

The Florida Senate
BILL ANALYSIS AND FISCAL IMPACT STATEMENT

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

Prepared By: The Professional Staff of the Committee on Banking and Insurance

BILL: SB 416

INTRODUCER: Senator Simpson

SUBJECT: Sinkhole Coverage

DATE: January 10, 2014

REVISED: _____

	ANALYST	STAFF DIRECTOR	REFERENCE	ACTION
1.	Knudson	Knudson	BI	Pre-meeting
2.			AGG	
3.			AP	

I. Summary:

SB 416 directs Citizens to establish the Citizens Sinkhole Stabilization Repair Program (Program). The bill states that the program is being created because the public interest is served by the performance of sinkhole repairs. All covered sinkhole loss claims made on a Citizens policy will be governed by the Program as of March 31, 2015. The Program must be managed by Citizens or a third-party administrator.

Under the Program, stabilization repair contractors are approved by Citizens to participate in the program if they meet statutory requirements. Approved stabilization repair contractors must contract with Citizens to perform stabilization repairs for a fixed price.

Each covered sinkhole loss claim is submitted to the approved stabilization contractors who have the opportunity to submit itemized offers to Citizens to the stabilization repairs recommended in the engineering report. Citizens then provides a list of contractors to the policyholder, based on quality, cost-effectiveness, and other criteria. The policyholder has 30 days to select a listed contractor. If the policyholder does not make a selection within 30 days, Citizens shall select the contractor. If an approved stabilization repair contractor does not offer to perform repairs within policy limits, Citizens may either resubmit the loss to the program or pay up to the policy limits to the policyholder.

Repairs must be warranted by the stabilization repair contractor for at least 5 years. The policyholder's sole remedy is the specific performance of sinkhole stabilization repairs in a dispute with Citizens over the method or extent of stabilization repairs. Citizens' liabilities under the Repair Program are limited to the policyholder's policy limits.

The bill also requires each residential insurance policy that provides coverage for sinkhole loss to include a deductible of 1 percent, 2, percent, 5 percent, or 10 percent of the policy dwelling limits.

II. Present Situation:

Sinkhole Insurance

Insurers offering property insurance must make available to policyholders, for an appropriate additional premium, sinkhole coverage for losses on any structure, including personal property contents.¹ Sinkhole coverage includes repairing the home, stabilizing the underlying land, and foundation repairs.² Insurance companies must also provide coverage for catastrophic ground cover collapse.³ Insurers may restrict catastrophic ground cover collapse and sinkhole loss coverage to the principal building as defined in the insurance policy.⁴ An insurer may require a property inspection prior to issuing sinkhole loss coverage.⁵ Residential property insurance policies may include deductibles applicable to sinkhole losses of 1 percent, 2, percent, 5 percent, or 10 percent of the policy dwelling limits and must provide a corresponding premium discount with each deductible amount.⁶ All Citizens sinkhole loss policies, however, have a 10 percent deductible.⁷

Sinkhole coverage is payable when a “sinkhole loss” occurs.⁸ A sinkhole loss is defined in statute as structural damage to the covered building, including the foundation, caused by sinkhole activity.⁹ Five distinct types of damage constitute structural damage, and each type of damage is tied to standards contained in the Florida Building Code or used in the construction industry.¹⁰ “Sinkhole activity” is the settlement or systematic weakening of the earth supporting the covered building that results from contemporaneous movement or raveling of soils, sediments, or rock into subterranean voids created by the effect of water on a limestone or similar rock formation.¹¹ Accordingly, in order for the policyholder to obtain policy benefits for sinkhole loss, the insured structure must sustain structural damage that is caused by sinkhole activity.

Sinkhole insurance claims increased substantially both in number and cost over the past 2 decades and most dramatically from 2009 to 2011.¹² According to data submitted in 2011 by 211

¹ S. 627.706(1)(b), F.S.

