

The Impact of Assignment of Benefits on Citizens' Depopulation

Failure this session to enact reforms halting the abuse of Assignment of Benefits (AOB) threatens the progress made in reducing the size of Citizens and its potential assessment burden on Florida's insurance consumers. Absent reform, there are stark signs that depopulation will reverse and Citizens will grow in risk level even as its own financial strength is sapped.

THE PROBLEM

Signs of rapid deterioration of Citizens' financial strength and rate adequacy include:

- Need for near-maximal (+10%) rate increases in Tri-County in 2016, nearly all due to trends in both frequency and severity of non-weather water claims. Wind costs of capital are near all-time lows and administrative expenses are reasonable and stable.
- Increase in 2015 loss ratios from about 56% to about 74%, meaning 18 fewer cents of every premium dollar are available to fund storm risk or return to consumers in rate filings. These funds are instead going primarily to water claims, particularly litigated cases.
- Worsening of those trends since the recent rate filing; fresh actuarial data shows that water claim frequency has doubled in Tri-County and tripled in the rest of Florida in the past two years. Severity (average claim cost) has increased by double digit percentages in Tri-County. And detailed sample data shows that over 40% of not yet litigated claims around the whole state have an AOB in place, priming the claim for litigation.
- Association of these trends with an explosion in the use of AOB and the evidence that AOB is a direct path to litigation. Citizens responded to an Office of Insurance Regulation data call in December and released a white paper based in part on that data. The paper shows that AOB doubles the average cost of a non-litigated water claim and then litigation doubles the cost of a non-litigated claim even with AOB, for a total impact of a factor of four.

Signs that the private market is ready to stop depopulation, and reverse the flow of policies out of Citizens include:

- Private insurer rate filings indicate for the first time in several years that monthly requested increases are outpacing requested decreases, even as reinsurance costs continue to fall to post-Andrew lows.
- Anecdotal statements that blocks of policies are set to be non-renewed. One active insurer alerted Citizens to planned non-renewal of over 9,000 policies due to loss experience, and is paying agents a bonus to find mid-term replacement coverage. Also, a top-10 and fast-growing Florida insurer has reported significant litigated claims trends from Citizens takeout customers.
- Far fewer multi-peril policies being selected and assumed in each depopulation month than in 2014 or early 2015. Ironically, wind-only depopulation now has the best success rate.
- Evidence showing AOB is significantly impacting private insurer claim trends as well, from the OIR's Report on the aggregate insights from the AOB data call. OIR shows that AOB use has nearly tripled since 2010, and that frequency has increased by 46% and average costs by 28%.

- Overall average costs have increased by 14% per year during the past five years, requiring water peril rate increases of more than 10% per year to maintain actuarially sound rates. AOB itself appears to inflate a typical claim by at least 50% in cost. These conclusions are true for all of eight regions of the state studied.

THE IMPACT

- Private insurer rate increases that outpace Citizens' limited rate increases under the "glide path" law would push Citizens toward its old role as a price floor. The Clearinghouse would screen out fewer applicants that can obtain a policy for no more than 15% more than Citizens premium.
- Depopulation will cease to the extent private insurers can no longer agree to take out a policy at Citizens rate levels, and hold it for at least three years, due to the consumer's option to decline a takeout and the requirement in most consent orders that policies be held for three years.
- Simultaneously, financial losses on existing policies would cause insurers to retrench by instantly closing certain ZIP codes or counties to new business and non-renewing existing business in line with Florida laws. The Clearinghouse would no longer show offers from those insurers, reducing the number of Citizens renewals made ineligible by a comparable, price-competitive private offer.
- As Citizens becomes financially weaker and loses surplus while suffering operating losses, the current reinsurance program that has eliminated assessment risk in the 100-year storm will become unaffordable, so assessment risk will reappear and grow toward the \$11.6 billion mark it reached in 2011, when Citizens held nearly 1.5 million policies and over \$500 billion in exposure value.

THE SOLUTION

Citizens has demonstrated the harm to consumers from AOB, particularly as a path to cost-driving litigation from vendors with access to one-way attorney fees. It is clear that the fate of Citizens is inextricably linked to the health of Florida's private insurance industry. The endgame for a healthy market with reasonable rates is to get claims out of the courtroom and back into the control of the consumer assisted by their insurer. Consumers must not be pressured to sign away their rights under duress. Vendors and their partner attorneys were never intended to benefit from a law designed to protect consumer access to the courts.

Enactment of reforms will allow Citizens to consider any projected improvements in its rate recommendations for 2017, for OIR to work with private insurers to assimilate these same projections into their rate requests, and remove a major uncertainty in private insurer business plans. The absence of reform will lead to a weaker yet larger Citizens, higher rates for years to come, and fewer private insurance options for many thousands of Floridians.