public adjuster fee that can be paid on reopened or supplemental claims. The fee amount is negotiated between the public adjuster and the policyholder. Starting June 1, 2011, the bill adds a fee cap to reopened or supplemental claims on residential and condominium unit owner policies, rather than condominium association policies, involving public adjusters. The public adjuster fee on these types of claims cannot exceed 20 percent of the claim payment obtained on the reopened or supplemental claim.

[22] The total amount of fines that can be assessed is $50,000 for all nonwillful violations arising out of the same action or $250,000 for all willful violations arising out of the same action (s. 626.9521(3)(c), F.S.).
[23] "Written advertisement" is defined in the bill as newspapers, magazines, flyers, brochures, and bulk mailers.

Policyholders of Citizens Property Insurance Corporation: The bill provides a different public adjuster fee cap for fees obtained due to claims against Citizens Property Insurance Corporation (Citizens). For all claims, the bill allows a public adjuster representing a Citizens' policyholder to be paid a maximum fee of 10 percent of the additional claim amount paid over the amount originally offered by Citizens.

Action Required of Public Adjusters and Insurance Companies
When a public adjuster becomes involved in certain types of property insurance claims, the bill requires the public adjuster to ensure:

- prompt notice of the claim is given to the insurance company;
- the public adjuster contract is timely given to the insurance company;
- the property insured is made available to the insurance company for inspection; and
- the insurance company is allowed to interview the policyholder about the claim.

The insurance company must also be allowed to obtain information required to investigate or respond to the claim and must meet or communicate with the public adjuster in order to reach an agreement on the claim.

The public adjuster cannot restrict the insurance company, or anyone acting on the company's behalf, from reasonable access to the policyholder or the damaged property. The insurance company, or anyone acting on the company's behalf, must give the policyholder or public adjuster 48 hours' notice before meeting with the policyholder or inspecting the damaged property. If the required notice is not given, the policyholder can deny access to the property. Both parties can waive the 48 hour notice requirement. The insurance company cannot exclude the public adjuster from its in-person meetings with the policyholder.

Public adjusters are forbidden from obstructing or preventing the insurance company or the company's adjuster from timely inspection of the damaged property. Public adjusters are allowed to be present when an insurance company inspects a damaged property. However, the insurance company is allowed access to the property for an inspection even if the public adjuster or policyholder is not able to be at the property for the inspection, if waiting for the adjuster or policyholder to attend the inspection delays a timely inspection.

Public adjusters are also required to make the written estimate of loss the public adjuster prepares on the claim available to the insurer.

Actions by Contractors and Subcontractors
Contractors licensed by the Department of Business and Professional Regulation or subcontractors are not allowed to adjust property insurance claims unless the contractor is also licensed as a public adjuster and is compliant with the public adjuster licensing requirements. Contractors, however, are allowed to prepare or submit a bid to repair damaged property and to discuss the bid with the policyholder or the insurance company if the contractor is preparing or submitting a bid at the request of the insurance company or the policyholder and the contractor is doing the bid submission for the contractor's usual and customary fee.

Public Adjuster Contracts

The bill codifies most of the content requirements of public adjuster contracts contained in administrative rules.[24] The bill requires public adjuster contracts relating to property and casualty claims to contain the name and address of the adjuster and the policyholder. The contract must also contain the license number of the public adjuster, the name of the public adjusting firm, a brief description of the loss, the public adjuster fee percentage, and the type of claim. The contract must also contain dated signatures of the public adjuster and all named policyholders.[25] The contract must be sent to the policyholder's insurance company within 30 days after the contract is executed by the public adjuster and the policyholder.

Statute of Limitations for Property Insurance Claims

A statute of limitations is a time period after which no legal case can be brought relating to an injury or wrong. Section 95.11, F.S., sets forth time limitations for commencing civil actions in Florida. The time limitations range from 30 days to 20 years, with five years applying to contract disputes.

Section 95.11, F.S., does not contain any specific statute of limitations for property insurance claims. Thus, the statute of limitations that applies to these claims is the five year statute of limitations applicable to contracts because an insurance policy is a contract. Under current law, the five year statute of limitations on property insurance claims begins to run when the property insurance contract is breached by the insurer (e.g., denial of a claim) because that is when the cause of action accrues.[26]

The bill provides the statute of limitations for property insurance claims is five years and begins to run on the date of loss, rather than when the property insurance contract is breached.

Filing Time Frame for Property Insurance Claims

Current law does not prescribe a time frame for a policyholder to give the insurer notice of a property insurance claim. The five year statute of limitations for filing suit on a property insurance policy (detailed previously) is the sole time period prescribed by law for disputes related to property insurance and that time period does not apply to a notice of claim.

Starting June 1, 2011, the bill requires notice of any claim, supplemental claim, or reopened claim on a property insurance policy to be filed with the insurance company within three years after the date of the landfall of the hurricane or windstorm causing damage. The bill specifies the three year claim filing time frame added by the bill does not affect the statute of limitations under s. 95.11, F.S.

Payment of Acquisition Costs by Insurance Companies

An insurer's acquisition costs are typically costs associated with acquiring, maintaining and renewing insurance business. These costs include agent commissions, company sales

[24] Rule 69B-220.051(6), F.A.C. Administrative rules promulgated by the DFS require public adjuster contracts to contain the adjuster's name, business address, phone number, and license number. The contract must also contain the policyholder's name, address, address of loss, description of the loss, insurer's name, insurer's policy number; the date the contract was signed by the policyholder, and the compensation amount to the adjuster. Rules also require the contract to be in writing and signed by the public adjuster.

[25] The bill allows the signature of all named policyholders to be avoided if an affidavit is submitted.

[26] *See* Passman v. State Farm Fire and Casualty, 779 So.2d 323 (Fla. 2nd DCA 1999), citing State Farm Mutual Automobile Ins. Co. v. Lee, 678 So.2d 818 (Fla. 1996). The Passman case involved a property insurance claim and the Lee case involved an automobile insurance claim.

expenses, and other related expenses. Agent commissions may vary based on numerous factors - the line of business, the agent's expertise, the functions the agent must perform, and competition among other insurers. Agents are prohibited from charging the policyholder any part of their commission. Agent commissions are typically based on a percentage of the total premium; however, insurers can apply the agent's percentage to only a portion of the premium (for example, the non-catastrophe portion).

Under current law the OIR cannot prohibit any insurer from paying acquisition costs based on the full amount of the premium or prohibit an insurer from including the full amount of acquisition costs in a rate filing, however, representatives of insurance agents allege the OIR has questioned the amount of acquisition costs, namely agent commissions, in recent rate hearings and has encouraged insurers to reduce these costs.[27] Therefore, the bill specifies the OIR cannot directly or indirectly prohibit an insurer from paying acquisition costs that are lawfully paid. The bill also prohibits the OIR from certain actions relating to an insurer's acquisition of policyholders, advertisement, agent commissions or agent appointment for property and casualty insurance.

Standard Rating Territories

The bill repeals language requiring the OIR to develop a proposed standard rating territory plan and submit the plan to the Legislature by January 15, 2006. Language in current law restricting implementation of the standard rating territory plan unless authorized by the Legislature is also repealed. The plan required by law was submitted to the Legislature in 2006 and the Legislature has not authorized implementation of standard rating territories since the plan submission.

Certification of Rate Filings

Current law requires all property insurance rate filings to include a certification from the insurance company's chief executive officer or chief financial officer and the chief actuary of the insurance company. The certification must be under oath, subject to the penalty of perjury, and on a form approved by the Financial Services Commission.[28] Contents of the certification are provided in s. 627.062(9)(a), F.S. Knowingly making a false certification subjects the officer and actuary to penalties under the Insurance Code. A property insurance rate filing must be disapproved if the filing does not contain a certification. The bill provides a rate filing certification is not rendered false if the insurance company, at the request of the OIR, provides the OIR with additional or supplementary information after the rate filing is submitted for approval. The bill further requires the insurer actuary submitting the additional information, rather than the chief actuary, the CEO, or the CFO, to provide the same certification for the additional information that is required under current law for all property insurance rate filings. The actuary certifying the additional information is subject to the same penalties under current law relating to the certification.

Nonrenewal Notice For Property Insurance

[27] s. 627.062(2)(i), F.S.
[28] The Financial Services Commission is comprised of the Governor and Cabinet (s. 20.121(3), F.S.)

Under current law,[29] personal lines or commercial lines residential property insurers must give policyholders a notice of cancellation, nonrenewal, or termination at least 100 days prior to the effective date of the cancellation, nonrenewal, or termination. Further, for any cancellation, nonrenewal, or termination that takes effect between June 1st and November 30th, an insurer must provide at least 100 days written notice, or notice by June 1st, whichever is earlier. The notice period is extended to 180 days if the property has been insured for at least a five year period immediately prior to the date of the notice.

The bill reduces the 180-day notice to 120 days. Thus, property insured with the same insurer for at least five years immediately prior to the notice will receive 120-days notice of cancellation, nonrenewal, or termination, rather than 180-days notice.

The bill reduces the notice period to 90 days if the policyholder in insured with a combination property and automobile policy.

The bill allows a 45-day notice of cancellation or nonrenewal, rather than the 100-day or 180-day notice required under current law, if the OIR determines early cancellation of some or all of an insurer's property insurance policies is necessary to protect the best interest of the public or the policyholders. The OIR must approve the insurer's plan for early cancellation or nonrenewal in order for the 45 day notice to apply. The OIR may base its finding on the insurer's financial condition, reinsurance inadequacy, or other relevant factor. The OIR's finding may be conditioned on the insurer's consent to be placed in administrative supervision or its consent to the appointment of a receiver.

The bill also requires Citizens to give a 45-day written notice of nonrenewal, cancellation, or termination, rather than the 100-day or 180-day notice provided in current law, for property insurance policies assumed by a private insurance company from Citizens (i.e., policies taken out of Citizens through depopulation).

Insurer Report Card

Section 627.0613(4), F.S., enacted in 2007,[30] requires the Insurance Consumer Advocate[31] to prepare a report card each year for each personal residential property insurance company. This report card must grade each company according to these factors:

- Number and nature of consumer complaints against a company;
- Disposition of complaints;
- Average length of time for claims payment by the company; and
- Any other factors to assist policyholders in making informed choices about homeowner's insurance.[32]

Current law does not specify a starting date for the report card issuance and to date no report cards have been issued. The bill repeals the law requiring report cards grading personal residential property insurers.

[29] s. 627.4133(2), F.S.
[30] Section 17, Ch. 2007-1, L.O.F.
[31] The Insurance Consumer Advocate is appointed by the Chief Financial Officer. The Advocate represents the public before the Office of Insurance Regulation (OIR) and the Department of Financial Services (DFS). In order to represent the public, the Advocate is given specific powers relating to actions taken by the OIR and the DFS. (see s. 627.0613(1)-(3), F.S.)
[32] As determined by the Financial Services Commission comprised of the Governor and Cabinet. (s. 20.121(3), F.S.)

Hurricane Mitigation Discounts and Premium Credits

Since 2003, insurers have been required to provide mitigation credits, discounts, other rate differentials, or reductions in deductibles (mitigation discounts) to reduce residential property insurance premiums for properties with mitigation features.[33] In 2003, the Office of Insurance Regulation (OIR) computed suggested mitigation discount amounts to apply to each mitigation feature installed on the property. Insurers must use the discount amounts computed by the OIR unless the insurer provides detailed alternate studies supporting modification of the discount amounts suggested by the OIR.[34]

Mitigation discounts were initially given at 50 percent of the actuarial value of the discount.[35] In 2006, the Legislature amended the mitigation discount law (s. 627.0629(1)(a), F.S.) to require the OIR to reevaluate the mitigation discounts and require insurers to give full actuarial value for them.[36] Thus, the OIR amended the mitigation discount administrative rule[37] to require insurers to provide mitigation discount amounts equal to 100 percent of the mitigation discount amount.[38] In 2008, the OIR obtained a new study to evaluate the appropriate mitigation discount amounts, however, the OIR has not changed the mitigation discount amounts due to the results of the 2008 study.

Section 627.711, F.S., requires insurers to clearly notify an applicant for or policyholder of a personal lines residential property insurance policy of the availability and range of each premium discount, credit, other rate differential, or reduction in deductibles, for wind mitigation. The notice must be provided when the policy is issued and renewed.