² See s. 627.706(5), F.S. Contents coverage is also available and, if included, paid in accordance with policy terms

³ S. 627.706(1)(a), F.S. Catastrophic ground cover collapse refers to extreme damage in which a property is essentially destroyed and uninhabitable. A catastrophic ground cover collapse occurs when geological activity causes the abrupt collapse of the ground cover, a depression in the ground cover clearly visible to the naked eye, structural damage to the covered building and its foundation, and the insured structure being condemned and ordered to be vacated by the governmental entity authorized to give such an order.

⁴ S. 627.706(1)(c), F.S.

⁵ S. 627.706(a)(b), F.S.

⁶ See *id.*

⁷ Citizens Property Insurance Corporation, *Sinkhole Loss Coverage Frequently Asked Questions for Policyholders*, pg. 5. https://www.citizensfla.com/shared/faqs/SinkholeFAQs_for_Consumers.pdf (Last accessed by Banking and Insurance Staff on January 13, 2014).

⁸ See s. 627.707(5), F.S.

⁹ S. 627.706(2)(j), F.S.

¹⁰ S. 627.706(2)(k), F.S.

¹¹ S. 627.706(2)(i), F.S.

¹² See Office of Insurance Regulation, *Report on Review of the 2010 Sinkhole Data Call*, (Nov. 8, 2010). http://www.floir.com/siteDocuments/Sinkholes/2010_Sinkhole_Data_Call_Report.pdf (Last accessed by Banking and Insurance Staff on January 13, 2014).

property insurers to the Office of Insurance Regulation (OIR), the insurers' total reported claims increased from 2,360 in 2006 to 6,694 in 2010, totaling 24,671 claims throughout that period.¹³ Total sinkhole claim costs for these insurers amounted to approximately \$1.4 billion for the same period.¹⁴

The 2011 Legislature enacted legislation in (CS/CS/CS/SB 408) to address the large increases in sinkhole policyholder premiums and losses.¹⁵ The 2011 reform bill changed the definition of structural damage that is used to determine if a sinkhole loss occurred, revised the process for investigating sinkhole losses, and enacted a number of reforms aimed at reducing fraud and unnecessary costs related to sinkhole loss coverage.

Investigation of Sinkhole Claims

The 2011 legislative sinkhole reforms substantially revised the statutory process for investigating sinkhole claims in s. 627.707, F.S.¹⁶ The process requires the insurer to determine whether the building has incurred structural damage that has been caused by sinkhole activity.¹⁷ Coverage for sinkhole loss is not available if structural damage is not present or sinkhole activity is not the cause of structural damage. The new process is as follows:

Initial Inspection & Structural Damage Determination: Upon receipt of a claim for sinkhole loss, the insurer must inspect the policyholder's premises to determine if there has been structural damage which may be the result of sinkhole activity.¹⁸ This inspection will often require the insurer to retain a professional engineer to evaluate whether the insured building has incurred structural damage as defined by statute.

Sinkhole Testing: The insurer is required to engage a professional engineer or professional geologist to conduct sinkhole testing pursuant to s. 627.7072, F.S., if the insurer confirms that structural damage exists and is either unable to identify a valid cause of the structural damage or discovers that the structural damage is consistent with sinkhole loss.¹⁹ If coverage is excluded under the policy even if sinkhole loss is confirmed, then the insurer is not required to conduct sinkhole testing.²⁰

Notice to the Policyholder: The insurer must provide written notice to the policyholder detailing what the insurer has determined to be the cause of damage (if the determination has been made) and a statement of the circumstances under which the insurer must conduct sinkhole testing.²¹ The policyholder must also be notified of his or her right to demand sinkhole testing and the circumstances under which the policyholder may incur costs associated with testing.²²

¹³ See *id.* at pg. 5.

¹⁴ See *id.*

¹⁵ Ch. 2001-39, L.O.F.

¹⁶ See fn. 15.

¹⁷ S. 627.707(1), F.S.

¹⁸ See *id.*

¹⁹ S. 627.707(2), F.S.

²⁰ See *id.*

²¹ S. 627.707(3), F.S.

