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October 5, 2012

The Honorable Frank Artiles
District 119
13501 SW 128th Street
Miami, FL 33186

Dear Representative Artiles:

Thank you for your letter dated September 28, 2012. I appreciate this opportunity to clear up several misconceptions regarding the details of the proposed Surplus Notes Program. I believe I can clarify the intent and details of the program and answer some of your concerns.

As you know, Citizens has been directed by the Governor, Cabinet and Legislature to identify opportunities to help our customers find quality coverage in the private insurance market. It was with this guidance in mind that Citizens, in partnership with private insurers, agents, the public and elected officials, developed the Surplus Notes Program. The goals of this program are twofold:

- Dramatically reduce Citizens' risk pool, reducing the Emergency Assessment potential for all Florida policyholders from \$3.06 billion to \$1.89 billion – which otherwise could cost Citizens \$2.4 billion in reinsurance over the next 10 years
- Free up to 300,000 Citizens policyholders from the potential for assessments totaling 45 percent of their premiums by providing them with the opportunity to secure preferred coverage from reputable, private-market Florida insurance companies

First, I assure you that the Surplus Notes Program has been designed to complement, not compete with, Citizens' traditional depopulation efforts. We agree that companies that receive loan incentives through the Surplus Notes Program should not remove a policy that another company is willing to take without loan incentives. To avoid this, we have deferred the start of the Surplus Notes Program from November to December to allow the companies participating in the traditional depopulation program to remove policies in advance of the launch of the new program.

While it is true that carriers assuming risks under the standard depopulation plan usually choose to assume policies with the lowest risk (often called "cherry picking"), the objective of the Surplus Notes Program is to encourage participants to take out policies while reducing cherry

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picking. In fact, the Surplus Notes Program is designed precisely to offer incentives for companies willing to take out higher-risk policies.

One of those incentives would be a one-time loan to be paid back over a 20-year period, with interest. The loans would help financially secure companies meet the regulatory surplus requirements necessary to take on the additional policies. Citizens would issue these loans to established, reputable insurance companies willing to take on large numbers of Citizens policies at current premium levels. In return, the companies would commit to:

- Providing comparable or better coverage
- Renewing the policies for at least ten years
- Not raising rates by more than 10 percent per year for at least three years.

Before moving forward, the program must be approved by the Citizens Board of Governors and the Office of Insurance Regulation (OIR). Citizens agrees with CFO Atwater's suggestion that we ensure our depopulation efforts receive all due consideration and careful scrutiny. That is why we have a team of professionals who have been working internally and with external partners for nearly six months to address every contingency and design adequate provisions, monitors and controls to ensure the program is a sound investment for Citizens, our policyholders and all Florida taxpayers.

Citizens also has provided multiple opportunities for members of the public to learn about and share their concerns about the program. In addition to our regular, publically noticed Board of Governors and Depopulation Committee meetings, the Surplus Notes Program also was discussed at our June 1 Depopulation Summit, which hosted more than 200 attendees and was open to the general public. I also have made myself available to meet with public officials and consumer advocacy groups to discuss the details and terms of this program.

Regarding Tower Hill Insurance's participation in the development of the program, although Tower Hill and other Florida insurance carriers have lobbied for this and other innovative depopulation proposals, this does not mean the program was developed for or, if approved, will be implemented with a bias toward any specific companies. No companies have been selected or approved for this program, and all participating companies will be required to meet the same stringent requirements and regulations.

If the program were approved today, more than 20 companies would qualify to apply. Any company that meets the program's requirements will be permitted to apply and given full consideration. If demand for participation exceeds program funds, priority would be given on the basis of national rating agency ratings, net writing ratio, length of time actively writing property business in Florida and net written premium volume. All applicants would be fully vetted by Citizens and OIR to ensure financial health and a sound business plan. Applicants also would have to obtain written approval of their surplus note participation proposals from OIR. A full list of program requirements is available on our [website](#).

