CITIZENS PROPERTY INSURANCE CORPORATION
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January 12, 2022

Citizens Board of Governors: Chairman Carlos Beruff, Vice Chair M. Scott Thomas, Marc Dunbar, Lazaro Fields, Jillian Hasner, Reynolds Henderson, Erin Knight, and Nelson Telemaco

RE: Citizens' 2022 Season Claims-Paying Resources

Dear Board Members:

In follow-up to the December 16th Board of Governor's meeting, the included white paper was prepared to address questions and comments regarding the role of reinsurance in Citizens' financial structure as well as evaluative factors considered in the proposed 2022 reinsurance program. Due to the public nature of Citizens' Board of Governors meetings and the discussion surrounding Citizens' participation in the risk transfer market, there is some uncertainty in the reinsurance marketplace concerning Citizens' risk transfer strategy for 2022 that, if left unresolved, could negatively impact Citizens' risk transfer rates, capacity, and financial position as well as the financial position of the State of Florida should a catastrophic event, or series of events, occur in Florida.

It is important that each Board member consider the essential elements in this white paper that underlie Citizens' risk transfer strategy, Plan of Operation and capital structure before adopting Citizens' risk transfer strategy for 2022. Public affirmation of the Board's support of Citizens' proposed risk transfer strategy for 2022 is critical to address any potential uncertainty or confusion of Citizens' intent to purchase reinsurance for the 2022 hurricane season and therefore staff is recommending that a special board meeting be scheduled in the next few weeks. This timeline will allow Citizens and its financial services team sufficient time to structure, market and place a risk transfer program over the following three to four months before coming back to the Board for final approval of the 2022 reinsurance program prior to the start of hurricane season on June 1st.

We look forward to having individual conversations to answer any additional questions and comments.

Thank you.

Barry J. Gilway
Barry J. Gilway
President/CEO and Executive Director

Jennifer Montero
Jennifer Montero
Chief Financial Officer

Claims Paying Resources for 2022

January 11, 2022

Table of Contents

Executive Summary

This white paper provides a general overview of insurance companies – how they are financially structured and their related claims-paying resources – and gives a detailed analysis of specific claims paying resources and options available to Citizens Property Insurance Corporation (“Citizens”) for the 2022 hurricane season. In line with the legislative intent underlying Citizens’ Statute Section 627.351(6) and its Plan of Operation, Citizens has liquidity mechanisms and risk management options to optimize the structure of its claims paying resources in order to preserve surplus and to reduce and/or eliminate the amount and likelihood of assessments on Florida residents. Without optimizing the use of these liquidity mechanisms and risk management options, Citizens must rely solely on its surplus, mandatory coverage through the Florida Hurricane Catastrophe Fund (“FHCF”), surcharges on its policyholders, and assessments or “taxes” on Florida residents after an event. The depletion of Citizens’ surplus resulting from sub-optimal structuring of risk management options, namely the absence of an effective risk transfer program, will result in a higher likelihood and greater amount of assessments on Florida residents. As further addressed in this white paper, the assessment burden on Florida residents created by an insufficient or absent risk transfer program could be significant if Citizens experiences multiple events or a single large event, the financial implications of which are summarized in the loss scenario discussion on pages 14 and 15 and in detail in the loss scenario tables in the appendix of this white paper.

The decision to purchase risk transfer is determined through an evaluation of current market conditions and Citizens’ current and future financial position while giving appropriate consideration to the objective in Citizens’ Statute Section 627.351(6)c(9) that obligates Citizens “to make its best efforts to procure catastrophe reinsurance at reasonable rates, to cover its projected 100-year probable maximum loss as determined by the board of governors”. Over the last decade, strong leadership from the Board and Citizens’ executive management in partnership with a world-class financial services team have ensured this objective is consistently met, the result of which is the placement of an optimal risk transfer program at efficient pricing and the achievement of Citizens’ current financial strength. More importantly, the result has been the elimination of potential assessment burdens on Florida residents after a 1 in 100-year event while preserving a portion of its surplus for future events.

Summary of Defined Terms

Assessments – in the context of Citizens, are levied when there is a deficit in any account. A deficit is determined based on audited Generally Accepted Accounting Principles ("GAAP") financial statements. Citizens has three assessment tiers: the first tier is the Citizens' Policyholder Surcharge, the second tier is the Regular Assessment (for the Coastal Account only), and the third tier is the Emergency Assessment. (Citizens' assessment authority is discussed in more detail on page 7 and the appendix).