²² See *id.*

Authorization to Deny Sinkhole Claim: Insurers deny the claim upon a determination that there is no sinkhole loss.²³

Policyholder Demand for Sinkhole Testing: The policyholder may demand sinkhole testing in writing within 60 days after receiving a claim denial if the insurer denies the claim without performing sinkhole testing and coverage would be available if a sinkhole loss is confirmed (i.e. the claim denial was not issued due to policy conditions or exclusions of coverage and instead was based the failure of the loss to meet the definition of sinkhole loss).²⁴ However, if the policyholder requests such testing, it must pay the insurer 50 percent of the sinkhole testing costs up to \$2,500.²⁵ If the requested testing confirms a sinkhole loss the insurer must reimburse the testing costs to the policyholder.²⁶

Payment of Sinkhole Claims

If a covered building suffers a sinkhole loss or catastrophic ground cover collapse, the insured must repair such damage in accordance with the insurer's professional engineer's recommended repairs.²⁷ However, if repairs cannot be completed within policy limits, the insurer has the option to either pay to complete the recommended repairs or tender policy limits without a reduction for any repair expenses already incurred.²⁸ The insurer may limit payment to the actual cash value of the sinkhole loss not including below-ground repair techniques until the policyholder enters into a contract for the performance of building stabilization repairs.²⁹

The two most commonly recommended stabilization techniques are grouting and underpinning.³⁰ Under the grouting procedure, a grout mixture (either cement-based or a chemical resin that expands into foam) is injected into the ground to stabilize the subsurface soils to minimize further subsidence damage by increasing the density of the soils beneath the building as well as sealing the top of the limestone surface to minimize future raveling.³¹ Underpinning consists of steel piers drilled or pushed into the ground to stabilize the building's foundation.³² One end of the steel pipe connects to the foundation of the structure with the other end resting on solid limestone. Underpinning repairs, when performed, are usually combined with grouting.

The contract for below-ground repairs must be made in accordance with the recommendations set forth in the insurer's sinkhole report issued pursuant to s. 627.7073, F.S., and must be entered into within 90 days after the policyholder receives notice that the insurer has confirmed coverage for sinkhole loss.³³ The time period is tolled if either party invokes neutral evaluation.

²³ S. 627.707(4)(a), F.S.

²⁴ S. 627.707(4)(b), F.S.

²⁵ S. 627.707(4)(b)2., F.S.

²⁶ S. 627.707(4)(b)3., F.S.

²⁷ S. 627.707(5), F.S.

²⁸ See *id.*

²⁹ S. 627.707(5)(a), F.S.

³⁰ Citizens Property Insurance Corporation, Sinkhole Repairs: Underpinning and Grouting, (Oct. 30, 2012). <https://www.citizensfla.com/shared/sinkhole/documents/GroutVersusUnderpinning.pdf> (Last accessed by Banking and Insurance Staff on January 13, 2014).

³¹ See *id.*

³² See *id.*

³³ See s. 627.707(5)(b), F.S.

Stabilization and all other repairs to the structure and contents must be completed within 12 months after the policyholder enters into the contract for repairs unless the insurer and policyholder mutually agree otherwise, the claim is in litigation, or the claim is in neutral evaluation, appraisal or mediation.³⁴

Sinkhole Claims – Citizens Property Insurance Corporation

The number of Citizens Property Insurance Corporation (Citizens) sinkhole claims is dropping in the aftermath of the 2011 sinkhole reforms. Citizens' sinkhole claim activity had increased from 1590 claims in 2009 to 4,605 in 2011.³⁵ After the legislative reforms, new Citizens sinkhole claims dropped to 2386 in 2012 and a projected 900 claims in 2013, an estimated 80 percent drop in claims from 2011.³⁶

Citizens' sinkhole claim activity from 2009 to 2013 is concentrated in Hernando, Hillsborough, Pasco, and Pinellas counties.³⁷ Miami-Dade, Broward, and Palm Beach counties also produced a significant number of sinkhole claims and had generally higher percentages of claims filed on sinkhole policies.³⁸ Approximately 90 percent of sinkhole claim litigation is from claims on properties located in Hernando, Pasco, and Hillsborough counties. A sample of 204 sinkhole claims in litigation by Citizens on August 31, 2013, indicated that over 56 percent of such claims are in litigation over issues related to Citizens efforts to repair the damaged property.

