**The following three articles appeared in the Florida Underwriter Magazine, as notated below, and forwarded to JS by The Florida Insurance News on Friday July 1, 2011. They are reproduced here because they appear to give a full and accurate overview of the current situation regarding assessments and exposure for Florida's citizens, those insured in the residual market and those not insured there. JS did not have any input into the articles and is providing them here for informational purposes and reference only.**

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**Florida Underwriter Magazine**

**New Figures Disclose Citizens Property Insurance Corp.'s Strengths, Weaknesses**

**By Gary Fineout**

**July 2011**

So if the "Big One" finally hits Florida, how much will it cost the average homeowner?

A lot, according to an analysis developed by Citizens Property Insurance Corp.

The state-created insurance carrier was asked to draw up detailed numbers for Gov. Rick Scott and members of the Florida Cabinet that would spell out just how much more policyholders-those in and out of Citizens-would have to pay if a large hurricane strikes.

Those homeowners with Citizens' policies could find themselves paying $1,000 more in the first year following a 1-in-100 year storm. That's the amount that they would pay between increased charges on both their property insurance policy and other assessments that can be placed on other types of coverage, including auto insurance policies. Those not insured by Citizens could still wind up paying as much as $323 more in assessments.

The study shows that Floridians could be paying an additional $39 to $47 per year on auto insurance policies after that first year for the next 29 years.

"Someone is going to pay the piper here,'' said Cabinet member and Chief Financial Officer Jeff Atwater.

Scott and the Cabinet asked for the analysis as part of an effort to understand the consequences if Citizens had to pay out huge claims associated with a large hurricane.

Since his days on the campaign trail the governor has been advocating making changes to Citizens to transform it once again into the state's insurer of last resort. Citizens right now is the state's largest property insurer with 1.35 million policyholders and a total exposure of $460 billion.

Lawmakers did not make any substantial changes to Citizens this past session, and Scott says that he wants more done to reduce its exposure.

"I don't think we'll be there until we have a robust system again and when Citizens is the insurance company of last resort,'' Scott said.

**Sizable Assets**

It's not that Citizens doesn't have a fair amount of resources to tap into if a storm hits.

Because Florida has had 5 hurricane-free years, the company has built up a decent-sized amount of surplus. The new numbers show that Citizens expects to have a total surplus of more than $5.7 billion by the end of 2011.

The company also has $2.9 billion worth of bond proceeds it can tap into, as well as $575 million worth of private reinsurance coverage and another $6.59 billion worth of reinsurance coverage from the state-created Florida Hurricane Catastrophe Fund. The carrier is also seeking to borrow an additional $900 million heading into this storm season.

The analysis conducted by Citizens shows that the carrier could easily withstand a 1-in-5 year storm similar to Hurricane Frances in 2004 or even a storm of a 1-in-25 year magnitude. That cushion, however, would be lost with a major storm.

A 1-in-50 year storm similar to 1992's Hurricane Andrew would occasion the need for nearly $3 billion worth of surcharges and assessments on insurance bills in Florida. A 1-in-100 year storm would trigger nearly $12 billion worth of additional charges.

The way these charges and surcharges work is somewhat complicated, and involves three separate accounts that the carrier manages.

Citizens' policyholders are grouped in one of three accounts: a personal lines account that provides residential multi-peril accounts; a commercial lines account that covers apartment buildings, condominium associations and office buildings; a coastal account that provides both wind-only coverage and multi-peril coverage along the state's high-risk areas closest to the water.

A deficit in any of the three accounts can trigger one of three assessments on insurance bills. The first assessment that is charged is called a Citizens' policyholder surcharge and it is paid only by Citizens' customers. However, the surcharge can be up to 15 percent for each account for 12 months. That means in the event of a truly large storm the surcharge could hike Citizens' policyholder bills by as much as 45 percent.

The second type of assessment is called a regular assessment. It is charged to non-Citizens' policyholders, including all property insurance and auto insurance policies in the state. (Worker's compensation, medical malpractice, and federal flood insurance policies are exempt.) This assessment can be up to 6 percent of premium or 6 percent of the deficit for one year.