Typically, policyholders are responsible for substantiating to their insurers the insured property has mitigation features. Policyholders submit a completed uniform mitigation verification inspection form to the insurer to substantiate mitigation features. Insurers can require mitigation forms provided to the insurer by mitigation inspectors or a mitigation inspection company be independently verified for quality assurance purposes before accepting the mitigation form as valid. The insurer must pay for the independent verification.[39] The bill allows the insurer to also independently verify, for quality assurance purposes, mitigation forms submitted by policyholders or insurance agents. The bill maintains current law requiring the insurer to incur the costs associated with independent verification of mitigation forms.

Change of Policy Terms In Insurance Policies

Under the 5th District Court of Appeals' holding in the case of U.S. Fire Insurance Co. and Hartford Insurance Company of the Southeast v. Southern Security Life Insurance Co., 710

[33] s. 627.0629(1)(a), F.S. Mitigation features are construction techniques used or items purchased and installed by a property owner to protect a structure against windstorm damage and loss. (e.g., hurricane shutters, hip roof, specified roof covering).
[34] Rule 69O-170.017, F.A.C.
[35] In an Informational Memorandum issued on January 23, 2003, the OIR notified insurance companies of its suggested mitigation credits for new and existing construction based on its analysis of the 2002 study completed by Applied Research Associates. However, the OIR tempered the mitigation credits derived from the study by 50 percent. As stated by the OIR in the memorandum, the 50 percent tempering of the credits was due to the large rate decreases that could result from application of the credits, the approximations needed to produce practical results, and the potential for differences in results using different hurricane models. The OIR cautioned in the memorandum that the tempering implemented would be curtailed in the future.
[36] Section 14, Ch. 2006-12, L.O.F.
[37] Rule 69O-170.017, F.A.C.
[38] The rule allowed insurance companies to modify the mitigation discounts if the insurer provided detailed alternate studies supporting the modification and allowed the OIR to review all assumptions used in the studies supporting the modification.
[39] s. 627.711(8), F.S.

So.2d 130 (Fla. 5th DCA 1998), when an insurance company changes a term or terms of a policy, the change constitutes a nonrenewal of the entire policy by the insurer and thus the insurer must send notice of the policy's nonrenewal to the policyholder in accordance with s. 627.4133, F.S. According to the court, providing the policyholder with a new policy that contains the changed policy term is not sufficient notice of the policy changes.

In response to the court's decision in this case, the bill allows insurance companies to change terms contained in a property and casualty policy without nonrenewing the entire policy and thus having to send a notice of nonrenewal in accordance with current law. To effectuate a change in policy terms, the insurer must give the policyholder a written "Notice of Change in Policy Terms" with the policy renewal notice and the policy renewal notice must be provided to the policyholder in accordance with current law. A policyholder is deemed to accept the policy term change if the renewal premium is paid. If the insurer does not provide a "Notice of Change in Policy Terms" to the policyholder, the terms of the insurance policy are not changed. The OIR still must approve the change in policy terms via a form filing.[40]

Payment of Replacement Costs In Property Insurance Claims

Property insurance claims are adjusted on the basis of replacement costs or actual cash value, whichever method is provided in the property insurance policy. Property insurers must offer policyholders an option for replacement cost coverage.[41] If a claim is adjusted by the actual cash value method, the policyholder is paid the depreciated value of the property damaged or lost that is being replaced or repaired.

Until 2005, if a claim was adjusted by the replacement cost method, insurers could make an initial payment on the claim based on the actual cash value of the claim and require the policyholder to complete the repair before the insurer paid the balance of the full replacement cost. Following the multiple hurricanes of 2004 and 2005, regulators received complaints from policyholders who were given the actual cash value of the property damaged or lost, but could not afford to fund the balance necessary to make the repairs or replacements. In 2005, the Legislature addressed this issue by requiring if a claim was adjusted by the replacement cost method, the insurer must pay the full replacement cost up front, whether or not the policyholder replaces or repairs the damaged property.

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

The bill changes current law relating to the payment of replacement costs. For partial dwelling losses, the insurer must initially pay at least the actual cash value of the claim, less any insurance deductible. The remaining amount owed on the claim (i.e., the difference between

[40] With limited exceptions, s. 627.410, F.S., requires every insurance policy, application, endorsement, or rider to be filed with and approved by the OIR prior to use by the insurance company.
[41] s. 627.7011, F.S.

the initial amount paid and the replacement cost) is paid by the insurer periodically as the repair work is done and expenses are incurred by the policyholder.

For total dwelling losses, the bill maintains current law which requires the insurer to pay full replacement cost up front without reservation or holdback of any depreciation, whether or not the policyholder replaces the dwelling.

For personal property losses (i.e., contents), the bill provides two options for replacement cost coverage. The first option requires the insurer to pay full replacement cost up front without reservation or holdback of any depreciation, whether or not the policyholder replaces or repairs the personal property damaged or destroyed. This is consistent with current law. The second option requires the insurer to initially pay the actual cash value of the claim with the remaining amount owed on the claim (i.e., the difference between the initial amount paid and the replacement cost) paid by the insurer as receipts are provided by the policyholder for the purchase of property that is replaced. The policyholder cannot be required to advance payment to replace the personal property lost. The insurer is not required to offer policyholders the second option for replacement cost coverage but is required to offer the first option. If the insurer decides to offer the second option, the policyholder must be given notice of the receipt submission process required to receive full payment of replacement costs under the policy and must be given an actuarially reasonable premium credit or discount for purchasing the policy.

Payment of Property Insurance Claims

With limited exceptions, s. 627.70131(5), F.S., requires insurance companies to pay or deny property insurance claims or portions of claims within 90 days of receipt of a notice of the claim from the policyholder. Insurance companies are excused from the 90-day claims payment requirement if factors beyond the control of the insurance company reasonably prevent payment within the 90-day period. The bill clarifies that the 90-day claims payment or denial requirement in current law applies to initial, reopened, or supplemental property insurance[42] claims. Current law does not specify whether the claim payment or denial provision applies to only initial claims, only to reopened claims, only to supplemental claims, or to all three types of claims.

Expedited Rate Filing

Section 627.062(2)(k), F.S., enacted in 2009,[43] allows property insurance companies to make a rate filing that is separate from the insurer's annual base rate filing and that is approved or disapproved by the OIR on an expedited basis (i.e., within 45 days of the filing, rather than 90 days). The OIR reviews the expedited rate filing to make sure the rates proposed in the filing are not excessive, inadequate, or unfairly discriminatory, the same review standards that apply to a base rate filing. Unlike a base rate filing, if the OIR does not approve or disapprove the expedited rate filing within the 45-day period, the rate requested is not deemed approved.

Costs that can be included in an expedited rate filing to justify a rate change are more limited than those that can be included in a base rate filing. An expedited rate filing can only request rate changes due to:

[42] Though not defined in law, initial claims are the first claim filed for a loss. Supplemental or reopened claims are claims derived from the same loss, but that are filed after the initial claim.
[43] Section 7, Ch. 2009- 87, L.O.F.

- the recovery of reinsurance or financing costs to replace or finance payment of amounts covered by the Florida Hurricane Catastrophe Fund Temporary Increase in Coverage Limit (TICL) option coverage;[44]
- the recovery of reinsurance or financing costs to replace TICL option coverage due to the yearly TICL option coverage reductions;[45]
- the costs of the price increase of TICL option coverage;[46] and
- the costs of the price increase of the Florida Hurricane Catastrophe Fund mandatory option coverage.[47]

Reinsurance costs to be recouped by an expedited filing may not be more than 10 percent for any individual policyholder. Thus, the maximum rate increase that can be implemented with an expedited rate filing is 10 percent per policyholder.

The insurance company must submit proof of the purchase of reinsurance or other financing product in order to recoup these costs in an expedited rate filing. The insurer cannot use company expenses or profits to justify a rate increase with an expedited rate filing. The OIR may disapprove an expedited rate filing as excessive, inadequate or unfairly discriminatory. An insurer can only make an expedited rate filing once every 12 months. Furthermore, an insurer cannot file an expedited rate filing if the insurer has implemented a rate increase in the six months before the expedited filing. In addition, an insurer cannot increase rates using the annual base rate filing for six months after the expedited rate filing.

Expedited Rate Filings Approved in 2010

In 2010, property insurers submitted 20 expedited rate filings to increase rates for property insurance. Nine of the 20 filings were withdrawn before the OIR made a decision on them. The remaining 11 rate filings were approved by the OIR. In every approved rate filing, the rate increase approved by the OIR equaled the rate increase the insurer requested. None of the expedited rate filings requested rate increases more than the 10 percent allowed by law.

The following expedited rate increases were approved in 2010:

- 9.9 percent increase for two filings;
- 7.2 percent increase for two filings;
- 6.2 percent increase for two filings;
- 4.6 percent increase for one filing; and
- 3.9 percent increase for four filings.

For the 11 expedited rate increases approved in 2010, the fastest approval time by the OIR was 13 days from the date the filing was received by the OIR to the final approval and the longest approval time was 44 days. The average approval time was 37 days. By law, the OIR has 45

[44] The Temporary Increase in Coverage Limit option coverage offers reinsurance from the Florida Hurricane Catastrophe Fund for insurers above the Fund's mandatory coverage. When this coverage was initially enacted in 2007, it provided an additional $12 billion in coverage. Starting in 2009, however, the coverage amount is decreased each year by $2 billion until it reaches zero in 2013.

[45] Legislation enacted in 2009 (Ch. 2009-87, L.O.F.) reduced the TICL option $2 billion a year for six years starting in the 2009-2010 contract year (June 1, 2009-May 31, 2010).

[46] Legislation enacted in 2009 (Ch. 2009-87, L.O.F.) increased the price for TICL coverage each year for five years. The price increase is in conjunction with the TICL coverage decreases discussed in prior footnotes.

[47] Legislation enacted in 2009 (Ch. 2009-87, L.O.F.) increased the price of the mandatory coverage from the Florida Hurricane Catastrophe Fund by requiring the Fund to include a cash build up factor of 5 percent in its reimbursement premium each year until the factor reaches 25 percent. When the factor reaches 25 percent (in 2013), it becomes a permanent part of the Fund's rate and is put into the rate yearly.

days to approve an expedited rate filing, so all expedited rate filings were approved by the OIR within the required statutory time.

Effect of the Bill:

The bill amends the expedited rate filing law enacted in 2009. The bill allows more types of costs to be included in an expedited rate filing than under current law. All reinsurance costs, the cost of financing products used to replace reinsurance, the financing costs incurred in the purchase of reinsurance, or the costs of the price increase of the FHCF mandatory option coverage are allowed to justify an expedited rate increase rate filing.

The bill allows an insurer to request a rate increase of a maximum of 15 percent per policy, rather than 10 percent, using an expedited rate filing. Current law prohibiting insurers from including expenses or profits paid by the insurer in an expedited rate filing is deleted by the bill. Thus, these expenses or profits will be allowed to justify an expedited rate increase.

As under current law, an insurer can only file an expedited rate filing once every 12 months. However, the bill removes current law that restricts insurers from using an expedited rate filing if the insurer has implemented a rate increase in the prior six months and restricts insurers from making any other rate filing for six months after the expedited rate filing.

Under current law, despite the two six month limitations in the expedited rate filing statute, an insurer can increase rates two times in a 12 month period - once with an expedited filing and once with an annual base rate filing. For example, under current law and in accordance with the two six month limitations in the expedited rate filing statute, an insurer can *implement* a base rate filing in January, *file and implement* an expedited rate filing in July, but cannot file another base rate filing until January of the next year. In this example, a consumer who renews a policy after July could incur two rate increases at renewal, one from the January base rate implementation and one from the July expedited rate implementation. However, according to the OIR, common practice is for insurers to file and implement only one rate filing in a 12 month period so that policyholders incur only one rate increase at renewal, with the insurer each year choosing whether to file an expedited rate filing or an annual base rate filing.

One advantage of an annual base rate filing is that the insurer can request a rate increase higher than 10 percent and can include numerous costs to justify an increase, but the compilation of data needed for the rate filing and assembly of the rate filing is time consuming and extensive and the OIR has 90 days to approve or disapprove the rate filing. Some advantages of an expedited rate filing are that the data compilation and assembly is easier and quicker than that needed in an annual base rate filing because only limited costs are included in the filing and the OIR has 45 days to approve or disapprove the rate filing (half the approval time for the annual base rate filing). Some disadvantages of an expedited rate filing are the filing can only request a rate increase up to 10 percent and limited costs can be used to justify the rate filing.