Though the costs associated with Citizens sinkhole loss claims has decreased, such claims continue to negatively affect the financial stability of Citizens and private market insurers.³⁹ Increased sinkhole claim losses has often made residential property insurance increasingly unaffordable or unavailable for consumers.

The Citizens Board of Governors considered the creation of a sinkhole stabilization managed repair program at its December 12, 2003 meeting.⁴⁰ The program would be similar to the program that would be created if SB 416 becomes law, with the primary difference being that Citizens policyholders would not be required to participate. Citizens solicited sinkhole repair

³⁴ See *id.*, and s. 627.707(5)(d), F.S.

³⁵ Citizens Property Insurance Corporation, *Litigation Analysis*, pg. 8. (October 2013). <http://miamiherald.typepad.com/files/corrected-citizens-litigation-analysis---final---oct-11-2013.pdf> (Last accessed by Banking and Insurance Staff on January 13, 2014).

³⁶ See *id.*

³⁷ The total number of sinkhole claims in these counties from January 1, 2009 to August 31, 2013 are: Hernando County (4947), Pasco County (2,817), Hillsborough (2,180), Pinellas (1,039). The percentage of sinkhole policies in each county that experienced a claim during this period is 3 percent in Hernando County, 6 percent in Pasco County, 5 percent in Hillsborough County, and 10 percent in Pinellas County.

³⁸ Miami-Dade had 419 sinkhole claims, but 19 percent of sinkhole policies in that county had a sinkhole claim from January 1, 2009 to August 31, 2013. Broward County had 291 claims on 14 percent of sinkhole policies and Palm Beach County had 114 claims on 10% of sinkhole policies.

³⁹ Citizens, in its 2014 Rate Filing Kit, detailed that the indicated rate change for sinkhole coverage was for an increase of 451 percent in Hernando County, 177 percent in Pasco County, and 235 percent in Hillsborough County. http://static-lobbytools.s3.amazonaws.com/press/59997_citizens_2014_rate_kit.pdf (Last accessed by Banking and Insurance Staff on January 13, 2014).

⁴⁰ Citizens Property Insurance Corporation, Action Item Summary: Sinkhole Stabilization Managed Repair Program (Dec. 13, 2013). https://www.citizensfla.com/bnc_meet/docs/500/05Ab_AI_Sinkhole_MRP_12_13_13.pdf (Last accessed by Banking and Insurance Staff on January 13, 2014).

contractors who would participate in the managed repair program through an initial Invitation to Bid (ITB No. 13-0020) and subsequently issued an additional Invitation to Bid (ITB No. 13-0028) for additional vendors dated January 8, 2014. Citizens' staff recommended that the Citizens' Claims Committee approve and recommend to the Board of Governors that Citizens' staff pursue contracts with vendors that would allow the implementation of a sinkhole stabilization managed repair program.⁴¹ Such contracts would not exceed \$50 million. Citizens' staff noted that the vendor contracts would not cause additional expenses because vendors will be paid through the claims indemnity process.⁴²

In an effort to settle sinkhole claim disputes over the method of sinkhole repairs, Citizens began in December 2013 sending letters to hundreds of its policyholders who are disputing the repair recommendations on their sinkhole claims.⁴³ The letters are targeted to policyholders who have a confirmed sinkhole loss for which the professional engineer who verified a sinkhole loss has recommended grouting repairs but not underpinning. The letters encourage policyholders to have the necessary repair work completed in accordance with the engineer's recommendations. Citizens is also encouraging policyholders to resolve differing engineering opinions through the neutral evaluation process in s. 627.7074, F.S. Citizens estimates that of its 2,100 disputed sinkhole claims, 1,329 deal with disagreements over repair methods.⁴⁴

III. Effect of Proposed Changes:

Citizens Sinkhole Stabilization Repair Program [s. 627.351(6)(ff), F.S.]