Capital Markets Risk Transfer or "Cat Bonds"– Citizens uses a special purpose vehicle ("SPV") named Everglades Re II, to issue a risk bearing bond. Horseshoe is the administrator and Citizens is the sponsor. This risk transfer mechanism is used in the high layers of the layer charts and from Citizens' perspective functions much in the same way as traditional reinsurance.

Florida Hurricane Catastrophe Fund ("FHCF") – a statutorily created entity provides a reimbursement mechanism similar to reinsurance. The FHCF covers losses, net of a percentage co-payment, once the insurer's attachment point is reached. Unlike private reinsurance, the FHCF is a reimbursement mechanism, meaning that each insurance company must first pay the underlying claims before reimbursement from the FHCF is received. It is mandatory for all Florida P&C insurance companies to participate in the FHCF at a level of 45%, 75%, or 90%. Citizens is statutorily required to participate at a level of 90%. Coverage is based on the amount of statewide premium a company writes as a percentage of the aggregate, at the level of participation chosen. Currently, the FHCF's statutory maximum liability is $17 billion.

Glide Path – in 2009, House Bill 1495 was passed that created the rate glide path for Citizens. The glide path language states that no individual policyholder can be charged more than a 10% rate increase. In 2021, Senate Bill 76 passed that stated the glide path cap will increase one percentage point each year for five consecutive years. In 2022 the cap increases from 10% to 11%; 11% to 12% in 2023; 12% to 13% in 2024; 13% to 14% in 2025; and from 14% to 15% in 2026.

HB1A – in 2007, House Bill 1A was passed during a special session on property insurance. The bill made several changes to Citizens rating law including deleting the requirement that Citizens rates be non-competitive with the top 20 insurers and rescinding the approved actuarially sound rate increase, an average of 23.1%, that took effect on January 1, 2007. The bill also required that Citizens provide refunds to persons who had paid the new rate. Additionally, the law froze Citizens rates at December 31, 2006 levels, except for any rate decreases, through the end of 2007. In subsequent sessions in each year between 2007 and 2009 additional changes to the statute were passed which ultimately froze rates until January 1, 2010 and created the 10% per policy rate glide path.

Post-Event Bonds – are municipal bonds issued by Citizens after a catastrophic event. The bonds provide funds to repay any pre-event bonds that were used to pay claims. The bond proceeds are repaid from assessments.

Pre-Event Bonds – are municipal bonds issued by Citizens. The bonds provide immediate liquidity to be used, if needed, as a bridge to pay claims until FHCF recoveries are received. This allows for timely payment of claims after an event while providing timing flexibility for the issuance of post-event bonds, if needed. Pre-event bonds are not a risk transfer mechanism and the bond proceeds must be repaid from premium, reinsurance recoveries, or assessment funds, which are all pledged to the bond holders.

Rate-on-Line – the premium paid for risk transfer as a percentage of the amount of risk transfer purchased. Pricing is based on the probability of expected loss where the rate-on-line decreases as the probability of expected loss decreases.

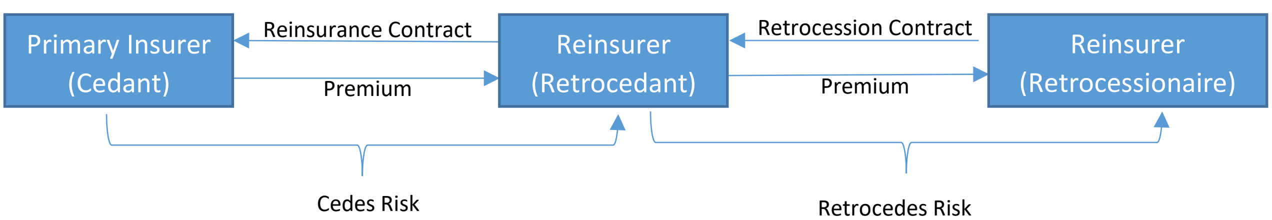
Risk Transfer – consists of traditional reinsurance, cat bonds and the FHCF.

Statute – Citizens was created in 2002 via the State of Florida Legislature. Citizens' governing statute is 627.351(6).