Then there is an emergency assessment, which can be up to 10 percent of premium and can be collected for any length of time, even as long as 30 years. Floridians right now are still paying off an emergency assessment of 1 percent triggered by 2005 storms.

However, the problem isn't just Citizens' ability to deal with the Big One.

A series of smaller storms in one year-similar to what happened in 2004 and 2005-could also trigger surcharges and assessments.

"Forget about the Andrews and Katrinas. We got in this decade a proven track record of multiple small to medium sized storms,'' said Agriculture Commissioner Adam Putnam during the Citizens' presentation.

Citizens' officials have acknowledged that is a concern. Earlier in the year Citizens did a presentation to state legislators that suggested two 1-in-10 year storms could trigger both the policyholder surcharge and the regular assessment.

**Building Up Resources**

This concern about multiple storms was one of the chief reasons Citizens took steps to shore up its finances heading into this year's hurricane season.

After a contentious debate, the board that oversees the carrier agreed in late May to borrow up to $900 million this year and spend $125 million to purchase $575 million worth of private reinsurance coverage.

By law, Citizens must purchase mandatory coverage from the Florida Hurricane Catastrophe Fund. However, the Citizens' board has usually not purchased additional private reinsurance.

Some of the board members questioned the expense of private reinsurance and said it should only be purchased in the event of a second storm. They noted that the odds were extremely low that losses would be high enough to even trigger a reimbursement.

But Sharon Binnun, the chief financial officer for Citizens, justified the purchase of private reinsurance as a way of "transferring the risk out of Florida." She said having private insurance would lessen the need to turn to Floridians to help cover massive losses.

The major difference between the bonds and the reinsurance is that the bonds will give Citizens access to cash that can be used as a bridge to help pay off claims right after a storm. By contrast, Citizens will only get a return on its reinsurance premiums in the event that losses are so high that it is forced to make a claim. The reinsurance policies are also only good for one year.

SOURCE:  [http://www.propertycasualty360.com/2011/06/28/new-figures-disclose-citizens-property-insurance-c](http://r20.rs6.net/tn.jsp?llr=q69aiodab&et=1106321233392&s=376&e=0019n8MEQLlVg-Uwyj25IR1su1u9DV8EPE97VXaJsQKnhPH7PbRlVl9fOhTVrdnMVVFT1djZEKw5HkJMjatPVWgs2GES4nXDchrhPEij2Gw54W99Wcf74Z-0M_1RWKOCKsy1AVDdhgqJjaglDC3FtzFHSWm_KU65gtJt0O6mJllwL8emdV4J7HpLmV1dvapJkoaz1cJQfxyRP0Vrtwv8ABNHQ==)

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**Florida Underwriter Magazine**

**Florida's Cat Fund: Healthy Enough for Another Year?**

**By Gary Fineout**

**July 2011**

Florida's fragile insurance market in many ways is deeply impacted by what happens twice a year inside a glass office building sheltered on a side road in northeast Tallahassee, far away from both the capitol and the state's financial sectors.

Inside a gray-carpeted conference room in this building an obscure panel signs off on an important number: Just how much money could the state-created reinsurance fund known as the Florida Hurricane Catastrophe Fund (Cat Fund) borrow if the state got hit by a big hurricane, or just as bad, a series of smaller storms?

The sophisticated guesswork that goes into this is more than some academic exercise. This number is a reflection of the stability of the Cat Fund, itself an important backstop for insurers that operate in the state, including Citizens Property Insurance Corp.

And this year the answer is somewhat troubling.

Hurt by the ongoing volatility in the municipal bond market, the latest round of estimates adopted in late May by the fund's advisory council conclude that the Cat Fund could borrow $12 billion to help cover its obligations for the 2011 season.

However, that borrowing power is a significant drop-roughly $4 billion less-than what the fund's financial advisors previously concluded in October.

"Our cushion has eroded,'' said Jack Nicholson, chief operating officer for the Cat Fund.

**Good News About Reserves**

These new estimates confirm that the Cat Fund remains largely dependent on swings in the global financial markets, and it continues to raise questions about the framework now in place to help bolster the state's entire property insurance market.