The bill repeals the restrictions in current law allowing an expedited rate filing only when insurers have not implemented a rate increase in the six months before the expedited rate filing and only if insurers do not file for a rate increase with an annual base rate filing for six months after the expedited filing. Repealing the six month restrictions allows insurers to continue to file an expedited and an annual rate filing in a 12 month period, but the rate filings no longer have to be six months apart and could occur closer together, with a 15 percent maximum rate increase allowed with an expedited rate filing.

"Use and File" Rate Filing

Under s. 627.062(2)(a)1. and 2., F.S., property insurers are required to file rates for approval with the OIR either 90 days before the proposed effective date ("file and use") or 30 days after the rate filing is implemented ("use and file"). Under the file and use option, the OIR must finalize its review by issuing a notice of intent to approve or disapprove within 90 days after receipt of the filing; otherwise the filing is deemed approved. Under the "use and file" option, an insurance company may implement the filing prior to approval, but may be ordered by OIR to refund to the policyholder that portion of the rate found by OIR to be excessive.

In the 2007 Special Session A, the Legislature enacted s. 627.062(2)(a)3., F.S., which prohibited insurers from using a "use and file" rate filing to increase property insurance rates from January 25, 2007 through January 1, 2009.[48] However, the ending date for the prohibition was extended by two subsequent legislative enactments until December 31, 2010.[49] Thus, starting January 1, 2011, insurers were allowed to increase property insurance rates using the "use and file" rate filing method. The bill enacts a new prohibition on use of the "use and file" rate filing method for increasing property insurance rates. The bill prohibits use of the "use and file" rate filing method until May 1, 2012.

Public Hurricane Model[50]

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

In 2001, the OIR provided funding to the Florida International University (FIU) for development of a public hurricane model for residential properties. The first completed version of the model was activated in March 2006 and certified by the Commission in 2007. An upgraded version of the model was recertified by the Commission in June 2009 and a new version of the model has been submitted to the Commission for certification, with certification of that model currently pending.

---

[48] Ch. 2007-1, L.O.F.

[49] Ch. 2008-66, L.O.F.; Ch. 20069-87, L.O.F.

[50] Most of the information about the public hurricane model is derived from Meeting materials from the meeting of the Government Operations Appropriations Subcommittee on February 1, 2011.

Although the public model is housed at FIU, faculty, staff and students at other universities and institutions form the team that updates and revamps the model when needed.[51] The OIR provides annual funding of about $600,000 for the public model.

The OIR, the FHCF, and Citizens Property Insurance Corporation are the major users of the public model. The OIR has used the model about 350 times, primarily to check the results of private models submitted to the OIR by an insurer to support a property insurance rate filing.

Although many private insurers purchase hurricane models from private modelers to use in setting property insurance rates, others use the public hurricane model. In 2008 legislation was enacted allowing private insurers to use the public hurricane model. This legislation also required insurers to pay for use of the public model and required the OIR to establish a fee schedule for access and use of the model by private insurers.[52] The legislation specified the fees charged for use of the public model should cover only the actual costs for access to and use of the public model. The public model has been used by private insurers about 45 times since 2008.

Effect of the Bill:

The bill repeals current law requiring the OIR to establish the fees for use of the public hurricane model by rule and requiring the fees to cover only the actual costs of providing access to and use of the public model. The bill replaces the repealed language with a requirement that the fees charged for use of the public model by private insurers be the reasonable costs associated with the operation and maintenance of the model and with an allowance for the OIR to use the model without paying a fee.

Insurance Capital Build-Up Incentive Program

In 2006, the Legislature created the Insurance Capital Build-Up Incentive Program (Capital Build-Up Program or program) within the State Board of Administration (SBA) to provide insurance companies a low-cost source of capital to write additional residential property insurance. The program's goal was to increase the availability of residential property insurance covering the risk of hurricanes and to ease residential property insurance premium increases.

To accomplish its goal, the program loaned state funds in the form of surplus notes to new or existing authorized residential property insurers under specified conditions. The insurers, in turn, agreed to write an additional minimum level of premium for residential property insurance in Florida and to contribute new capital to their company. The maximum dollar amount of a surplus note was $25 million. The surplus note was repayable to the state, with a 20 year term, at the 10-year Treasury Bond interest rate (with interest only payments the first three years). The Legislature appropriated $250 million non-recurring funds from the General Revenue Fund to fund the program at its inception in 2006. Any unexpended balance reverted back to the General Revenue Fund on June 30, 2007.

As of June 28, 2007, the program issued $247,500,000 in funds to thirteen qualifying insurers. Administrative expenses for the program totaled $2,500,000. Thus, by June 2007 the entire

[51] Institutions participating in the public model are: FIU, Florida State University, Florida Institute of Technology, Hurricane Research Division of NOAA, University of Florida, and University of Miami. A team of experts in computer science, finance, statistics, meteorology, and engineering from the various institutions reviews, updates, and revamps the public model.
[52] Ch. 2008-66, F.S.; creating s. 627.06281(3), F.S.

2006 legislative appropriation for the program was exhausted ($247.5 million in loans, and $2.5 million in administrative costs) and no funds reverted back to the General Revenue Fund.[53] Although legislation enacted in 2008 (CS/CS/SB 2860) provided an additional funding of $250 million for the program from the Citizens Property Insurance Corporation, this funding was vetoed by Governor Crist.[54]

Thirteen insurers have received surplus notes under the program. The program required the participating insurers to begin repayment of the principal loaned to the insurers in the third year of the loans. All of the insurers participating in the program have reached the three year mark and have begun making the required principal payments. Interest and principal payments made on the loans are transferred from the SBA to the General Revenue Fund in accordance with s. 215.5595, F.S. Investment earnings and late fees for the program are also transferred to the General Revenue Fund. To date, over $116 million has been transferred from the SBA to the General Revenue Fund.[55]

In 2009, two insurers participating in the program made voluntary principal payments to pay off their surplus note in full.[56] In 2010, an insurer made an additional principal payment of $12.5 million to partially pay down its surplus note.[57] Thus, 11 insurers still have loans from the state under the program and one of the 11 has repaid the state over half of the loan amount. As of January 15, 2011, the aggregate outstanding principal balance for the program is $188.7 million.[58] Additionally, as of February 1, 2011, no insurer with an outstanding surplus note is in default on the note.[59]

Quarterly, the SBA adjusts the interest rate for the term of the surplus notes based on the 10-year Constant Maturity Treasury rate. Total interest paid by insurers in the program since inception of the program is almost $49 million.[60] The interest rate for the first quarter of the program (which ended on 9/30/2006) was 5.22 percent. The interest rate for the latest quarter of the program (which ended December 31, 2010) was 2.52 percent.[61]

Current law allows the SBA to charge additional interest to insurers failing to meet the minimum writing ratio and/or the minimum required surplus set out in s. 215.5595, F.S. The additional interest charged is 25 or 450 basis points, depending on the degree the insurer is out of compliance with the statutorily required writing ratio and/or surplus.[62] The minimum writing ratio required by law is 2:1 for net written premium and 6:1 for gross written premium. Several insurers were not able to meet the required minimum writing ratio and have paid additional interest charges on the surplus note.[63] For the quarter ending in September 2010, 6 of the 11

---

[53] Information obtained from the Final Report of the Insurance Capital Build-Up Incentive Program available at http://www.sbafla.com/fsb/LinkClick.aspx?fileticket=TYIOUbPBbDM%3d&tabid=975&mid=2692 (last viewed February 1, 2011).
[54] Section 16 of CS/CS/SB 2860 which required the $250 million transfer from Citizens to the General Revenue Fund for use in the Capital Build Up Program was vetoed on May 28, 2008. CS/HB 5057 also required the $250 million transfer and this bill was vetoed on June 10, 2008. (Letter to Secretary Kurt S. Browning, Secretary of State, from Governor Charlie Crist dated June 10, 2008, on file with staff of the Insurance & Banking Subcommittee).
[55] Annual Report to the President of the Senate and the Speaker of the House of Representatives on the Insurance Capital Build-Up Incentive Program prepared by the State Board of Administration dated February 1, 2011 at page 8, available at http://www.sbafla.com/fsb/Newsroom/InsuranceCapitalBuildUpIncentiveProgram/tabid/975/Default.aspx (last viewed April 16, 2011).
[56] *Id.* at page 3.
[57] *Id.*
[58] *Id.*
[59] *Id.* at page 5.
[60] *Id.* at page 4.
[61] *Id.*
[62] *Id.* at page 5.
[63] *Id.*

insurers in the program paid penalty interest for not meeting the required writing ratios. Four of the five insurers paid penalty interest of 450 basis points, and one paid 25 basis points.[64] Over the four years the program has been active, all 11 insurers have paid penalty interest at some point for not meeting the required writing ratios.[65] No minimum writing ratio is required for insurers that write property insurance for only manufactured housing, two insurers participating in the program, so no penalty interest has been collected from these two insurers.[66]

As a condition of the surplus note, each insurer must maintain a minimum surplus of $50 million ($14 million for insurers writing only manufactured housing policies) which includes the surplus note proceeds and new capital. In 2009, two of the 13 insurers participating in the program had surplus below the minimum required for one or more quarters and additional penalties were assessed on these insurers. Both insurers have now repaid their surplus notes in full.[67] Two other insurers paid penalties in 2010 for failing to meet the minimum surplus requirements. The total penalty amount collected in 2010 was almost $300,000.[68] As of February 1, 2011, there are no insurers with an outstanding surplus note in default with the minimum required surplus provision of the note.[69]

Effect of the Bill:

The bill allows an insurer to request the SBA to renegotiate the terms of a surplus note issued under the Insurance Capital Build-Up Incentive Program before January 1, 2011. The insurer's request must be submitted to the board by January 1, 2012. If the insurer agrees to accelerate the payment period of the note by at least 5 years, the board must agree to exempt the insurer from the required premium-to-surplus writing ratios. If the insurer agrees to an acceleration of the payment period for less than 5 years, the board may, after consultation with the Office of Insurance Regulation, agree to an appropriate revision of the required premium-to-surplus writing ratios if the revised ratios are not lower than a net premium to surplus of at least 1:1 and, alternatively, a gross premium to surplus of at least 3:1.

Citizens Property Insurance Corporation (Citizens)

Citizens Property Insurance Corporation (Citizens or corporation) is a state-created, not-for-profit, tax-exempt governmental entity whose public purpose is to provide property insurance coverage to those unable to find affordable coverage in the voluntary admitted market. It is not a private insurance company.

As of January 31, 2011, Citizens is the largest property insurer in Florida with over 1.3 million policies extending approximately $462 billion of property coverage to Floridians.[70] As of June 30, 2010, Citizens represented approximately 18 percent of the residential property admitted market based on insured value for policies.[71]

Citizens was created by the Legislature in 2002 by the merger of two existing property insurance associations: The Florida Residential Property and Casualty Joint Underwriting Association (FRPCJUA) and the Florida Windstorm Underwriting Association (FWUA). The

[64] *Id.* at pps. 9-10.
[65] *Id.*
[66] *Id.*
[67] *Id.* at pg. 6.
[68] *Id.*
[69] *Id.*
[70] https://www.citizensfla.com/ (last viewed February 27, 2011).
[71] Meeting materials from Citizens presented at the Insurance & Banking Subcommittee meeting held on January 12, 2011.

FRPCJUA provided full-coverage personal and commercial residential property policies in all counties of Florida while the FWUA provided personal and commercial residential property wind-only coverage in designated territories.

Eligibility for Insurance in Citizens
Citizens writes various types of property insurance coverage for its policyholders. The types of coverage are divided into three separate accounts within the corporation:

1. Personal Lines Account (PLA) – Multiperil Policies[72]
   Consists of homeowners, mobile homeowners, dwelling fire, tenants, condominium unit owners and similar policies;
2. Commercial Lines Account (CLA) – Multiperil Policies
   Consists of condominium association, apartment building, homeowner's association policies, and commercial non-residential multiperil policies on property located outside the High-Risk Account area; and
3. High-Risk Account (HRA) – Wind-only[73] and Multiperil Policies
   Consists of wind-only and multiperil policies for personal residential, commercial residential, and commercial non-residential issued in limited eligible coastal areas.

The bill renames the High-Risk Account to the Coastal Account.