Surplus – is the excess premium and investment income for an account over the projected losses and expenses for the account, attributable to that year. Such surplus accumulation must be available to defray deficits in that account as to future years and used for that purpose before levying assessments. The complete statutory definition can be found on page 4.

Surplus Notes – are unsecured debt instruments issued by insurers to raise capital. State insurance regulators treat surplus notes as statutory capital as they are subordinate to all claims by policyholders and creditors.

Traditional Reinsurance – is a risk transfer mechanism that acts as "insurance for insurance companies" while retrocession acts as insurance for reinsurers providing additional capacity to the marketplace.



Overview of Insurance

An insurance company is a financial institution which underwrites the risk of loss of, or damage to, personal and/or commercial assets in the instance of property insurance. Insurance companies issue insurance policies to cover a variety of policy types involving potential financial loss to policyholders in return for premium payments. An insurance company operates by pooling risk among a large number of policyholders. An insurance company's primary mission is to pay claims in a timely manner and to remain sustainable through efficient risk management.

The premiums charged to policyholders are based on the probability of a particular event occurring and the average financial loss associated with each event and includes operating expenses and costs associated with risk transfer. The rate setting is done by the company's actuarial staff using statistical techniques and models to analyze past claims.

Insurance companies use the premiums they receive not only to settle day-to-day claims but also to generate additional income and profit by investing their accumulated surplus according to an investment policy that maintains a balance between liquidity needs, risk, and investment returns.

Insurance Company Capital Structure

A property and casualty insurance company's capital structure is comprised of surplus, surplus notes, and risk transfer. Citizens' capital structure is unique versus a private insurance company in that it also includes assessments (if any) as a form of contingent capital, but not a primary form of capital.

The definition of Citizens' surplus provided in Florida Statutes Section 627.351(6)(c)1.c.7 by way of reference to its Plan of Operation:

> *Must provide that if premium and investment income for an account attributable to a particular calendar year are in excess of projected losses and expenses for the account attributable to that year, such excess shall be held in surplus in the account. Such surplus must be available to defray deficits in that account as to future years and used for that purpose before assessing assessable insurers and assessable insureds as to any calendar year.*

For insurance companies, the minimum amount of capitalization is set by state insurance regulators, which have specific capital requirements for insurance companies writing business within their state – in the State of Florida, private insurance companies must have a minimum of $25 million of capital and surplus, which can be funded from surplus, premiums written, and/or surplus notes. Additionally, the capital structures of insurance companies are regularly reviewed by rating agencies (for example, A.M. Best or Demotech) to ensure their financial strength is in-line with their assigned rating to maintain the privilege of writing insurance.

The level of reinsurance purchased by an insurance company is dependent upon its exposure and capital levels, with the goal of structuring a risk transfer program that optimally transfers risk at the most efficient cost. Reinsurance, or risk-transfer, is comprised of traditional reinsurance, capital markets risk transfer (or "cat bonds"), and for Florida residential property insurers – mandatory participation in the FHCF which acts as a reimbursement mechanism akin to reinsurance.

Assessments are a mechanism available to some public insurers, or residual market entities, in order to generate additional funds to pay claims after event losses. Assessments in Florida and Louisiana and to a limited extent in North Carolina, South Carolina, and Texas are a burden on residents and should always be avoided. Assessments are treated as contingent capital in extremely remote scenarios and are generally used to manage "unknown known" risk scenarios beyond the 1- 100 year level, or more preferably those at the 1-150 or 1-250 levels.

For mortgages written by Fannie Mae and Freddie Mac, the mortgagee must utilize an insurance company that is rated by A.M. Best or Demotech. If rated by A.M. Best, the insurance company must have a rating of "A-" or better, and a financial size category of VI or better; or if rated by Demotech, the insurance company must have a rating of "A" or better, and policyholder surplus of at least $40 million. Additionally, Demotech requires insurance companies' first-event reinsurance requirements to mandate that a 1-in-130 year loss event be covered followed by a second 1-in-75 year loss event. Conversely, Citizens does not have any reinsurance requirements mandated by rating agencies and is not required to hold ratings from A.M. Best or Demotech. Citizens, however, upholds a strong risk transfer philosophy and has a statutory requirement to make its best efforts to procure reinsurance to a 1-100 year level, which is significantly less stringent than private insurance entities in the state. In addition, Citizens has long-term debt ratings from Moody's, Standard & Poor's ("S&P"), and Fitch, which are essential for the issuance of pre-event and post-event bonds. Based on significant long-term efforts from Citizens' staff, its financial advisor, and through Board leadership, Citizens' credit rating has evolved over time from being viewed purely as an insurance entity to one that provides a significant economic benefit. As a result, Citizens' ratings have improved 1 to 2 notches since 2005 to the current rating levels of "A1" from Moody's, "A+" from S&P, and "AA" from Fitch. As Citizens is an integral component of the State of Florida, its financial strength, including risk management, and ratings are also part of the Moody's, S&P's, and Fitch's analyses of the state's ratings.

