

# Florida Property Insurers Avoid Ratings Downgrades From Demotech, For Now

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By [Amy O'Connor](#) | April 3, 2017

Ratings company Demotech is holding off on issuing large-scale ratings downgrades of Florida property insurers for now, after a number of insurers heeded its warning about the effects of assignment of benefits abuse and state court rulings by boosting their claims reserves and policyholder surplus.

After warning in February that at least 10 to 15 Florida property/casualty carriers would face downgrades if they did not take immediate action to shore up their reserves in light of deteriorating conditions in the state, Demotech said March 16 that, after working with insurers to make adjustments, it slightly downgraded only one carrier.

The ratings firm said it is also monitoring three insurers — Prepared, Mount Beacon and Elements— that have been or are in the process of being sold as a result of the situation in Florida.

Joseph Petrelli, president and CEO of Ohio-based Demotech, which rates 57 carriers in Florida and 397 nationwide, said his company worked individually with companies in Florida to analyze their financial standing, strengthen their claims reserves, and provide other guidance on what they could do to avoid a ratings downgrade. The result has been \$355 million in additional reserves and policyholder surplus among the Florida carriers it rates, Demotech said in a statement March 16.

Downgrades have been largely avoided at this time.

Demotech warned in February that Florida's property insurers are facing an "uncertain operating environment" as a result of the escalating AOB crisis that has caused the number of litigated water loss claims to skyrocket over the past few years, particularly for the state-run insurer Citizens.

As the abuse spreads from south Florida across the state, Florida's private market insurers have also started feeling the effects, with some pulling out of areas of the state and filing for rate increases.

Demotech said AOB, as well as two court cases decided at the end of 2016 that reversed industry claims procedures, have led to unanticipated challenges for insurers. Demotech also warned about the effects of Florida Supreme Court decisions involving the reversal of claims procedures, protocols and practices as contributing to the state's uncertainties.

"In an industry where past is prologue of the future, this is extremely detrimental to efficiently operating an insurance company," Demotech said in its March 16 release.

In response to the events, Demotech withdrew its ratings guidance for Florida's property insurance writers and undertook what it said was a "comprehensive effort" to review the financial statements and business models of 57 Florida carriers to "determine if they continued to meet or exceed the objective financial criteria associated with the assignment of Financial Stability Ratings (FSRs)," which reflect Demotech's opinion as to an insurer's financial stability and provide a baseline of the future solvency of an insurer.

According to Petrelli, Demotech advised carriers to take advantage of statutory accounting rules before Feb. 28 to infuse capital into their surplus to improve their year-end results and avoid ratings downgrades. Petrelli estimated that about 10 to 15 companies would face downgrades if they didn't strengthen their claims reserves.

Demotech said in March that the carriers it reviews and rates in Florida responded by adding approximately \$200 million in loss and loss adjustment expense reserves, as well as approximately \$155 million to policyholders' surplus (net worth) through capital contributions or operating results.

"This additional \$355 million to benefit policyholders or claimants indicate the insurers' recommitment to Floridians and financial stability," Demotech said.

Demotech said that in certain cases, it also reviewed carriers' rate levels for adequacy and found that "the overwhelming majority of the carriers reviewed appeared to have the situation under control."

Demotech affirmed the FSRs of the carriers it rates as appropriate, saying "due to recommitments and recapitalization to meet the requirements of maintaining an FSR of A or better, downgrades have been largely avoided at this time."

Only one company was slightly downgraded – Cypress Property & Casualty Insurance Co. was revised from A' (A Prime) to A (Exceptional). Demotech said this move was made in part due to Cypress' significant underwriting loss reported in 2016, but added "based on our interpretation of the current operating environment in Florida, FSRs above A are extremely difficult for Florida property writers to achieve and maintain."

Insurers in the state are hoping AOB relief will come during the current Florida Legislative Session, which opened March 7. Under Florida's current law, policyholders suing their insurer over a claim dispute can recover their attorney's fees if the insurer is shown to have underpaid the claim, by any amount. The industry says third party contractors and attorneys have been abusing the policyholder benefit, particularly for water losses, to inflate claims and fees.

The Florida Office of Insurance Regulation drafted legislation to address the problem, but it is facing significant opposition from attorneys and restoration companies.

Demotech warned that absent meaningful improvement in the AOB situation, it is likely insurers could face downgrades in the future, consumers may face higher and frequent rate increases, and

investors who would otherwise capitalize or fund Florida-based insurance companies will deploy their capital elsewhere.

“Whether a property insurance carrier is privately-held or owned by a publicly traded entity, Demotech believes the primary focus of carriers should be adequate loss and loss adjustment expense reserves, realistic pricing in support of a business plan, along with a catastrophe reinsurance program whose horizontal and vertical protection addresses the needs of policyholders and investors by assuring, at a high yet reasonable level of maximum loss, the survival of the insurer,” the company said.

Demotech will review carriers’ March 31 financial statements as well as preliminary and final catastrophe reinsurance programs by June 1 before any further moves.

Demotech noted, however, that it is monitoring several other companies:

### **Elements Property Insurance Co. / Avatar**

Although the company met or exceeded the level of capital and surplus required and management has committed to do so into the future, the company did not report financials acceptable to Demotech. The investors controlling the company have opted to sell the company rather than recommit to Florida or adapt its business model to the emerging operating environment. Elements Property Insurance Co. has been acquired by Avatar Partners LP, the parent company of Avatar Property & Casualty Insurance Co. Elements will maintain the FSR previously assigned as the pending transaction proceeds towards closure, Demotech said.

### **Mount Beacon Insurance Co. / Florida Specialty**

Although the company met or exceeded the level of capital and surplus required, the company did not report financials acceptable to Demotech. The investors controlling the company opted to sell the company rather than recommit to Florida or adapt its business model to the emerging operating environment. Mount Beacon Insurance Co. has been acquired by Florida Specialty Acquisition, LLC. Mount Beacon will maintain the FSR previously assigned while the remainder of its policies are moved to Florida Specialty Insurance Co. by May 15, 2017, according to Demotech.

### **Prepared Insurance Co. / PLW Investments, LLC**

Although the company raised additional capital to meet the level requested by Demotech, the successful implementation of its business model and plan under the current operating environment would have likely required additional capitalization in the future. In response, the investors controlling the company recommitted to Floridians by selling a majority interest to PLW Investments LLC. The FSR assigned to Prepared Insurance Co. has been affirmed based on its current situation, business plan, and management underlying future operations, Demotech said.

**About Amy O'Connor** O'Connor is the Southeast editor for Insurance Journal and associate editor of MyNewMarkets.com.