Citizens' Wind-Only Policies
Citizens provides coverage in the high risk account for specially designated areas, called wind-only zones,[74] which have been determined to be particularly vulnerable to severe hurricane damage. In these areas, a property owner can obtain a property insurance policy from Citizens covering property damage from only wind events and can obtain a property insurance policy from a private market insurance company covering property damage and liability from non-wind events (other peril/non-wind coverage).

The wind-only zones that currently exist have evolved over three decades, but originated with the creation of the FWUA in 1970. The FWUA was created to cover residential and commercial policyholders unable to secure windstorm coverage in the voluntary market. This coverage was limited to defined geographical areas in the state determined by the then Department of Insurance (Department). Eligibility was limited to structures in areas found by the Department, after public hearings, to meet three criteria:

- the lack of windstorm coverage in the area was deterring development, causing mortgages to be in default, and causing financial institutions to deny loans;
- the area was subject to the requirements of the Southern Standard Building Code or its equivalent; and
- extending windstorm coverage to the area was consistent with the policies and objectives of environmental and growth management.

The wind-only zones currently apply to 29 Florida counties. When the wind-only zones were established, only Monroe County was included. In 1992, when Hurricane Andrew hit South

[72] A multi-peril policy is defined as a package policy, such as a homeowners or business insurance policy that provides coverage against several different perils. It also refers to the combination of property and liability coverage in one policy. (http://www2.iii.org/glossary/) Multi-peril property insurance policies include coverage for damage from windstorm and from other perils, such as fire, theft, and liability.
[73] A wind-only policy is a property insurance policy that provides coverage against windstorm damage only. Coverage against non-windstorm events such as fire, theft, and liability are available in a separate policy.
74 Also called windstorm areas or windstorm boundaries.

Florida, the wind-only zone did not include Miami-Dade, Broward, or Palm Beach counties. After Hurricane Andrew, the Department and the Legislature expanded the boundaries of the wind-only zones to the current ones. In July 2002, when Citizens was created, Citizens maintained the wind-only zones from the FWUA.

As noted previously, in the wind-only zones private insurers may offer other peril/non-wind coverage, but are not required to provide windstorm coverage. Under current law,[75] beginning December 1, 2010, if Citizens' 100 year probable maximum loss[76] (PML) for the wind-only policies is not 25 percent less than the PML in February 2001, Citizens must reduce the boundaries of the wind-only zones so that the PML reaches that amount. Current law requires a further PML reduction by February 1, 2015. If Citizens' 100-year PML is not 50 percent less than the PML in February 2001 by February 1, 2015, the boundaries of the wind-only zones are restricted to only areas seaward of 1,000 feet from the Intercoastal Waterway.

Citizens was not able to reduce its PML by the required 25 percent by December 1, 2010. One reason Citizens could not reduce the PML is because Citizens has grown, in part, due to the reluctance of private insurers to expand their writings in Florida because of the significant losses sustained in the 2004 and 2005 hurricane seasons. Although Citizens developed a plan to reduce the wind-only zones as the statute directs, the plan has not been implemented. Once Citizens implements the plan, private insurers writing the other peril (non-wind coverage) in the current wind-only zones must either drop that coverage or write the windstorm coverage for policies.

The bill repeals current law requiring the Citizens to reduce the wind-only zones if the Citizens' PML is not reduced by December 1, 2010 and February 1, 2015.

Citizens' Board of Governors

Citizens operates under the direction of an 8-member Board of Governors. The Governor, Chief Financial Officer, Senate President, and Speaker of the House of Representatives each appoint two members of the Board. Board members serve 3-year staggered terms.[77] At least one of the two board members appointed by each appointing officer must have demonstrated expertise in insurance. The board members are not Citizens' employees and are not paid.

The bill prohibits Citizens' board members from voting on any measure before the board that would inure:

- to the gain or loss of the board member;
- to the gain or loss of any principal retaining the board member;
- to the gain or loss of a parent or subsidiary organization of the principal retaining the board member; or
- to the gain or loss of a relative or business associate of the board member.

When the board member abstains from voting, the member must state the nature of the interest in the matter which the member is abstaining from and disclose the nature of the interest in a memorandum filed with the person responsible for recording the Citizens' board meeting minutes.

[75] s. 627.351(6)(y), F.S. This law was enacted in 2002.
[76] Probable maximum loss is an estimate of maximum dollar value that can be lost under realistic situations.
[77] s. 627.351 (6)(c)4., F.S.

The bill further provides Citizens' board members with the required insurance expertise fall within the exemption in the conflicting employment or contractual relationship statute that applies to public officers and agency employees.[78] Thus, the bill allows Citizens' board members with insurance expertise to maintain employment in the private sector in jobs involving business with Citizens without violating the conflict of interest statute because the board member is required by law to have insurance expertise in order to sit on the board.

Outsourcing of Claims Functions

As of December 2010, Citizens has over 1,160 employees in-house, and almost 8,500 insurance agents selling Citizens' insurance. Citizens handled almost 1.7 million calls in 2010. Citizens has in-house claims adjusters on staff and has contracts with external independent adjusting firms. Both in-house and outside adjusters handle daily claims for Citizens. Catastrophe claims are all handled by independent adjusters, with Citizens staff overseeing and directing the independent adjusters.[79]

Virtually all of Citizens' claims adjusting was outsourced prior to the 2004 and 2005 hurricanes. During the 2004 hurricane season, Citizens' Catastrophe Claims Team consisted of two Citizens' employees and 1,230 contracted independent adjusters. During the 2005 hurricane season, Citizens' Catastrophe Claims Team consisted of eight Citizens' employees and 2,001 contracted independent adjusters.[80] Although Citizens had a large number of claims adjusters under contract, after the 2004 and 2005 hurricanes, many of these adjusters broke their contracts with Citizens in order to adjust claims for private insurers. Thus, Citizens' policyholders experienced delays in claim adjusting and payment. To strengthen its ability to handle catastrophe claims, since 2005, Citizens has hired more in-house claims staff and contracted with many more independent adjusters. In 2010, Citizens' Catastrophe Claims Team consisted of 18 Citizens' employees and over 4,500 contracted independent adjusters.[81]

The bill requires a third party to report on the costs and benefits of outsourcing Citizens' policy issuance and service functions to outside parties for a fee. Service functions include claims handling. The outsourcing report is due to the Citizens' board by July 1, 2012. The board must develop a plan to implement the report and submit the implementation plan to the Financial Services Commission (Commission). Citizens must implement the plan by January 1, 2013, after the Commission's approval.

Rates Charged by Citizens

Current law requires Citizens' rates to be actuarially sound. Citizens' rates are set by the Office of Insurance Regulation (OIR) based on a rate filing made by Citizens setting out actuarially sound rates for the corporation. However, although current law requires Citizens' rates to be actuarially sound, the law also restricts Citizens' rates from increasing more than 10 percent a year per policy until the rates are actuarially sound. Once the rates are actuarially sound, the rate increase percentage is not capped.

---

[78] Board members of Citizens fall under the definition of "public officer" in s. 112.313(1), F.S., because that definition includes any person appointed to hold office in any agency, including serving on an advisory board. "Agency" is defined in s. 112.312, F.S.

[79] Information obtained from a representative of Citizens, on file with the Insurance & Banking Subcommittee.

[80] Task Force on Citizens Property Insurance Claims Handling and Resolution, First Report, dated July 2, 2007, available at http://www.taskforceoncitizensclaimshandling.org/images/FirstReport.pdf (last viewed March 14, 2011).

[81] Citizens has other claims personnel that can be moved to catastrophe operations if needed (Information received from Citizens on March 26, 2011).

Citizens' rates were frozen by law at 2005 levels from January 2007 to December 31, 2009.[82] Citizens implemented an overall statewide average rate increase of 10.3 percent to be implemented in 2011 for homeowners in the PLA and HRA.[83] Citizens implemented an overall statewide average rate increase of 5.4 percent for implementation in 2010 for homeowners in the PLA.[84] Citizens implemented an overall statewide average rate increase of 5.2 percent for implementation in 2010 for homeowners in the HRA.[85]

The bill provides that the rate cap in current law for Citizens' rates does not apply to sinkhole coverage. Thus, rates for a Citizens' policyholder can increase more than 10 percent per policy if the policyholder purchases sinkhole coverage from Citizens and a rate increase of more than 10 percent is actuarially justified for the sinkhole risk.

Financial Resources to Pay Claims[86]

Citizens' financial resources include both resources typically available to private insurance companies and resources uniquely available to Citizens as a governmental entity with the statutory authority to levy assessments in the event of a deficit in Citizens' financial resources. Like typical private insurance companies, Citizens' financial resources include:

- insurance premiums;
- investment income;
- accumulated surplus;
- reimbursements from the Florida Hurricane Catastrophe Fund due to Citizens' purchase of reinsurance from the Florida Hurricane Catastrophe Fund; and
- reimbursements from private reinsurance companies if Citizens purchases private reinsurance.

Financial resources unique to Citizens include: Citizens Policyholder Surcharges, regular assessments, and emergency assessments.

Citizens projects the corporation will have $5.4 billion in surplus to pay claims during the 2011 hurricane season.[87] In addition, Citizens could be reimbursed another $6.35 billion for claims it pays by the Florida Hurricane Catastrophe Fund. Thus, the maximum amount Citizens has to pay claims for the 2011 hurricane season is approximately $11.75 billion.[88]

As of January 31, 2011, Citizens' total exposure is almost $462 billion. Citizens estimates the 1-in-100 year hurricane would cost over $23.4 billion.[89] The $11.65 billion difference between Citizens' resources to pay claims ($11.75 billion) and its 1-in-100 year exposure ($23.4 billion)

---

[82] s. 627.351(6)(m)4., F.S.

[83] Press Release from the OIR dated September 23, 2010 available at http://www.floir.com/PressReleases/viewmediarelease.aspx?ID=3699 (last viewed March 24, 2011).

[84] Press Release from the OIR dated October 30, 2009 available at http://www.floir.com/PressReleases/viewmediarelease.aspx?ID=3321 (last viewed March 24, 2011).

[85] Press Release from the OIR dated November 20, 2009 available at http://www.floir.com/PressReleases/viewmediarelease.aspx?ID=3339 (last viewed on March 24, 2011).

[86] All Citizens' projections about claims paying capacity for the 2011 hurricane season are found in meeting materials from Citizens presented at the Insurance & Banking Subcommittee meeting held on January 12, 2011.

[87] Meeting materials from Citizens presented at the Insurance & Banking Subcommittee meeting held on January 12, 2011.

[88] Although Citizens has another $2.9 billion in pre-event bonding that would be available to pay claims, this bonding would have to be repaid through assessments, so is not included in the calculations. If this amount were included, Citizens would have $14.672 billion to pay claims during the 2011 hurricane season.

[89] A 1-in-100 year hurricane has a 1 percent probability of occurring.

would be covered by assessments levied by Citizens on its own policyholders and on policyholders of most property and casualty insurance.

Assessments Levied by Citizens

In the event Citizens incurs a deficit (i.e. its obligations to pay claims exceeds its capital plus reinsurance recoveries), it may levy assessments on most of Florida's property and casualty insurance policyholders in a specific sequence set by statute.[90] The three Citizens' accounts calculate deficits and resulting assessment needs independently.

Citizens Policyholder Assessments

If Citizens incurs a deficit, Citizens will first levy surcharges on its policyholders of up to 15 percent of premium per account in deficit, for a maximum total of 45 percent. This surcharge is collected over twelve months and is collected at the time a new Citizens' policy is written or an existing Citizens' policy is renewed. Thus, a policyholder insured by Citizens when the Citizens Policyholder Surcharge is levied is subject to the surcharge only if the policyholder renews with Citizens during the 12 month surcharge collection period.

Regular Assessments

Upon the exhaustion of the Citizens Policyholder Assessment for a particular account, Citizens may levy a regular assessment of up to 6 percent of premium or 6 percent of the deficit per account, for a maximum total of 18 percent.[91] The regular assessment is levied on virtually all property and casualty policies in the state, but is not levied on Citizens' policies. The assessment is also not levied on workers' compensation, medical malpractice, accident and health, crop or federal flood insurance policies. Mechanically, property casualty insurers with policies subject to the regular assessment "front" the assessment to Citizens and recover it from their policyholders at the issuance of a new policy or at renewal of existing policies. Thus, Citizens will collect funds raised by a regular assessment quickly after the assessment is levied, usually within 30 days after levy.