Assessments and Reinsurance

Assessments

In the context of Citizens, assessments do not transfer risk and are akin to taxes. However, taxes are charged for a direct public benefit and assessments do not provide any direct or indirect public benefit or public good to assessment payers. Assessments only subsidize Citizens' policyholders, thereby creating disincentives and inefficiencies in the marketplace. Citizens does not rely on the use of assessments as a form of capital but rather as a last resort, instead relying on its accumulated surplus and risk transfer to help fund actual and potential storm losses.

Reinsurance

Reinsurance transfers risk from primary insurers to the global marketplace and provides stand-by capital to insurers ceding the risk. The rate-on-line is based on the probability of expected loss, peril, and geography. The global reinsurance market has continued to increase the amount of dedicated capital despite large industry losses from global catastrophic events over the last five years. According to Aon, global reinsurance capital stands at $660 billion as of June 2021.

Citizens' Framework

Citizens was created by the Florida Legislature in August 2002 as a not-for-profit, tax-exempt, governmental entity to provide property insurance to eligible Florida property owners unable to find comparable insurance coverage in the private market. While Citizens is funded through policyholder premiums, Florida law also requires that Citizens levy assessments on most Florida policyholders if it incurs a deficit in any account. Citizens operates according to statutory requirements established by the Florida Legislature and is governed by a Board of Governors. Citizens' statute is regularly modified by legislative action based on politics, insurance marketplace dynamics, abusive litigation, and hurricane losses in the state.

The purpose of Citizens is to act as a true residual market insurer for property owners who are, in good faith, entitled to obtain coverage through the private market but are unable to do so. Citizens can only act as a true residual market insurer by charging actuarially sound rates, but its ability to do so is restricted by statute, which is further exacerbated by abusive litigation. In order to ensure financial sustainability, Citizens' statute allows for assessments if there is a deficit in any account after the exhaustion of Citizens' accumulated surplus.

Per statute, Citizens is required to make its best efforts to procure risk transfer for 1-in-100 years:

> *Section 627.351(6)c(9)*
> *Must provide that the corporation make its best efforts*[1] *to procure catastrophe reinsurance at reasonable rates, to cover its projected 100-year probable maximum loss as determined by the board of governors.*

With the leadership of the board, Citizens can continue to achieve its objective as there remains significant capacity in the marketplace at efficient prices. Citizens' need for risk transfer is greater this year as its policy count and related exposure has grown significantly from policies leaving private carriers and going to Citizens. However, that does not mean additional capacity for Florida risk, but rather a shift from some of the Florida insurers to Citizens, and therefore has no impact on overall capacity. Based on discussions prior to the December 2021 Board meeting, Citizens' financial advisor, reinsurance broker, investors, and reinsurers, Citizens' staff was confident that Citizens would be able to place the proposed risk transfer program for 2022 at efficient rates.

Citizens could accomplish its mission if it had actuarially sound rates and a risk transfer program which allows for surplus accumulation thereby reducing or eliminating surcharge risk for Citizens' own policyholders and assessments for all assessable Florida policyholders.

