Commissioner's Presentation
Cabinet Meeting

March 23, 2010

Thank you for the opportunity to update the Financial Services Commission about the status of the Florida property insurance market. I last spoke to the Financial Services Commission in September 2009 about the financial conditions of the marketplace based on results for the first two quarters. I now can share results with you for the Florida insurance marketplace based on financial reports filed for end of year 2009. The year-end results show no appreciable change; and the marketplace still faces serious challenges.

Let me begin today by providing a brief analysis of the financial statements of the 206 companies that are currently reporting active policies in force. At the end of 2009, 60 companies reported reductions in surplus, while 144 companies reported surplus gains. Two companies did not file financial statements for various reasons.

Reviewing the year-end data, for underwriting losses and gains, (underwriting gains and losses are the premiums that remain after a company has paid its claims and expenses. Underwriting gains and losses excludes investment income, or income from non-insurance sources.) 81 companies reported underwriting gains, while 100 companies reported underwriting losses. We should note that some companies have pooling arrangements with reinsurers and do not directly report underwriting gains and losses. The majority of companies operating in Florida reported *increases in* their surplus; many of these companies also reported *losses* from their underwriting. One explanation for this difference is that some companies have put additional funds into their company, sometimes at the request of the Office, and sometimes of their own volition.

The year-end financial data for the Florida property market were included in the Cabinet meeting materials. Please note, although these data are for companies operating in Florida – the financial numbers themselves are *national* numbers; and per the CFO's request, we also provided a spreadsheet specific to the Florida domestic companies. The reason that insurance companies are struggling nationally is that the property & casualty industry has been under some pressure from reduced investment yields, increases in potentially fraudulent claims, and an overall soft market. As I previously reported to the FSC, the cost-drivers relating to companies operating in Florida include:

- Increased Reinsurance Costs
- Replacement Cost Methodology
- Fraud
- Reported Sinkhole Claims; and
- Premium Reductions from the Full Implementation of Mitigation Discounts

These cost-drivers were identified during meetings between the Office and Florida insurers. To address these cost-drivers, the Florida Office of Insurance Regulation and the Florida domestic industry supports changes included in Senator Richter's bill, S.B. 2044, the Property Insurance Solvency Act, which will go a long way to address these cost-drivers.

Since my presentation in September, the Office has completed a survey of many of our domestic insurers regarding re-opened claims. The survey showed that a considerable number of re-opened claims were re-opened three, four or even five years after the storm. Many of these were initiated with the help of public adjusters. While we do believe that public adjusters can be an important part of the claims process, we do not believe financial incentives for public adjusters should encourage the re-opening of settled claims, or provide any incentives to game the system. Therefore, we support the public adjuster bills, specifically, Senator Bennett's S.B. 2264, and its companion bill, Representative Long's H.B. 1181 in the current form.

We agree there should be statutory limitations on re-opening hurricane claims, and that financial incentives should be reduced to re-open settled claims. We favor revising the replacement cost calculation to ensure that homeowners make the required structural repairs. Finally, we support strengthening solvency regulation by increasing minimum reserves for start-up companies from the current $5 million to $15 million or more. These approaches, combined with a recovering Florida economy, are the best strategy we can employ to improve our marketplace.

I would also like to clarify some misinformation that has been circulating about the Florida property insurance market. In 2009 and so far in 2010, we have had two homeowners' insurers companies that have been placed into receivership. There was a third company, First Commercial Insurance Company, that wrote Workers' Compensation and Commercial Auto that was also placed into receivership. First Commercial Insurance Company engaged in criminal activities that contributed to the failure of the company. We have already referred this matter to the Division of Fraud. Finally, the Office currently has two companies under administrative supervision that may or may not result in a referral to the Division of Rehabilitation and Liquidation.

As a result of the Office's intervention, and with the cooperation of the Division of Rehabilitation and Liquidation, we have been able to minimize the impact of insolvencies on the Florida Insurance Guarantee Association (FIGA). As unfortunate as these financial failures are, having three to four insurer failures a year is typical in Florida even with a strong economy. Inevitably, in a competitive environment some well-managed companies are profitable, while others experience financial distress. Let me reassure you, we will not allow known troubled companies to enter hurricane season without the financial capacity to pay claims; those companies that do not have the financial wherewithal to pay these claims will be either re-capitalized, acquired, merged, or liquidated. Because Florida has a safety net, Florida policyholders are guaranteed a payout for their losses pursuant to Florida law in the event of an insolvency.

The Office has conducted a series of financial reviews. As a result, the office ordered one company to undo an unapproved affiliated transaction and return over $ 8 million to the insurance company. The Office also ordered a different company to reduce its MGA fees, and return money to its company. There will be more orders or consent orders to follow. Furthermore, the Office has worked with legislative staff to strengthen our regulatory oversight over affiliated transactions. In April, the Office will again initiate our annual reinsurance data call to confirm that reinsurance contracts are in place to allow companies to pay claims if we encounter an active hurricane season.

Some have criticized the Office for not informing the public earlier about insurers experiencing financial problems. However, it should be noted that the insurance industry is the most transparent of all industries in the financial marketplace. Similar to the banking industry, under the laws of Florida some of the Office's regulatory work is, and should be, confidential as to not cause the proverbial "bank run" by policyholders, or frighten potential investors.

This brings us back to the underlying structure of the Florida insurance marketplace, and why the Governor and Legislature have made critical decisions to stabilize the marketplace. Following Hurricane Andrew in 1992, national insurers began their exposure reduction in Florida; this was further exacerbated by the unprecedented eight named storms that reached landfall in Florida in 2004-2005. After these storms, many of the national carriers continued to reduce risk in our state, and it is important to note that this exposure reduction is not unique to Florida. It is occurring in other coastal states. The Governor and Legislature explicitly recognized a need to grow capital in Florida, and to encourage "home-grown" Florida insurers. The Florida domestic companies are the gateway to global capital from the reinsurance market, resulting in billions of dollars in risk transfer to the private market that would otherwise need to be directly insured by Citizens or the Cat Fund.

To achieve this goal, the Legislature implemented several strategies to address this shortfall including approving $250 million capital build-up incentive program. This attracted new capital and new insurers to help fill this void in the marketplace; furthermore, these companies employ Floridians and pay taxes into our state coffers – not simply premium taxes. We have had many success stories including companies that have grown and expanded, and now write insurance in other states. In addition, combining new capital insurers with national insurers has added to the diversification of the property insurance marketplace. While many national insurers have reduced their exposure, it is important to realize that large insurers have not left the state, and continue to play an important role in assuming risk in Florida.

In conclusion, our state has overcome multiple challenges over the years. In the aftermath of Hurricane Andrew, the Florida Legislature created the Florida Hurricane Catastrophe Fund, which became the cornerstone of the recovery of the Florida marketplace at that time. Governor Crist and the Legislature acted decisively in January 2007 by enacting House Bill 1A to address rapid increases in reinsurance as the result of the unprecedented storms of the 2004-2005 hurricane seasons. Now we have new set of challenges that include cost-drivers and unfavorable economic environment. While we do not have a perfect system, I am confident we can continue to work together to create a better regulatory framework and a better Florida insurance marketplace.