Emergency Assessments

Upon the exhaustion of the Citizens Policyholder Assessment and regular assessment for a particular account, Citizens may levy an emergency assessment of up to 10 percent of premium or 10 percent of the deficit per account, for a maximum total of 30 percent.[92] This assessment can be collected for as many years as is necessary to cure a deficit. Emergency assessments are levied on virtually all property and casualty policies in the state, including Citizens' own policies. However, this assessment is not levied on workers' compensation, medical malpractice, accident and health, crop or federal flood insurance policies. Mechanically, property and casualty insurers with policies subject to the emergency assessment collect the assessment from policyholders at the issuance of a new policy or at renewal of existing policies and then remit the assessments periodically to Citizens. Thus, Citizens will not collect funds raised by an emergency assessment immediately after the assessment is levied but will collect funds intermittently throughout the collection period as policies are renewed and new policies written.

[90] s. 627.351(6)(b)3.a.,d., and i., F.S.
[91] s. 627.351(6)(b)3.a. and b., F.S.
[92] s. 627.352(6)(b)3.d., F.S.

Effect of the Bill:

Acknowledgment of Assessment Potential

Starting January 1, 2012, the bill requires insurance agents issuing property insurance in Citizens to obtain an acknowledgement signed by the applicant for insurance relating to the potential assessments imposed on the policy by Citizens. Citizens must keep a copy of the signed acknowledgement. Thus, potential policyholders of Citizens will be informed about the potential assessments that can be imposed on their policy. The signed acknowledgement creates a conclusive presumption the policyholder understood and accepted the Citizens' assessment liability.

Levy of Assessment

Under current law, Citizens collects a Citizens Policyholder Surcharge (surcharge) for 12 months and can only collect the surcharge on new policies issued by Citizens during the 12 month collection period or on current policies renewed by Citizens during the 12 month collection period. Thus, under current law a policyholder insured in Citizens when the Citizens Policyholder Surcharge is levied can avoid paying the surcharge:

1. By canceling the Citizens' policy mid-term during the 12 month collection period and moving to a private company; and
2. By not renewing a Citizens' policy that ends during the 12 month collection period.

In both cases, a policyholder who was insured in Citizens when the Citizens Policyholder Surcharge was levied is not required to pay the surcharge.

The bill prevents the first scenario by requiring Citizens' policyholders to pay the surcharge when their Citizens' policy is cancelled. The second scenario is not addressed by the bill. The bill also requires the surcharge to be paid when a Citizens' policy is terminated or renewed or a new policy is issued within 12 months after a surcharge levy. If the surcharge is levied for less than 12 months, Citizens' policyholders must pay the surcharge during the collection period. Policyholders who are not insured by Citizens on the day of the order levying the surcharge are also responsible for paying the surcharge if they obtain insurance in Citizens during the 12 months after a surcharge levy or during the time the surcharge is collected.

Timing of Regular Assessments

The bill also clarifies current law relating to the timing of Citizens' levy of regular assessments against insurance companies. The bill does not allow Citizens to levy regular assessments against insurance companies until Citizens levies a Citizens Policyholder Surcharge in the maximum statutorily allowed amount against Citizens' policyholders. According to a representative of Citizens, this is consistent with how Citizens currently levies regular assessments.[93]

Sinkholes

Background

A sinkhole is defined in Florida law as a landform created by subsidence of soil, sediment, or rock as underlying strata are dissolved by groundwater.[94] Sinkholes occur in certain parts of Florida due to the unique geological structure of the land. Sinkholes are geographic features formed by movement of rock or sediment into voids created by the dissolution of water-soluble

[93] Conversation with a representative of Citizens on March 15, 2011.
[94] s. 627.706(2)(b), F.S.

rock. This type of subsidence formation may be aggravated and accelerated by urbanization and suburbanization, by water usage and changes in weather patterns.

Since 1981, insurers offering property coverage in Florida have been required by law to provide coverage for property damage from sinkholes.[95] In 2007, Florida law was amended to require insurers in Florida to cover only catastrophic ground cover collapse, rather than all sinkhole loss, in the base property insurance policy.[96] However, insurers must also offer policyholders, for an appropriate additional premium, sinkhole loss coverage covering any structure, including personal property contents.[97] Sinkhole loss coverage includes repairing the home, repairing the foundation, and stabilizing the underlying land.

Generally, insurers that currently offer sinkhole loss coverage in the base property insurance policy must nonrenew all their property insurance policies in order to change the policy to only include catastrophic ground cover collapse in the base policy and to offer sinkhole loss coverage for an additional premium. Current law, however, provides one exception to this nonrenewal rule. Property insurers can nonrenew policies in only Pasco and Hernando counties that contain sinkhole loss coverage in the base property insurance policy and offer policyholders in these two counties a base policy containing coverage for only catastrophic ground cover collapse and offer coverage for sinkhole loss as an endorsement to the base policy for an additional premium.

Effect of the Bill:

The bill maintains current law requiring coverage for catastrophic ground cover collapse in the base property insurance policy and requiring insurers to offer sinkhole loss coverage for an additional premium. However, the bill allows insurers to restrict catastrophic ground cover collapse and sinkhole loss coverage to the property's principal building. The bill also allows insurers to require an inspection of the property before the insurer provides sinkhole loss coverage.

The bill changes what is covered under sinkhole loss coverage offered by Citizens. Starting January 1, 2012, sinkhole loss coverage by Citizens will not cover sinkhole losses to appurtenant structures, driveways, sidewalks, decks, or patios.

In addition, in all counties, the bill allows insurers to nonrenew policies that contain sinkhole loss coverage in the base policy and offer the policyholder a policy covering only catastrophic ground cover collapse in the base policy but also offer the policyholder an endorsement providing insurance coverage for sinkhole loss for an additional premium. Thus, the provision in current law on this issue that applies only to policies in Pasco and Hernando counties is extended statewide.

Increase in Sinkhole Claims

Sinkhole insurance claims have increased substantially in number and cost over the last several years.[98] Both increases negatively impact the financial stability of property insurers, including Citizens, and have been used by property insurers to justify recent property insurance rate increases.[99]

---

[95] Ch. 1981-280, L.O.F.
[96] Section 30, Ch. 2007-1, L.O.F.
[97] s. 627.706, F.S.
[98] The increase in claims frequency and severity is based on data collected from 211 insurers by the Office of Insurance Regulation (OIR) in the Fall of 2010, (*Report on Review of the 2010 Sinkhole Data Call* (OIR Report).
[99] Testimony at the Insurance & Banking Subcommittee Meeting on February 9, 2011.

Frequency and Cost of Sinkhole Claims on the Insurance Industry

In 2010, because of anecdotal evidence of increasing sinkhole claims and costs in recent years, the OIR conducted a data call to collect specific information about sinkhole claims from 211 insurers, including Citizens. The OIR compiled and analyzed the data collected to determine claim payment trends and other related data.

On November 8, 2010, the OIR reported its findings from the data call.[100] The report indicates the OIR received information on 8,959 open sinkhole claims and 15,712 closed sinkhole claims (24,671 total claims) for 2006-2009. Specifically, the data showed:

- Total sinkhole claims increased from 2,360 in 2006 to 6,694 in 2010.[101]
- Total sinkhole costs for open and closed claims combined increased from $209 million in 2006 to $406 million in 2009.[102]
- Total costs for open and closed claims exceeded $1.4 billion over the 4-year period.[103]
- One percent of the closed claims were for catastrophic ground collapse.[104]

The data indicates a wide variation in the frequency of claims, depending on the geographic region. Over 88 percent of the sinkhole claims reported to the OIR occurred in eleven counties: Hernando, Pasco, Hillsborough, Pinellas, Marion, Polk, Orange, Alachua, Citrus, Miami-Dade, and Broward, with 66 percent (11,872) of the claims concentrated in three counties: Hernando, Pasco and Hillsborough.[105] Sinkhole claims are increasing in Miami-Dade and Broward counties, according to the data collected by the OIR. These counties represented 2.9 percent of total sinkhole claims from 2006-2009, but increased to 4.2 percent through the third quarter of 2010. This is significant because sinkhole activity is not typically found in these counties.[106]

Sinkhole testing under Florida law includes an inspection and a report by a geologist or engineer. The data collected by the OIR indicates insurers incur testing costs for most sinkhole claims. Insurers conducted testing procedures in order to adjust a sinkhole claim in over 80 percent of the sinkhole claims and more than one testing procedure was used to test for sinkhole activity in most claims. In 2006, insurers incurred expenses of $20.4 million for the sinkhole inspection and engineering report. By 2009, that amount increased to almost $58 million. This increase is likely due to the increase in the number of sinkhole claims from 2006 to 2009. Despite the large increase in the aggregate amount of expenses for inspections and engineering reports from 2006-2009, these expenses on a per claim basis were fairly steady during the time period (approximately $8,000 – $9,300 per claim).[107]

Frequency and Severity of Sinkhole Claims Filed Against Citizens

Like insurers in the private market, Citizens has seen an increase in the number of sinkhole claims filed in recent years. Statewide, the number of sinkhole claims filed on personal residential policies insured by Citizens increased from 660 in 2005 to 1,519 in 2009 and 1,145 in

[100] http://www.floir.com/pdf/2010_Sinkhole_Data_Call_Report.pdf (last viewed February 12, 2011).
[101] 2010 Sinkhole Data Call Report pg. 6.
[102] 2010 Sinkhole Data Call Report pg. 5.
[103] 2010 Sinkhole Data Call Report pg .5.
[104] 2010 Sinkhole Data Call Report pg. 8.
[105] 2010 Sinkhole Data Call Report pg. 12.
[106] 2010 Sinkhole Data Call Report pg. 13.
[107] 2010 Sinkhole Data Call Report pg. 10.

2010.[108] The increase in sinkhole claims is the primary cost driver for Citizens' significant sinkhole losses. In 2009, Citizens incurred almost $84 million in sinkhole losses plus adjustment expenses, yet obtained a little over $22 million in earned sinkhole premium to cover those losses.[109]

The increase in Citizens' sinkhole claims has occurred even though significant numbers of Citizens' policyholders dropped sinkhole loss coverage after it became an optional endorsement in 2007. The percent of Citizens' statewide policies with sinkhole loss coverage fell from 100 percent in 2006 (when it was mandatory) to 61 percent in 2009 and 60 percent in 2010.[110] In 2009, only 37 percent of policyholders in Hernando County and 22 percent of policyholders in Pasco County purchased Citizens' policies with sinkhole loss coverage. In 2010, these percentages increased slightly to 40 percent and 23 percent respectively.[111]

Of the sinkhole claims reported in the OIR data call in Hernando, Pasco, and Hillsborough counties, Citizens insured 36 percent of the claims (4,261). Citizens' data shows the sinkhole loss ratio for Hernando County in 2009 is about 647 percent, meaning for every $1 in premium Citizens collects in Hernando County, $6.47 is paid for a sinkhole claim in the county. Citizens' 2009 loss ratio is almost 285 percent in Pasco County and is almost 526 percent in Hillsborough County. The loss ratio for all other counties combined is 175 percent.

Impact on Property Value of Increase in Sinkhole Claims

Sinkholes negatively impact property values. Sinkhole claims reduce the property value of the land which contains the alleged sinkhole and on neighboring property, even if the sinkhole is stabilized or repaired and even if the sinkhole is not verified.[112] For example, the Pasco County Property Appraiser's office indicated a property which contains a repaired sinkhole has a five percent reduction in value and in some cases, neighboring property has a three percent reduction in value.[113] Since 2004, Pasco County has a total property value loss of almost $55 million due to unrepaired sinkholes, a total property value loss of over $14 million to stabilized sinkholes, and a total property value loss of over $4 million to unverified sinkhole loss.[114] Reductions in property value directly reduce local government revenue.

Effect of the Bill:

The bill provides legislative findings relating to sinkhole issues and the impact of the increasing number of sinkhole claims and the severity of the claims on the property insurance market, on the local property tax base, and on the real estate market. Legislative intent is also provided in the bill.