Citizens is not fully in control of its rates due to the "glide path" constraint, losses from events, and abusive litigation. Despite its inability to charge actuarially sound rates, Citizens was able to accumulate surplus from 2006 to 2016 without any major events occurring. However, in recent years Citizens has experienced significant losses from Hurricanes Irma and Michael and non-event losses from assignment of benefits and other abusive litigation. Losses from Hurricane Irma, however, were

[1] Please refer to the legal memorandum from Citizens' senior counsel to general counsel dated January 11, 2022 in the appendix regarding the best efforts terminology used in this section of the Statute.

tempered due to Citizens' effective placement of risk transfer – Citizens' Hurricane Irma losses were $2.27 billion and combined reinsurance recoveries (FHCF and private reinsurance market) were $936 million while the total risk transfer premium for 2017 was $247 million. Citizens' exposure has also grown in recent years due to instability in the property insurance market, primarily due to litigation, and Citizens' rate structure from HB1-A and subsequent legislation in 2008 and 2009 that affected Citizens' rates. The reduction in accumulated surplus and increase in exposure increases the probability and amount of assessments on state-wide insurance policyholders. Citizens is empowered to mitigate this increase in the probability and amount of assessments through the use of risk transfer. Citizens' risk transfer program is structured to provide liquidity by allowing Citizens to obtain reinsurance recoveries in advance of the payment of claims after a triggering event while reducing or eliminating the probabilities of assessments and preserving surplus for multiple events and/or subsequent seasons.

Citizens has access to the municipal market and the risk transfer markets to strengthen its claims-paying capacity. Citizens evaluates all financial options as part of its annual planning process prior to each season. Citizens works with its financial services team, including its senior managing underwriters, reinsurance broker, catastrophe bond underwriters, and special purpose vehicle administrator. Citizens' financial services team is comprised of some of the largest and most experienced firms within their respective markets.

For the 2022 season, Citizens is already in a strong liquidity position but can issue pre-event bonds in order to bolster its liquidity position if needed. ***While pre-event bonds and reinsurance both improve Citizens' liquidity position, they are not comparable from a capital structure perspective as they serve separate purposes within Citizens' claims-paying structure.*** A more in-depth explanation and analysis is included in the following pages.

Citizens' financial team represents the leading specialized insurance related firms. Citizens has a nationally leading insurance advisor – Raymond James, one of the largest global reinsurance brokers – Gallagher Re (formerly known as Willis Re), two of the leading catastrophe bond underwriters – Aon and Guy Carpenter, and a municipal bond underwriting team comprised of four of the largest underwriters – Bank of America / Merrill Lynch, Citigroup, Goldman Sachs, and JPMorgan. Additional details regarding Citizens' financial team are included in the appendix.

<u>Citizens' Surcharge and Assessment Authority</u>

If there is a Plan Year Deficit in any account, Citizens is required by Statute to levy surcharges and assessments in the following order.

- Citizens' policyholder surcharge can be levied in an amount of up to 15% per account for a total of 45% for all three accounts on a projected 2022 premium base of approximately $3 billion
- Regular assessments <u>for the Coastal Account only</u> on the state-wide insurance industry excluding Citizens' policyholders in the amount of up to 2% on a 2020 premium base of approximately $55 billion

- Emergency assessments on state-wide policyholders in the amount of up to 10% per account, per year for as many years as needed, for a total of 30% for all three accounts on a 2020 premium base of approximately $56 billion

Additional details regarding Citizens' assessments are included in the appendix.

Citizens' History of Assessments

Prior to the start of the 2004 hurricane season, Citizens had comparably minimal surplus totaling $1.5 billion and Citizens' ability to effectively manage its risk transfer program was still evolving. Citizens only had FHCF coverage in 2004 and FHCF and private reinsurance in the amount of $450 million for 2005. Due to the minimal amount of surplus and limited risk transfer program, Citizens had incurred significant deficits in 2004 and 2005 following the storm activity during those years.

For Plan Year 2004, Citizens levied a Regular Assessment in the amount of approximately $515 million, or 6.8%, for the Coastal Account (formerly known as the High Risk Account). This was Citizens' first Regular Assessment. Citizens also imposed a policyholder surcharge (formerly known as Market Equalization Surcharge) on the premiums paid by Citizens policyholders for all accounts upon renewal or issuance in an amount equal to the Regular Assessment levied.