The Cat Fund was created in the wake of 1992's Hurricane Andrew to help stabilize the Florida property insurance market by offering low-cost reinsurance coverage to insurers who do business in the state. Every carrier that sells policies in the state is required to purchase a mandatory level of coverage.

The fund has certain advantages, including that it is a tax-exempt organization with low-administrative costs. Also, in the event of large losses, it has the power to levy assessments on nearly every insurance policy in the state to recoup the expenses.

But in the last decade-as Florida has been battered by a series of hurricanes and some insurers have fled the state-state policymakers have come to increasingly rely on the Cat Fund as a lever on insurance rate hikes. Four years ago, they created an optional layer of reinsurance that added billions in potential exposure.

The good news right now is that the Cat Fund has a large amount of money at its disposal. After 5 years without storms, the reinsurance fund has built up its resources and has access to more than $7 billion.

Still, that means the Cat Fund would have to rely on borrowing to cover the rest of its obligations, now estimated for this hurricane season at more than $18.5 billion.

Fortunately, the math has worked out, at least for now.

**Numbers Continue to Move**

New estimates drawn up by consulting with Wall Street firms conclude that the fund could now borrow about $12 billion. That is slightly higher than the $11.3 billion the fund would need.

Yet, these estimates continue to fluctuate greatly. This is the third major change in the last 3 years.

During the height of the 2008 financial meltdown, the Cat Fund was confronted with the sobering estimate that it could borrow only $3 billion. That gradually changed over the last 2 years as credit loosened up.

Last year financial advisors concluded the fund could borrow as much as $16 billion if the state was struck with devastating storms and needed to pay off reinsurance claims.

The fund's financial advisors, however, acknowledge that this year's estimate is one built on assumptions and that "significant uncertainty still exists."

The fund's financial advisor, John Forney of Raymond James & Associates, made a presentation to the advisory council in which he noted there has been a significant drop in the amount of municipal bonds issued this year. There has been a bit of volatility in municipal bond markets as some investors earlier this year fled the markets amid fears of financial instability.

"The ability of the Cat Fund to handle it from a theoretical standpoint is there," Forney said. "It's a question of what the market will bear."

Another item that could hurt Cat Fund resources is the fact that it will lose access to $3.5 billion in bond proceeds next year as those bonds mature.

Despite the new estimates, there are some positive trends.

Insurers continue to pare back the amount of optional reinsurance they are purchasing from the Cat Fund, which in turn lowers its obligations. The latest figures for this storm season show that private carriers were expected to purchase only $1.14 billion worth of optional coverage despite $6 billion being offered. Part of the drop is because of the increasing cost of the optional coverage.

Additionally, Citizens made the decision to purchase private reinsurance and borrow money this year instead of purchasing additional coverage from the Cat Fund.

Nicholson also took comfort in the amount of cash that the Cat Fund is expected to have by the end of the 2011 hurricane season.

"The projected cash balance of $7.245 billion is a big plus," Nicholson said, adding that it would "buy us some time" if a major storm hits.

**Time to "Right Size'' Cat Fund?**

However, the ongoing volatility associated with the bond market is one of the reasons that Nicholson says the time has come to rethink just how much exposure the Cat Fund has right now.

"What really causes concern is the level of our capacity and how we plan financially to address that," he said.

Nicholson pointed out that state leaders have increased the capacity of the Cat Fund twice in the last decade. Back in 2004, state lawmakers increased the size of the mandatory layer from $11 billion to $15 billion.

They followed that up 3 years later in a special session when they created the second layer of coverage known as the Temporary Increase in Coverage Limit (TICL). Legislators signed off on this second layer in the wake of voter anger at insurance rate hikes following the storm seasons of 2004 and 2005.

The initial amount of TICL was $12 billion, which greatly expanded the total potential exposure of the fund. However, this led to criticism that the Cat Fund was overexposed and that the state of Florida itself would be held financially responsible if the reinsurance fund was unable to pay off its obligations.

Lawmakers have since taken some steps to whittle down TICL and agreed to phase it out completely over the next several years.