In addition, the bill requires notice of all sinkhole claims, including initial, reopened, or supplemental claims to be given to the insurer in accordance with policy terms within two years of the policyholder knowing about the sinkhole loss or within two years from when the

[108] Information received from Citizens on March 2, 2011, on file with the Insurance & Banking subcommittee. In 2009, Citizens received 118 sinkhole claims on commercial residential and commercial nonresidential policies located outside the wind zones and in 2010 received 57 claims on these policies.
[109] Information received from Citizens on March 2, 2011, on file with the Insurance & Banking subcommittee.
[110] Information received from Citizens on March 2, 2011, on file with the Insurance & Banking subcommittee.
[111] Information received from Citizens on March 2, 2011, on file with the Insurance & Banking subcommittee.
[112] Testimony at the Insurance & Banking Subcommittee Meeting on February 9, 2011.
[113] Testimony at the Insurance & Banking Subcommittee Meeting on February 9, 2011.
[114] Information received from the Pasco County Property Appraiser's office for the Insurance & Banking Subcommittee Meeting on February 9, 2011, available at http://myfloridahouse.gov/Sections/Documents/loaddoc.aspx?PublicationType=Committees&CommitteeId=2607&Session=2011&DocumentType=Meeting Packets&FileName=IBS 02_9_2011_online.pdf. (last viewed March 13, 2011).

policyholder reasonably should have known about the sinkhole loss. Current law does not prescribe a time frame for filing a property insurance claim, including a sinkhole claim.

Insurance Adjusting of Sinkhole Claims

The Legislature in 2005 and 2006 substantially amended the laws on sinkhole claims in response to a continuing crisis regarding the availability and affordability of sinkhole coverage. Prior to 2005, the law governing sinkhole claims was very general. The 2005 and 2006 legislation enacted a specific process for investigation of sinkhole claims by insurance companies according to standards in the law, for completion and utilization of sinkhole reports in the adjusting and settling of sinkhole claims, for reporting sinkhole claims to the county clerk of courts for recording and to future buyers of the property subject to the sinkhole claim, and for utilization of an alternative dispute procedure for resolution of sinkhole insurance claims.

Under current law, when a claim is made for sinkhole loss, the insurer must inspect the premises and determine whether there has been physical damage to a structure that may be the result of sinkhole activity. "Sinkhole loss" is defined by statute as "structural damage to the building, including the foundation, caused by sinkhole activity." "Sinkhole activity," used in the definition of "sinkhole loss," is defined in statute, but "structural damage" used in the definition is not. The lack of a statutory definition of "structural damage" has led to disparate definitions of the term being used in sinkhole claims and has led to litigation over the meaning of the term.[115]

Following the insurer's initial inspection, the insurer must provide written notice to the policyholder that details the insurer's initial determination, when the insurer is required to engage a professional engineer or professional geologist to perform testing, and a statement of the policyholder's right to demand certain testing to be conducted by a geologist or engineer. If the insurer is unable to determine the cause of the damage during the inspection or if the inspection reveals damage consistent with sinkhole loss, then the insurer must retain a qualified engineer or geologist to perform testing on the property.

Testing standards for sinkholes are established in s. 627.7072, F.S. The professional geologist or engineer must perform whatever tests are sufficient to determine the presence or absence of sinkhole loss within reasonable professional probability and to allow the engineer to make recommendations regarding any necessary building stabilization and foundation repair. The most common testing procedures used in the closed sinkhole claims reported to the OIR during the data call were shallow boring, ground penetrating radar, and deep boring.

Once testing is complete, the engineer or geologist performing the testing issues a report and certification to the insurance company and policyholder verifying sinkhole loss or eliminating sinkhole activity as the cause of damage to the property.[116] Florida law specifies the contents of the sinkhole report and gives the findings of the report a presumption of correctness.

Currently on appeal before the Florida Supreme Court is *Warfel v. Universal Ins. Co. of N.A.*,[117] in which the Supreme Court will determine whether the presumption of correctness for sinkhole reports shifts the burden of proof to the policyholder or merely requires the policyholder to produce evidence regarding the facts at issue, at which point the presumption disappears. The Second District Court of Appeal's decision in *Warfel,*[118]which is on appeal to the Florida

[115] For example, see Thomas Harris and Richard Braunshweig v. Homewise Preferred Insurance Company, CA-10-153 (Fla. Cir. Ct, Hernando County).
[116] s. 627.7073, F.S.
[117] SC 10-948 (oral argument held on February 11, 2011).
[118] 36 So.3d 136 (2nd DCA 2010).

Supreme Court, eliminated the presumption in favor of the insurer when the report was challenged in court. The Second District Court of Appeal (DCA) held the sinkhole report presumption was a "vanishing" or "bursting bubble" presumption, rather than a public policy-related presumption that shifted the burden of proof to the policyholder. Thus, the Second DCA determined the sinkhole report's presumption of correctness vanished when the homeowner in the case presented credible evidence contradicting facts giving rise to the presumption. With vanishing presumptions, the jury is not told of the presumption and must decide the case based on the evidence presented by the parties as though no presumption ever existed.

If the insurer determines there is no sinkhole loss, the insurer can deny the sinkhole claim. If the insurer denies the sinkhole claim without performing testing, the policyholder can demand testing and the insurer must provide testing.

If the insurer verifies there is a sinkhole loss, the insurer must pay to stabilize the land and building and repair the foundation in accordance with the recommendation of the professional engineer and in consultation with the policyholder.[119] The insurer must pay for repairs to the structure and contents as required in the insurance policy.

In cases of a verified sinkhole loss, the insurer can limit its payment for the sinkhole loss to actual cash value of the loss until the policyholder enters into a contract for building stabilization or foundation repairs. However, payment for the underpinning or grouting or other repair technique performed below the foundation cannot be limited to actual cash value.[120] Once the policyholder enters into a contract for stabilization or repair of the damaged property, the insurer can pay the repair costs as the repair work is completed. The insurer cannot require the policyholder to advance any funds for the repair work. Repair payments may be paid by the insurer directly to the repair contractor, if written approval is obtained from the policyholder or property lienholder. If the required sinkhole repairs are started, but a determination is made before the repairs are complete that the repair costs will exceed the property insurance policy limits, the insurer must either complete the repair work recommended by the engineer or tender policy limits to the policyholder, without reducing the amount tendered for the repair costs already incurred. Accordingly, insurers can pay over policy limits for sinkhole claims.

Although current law requires the homeowner to repair the property affected by a verified sinkhole, often times the insurer and homeowner settle the sinkhole claim before repair work is started. The OIR and insurers believe sinkhole claims are increasing because homeowners that settle sinkhole claims are not required to use claim settlements to repair or remediate the home and land.[121] Thus, homeowners are incentivized to file sinkhole claims, reach a settlement with the insurer, and use the settlement proceeds for something other than repair and replacement of the sinkhole and resulting damage. The OIR noted in its data call repairs were initiated in only 20 percent of the total claims reported.

[119] The meaning of the term "in consultation with the policyholder" has caused confusion as to its meaning which has resulted in litigation. Insurers assert that the phrase means providing notice to the policyholder regarding payment of claim proceeds to conduct repairs. Some policyholders and their representatives assert the phrase requires the insurer and policyholder to essentially agree on the method of repair to be used to remediate the confirmed sinkhole.

[120] Under the grouting procedure, a grout mixture (composed of cement, sand, fly ash, and water) is injected into the ground to stabilize the subsurface soils to minimize further subsidence damage by densifying the soils beneath the building as well as sealing the top of the limestone surface to minimize future raveling. Underpinning consists of steel pipes drilled or pushed into the ground to stabilize the building's foundation.

[121] Testimony at the Insurance & Banking Subcommittee Meeting on February 9, 2011.

Insurers cannot nonrenew a property insurance policy because a sinkhole claim was filed as long as the property was repaired in accordance with the engineer's recommendation and the total payment for the sinkhole claim or claims did not exceed the policy limits of the property insurance policy.

Insurers who pay a claim for sinkhole loss must file a copy of the engineer or geologist report and a certification, including the legal description of the property, with the county clerk of court. The clerk must record the report and certification. When property that is the subject of a paid sinkhole claim is sold, the seller who filed the sinkhole claim must disclose to the buyer that a sinkhole claim has been paid. In addition, the seller must disclose whether or not the full amount of claim payment was used to repair the sinkhole damage.

Effect of the Bill:

Changes to Definitions Applying in Sinkhole Claims

The bill limits the current definition of "catastrophic ground cover collapse" to structural damage to the covered building, rather than any building. Similarly, the bill limits the current definition of "sinkhole loss" to structural damage to the covered building, rather than any building. The current definition of "sinkhole activity" is amended to require weakening of the earth supporting property due to contemporaneous movement or raveling of soils, sediments, or rock materials. The current definition does not include contemporaneous movement.

The qualifications of professional engineers and professional geologists that are used in sinkhole claims are revised by the bill. For professional engineers, the bill removes the requirement that the engineer have a specialty in geotechnical engineering. For professional geologists, the bill removes the requirement that the geologist have expertise in the geology of Florida in order to be qualified to opine in sinkhole claims.

The bill provides a definition of "structural damage." The definition provided is based on descriptions of structural damage in the Florida Building Code that are applicable to sinkholes. Current law does not have a definition of "structural damage," even though the definitions of "catastrophic ground cover collapse" and "sinkhole loss" in current law are conditioned on structural damage. The lack of a definition of "structural damage" has lead to disparate definitions being used in sinkhole claims and has resulted in litigation.[122]

Changes to Insurance Adjusting of Sinkhole Claims and Payment of Sinkhole Testing and Sinkhole Report Fees and Costs

When a sinkhole claim is filed, the bill requires the insurer to inspect the property to determine if there is structural damage resulting from sinkhole activity. Current law requires an inspection to determine if there is physical damage to the structure, instead of structural damage.

The bill maintains current law providing if the insurer's inspection of damaged property confirms damage to the property but does not identify the cause of the damage or if the damage seen on inspection is consistent with sinkhole loss, the insurer must hire, and pay for, an engineer or geologist to conduct sinkhole testing to determine the cause of the damage to the property. However, the bill adds testing in these circumstances is required only if the insurance policy covers sinkhole loss. Current law does not require sinkhole loss to be covered by the policy in order for testing to occur. Thus, a policyholder can demand testing for sinkhole damage paid for by the insurer even if the policyholder would not be covered for sinkhole damage if the testing revealed sinkhole damage was present.

[122] See footnote #64.

If an insurer determines there is no sinkhole loss and denies the sinkhole claim without sinkhole testing, current law allows the policyholder to demand testing. In such case, the bill requires the policyholder's demand for testing to be communicated to the insurer within 60 days after the receipt of the denial of the sinkhole claim. Current law does not include a time period during which the policyholder must demand testing. In addition, before the testing can occur, the policyholder demanding testing must pay the lesser of 50 percent of the sinkhole testing and sinkhole reporting costs or $2,500. But, the policyholder can be reimbursed for these testing costs by the insurer if the testing reveals a sinkhole loss. Current law requires the policyholder to reimburse the insurer the lesser of 50 percent of the testing costs or $2,500 if the policyholder submitted the sinkhole claim without good faith grounds. This requirement is not changed by the bill and occurs after the testing requested by the policyholder is completed. Finally, the bill allows the policyholder to demand testing only if the insurance policy covers sinkhole loss to prevent insurers from having to pay for sinkhole testing if the policy would not cover sinkhole damage.

The bill adds a requirement to the sinkhole report and certification rendered after and based upon sinkhole testing. Current requirements of the report and certification are found in s. 627.7073(1), F.S. If sinkhole loss is verified in the sinkhole report and certification, in addition to the other statements required by law, the sinkhole report and certification issued by the engineer or geologist must state structural damage to the covered building has been identified within a reasonable professional probability. In addition to other statements required by current law, if there is no structural damage or if sinkhole activity is eliminated as the cause of damage to a covered building, the sinkhole report and certification must state there is no structural damage or the cause of structural damage found is not sinkhole activity within a reasonable professional probability.

In addition to the information about sinkhole claims required to be filed under current law by the insurer with the clerk of court, the bill also requires the insurer to file with the clerk of court the neutral evaluation report verifying sinkhole activity as the cause of the damage to the property, a copy of the certification indicating sinkhole stabilization has been completed, and the amount paid on a sinkhole claim. The bill also requires the policyholder to file a copy of any sinkhole report prepared for the policyholder with the clerk of court before accepting payment from the insurer on a sinkhole claim. The engineer overseeing repairs to the property must also file a copy of the report certifying the repairs are properly performed with the clerk of court.