For Plan Year 2005, Citizens determined that its consolidated deficit was approximately $1.766 billion and a Regular Assessment, up to 10%, per account, of the $7.863 billion assessment base, or up to $786.3 million for each account. However, the Florida Legislature appropriated $715 million to Citizens, of which $91.7 million was used to cure the deficits in both the PLA and the CLA. The remaining $623.3 million of appropriated funds was used to offset the Regular Assessment in the Coastal Account. The remainder of the Regular Assessment was levied in the Coastal Account in the amount of approximately $163.1 million, or 2.07%. Citizens also imposed a Citizens policyholder surcharge on the premiums paid by Citizens' policyholders for all accounts upon renewal or issuance in an amount equal to the Regular Assessment levied. This appropriation underscores the state's desire to not levy taxes and for Citizens to manage its risk efficiently. However, there is no permanent commitment from the state to provide funding in the future. This also confirmed the state's decision-makers' intent to not levy assessments as a first choice but instead to use it as a last resort.

Once the Plan Year deficit exceeds the maximum Regular Assessment amount, any remaining deficit is to be levied as an Emergency Assessment. The Emergency Assessment is up to 10% of premium, per account, for as many years as needed. If the Emergency Assessment is being levied over multiple years, Citizens' statewide assessment authority enables it to issue post-event bonds secured by the Emergency Assessment. The assessment authority also allows the financing costs related to the post-event bond issuance to be added to the assessment amount. In 2007, Citizens levied an Emergency Assessment to cure the remaining Plan Year 2005 deficit in the Coastal Account of $887.5 million and financing costs for the sole post-event bond issuance, or 1.4%. Citizens issued $1.1 billion of tax-exempt bonds with a ten-year final maturity payable from the 1.4% emergency assessment levied over ten-years in the total amount of approximately $1.4 billion. However, the growth in Citizens' direct written premium resulted in excess emergency assessment collections, which allowed Citizens to cease the collection of the emergency assessment two years early and allowed Citizens to defease the bonds in 2015, or two years prior to their final maturity.

Citizens' Use of Risk Transfer

Citizens' enabling statute requires it to make its best effort to procure catastrophe reinsurance in the private market at reasonable rates. In addition to Citizens' primary goal of paying claims expeditiously, when and if needed, and central to Citizens' goal of reducing exposure and, by extension, reducing or eliminating the amount and likelihood of any potential assessment burden on Florida taxpayers, is the transfer of risk through reinsurance mechanisms, traditionally accomplished via participation in the FHCF, traditional reinsurance and cat bonds.

As required by statute, Citizens purchases the mandatory layer of 90% coverage available from the FHCF for all accounts (PLA, CLA and Coastal). Whereas private insurers have an ability to select 45%, 75%, or 90% participation. Again, through the mandatory FHCF layer of 90%, the intent of legislature is to make sure Citizens transfers its risk in the maximum possible amount to meet the statute and to reduce the assessment burden. This coverage provides risk transfer at a relatively lower cost for the Florida market than the private reinsurance market would as the FHCF has no load factor and is a tax-exempt entity.

Reinsurance results in pure risk transfer in the event of a storm. From 2017 through 2021, Citizens has paid an average annual risk transfer costs of approximately $276 million for FHCF, private reinsurance, and cat bonds, for an average annual coverage amount of approximately $3.9 billion for an average rate-on-line of approximately 7.2%. Citizens' average direct written premium from 2017 through 2021 was $1.1 billion resulting in a combined risk transfer cost of approximately 24%.

Citizens' budgeted risk transfer program for 2022 includes risk transfer costs of approximately $722 million for FHCF, private reinsurance, and cat bonds, and a coverage amount of $8.9 billion for an average rate-on-line of approximately 8.1%. Citizens' projected direct written premium for 2022 is approximately $3.0 billion resulting in combined risk transfer costs of approximately 24%, similar to its average for the past five years. Citizens' combined risk transfer cost average of approximately 24% is approximately half of the Florida Markets average which ranges from 40% to over 50%.

Citizens' participation in the risk transfer markets reduces the potential assessments that result from losses reducing or exhausting Citizens' surplus and FHCF coverage and provide resources for multiple events and/or for multiple years. Without reinsurance, Citizens would only be able to pay claims from its surplus and FHCF coverage, which significantly increases the probability of state-wide assessments on Florida residents and not just Citizens' policyholders.

Risk transfer has the benefit after an event (as noted above) of providing significant claims-paying capacity and relieving a broad base of state-wide insurance policyholders from the burden of assessments at the worst possible times. Emergency assessments are levied on Florida residents who have no direct relation to Citizens[2] or in some cases are not even aware of Citizens as they do not own a home.

