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 Fiscal Policy

BILL: CS/CS/SB 940

INTRODUCER: Commerce and Tourism Committee; Banking and Insurance Committee; and Senator Bradley

SUBJECT: Title Insurance

DATE: February 3, 2016 REVISED:

	ANALYST	STAFF DIRECTOR	REFERENCE	ACTION
1.	Billmeier	Knudson	BI	**Fav/CS**
2.	Little	McKay	CM	**Fav/CS**
3.	Pace	Hrdlicka	FP	**Pre-meeting**

Please see Section IX. for Additional Information:

COMMITTEE SUBSTITUTE - Substantial Changes

I. Summary:

CS/CS/SB 940 changes the unearned premium reserve requirement for title insurers that are members of an insurance holding company system having $1 billion or more in surplus as to policyholders and have a financial strength rating of "superior," "excellent," "exceptional," or an equivalent rating by a rating agency acceptable to the Office of Insurance Regulation.

The bill removes the requirement that a title insurer that transfers its domicile to Florida must set an unearned premium reserve and release its unearned premium reserve under the laws of its previous domicile state. Instead, the bill requires a title insurer that transfers its domicile to Florida to calculate an adjusted statutory or unearned premium reserve as if, on the effective date of redomestication, the insurer had been domesticated in Florida for the previous 20 years and authorizes the release of such reserve.

The bill is not anticipated to have an impact on state funds.

II. Present Situation:

Title insurance is (1) insurance of owners of real property or others having an interest in real property or contractual interest derived therefrom, or liens or encumbrances on real property, against loss by encumbrance, defective titles, invalidity, or adverse claim to title; or (2) insurance of owners and secured parties of the existence, attachment, perfection, and priority of security interests in personal property under the Uniform Commercial Code.[1] Title insurance serves to indemnify the insured against financial loss caused by defects in the title arising out of events that occurred before the date of the policy.[2]

Title insurance agents and agencies are licensed and regulated by the Department of Financial Services (DFS), while title insurance companies are licensed and regulated by the Office of Insurance Regulation (OIR).[3]

Title Insurance Reserve Requirements

Insurance companies must maintain adequate reserves (cash or liquid assets) to pay claims and satisfy other liabilities and must report its reserves to the OIR.[4] Generally, an insurer's reserve is a fund of capital that it keeps to meet its best estimate of known or expected losses for claims on policies it has written or assumed.[5] A title insurer must maintain two types of reserves. First, a title insurer must maintain reserves sufficient to pay all of its unpaid losses.[6] Second, a title insurer must maintain a guaranty fund or unearned premium reserve to be used for reinsurance in the event the insurer becomes insolvent.[7]

Since 2014,[8] Florida has implemented different unearned premium reserve requirements depending on whether a title insurer has $50 million or more in surplus.[9] For title insurers with less than $50 million in surplus, the unearned premium reserve must consist of at least the sum of:

- For unearned premiums for policies written or title liability assumed in reinsurance before July 1, 1999, a reserve equal to the reserve established on June 30, 1999;[10]
- A total amount equal to 30 cents for each $1,000 of net retained liability[11] for policies written or title liability assumed in reinsurance on or after July 1, 1999.
- An additional amount, if deemed necessary by a qualified actuary.[12]

[1] Section 624.608, F.S.
[2] *See Lawyers Title Insurance Co., Inc., v. Novastar Mortgage, Inc.*, 862 So.2d 793, 797 (Fla. 4th DCA 2003).
[3] *See* ss. 626.016, 626.8417, 624.404, and 626.8418, F.S.
[4] Section 624.424, F.S.
[5] INSURANCE INFORMATION INSTITUTE, *Glossary: Reserve*, http://www.iii.org/services/glossary (last viewed Nov. 25, 2015).
[6] *See* ss. 625.041(2) and 625.111, F.S.
[7] *See* s. 625.111, F.S. "It is common for title defects to go undiscovered many years after the issuance of a title insurance policy. The purpose of the statutory or unearned premium reserve is to provide a fund for the payment of these late-reported claims." *See infra* note 21 at 8.
[8] The reserve requirements were changed by ch. 2014-132, L.O.F.
[9] The capital and surplus of an insurance company is sometimes referred to as "surplus as to policyholders" or "policyholders' surplus." Policyholders' surplus is equal to net admitted assets, or admitted assets minus liabilities. *See* ss. 627.778(2), and 624.408, F.S.
[10] For domestic title insurers, the amounts must be calculated according to law in effect at the time the associated premiums were written or assumed and as amended prior to July 1, 1999.
[11] Section 625.111(6)(b), F.S., defines "net retained liability" as the "total liability retained by a title insurer for a single risk, after taking into account the deduction for ceded liability, if any."
[12] Section 625.111(1)(a),(b), and (d), F.S.

For title insurance with $50 million or more in surplus, the unearned premium reserve must be the sum of:

- A minimum of 6.5 percent of the total of (1) direct premiums written and (2) premiums for reinsurance assumed, plus other income, less premiums for reinsurance ceded as displayed in Schedule P of the title insurer's most recent annual statement filed with the OIR.
- An additional amount, if deemed necessary by a qualified actuary.[13]

Releasing Unearned Premium Reserve

Title insurance policies cover an exceptionally long period of risk, therefore, the conversion of reserves to surplus capital occurs quarterly over a period 20 years.[14] Section 625.111, F.S., sets the following schedule for release of reserves. Once the reserve money is released, it is available for use by the title insurer. For policies written before July 1, 1999, an insurer must release:

- 30 percent of the initial aggregate sum during 1999;
- 15 percent during calendar year 2000;
- 10 percent during each of calendar years 2001 and 2002;
- 5 percent during each of calendar years 2003 and 2004;
- 3 percent during each of calendar years 2005 and 2006;
- 2 percent during each of calendar years 2007-2013; and
- 1 percent during each of calendar years 2014-2018.[15]