Changes to the Sinkhole Repair Requirement

The bill also makes changes to current law relating to the repair of sinkholes paid for by the insurer. The bill maintains current law allowing the insurer to initially pay actual cash value of the sinkhole claim, except for the underpinning and other below foundation repair costs, until the policyholder enters into a contract to repair the sinkhole damage. However, the bill requires the insurer to pay for only repairs recommended in the sinkhole report prepared by the insurer's geologist or engineer. The insurer must obtain approval of only the property lienholder, rather than the policyholder and the lienholder, in order to pay repair costs directly to the repair contractor.

For verified sinkholes, the bill requires the policyholder to repair the property in accordance with the repair recommendations made in the insurer's sinkhole report. If the insurer's engineer determines that repairs cannot be completed within policy limits, the bill requires the insurer to tender policy limits or complete the repairs.

The bill requires the policyholder to enter into a contract to repair the sinkhole damage within 90 days after the insurer confirms coverage for the sinkhole loss and notifies the policyholder of the confirmation. The 90-day time period is tolled during the neutral evaluation and begins again 10 days after the neutral evaluation is completed. Current law does not prescribe a time period for the policyholder to enter into a repair contract for sinkhole damage.

Sinkhole repairs must be complete within 12 months after the repair contract is entered into. The exceptions to this 12-month limitation are: mutual agreement between the insurer and the policyholder, neutral evaluation of the claim, litigation of the claim, or appraisal or mediation of the claim. Current law does not prescribe a time period for completing sinkhole repairs. Once the repairs are completed, the engineer overseeing the repairs must issue a report certifying the repairs are properly performed.

The bill prohibits a contractor from offering a rebate for sinkhole repair on the property and provides offering a rebate is insurance fraud punishable as a third degree felony. The bill also makes the homeowner's property insurance coverage void if a rebate is accepted by the homeowner and requires the homeowner to refund the rebate to the insurer.

The bill prohibits insurers from nonrenewing a property insurance policy because a sinkhole claim is filed if the sinkhole claim payment equals or is less than policy limits or if the property was repaired. Also, insurers can nonrenew a property insurance policy if policy limits or more are paid.

Alternative Dispute Resolution Process for Sinkhole Claims

Background on the Alternative Dispute Resolution Process

Section 627.7074, F.S., provides an alternative dispute resolution process for sinkhole claims. The process supersedes the mediation procedures for property insurance claims contained in s. 627.7015, F.S. The process begins once an insurer receives the sinkhole report under s. 627.7073, F.S., or denies a sinkhole claim. When either occurs, the insurer must notify the policyholder of the right to participate in the neutral evaluation process. The insurer must also send a pamphlet on the neutral evaluation process prepared by the DFS to the policyholder.

Participation in the neutral evaluation process is optional and nonbinding. Either the policyholder or insurer can decline to participate. If either party desires neutral evaluation, the request for neutral evaluation must be filed with the DFS on the appropriate form. The request must state the reason why neutral evaluation is being sought and include an explanation of all issues in dispute. The filing of a request for neutral evaluation tolls the time period for filing suit for 60 days following the conclusion of neutral evaluation or the time prescribed in s. 95.11, F.S., whichever is later.[123]

Once the DFS receives a request for neutral evaluation, the department provides each party with a list of certified neutral evaluators. The neutral evaluators are professional engineers or professional geologists who have completed an alternative dispute resolution course designed or approved by the DFS. The evaluators are fair and impartial and attempt to resolve the dispute at issue. The parties mutually select a neutral evaluator from the list, with the DFS choosing the evaluator if the parties cannot agree.

[123] Section 95.11, F.S., requires all suits filed for breach of contract to be filed within five years of the breach. Because insurance policies are contracts, a policyholder must file a lawsuit within five years of the insurance company's breach of the policy.

Because the neutral evaluation is an informal process, the formal rules of evidence and procedure do not apply and rules of procedure adopted by the DFS apply. All parties must participate in the neutral evaluation process in good faith. The neutral evaluation conference must be held within 45 days of the department's receipt of a request. The neutral evaluator must notify the policyholder and insurer when and where the neutral evaluation conference will be conducted. The conference may be held by telephone. A party does not have to attend the neutral evaluation if a representative attends and has the authority to make a binding decision on behalf of the party. If a policyholder is not represented by an attorney, a consumer affairs specialist of the DFS or an employee of the DFS designated as the primary contact for consumers on issues related to sinkholes must be available to consult with the policyholder.

For matters not resolved by the parties during the neutral evaluation, the neutral evaluator must prepare a report stating whether the sinkhole loss has been verified or eliminated. If a sinkhole loss is verified, the report must include the evaluator's opinion regarding the need for and estimated costs of stabilizing the land and any covered structures as well as appropriate remediation or structural repairs. The evaluator's report must be sent to all parties in attendance at the neutral evaluation and to the DFS. The recommendation of the neutral evaluator is admissible in any subsequent action or proceeding relating to the sinkhole claim.

Evidence of an offer to settle a sinkhole claim during the neutral evaluation process, or other relevant conduct or statements made concerning an offer to settle are inadmissible to prove or disprove liability or a sinkhole claim's value. However, the recommendation of the neutral evaluator is admissible in any subsequent action or proceeding, but only for a determination regarding the award of attorney's fees.

If a policyholder does not follow the recommendations of the neutral evaluator, the insurer is not liable for attorney's fees under the Insurance Code or s. 627.428, F.S., unless the policyholder obtains a judgment that is more favorable than the neutral evaluator's recommendation. Further, the insurance company is not liable for extra contractual damages on a sinkhole claim related to the issues determined by the neutral evaluator. If the neutral evaluator verifies a sinkhole and recommends costs that exceed the amount the insurer has offered to pay the policyholder, the insurer is liable for up to $2,500 in attorney's fees for the policyholder's attorney's participation in the neutral evaluation.

Effect of the Bill:

Appraisal Clause

An appraisal clause is found in all insurance policies. The purpose of the appraisal clause is to establish a procedure to allow disputed amounts to be resolved by disinterested parties. The appraisal clause is used only to determine disputed values. An appraisal cannot be used to determine what is covered under an insurance policy. Coverage issues are litigated and determined by the courts.

The appraisal process works as follows:

- The insurance company and the policyholder each appoint an independent, disinterested appraiser.
- Each appraiser evaluates the loss independently.
- The appraisers negotiate and reach an agreed amount of the damages.

- If the appraisers cannot agree on the amount of damages, they together choose a mutually acceptable umpire.[124]
- Once the umpire has been chosen, the appraisers each present their loss assessment.
- The umpire will subsequently provide a written decision to both parties.

If the two parties agree to the amount of the loss, that amount becomes the claim amount. However, if one of the parties does not agree, then the case can still be litigated in court.

Although the neutral evaluation used in sinkhole claims supersedes the mediation procedures for property insurance claims contained in s. 627.7015, F.S.,[125] the bill specifies the neutral evaluation will not invalidate the appraisal clause in the property insurance policy. Thus, a sinkhole claim can go to appraisal and neutral evaluation.

Changes to the Neutral Evaluation Process
The bill makes the alternative dispute resolution process for sinkhole claims available to either party if a sinkhole report is issued. The bill also requires any court proceeding related to the sinkhole claim to be stayed during the neutral evaluation and for five days after the neutral evaluation report is filed with the court.

The bill allows either party to request disqualification of the neutral evaluators on the list provided to the parties by the DFS. Two neutral evaluators can be disqualified without cause by either party. Furthermore, the bill allows disqualification of a neutral evaluator for cause and specifies what grounds constitute cause. The DFS must appoint a neutral evaluator from the neutral evaluator list if the parties cannot agree to a neutral evaluator within 14 days of receiving the neutral evaluator list.

The neutral evaluator must notify the parties of the specifics of the neutral evaluation within 14, rather than 5, business days after the referral of the sinkhole claim to neutral evaluation. The neutral evaluator must make reasonable efforts to hold the neutral evaluation within 90, rather than 45, days after the DFS receives the request for neutral evaluation from either party. Neutral evaluation of a sinkhole claim can still be held outside the 90 day time period.

The bill sets forth issues that must be decided by the neutral evaluator. The bill allows the neutral evaluator access to inspect the property alleged to be damaged by a sinkhole. The homeowner or homeowner's agent must provide all sinkhole reports received to the neutral evaluator before the neutral evaluator inspects the damaged property. The neutral evaluator can request the engineer or geologist who completed the sinkhole testing on the claim to perform additional testing the neutral evaluator believes is necessary to determine all issues in dispute in the sinkhole claim.

If a neutral evaluator who is not qualified to determine all the issues in dispute in the sinkhole claim is chosen, the evaluator can obtain assistance from another neutral evaluator on the neutral evaluator list, as long as the evaluator to provide assistance has not been disqualified. The evaluator chosen to assist the original evaluator must be qualified to decide the issues in

[124] An umpire must also be a disinterested party, and must be impartial, of good moral character and possessing a good reputation. No umpire should be chosen that has any financial interest in the outcome of the appraisal. If the two appraisers cannot agree on the selection of an umpire, either side may appeal to the local court for the appointment of someone to serve in that capacity.
[125] This mediation procedure is run by the Department of Financial Services and is a nonbinding process for the insurance company and the policyholder to meet with an neutral third party (the mediator) to discuss their property insurance claim disputes. The mediation facilitates discussions and negotiations between the insurance company and the policyholder but does not render an opinion or determine a resolution of the issues in dispute.

dispute the original evaluator is not qualified to decide. Professional engineers and geologists and building contractors can also assist the original neutral evaluator, even if these professionals are not certified neutral evaluators. However, professional engineers and geologists and building contractors can be disqualified from assisting the neutral evaluator on the claim for the same reasons a neutral evaluator can be disqualified.
The bill provides what issues must be contained and decided by the neutral evaluator in the neutral evaluation report. The neutral evaluation report must be sent to all parties and to the DFS within 14 days of the completion of the neutral evaluation conference. If the insurer agrees to comply with the neutral evaluation report, then the sinkhole claim payments made by the insurer must be in accordance with the insurance contract between the insurer and the policyholder.

If the neutral evaluation does not resolve the claim and the claim proceeds to litigation, then the oral testimony and neutral evaluation report must be admitted into evidence in the litigation. Current law requires only the neutral evaluator's written recommendation to be admitted into evidence. Furthermore, if the insurer agrees to comply with the neutral evaluation report, but the policyholder refuses to resolve the sinkhole claim in accordance with the report, the actions of the insurer cannot be considered to be a confession of judgment or admission of liablility.

The bill provides neutral evaluators immunity from suit as agents of the state under s. 44.107, F.S. This is consistent with current law relating to mediators.

The Florida Geological Survey and the Florida Sinkhole Database

The Florida Geological Survey (Survey) within the Department of Environmental Protection (DEP) is the state agency responsible for identifying, tracking, and investigating mines, minerals, sinkholes, the water supply, and other natural resources in the state. The State Geologist, a registered professional geologist, is designated as the head of the Survey.[126]

There is currently no single state agency in Florida with responsibility and authority for sinkhole inspections, although the Survey maintains a database of reported sinkholes. This database is available through the website of the Department of Environmental Protection (DEP), along with a form to be used to report suspected new sinkholes. The Survey reports that it lacks sufficient staff to visit all new sinkholes, although some of the state's water management districts have staff available to check local sinkholes, particularly if they contain water.[127]

The sinkhole database maintained by the Survey dates to the early 1950s, but it contains only those sinkholes officially reported by observers. As a result, the Survey notes the sinkholes reported and included in the database tend to cluster in populated areas where they are readily seen and commonly affect roads and dwellings. However, sinkholes also occur in more remote and less populated areas, and are unseen and unreported.[128]

Section 627.7065, F.S., enacted in 2005,[129] creates a sinkhole information database for the purpose of tracking sinkhole claims made against property insurance policies. The Department of Financial Services (DFS) is primarily responsible for the development of this database, with input from the DEP and the Survey. The DEP must investigate reports of sinkhole activity and report its findings to the DFS sinkhole database.

[126] s. 377.075, F.S.
[127] Florida Geological Survey; Department of Environmental Protection; *Sinkholes: Frequently Asked Questions*, available at http://www.dep.state.fl.us/geology/feedback/faq.htm#9, (last viewed February 27, 2011).
[128] *Id*.
[129] Section 18, Ch. 2005-111, L.O.F.