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[2] Citizens' policyholders also pay emergency assessments on Citizens' direct written premium as well as any other assessable lines of business such as autos.

Advantages:

1. **Reinsurance Requires No Repayment.** The purchase of reinsurance transfers risk to the private reinsurance market and provides stand-by capital for losses that would otherwise be financed with surplus and with assessments. This helps to preserve surplus and to relieve the assessment burden from Florida policyholders as it reduces the probability of Citizens' needing to finance losses after the exhaustion of its surplus.

2. **The Cost of Reinsurance is Borne by Those That Benefit from Risk Transfer Coverage and Reinsurance Reduces the Probability and Amount of Assessments.** Citizens' reinsurance cost is borne by its own policyholders, who are currently at risk for hurricane losses and thus have policies in effect and its premiums generated are paying for reinsurance.

   Reinsurance results in a dollar-for-dollar reduction in potential assessments. ***Emergency assessments are often viewed by policyholders as unfair and inequitable as they are a form of subsidizing Citizens' policyholders and they lead to further distortion of Florida's homeowners' insurance market.*** Additionally, emergency assessments tend to be unknown to most policyholders until after a large event when they surprisingly show up in a policyholder's premium notice and have the least ability to pay as they are paying for their own losses.

3. **Surplus Preservation**. Reinsurance allows Citizens to preserve accumulated surplus after an event for future events, to continue to earn investment income, and to minimize risk transfer cost and the probability of assessments as they are only needed for larger losses with lower expected losses.

Disadvantages:

1. **Reinsurance costs**, just like any insurance, remain whether or not an event(s) triggers reinsurance.

2. Traditional reinsurance generally needs to be **renegotiated and renewed each year**.

3. **The annual purchase of reinsurance may not be predictable** in the long run as pricing conditions are inherently volatile.

Pre-Event Bonds

In conjunction with its financial advisor, Citizens evaluates the financial markets and its capital structure to determine the optimum use of pre-event bonds. The advantages and disadvantages of pre-event bonds are discussed below.

Advantages:

1) **Pre-event Bonds May Allow for the Locking-in of Interest Rates for Long Periods**. Pre-event bonds allow for the locking in of interest rates over multiple years depending on the maturity structure of the pre-event bonds.

2) **Current Market Conditions are Conducive for Pre-Event Bonds.** Depending on market conditions, issuing pre-event bonds could generate incremental investment income. The market conditions for pre-event fixed rate bonds are conducive since interest rates are currently at historically low levels, especially on the short end. In the current market environment, Citizens can generate incremental income which can contribute marginally to surplus in the amount of approximately $10 million in incremental income for every $1 billion in pre-event bonds issued based on the issuance of one-year bonds.

3) **Pre-event Bonds Provide Sustainability and Liquidity**. Pre-event bonds provide sustainability and liquidity. They give Citizens flexibility and could potentially be used to delay post-event bonds if needed after a large event. In addition, the surplus can be invested with a longer duration to maximize investment income.

Disadvantages:

1) **If Pre-event Bonds are Used to Pay Losses, They May Need to be Refinanced with Post-Event Bonds When They Mature.** The issuance of post-event debt may be financed with emergency assessments that will be paid by a broad base of policyholders who are not the direct beneficiaries of Citizens' property insurance coverage. Ultimately, post-event bonding will result in placing a cost on insurance lines of business that are used to subsidize Citizens' policyholders. This has been viewed as an unfair "hurricane tax." Excessive emergency assessments can operate as a drain on Florida's economy at the worst possible time (after a large event or multiple events).

2) **Based on the Current Statutory Provisions, Pre-event Bonds Cannot be Issued on a Consolidated Basis for all Three Accounts.** For as long as pre-event bonds are outstanding for a respective account, all three Citizens' accounts cannot be combined. After the June 1, 2022 maturity of the PLA/CLA bonds, the only remaining outstanding pre-event bonds will be the June 1, 2025 maturity (callable on December 1, 2024) of the Coastal Account bonds. If the legislature changes Citizens' statute to permit the consolidation of all three accounts and Citizens defeases its outstanding Coastal

Account bonds, Citizens could issue pre-event bonds for the consolidated account. The projected defeasance cost as of June 1, 2022 is approximately $14 million and approximately $7.5 million as of June 1, 2023. Until then, Citizens would be statutorily required to issue bonds separately for the Coastal Account and PLA/CLA.