Nicholson, however, said the "major over-expansion" of the Cat Fund's exposure does not serve to stabilize the state's economy. He said the time has come to consider forcing insurers-and ultimately consumers-to have "more skin in the game" by reducing the capacity and size of the Cat Fund over the next few years.

Nicholson has suggested lowering the current mandatory layer of coverage from $17 billion to $12 billion while increasing the amount of co-pay insurers must pay to access the coverage.

"It is hard to say what the 'right size' is for the fund, but I've defined it in terms of how comfortable and certain we can be issuing a level of debt,'' Nicholson said. "Like I have said, $5 to $7 billion is doable and reasonable, but over $10 billion gets risky. Theoretically, the 'right size' for the fund is big enough to accomplish its mission (stabilize the insurance market as well as stabilize and help avoid disruptions to Florida's economy), but not so large that the issuance of debt is questionable and highly volatile over time.

"The fund needs to be more of a 'guarantee' of coverage, not speculation," Nicholson continued. "The idea of right sizing is more of an art than an exact science, but it has a lot to do with common sense and judgment."

The trade off would be that the threat of assessments would be reduced because a smaller Cat Fund could more easily manage its obligations without having to borrow massive amounts of money.

**A Reality Check on Rates, Expansion**

However, it is likely that insurers will be forced to raise rates if they have to purchase private reinsurance instead of relying on the Cat Fund. State lawmakers remain skittish about allowing anything that could sharply increase insurance rates.

Don Brown, a former state lawmaker who was one of the few to vote against the expansion of the Cat Fund back in 2007, is already taking up Nicholson's cause. He wrote an op-ed for newspapers where he said the time for Nicholson's reforms has come.

"A reduction in the mandatory layer-which would more accurately reflect our ability to borrow-would have some upward pressure on rates but that, my friend, is the hard reality and at the very heart of our problem,'' Brown wrote.

He cited the "dynamic changes in the financial markets" as a key reason for the change but also pointed out that there are fears that huge losses during one hurricane season would render the Cat Fund unable to provide significant coverage the following year.

"Any expectation of coverage for second season events, and maybe subsequent events in the season, is 'pie in the sky,'" Brown wrote. "...For too long we have been fooling ourselves and Florida homeowners into thinking that if we ignore this problem it will go away. In the meantime, consumers, deprived of the correct pricing signals, continue to build beyond their means and, in some cases, in very dangerous places."

Brown also said, "It's not just folks who build on the beach...It's also folks who live in Orlando who divvy up their monthly mortgage and insurance budgets based on real mortgage costs but imaginary insurance cost.  We don't do anyone a service when we mislead them."

SOURCE:  [http://www.propertycasualty360.com/2011/06/28/floridas-cat-fund-healthy-enough-for-another-year](http://r20.rs6.net/tn.jsp?llr=q69aiodab&et=1106321233392&s=376&e=0019n8MEQLlVg_ZdDrx3ZOZG1hAmqxux9XPSEtQIne33DIamjxR6BMVP817sTRb92NoP2a2jn5AmF7q6ytm8tHOoAq3igFFfTlpV1cPHsbIik-dkqIE5OGWl_XxnE4e4KoUktoBmXM8jX9CK2Lwjj2VI7q94QYwNeHeb-xkPdhGK-i3_6ownYaoaTCsTs5iwiib2vGCzhVT9rLp_MUvinwLHg==)

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**Florida Underwriter Magazine**

**The Real Story About Reinsurance Rate Hikes**

**Setting the Record Straight on SB 408 Changes**

**By Lynne McChristian**

**July 2011**

**They Say, Hearsay**

I read that the property insurance bill Gov. Rick Scott signed has something in it that will make my homeowners' premium go up by 15 percent a year because of rising reinsurance costs. What the heck is this reinsurance, and why am I paying for it?

**We Say**

Remaining fully informed about legislative changes to property insurance-and their impact-is a little like trying to follow the storyline in one of those too-cleverly written spy thrillers that keep you on edge. Keeping up with the twists and turns of annual legislative manipulation of property insurance law is hard enough for those of us in the business.