The DFS can require insurers to report past and present sinkhole claims to the DFS sinkhole database. Administrative rules requiring property insurers to report sinkhole and catastrophic ground cover collapse claim information to the DFS database were promulgated by the DFS in 2009. The rules require all sinkhole and catastrophic ground cover collapse claim information for claims closed by the insurer from January 1, 2005 – April 28, 2010 to be reported to the database by April 28, 2011. In addition, for claims closed after April 28, 2010, insurers must report claim information to the DFS database within 60 days after the claim is closed.[130] According to a representative of the DFS, insurers are complying with the rules and reporting claim information on sinkhole and catastrophic ground cover collapse claims for the DFS sinkhole database.

Although the DFS sinkhole database is not yet available on the internet, information about claims in the database can be obtained by calling the DFS or by filing a public records request with DFS for sinkhole claim information.

This bill repeals the DFS sinkhole database. Accordingly, insurers will no longer have to report sinkhole information to the sinkhole database and information relating to sinkhole and catastrophic ground cover collapse claims filed against property insurance policies will no longer be compiled and kept by the DFS and available to the public.

Guaranty Associations - Background

Chapter 631, F.S., relates to insurer insolvency and guaranty payments and governs the receivership process for insurance companies in Florida. Federal law specifies that insurance companies cannot file for bankruptcy.[131] Instead, they are either "rehabilitated" or "liquidated" by the state. In Florida, the Division of Rehabilitation and Liquidation in the DFS is responsible for rehabilitating or liquidating insurance companies.[132]

Florida operates five insurance guaranty funds to ensure policyholders of liquidated insurers are protected with respect to insurance premiums paid and settlement of outstanding claims, up to limits provided by law.[133] A guaranty association generally is a not-for-profit corporation created by law directed to protect policyholders from financial losses and delays in claim payment and settlement due to the insolvency of an insurance company. A guaranty association accomplishes its mission by assuming responsibility for settling claims and refunding unearned

[130] A Notice of Development of Rulemaking to change the time period for claim reporting to the database was filed on October 8, 2010 with a rule workshop held on October 27, 2010. No proposed rule changes have been published to date.

[131] The Bankruptcy Code expressly provides that "a domestic insurance company" may not be the subject of a federal bankruptcy proceeding. 11 U.S.C. § 109(b)(2). The exclusion of insurers from the federal bankruptcy court process is consistent with federal policy generally allowing states to regulate the business of insurance. See 15 U.S.C. § 1012 (McCarran-Ferguson Act).

[132] Typically, insurers are put into liquidation when the company is insolvent whereas insurers are put into rehabilitation for numerous reasons, one of which is an unsound financial condition. The goal of rehabilitation is to return the insurer to a sound financial condition. The goal of liquidation, however, is to dissolve the insurer. *See* s. 631.051, F.S., for the grounds for rehabilitation and s. 631.061, F.S., for the grounds for liquidation.

[133] The Florida Life and Health Insurance Guaranty Association generally is responsible for claims settlement and premium refunds for health and life insurers who are insolvent. The Florida Health Maintenance Organization Consumer Assistance Plan offers assistance to members of an insolvent Health Maintenance Organization (HMO) and the Florida Workers' Compensation Insurance Guaranty Association is directed by law to protect policyholders of insolvent workers' compensation insurers. The Florida Self-Insurers Guaranty Association protects policyholders of insolvent individual self-insured employers for workers' compensation claims. The Florida Insurance Guaranty Association is responsible for paying claims for insolvent insurers for most remaining lines of insurance, including residential and commercial property, automobile insurance, and liability insurance, among others.

premiums[134] to policyholders. Insurers are required by law to participate in guaranty associations as a condition of transacting business in Florida.

The bill makes changes to the Florida Insurance Guaranty Association which is the guaranty association for property and casualty insurance.

Florida Insurance Guaranty Association (FIGA)
Statutory provisions relating to FIGA, which was created in 1970, are contained in part II of chapter 631, F.S. FIGA operates under a board of directors and is a nonprofit corporation. FIGA is composed of all insurers licensed to sell property and casualty insurance in the state.

By law, FIGA is divided into two accounts:

- the auto liability account and auto physical damage account; and
- the account for all other included insurance lines (the all-other account).[135]

When a property and casualty insurance company becomes insolvent, FIGA is required by law to take over the claims of the insurer and pay the claims of the company's policyholders. This ensures policyholders that have paid premiums for insurance are not left without valid claims being paid. FIGA is responsible for claims on residential and commercial property insurance, automobile insurance, and liability insurance, among others.

The maximum claim amount FIGA will pay is $300,000 but special limits apply to damages to structure and contents on homeowners', condominium, and homeowners' association claims. For damages to structure and contents on homeowners' claims FIGA pays an additional $200,000, for a total of $500,000. For condominium and homeowners' association claims FIGA pays the lesser of policy limits or $100,000 multiplied by the number of units in the association. All claims are subject to a $100 FIGA deductible, in addition to any deductible in the insurance policy.

FIGA obtains funds to pay claims of insolvent insurance companies primarily from the liquidation of assets of these companies done by the Division of Rehabilitation and Liquidation in the Department of Financial Services. FIGA also obtains funds from the liquidation of assets of insolvent insurers domiciled in other states but having claims in Florida.

In addition, after insolvency occurs, FIGA can issue two types of assessments against property and casualty insurance companies to raise funds to pay claims – regular and emergency[136] assessments. FIGA assesses member insurance companies directly for both assessments and the insurance company is allowed by law (s. 631.57(3)(a), F.S.) to pass the assessment on to their policyholders.

FIGA only pays "covered claims" as defined by s. 631.54(3), F.S. Current law provides two exceptions to the definition of "covered claims." One prevents FIGA from paying subrogation, contribution, or indemnification claims of the insolvent insurer. The other exception prevents FIGA from paying claims that have been rejected by another state's guaranty fund for payment because the policyholder's net worth is more than what is allowed under the other state's

[134] The term "unearned premium" refers to that portion of a premium that is paid in advance, typically for six months or one year, and which is still owed on the unexpired potion of the policy.
[135] s. 631.55(2), F.S.
[136] Emergency assessments can only be issued to pay claims of insurers rendered insolvent due to a hurricane.

guaranty law. FIGA cannot pay these claims even if the claim otherwise meets the definition of "covered claim" in Florida law.

The bill adds another exception to the definition of "covered claim" for FIGA. The added exception prevents FIGA from paying sinkhole claims of insolvent insurers but allows payment of sinkhole testing or sinkhole repair up to policy limits. The bill further prohibits FIGA from paying attorney's fees or public adjuster fees associated with sinkhole claims.

II. FISCAL ANALYSIS & ECONOMIC IMPACT STATEMENT

A. FISCAL IMPACT ON STATE GOVERNMENT:

1. **Revenues:**
   None.

2. **Expenditures:**

Creation of Third Degree Felony for Insurance Fraud for Rebating in Sinkhole Claims

The Criminal Justice Impact Conference has not met to determine the prison bed impact of this bill. However, because the bill creates a new third degree felony relating to insurance fraud for rebating in sinkhole claims, there may be a prison bed impact on the Department of Corrections.

Repeal of Sinkhole Database

Repeal of the sinkhole database should not have a fiscal impact on the DFS. The DFS receives no funding or FTEs for the database and implements the database within existing resources.[137]

B. FISCAL IMPACT ON LOCAL GOVERNMENTS:

1. **Revenues:**
   None.

2. **Expenditures:**
   None.

C. DIRECT ECONOMIC IMPACT ON PRIVATE SECTOR:

Impact of Increased Surplus To Obtain And Keep A Certificate of Authority
Certain insurance companies will need more funds to start an insurance company. Likewise, certain licensed insurance companies will need more funds to maintain their licensure. Increased surplus means companies have more funds to pay claims.

Impact of Revisions to Procedure and Payment of Replacement Costs
Revising the procedures relating to payment of replacement costs for property insurance claims for partial dwelling losses ensures policyholders make necessary repairs to their dwellings that

[137] Conversation with representative from DFS on March 2, 2011.

are partially damaged in order to receive full payment on the claim. However, policyholders who do not repair their dwelling will not receive the full replacement cost for the dwelling, even though the policyholder purchased full replacement cost.

If the revisions to the procedure and payment of replacement costs reduce the amount of losses paid by insurers on property claims, rates should correspondingly decrease given the loss reduction.

Impact of Allowing Insurers To Pay Acquisition Costs Without OIR Interference
Insurance agents should benefit under the bill because the OIR is precluded from directly or indirectly impeding or compromising an insurer's right to acquire policyholders, advertise, or appoint agents, including the amount of agent commissions, during a rate filing procedure for property and casualty insurance.

If the OIR has questioned the amount an insurer is paying in acquisition costs and pressured insurers to cut these costs, as representatives of insurance agents allege, and OIR's questioning has resulted in lower costs, then prohibiting OIR from interfering with the payment of these costs may result in higher costs which are included in an insurer's rate filing and correspondingly lead to increased insurance rates.

Impact of Repeal of the Sinkhole Database
The repeal of the sinkhole database will prevent insurance companies from having to expend funds to collect and report the required sinkhole claim information to the database.

Impact of Restricting Public Adjuster Fees
The fee restrictions on reopened or supplemental claims contained in the bill could reduce the income of public adjusters.

The restrictions on public adjuster solicitation could deter policyholders from obtaining the claims adjusting services provided by public adjusters which could reduce the claim payment obtained by the policyholder.

Impact of Changing the Statute of Limitations for Property Insurance Claims
Imposing a 5-year statute of limitations, starting from the date of loss, for property insurance claims will help insurers quantify the amount of exposure on these claims.

Impact of Time Frame for Property Insurance Claims
Imposing a 3-year time period for property insurance claims other than sinkhole claims and a 2-year time period for sinkhole claims to be filed with the insurer will help insurers quantify the amount of exposure on these claims.

Impact of Changes to the Expedited Rate Filing
Because the bill allows residential property insurers to increase rates a maximum of 15 percent, rather than 10 percent, using an expedited rate filing, policyholders could incur increased property insurance premiums. Increased premiums, however, will only be realized if the insurance company incurs reinsurance costs to justify the increased premiums. Furthermore, because the increase would be due to reinsurance costs the insurer would otherwise recover in an annual base rate filing, the rate increase allowed under the changes to the expedited rate filing made by the bill would be the same amount as the rate increase allowed under an annual base rate filing under current law.

Because the bill allows additional types of costs and allows expenses and profits to justify an expedited rate filing, more expedited rate filings requesting the maximum rate increase allowed under an expedited rate filing (15 percent under the bill) could be filed and approved by the OIR. Some policyholders could incur two rate increases at renewal because the bill repeals the two six month filing restrictions in current law for expedited rate filings. However, any rate increase due to the expedited rate filing is limited to 15 percent. In addition, under current law policyholders can incur two rate increases at renewal, but it is the practice of insurers to require policyholders to incur one rate increase.

Allowing more types of costs to be included in an expedited rate filing and raising the rate increase amount allowed by the filing to 15 percent allows property insurers more flexibility in ratemaking with a faster rate approval time.

Impact of Prohibition on Use of A "Use and File" Rate Filing for Property Insurance

Prohibiting insurers from using a "use and file" rate filing for property insurance until May 1, 2012, prevents homeowners from having property insurance rate changes implemented by their insurer that are not justified. Rate changes will only be allowed to be implemented after the OIR reviews the insurer's justification of the rate change and approves the change.

Impact of Changing Sinkhole Laws

Taken as a whole, the revisions to the sinkhole laws provided by the bill should reduce the number of sinkhole claims and disputes, ultimately reducing the costs associated with such claims. The revisions also provide for a more thorough and meaningful neutral evaluation which may cause more resolution of sinkhole claims by neutral evaluation.

Policyholders who elect to drop sinkhole loss coverage from the base property insurance policy and have only catastrophic ground cover collapse coverage in the base policy should incur reduced premium costs for property insurance.

In limited instances, policyholders could incur fees and costs associated with sinkhole testing and reports.

Policyholders have to abide by the 90-day and 12-month time periods for sinkhole repair provided in the bill.

Adding a definition of "structural damage" to the sinkhole law should reduce sinkhole claims and give insurers more certainty regarding whether a sinkhole claim is covered.

Allowing catastrophic ground cover collapse and sinkhole loss coverage to apply to only principal buildings should reduce sinkhole claim costs and sinkhole exposure for insurers.

D. FISCAL COMMENTS:

None.