For policies written on or after July 1, 1999, an insurer must release:

- 30 percent of the initial sum during calendar year next succeeding the year the premium was written
- 15 percent during the next succeeding year;
- 10 percent during each of the next succeeding 2 years;
- 5 percent during each of the next succeeding 2 years;
- 3 percent during each of the next succeeding 2 years;
- 2 percent during each of the next succeeding 7 years; and
- 1 percent during each of the next succeeding 5 years.[16]

For companies with more than $50 million in surplus, the title insurer must release:

- 35 percent of the initial sum during the year following the year the premium was written or assumed;
- 15 percent during each year of the next succeeding 2 years;
- 10 percent during the next succeeding year;
- 3 percent during each of the next succeeding 3 years;
- 2 percent during each of the next succeeding 3 years; and
- 1 percent during each of the next succeeding 10 years.[17]

[13] Section 625.111(1)(c) and (d), F.S.
[14] Section 625.111(2)(a), F.S.
[15] Section 625.111(2)(a), F.S.
[16] Section 625.111(2)(b), F.S.
[17] Section 625.111(2)(c), F.S.

Reserve Requirement When a Title Insurer Moves to Florida

Currently, a title insurer organized under the laws of another state that transfers its domicile to Florida has the same unearned premium reserve requirement as set by the laws of the title insurer's former state of domicile. The reserve is released according to the requirements of law in effect in the former state at the time of domicile. For business written after January 1, 2014, the title insurer must add to and set aside in the statutory or unearned premium reserve the appropriate amount as determined by the company's surplus.[18]

Rating Agencies

Rating agencies issue financial strength ratings for insurance companies. The opinions of rating agencies such as Standard & Poor's, Moody's Investors Service, Fitch Ratings, A.M. Best Company, and Demotech are used by the OIR in regulation of the insurance industry.[19] Financial strength ratings are an attempt by the rating agencies to judge whether an insurance company can survive an economic downturn or meet policy obligations.[20] For example, the A.M. Best Company ratings range from "A+" to "D." A rating of A- or higher by A.M. Best Company is considered "superior" or "excellent" under that company's rating system. Under the Demotech rating system ratings range from "A''" to "M," with an "A" rating considered "exceptional".

III. Effect of Proposed Changes:

The bill allows title insurers that are members of an insurance holding company system having $1 billion or more in surplus as to policyholders and a "superior," "excellent," "exceptional," or equivalent financial strength rating, as determined by a rating agency acceptable to the OIR, to set an unearned premium reserve in the same manner as companies with $50 million or more in surplus as to policyholders. This unearned premium reserve requirement will give smaller insurers access to additional surplus capital if they are members of larger holding companies.

The bill removes the requirement that a title insurer that transfers its domicile to Florida must set an unearned premium reserve and release its unearned premium reserve under the laws of its previous domicile state. Instead, the bill requires a title insurer that transfers its domicile to Florida to calculate an adjusted statutory or unearned premium reserve as if, on the effective date of redomestication, the insurer had been domesticated in Florida for the previous 20 years.

If the calculated adjusted statutory or unearned premium reserve exceeds the amount set aside for statutory or unearned premiums in the insurer's annual statement, then the insurer is required to increase its statutory or unearned premium reserve by an amount equal to one sixth of the excess over a specific timeframe. However, if the adjusted statutory or unearned premium is less than the aggregate amount set aside for statutory or unearned premiums in the insurer's annual statement, the insurer can release the excess into surplus.

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[18] Section 625.111(3), F.S.

[19] *See* s. 624.610(3)(e), F.S.

[20] Demotech, Inc., Financial Stability Ratings Definitions, available at http://www.demotech.com/fsr_definitions.asp; and A.M. Best Company, Best's Financial Strength Rating Guide, (version 061515) available at http://www.ambest.com/ratings/guide.pdf (both sites last accessed January 28, 2016).

The new reserve and release requirements for a title insurer that transfers its domicile to Florida conform to the provisions under the National Association of Insurance Commissioner's Title Insurance Model Act.[21]

This bill takes effect July 1, 2016.

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:

This bill could allow some title insurers to have access to additional surplus capital due to revised reserve requirements.

C. Government Sector Impact:

The OIR does not anticipate a fiscal impact on the agency due to this bill.

VI. Technical Deficiencies:

None.

VII. Related Issues:

None.

VIII. Statutes Affected:

This bill substantially amends section 625.111 of the Florida Statutes.

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[21] The purpose of the model act is to provide effective regulation and supervision of title insurance and title insurers. *See* National Association of Insurance Commissioners, *Title Insurers Model Act*, MDL-628 (April 1996) p. 8-9, *available at* http://naic.org/store/free/MDL-628.pdf (last accessed January 28, 2016).

IX. Additional Information:

A. Committee Substitute – Statement of Substantial Changes:

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

CS/CS by Commerce and Tourism on January 25, 2016:
The CS amends the bill to require a title insurer that transfers its domicile to Florida to calculate an adjusted statutory or unearned premium reserve as if, on the effective date of redomestication, the insurer had been domesticated in Florida for the previous 20 years.

CS by Banking and Insurance on January 11, 2016:
The CS allows a title insurer that is a member of an insurance holding company system that has $1 billion or more in surplus and a superior, excellent, exceptional or equivalent financial strength rating from a rating agency acceptable to the OIR to have different reserve requirements from companies with less than $50 million in surplus. The original bill only applied to companies with a specified rating by the A.M. Best Company. The CS allows companies to use different rating agencies if the agency is acceptable to the OIR.

B. Amendments:

None.

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