Section 1 directs Citizens to establish the Citizens Sinkhole Stabilization Repair Program (Program). The bill states that the program is being created because the public interest is served by the performance of sinkhole repairs. All covered sinkhole loss claims made on a Citizens policy will be governed by the Program as of March 31, 2015. The Program must be managed by Citizens or a third-party administrator.

Under the Program, stabilization repair contractors are approved by Citizens to participate in the program if they meet statutory requirements. Approved stabilization repair contractors must contract with Citizens to perform stabilization repairs for a fixed price.

Each covered sinkhole loss claim is submitted to the approved stabilization contractors who have the opportunity to submit itemized offers to Citizens to the stabilization repairs recommended in the engineering report. Citizens then provides a list of contractors to the policyholder, based on quality, cost-effectiveness, and other criteria. The policyholder has 30 days to select a listed contractor. If the policyholder does not make a selection within 30 days, Citizens shall select the contractor. If an approved stabilization repair contractor does not offer to perform repairs within policy limits, Citizens may either resubmit the loss to the program or pay up to the policy limits to the policyholder.

⁴¹ See *id.*

⁴² See *id.*

⁴³ Citizens Property Insurance Corporation, *Citizens Chairman: Settlement Proposal Benefits Consumers*, (Press Release Dated Dec. 12, 2013). <https://www.citizensfla.com/shared/press/articles/135/12.12.2013.pdf> (Last accessed by Banking and Insurance Staff on January 13, 2014).

⁴⁴ See *id.*

Repairs must be warranted by the stabilization repair contractor for at least 5 years. The policyholder's sole remedy is the specific performance of sinkhole stabilization repairs in a dispute with Citizens over the method or extent of stabilization repairs. Citizens' liabilities under the Repair Program are limited to the policyholder's policy limits.

The following provides a detailed explanation of the provisions of the Repair Program:

Prohibition against Requiring Citizens Policyholders to Advance Sinkhole Repair Costs [s. 627.351(6)(ff)2.a., F.S.]

Citizens is prohibited from requiring a policyholder from advancing the cost of sinkhole repairs.

Stabilization Repair Contractor - Qualification Requirements [s. 627.351(6)(ff)2.b., F.S.]

Each stabilization repair contractor approved by Citizens must be qualified based on the following criteria:

- Experience in stabilizing sinkhole activity pursuant to requirements established by Citizens;
- Certification as a contractor under s. 489.113(1), F.S.;
- Demonstrating the capacity to be bonded and actually providing required performance, surety, or other bonds, which may be supplemented by additional requirements;
- Demonstrating the ability to meet insurance coverage required by Citizens, including commercial general liability and workers' compensation insurance;
- Maintaining a valid drug-free workplace program; and
- Other requirements established by Citizens.

Stabilization Repair Contract [s. 627.351(c)(ff)2.d., F.S.]

Citizens must develop a standard stabilization repair contract that requires:

- The stabilization repair contractor to be paid a fixed price to complete the stabilization repairs identified in the engineering report;
- The stabilization repair contractor to post a payment bond in favor of Citizens for each project assigned and to post a performance bond in favor of Citizens in the amount of the total cost of all fixed-price repairs annually awarded to the contractor;
- The stabilization repair contractor must provide a warranty of at least 5 years to the policyholder. The warranty must be secured by a third-party surety;
- The engineer must monitor the performance of stabilization repairs and confirm their completion and that no further repairs are required;
- The stabilization repair contract must perform any additional repairs found necessary by the engineer. The repairs must be performed at no cost to the policyholder or Citizens;

Process for Selection of Stabilization Repair Contractors [s. 627.351(c)(ff)2.e., F.S.]