Our policyholders are even more confused, and not only feel on the edge of a cliff, but maybe over it. Help them back away by bringing context to inquiries over how the change in SB 408 related to reinsurance works.

First off, we need to correct the misrepresentation that premiums are going to rise by 15 percent a year now that insurers can pass along reinsurance costs to customers. Insurers previously were allowed to do this (at 10 percent), so it is nothing new. What SB 408 does is raise the pass-along ceiling from 10 percent to 15 percent. More than a few people figured (incorrectly) that rates would double in 5 years due to this change because they were unaware that a pass-along already existed. Raising the ceiling by 5 percent is a relatively small change. It also is worth noting that if reinsurance rates do not rise, then there is no change at all.

Policyholders also should know that insurers are prohibited from passing along any costs without approval from state regulators. In 2009, a law allowed expedited rate filing reviews for reinsurance costs, meaning that the Florida Office of Insurance Regulation (OIR) must approve or disapprove a reinsurance-related rate increase within 45 days, rather than the 90 days it has to look at a regular rate increase.

The faster review enables insurers to account for fluctuating reinsurance prices, and this has an upside to insurance consumers: If an insurance company can more quickly recoup the costs of doing business, then it can do more business. The existence of reinsurance allows insurers to write more risk, therefore bringing competition to the market.

Buying reinsurance is not optional in Florida. All insurers are required to purchase a mandatory layer of reinsurance from the state-sponsored Florida Hurricane Catastrophe Fund (Cat Fund). Because it funds a good portion of the coverage it provides by selling bonds after a major storm occurs, there is always the specter of falling short of what is needed.

So, insurers who have limited financial flexibility with their own on-hand funds seek sources of protection with private reinsurers in addition to the Cat Fund. This enables them to pay claims that may come with a major hurricane, continue to service policyholders after storm claims are paid, and earn a decent grade from rating companies.

(By the way, the state's Citizens Property Insurance Corp. is buying private reinsurance this year for the first time since 2006.)

Taking on the extreme risk of writing wind insurance in the nation's most hurricane-prone state is made possible through reinsurance. Smaller, Florida-only companies rely most heavily upon it. Without access to the worldwide resources of reinsurers, only very large national companies could write any business in Florida, and most of them have curtailed their exposure here. The truth is, reinsurance is often the cheapest and best form of capital for many of Florida's insurance companies.

It is hard for policyholders to believe that the money Florida insurers have on hand is not enough to pay for actual claims, especially following a natural disaster. Yet it is painfully true. It is challenging to figure out how the cost of reinsurance affects an individual insurer's rates because while regulators review all reinsurance contracts, reinsurance is not considered a statutory asset until reinsurance losses are incurred. That helps explain why there is a big disconnect when one looks at the annual report developed by the OIR. It shows premiums collected and claims paid out, but does not reflect the value of reinsurance. Without it, however, many Florida insurance companies would not be able to pay claims after even a relatively small hurricane.

A well-planned reinsurance program preserves policyholder surplus to pay for ordinary, everyday claims. Reinsurance pays for the extraordinary claims, such as the $11.3 billion (in 2009 dollars) in losses from Hurricane Wilma in 2005.

**About the Author**

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SOURCE:  [http://www.propertycasualty360.com/2011/06/28/the-real-story-about-reinsurance-rate-hikes?t=reinsurance](http://r20.rs6.net/tn.jsp?llr=q69aiodab&et=1106321233392&s=376&e=0019n8MEQLlVg_U8X8WOn_DwIUQV2fZdY82glJ-_Ico33vSw2JZXXjs6_GztY3A2T7rxiLw-j8s1xoX9tt4CITI6f3Mbkxd91o4luLJHGl0Bl0fhKDjIcGnf1V3tAl5Pqv3Ukp9TXUkTQ2JJ6rJZzPbxbL_pqlsaTPkK_KmV5W5pO1nr10u0SYIrRGRXh_A0lXVfVIgpGlJWbYSjHcOzDT1SEZAj2jTV0PFjPmVSK962TE=)

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