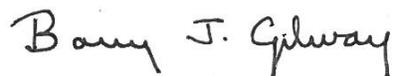
I assure you that the only sense of urgency I feel is to do what I was hired to do: provide a complete and thorough analysis of all options available to Citizens to help return it to its original

purpose and to do so in a way that benefits both taxpayers and Citizens' policyholders. I do not feel pressure specifically to depopulate and have received no pressure or direction from the Legislature, the Cabinet or my board other than to proceed with caution and ensure the end product is in the best interest of Citizens' policyholders and all Floridians.

I am committed only to making recommendations that I believe are in the best interest of Citizens, its customers and Florida's insurance consumers. Citizens is considering the Surplus Notes Program because my staff and I truly believe this program will help our policyholders and serve the public interest. We are recommending the program to the board now because we believe it is a strong program and we want to secure the benefits of private market coverage for our policyholders before the wind blows and subjects them to the risk of 45 percent assessments.

I hope this letter answers some of your concerns regarding the Surplus Notes Program. I also have included a *Surplus Notes Program Fast Fact Sheet* that provides additional details about how the program will work and the benefits it will provide. Please do not hesitate to contact me or my staff if you have any additional concerns or would like to discuss other proposals to help return Citizens to its role as Florida's insurer of last resort.

Sincerely,

A handwritten signature in cursive script that reads "Barry J. Gilway".

Barry Gilway
President/CEO and Executive Director

Surplus Notes Program Fast Facts



The Surplus Notes Program

- The goal of this program is to facilitate the return of Citizens policies to the private market by issuing one-time loans to selected private Florida insurers totaling approximately \$350 million.
- The Surplus Notes Program would *not* give payments or bonuses to private companies. It would provide one-time loans that must be paid back with interest over a 20-year period.
- A company that fails to make payments on its loan or fulfill other obligations laid out in the program agreement would be subject to penalties, including interest rate increases, acceleration of the repayment of principal and interest, reduction in the loan term, or a demand for full and immediate repayment of the surplus note.
- To receive a loan, companies would have to remove large blocks of policies (a minimum of roughly 25,000-30,000 policies) that would reduce Citizens' exposure by a minimum of \$5.5 billion for at least 10 years. This reduction in exposure directly would reduce the potential assessment burden for all Floridians.

Requirements for Program Applicants

- No companies have been approved for the program at this time. Any company meeting program requirements may apply and will be given full consideration.
- If demand for participation exceeds dedicated funds, priority will be given on the basis of national rating agency ratings, net writing ratio, length of time actively writing property business in Florida and net written premium volume.
- There are currently approximately 20 companies identified that would qualify for the new Surplus Notes Program.
- Citizens has developed a detailed set of requirements to ensure that program applicants are financially healthy and have sound business plans. The proposed requirements for program participation are available on Citizens' [website](#).
- The Florida Office of Insurance Regulation (OIR) would verify the financial viability of program applicants.

Policyholder Benefits

- Participating policyholders would have their policies placed with established, reputable, private-market companies that commit to:
 - Renew coverage for a minimum of 10 years
 - Increase rates by no more than 10 percent per year (the same rate increase restrictions currently in place at Citizens) for the first three years following their removal from Citizens.
- Participating policyholders could expect greater continuity in their property insurance policy, knowing that the new company cannot drop their policy and is financially solid and ready to handle any claim.
- Participating policyholders would be freed from the risk of Citizens policyholder assessments and surcharges of up to 45 percent of their premiums.

Florida Taxpayer Benefits

- The Surplus Notes program will transfer approximately \$1.5-\$2 billion in risk back to the private market, dramatically reducing the risk of assessments for all Florida policyholders.
- Estimates show that the Surplus Notes program could cut the potential of paying Citizens Emergency Assessments, which is faced by all Florida policyholders, almost in half, reducing the potential Citizens shortfall from \$3.06 billion to \$1.89 billion (a \$1.17 billion reduction).
- The program would reduce the reinsurance needs for Citizens and Florida taxpayers by \$2.4 billion over 10 years.
- Even in the unlikely event that a major storm led to conditions where Citizens would forgive one or more surplus notes, Florida taxpayers still would be better off than if Citizens retained the risk and purchased reinsurance over the next 10 years.