Citizens must establish a process for the selection of a stabilization repair contractor that includes:

- An opportunity for all stabilization repair contractors within the Citizens stabilization repair pool to submit an offer to perform the repairs recommended in the engineering report. The offer must include an itemized statement of work.
- Citizens must review the contractors' offers and provide the policyholder with a list of stabilization repair contractors. Citizens may include contractors on the list based on quality, cost-effectiveness, and other criteria.
- The policyholder has 30 days to select a stabilization repair contractor. If the policyholder does not select a contractor within 30 days, Citizens does.
- If no contractors offer to perform stabilization repairs or all such offers exceed the policy limit, Citizens may resubmit the property to the repair process. Alternatively, Citizens may pay the policyholder an amount up to the policy limits on the structure.

Citizens Liability Under the Sinkhole Stabilization Repair Program [s. 627.351(6)(ff)3. and 4., F.S.]

The bill limits Citizens legal responsibilities under the stabilization repair program. Citizens is not responsible for serving as a stabilization repair contractor. Citizens' obligations under the repair program are not an election to repair by Citizens and do not create a new contractual relationship between a policyholder and Citizens.

Citizens is not obligated to the policyholder for more than the policy limits.

Specific Performance of Repairs Policyholder's Sole Remedy [s. 627.351(6)(ff)6., F.S.]

If a dispute arises between a policyholder and Citizens regarding the type of stabilization repairs or their extent, the policyholder's sole remedy is the specific performance of repairs.

Repairs Other Than Sinkhole Stabilization [s. 627.351(6)(ff)5. and 7., F.S.]

Citizens must pay for repairs other than sinkhole stabilization to the structure and contents in accordance with the terms of the policyholder's insurance policy. The sinkhole repair program statute does not prohibit Citizens from establishing managed repair programs for other repairs to the structure in accordance with the terms of the insurance policy.

The Repair Program Supersedes the Statutory Process for the Investigation and Payment of Sinkhole Loss Claims [s. 627.351(6)(ff)8., F.S.]

The sinkhole repair program statute supersedes the provisions of s. 627.707(5)(a)-(d), F.S., which contain the statutory criteria for the investigation and payment of sinkhole loss claims.

Citizens Reports on Residential Sinkhole Loss Coverage [s. 627.351(6)(ee), F.S.]

Citizens must submit a report to the OIR detailing the requests it receives for residential sinkhole loss coverage. The report must be submitted at least once every 6 months. Citizens must report the number of requests for residential sinkhole loss coverage received, the number of sinkhole loss coverage requests accepted or declined, and Citizens' reasons for declining requests for residential sinkhole coverage.

Deductibles for Sinkhole Loss Coverage [s. 627.706(1), F.S.]

Section 2 amends s. 627.706(1), F.S., to require that each residential insurance policy that provides coverage for sinkhole loss must include a deductible of 1 percent, 2, percent, 5 percent, or 10 percent of the policy dwelling limits.

Effective Date

Section 3 provides an effective date of July 1, 2014.

IV. Constitutional Issues:**A. Municipality/County Mandates Restrictions:**

None.

B. Public Records/Open Meetings Issues:

None.

C. Trust Funds Restrictions:

None.

V. Fiscal Impact Statement:**A. Tax/Fee Issues:**

None.

B. Private Sector Impact:

Citizens policyholders only remedy under this bill will be limited to the specific performance of sinkhole repairs. Citizens' policyholders may benefit from the quick performance of repairs. If sinkhole loss costs are reduced by the program, premium increases for Citizens sinkhole insurance may be reduced.

C. Government Sector Impact:

Citizens' staff has recommended to the Citizens Board of Governors the pursuit of vendor to serve as sinkhole repair contractors for the purpose of establishing a sinkhole stabilization managed repair program. Vendors would be paid through the claim indemnity process (i.e. for repairs performed) and thus Citizens staff does not consider the vendor contracts an additional expense to Citizens.

VI. Technical Deficiencies:

None.

VII. Related Issues:

None.

VIII. Statutes Affected:

This bill substantially amends the following sections of the Florida Statutes: 627.351, 627.706

IX. Additional Information:

A. Committee Substitute – Statement of Changes:

(Summarizing differences between the Committee Substitute and the prior version of the bill.)

None.

B. Amendments:

None.

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