Claims-Paying Resources and Loss Scenarios Analysis

Citizens' capital structure is comprised of accumulated surplus, risk transfer through the statutorily mandated purchase of FHCF coverage at the 90% level, risk transfer through traditional reinsurance markets and capital markets, policyholder surcharges, and regular and emergency assessments. Citizens' liquidity position for an initial event is strong based on the current surplus levels and the proposed risk transfer program for 2022. Without the use of private risk transfer, Citizens will expose 100% of its surplus for a 1-100 year event for both Coastal and PLA. Due to Citizens' increase in exposure approximately $1.0 billion and $1.4 billion of surplus is exposed for Coastal and PLA[3], respectively, below the attachment point of the FHCF. Therefore, the impact of multiple small events or a singular large event would be dramatic for Citizens' surplus levels for the Coastal Account and even more significant for PLA.

The results of our analysis of Citizens' Coastal Account and PLA claims-paying structure for the 2022 season are summarized in the following pages while the detailed tables are included in the appendix. These scenarios shown are:

- Base Case: No new risk transfer purchased in 2022
- Alternative Case: Proposed risk transfer program of approximately $2.5 billion for the Coastal Account and approximately $2.0 billion for PLA as in the approved budget

Both scenarios are shown without any event losses as well as loss scenarios for an initial event of 1-50 years followed by a subsequent 1-in-50 event as well as an initial event of 1-in-100 years followed by a subsequent 1-in-100 year event. As illustrated in the tables in the appendix, Citizens' surplus levels and assessment burden on Florida residents is significantly adversely affected by back-to-back events or a singular 1-in-100 year event if Citizens does not purchase any new reinsurance for 2022.
Key takeaways from the scenario of not purchasing any new risk transfer for 2022:

- A 1-in-50 year event (approximately $3.8 billion gross losses and LAE) in the Coastal Account would eliminate approximately $2.0 billion of its $3.2 billion surplus and would leave the Coastal Account with only approximately $1.8 billion of claims-paying resources before surcharges and assessments for a subsequent event – *approximately $1.2 billion of surplus and $565 million of its existing 2021 catastrophe bonds would remain for a subsequent event*

- A 1-in-50 year event (approximately $3.7 billion gross losses and LAE) in PLA would eliminate approximately $1.6 billion of its $1.8 billion surplus and would leave PLA with only approximately $677 million of claims-paying resources before surcharges and assessments for a subsequent event – *approximately $242 million of surplus and $435 million of existing 2020 and 2021 catastrophe bonds would remain for a subsequent event*

- *A 1-in-100 year event in both the Coastal Account* (approximately $6.2 billion gross losses and LAE) and PLA (approximately $6.3 billion gross losses and LAE) would completely eliminate all of Citizens' surplus in the Coastal Account and PLA and *would require a total of approximately*

[3] CLA has sufficient surplus and does not require any reinsurance.

\$1.9 billion of surcharges and assessments – approximately \$447 million of surcharges on Citizens' policyholders and approximately \$1.5 billion of assessments on Florida residents

- *Back-to-back 1-in-50 year events* would be catastrophic *for both the Coastal Account and PLA* – this loss level would eliminate all of Citizens' surplus in the Coastal Account and PLA and *would require a total of over \$4.5 billion of surcharges and assessments* – \$447 million of surcharges on Citizens' policyholders and approximately \$4.1 billion of assessments on Florida residents

Some key takeaways from the scenario of purchasing the proposed risk transfer program for 2022:

- ***In the event of a 1-in-100 year event in both the Coastal Account*** (approximately \$6.2 billion gross losses and LAE) ***and PLA*** (approximately \$6.3 billion gross losses and LAE) – ***Citizens would not levy any assessments on Florida residents***. However, if Citizens does not purchase any risk transfer for 2022, Citizens would levy an assessment on Florida residents of approximately \$1.5 billion for the same loss scenario

- ***In the event of back-to-back 1-in-50 year events for both the Coastal Account and PLA – Citizens' assessment burden on Florida residents would be approximately \$978 million*** as compared to \$4.1 billion for the same loss scenario without any new risk transfer purchased in 2022, or approximately \$3.1 billion in additional assessments on Florida residents versus the assessment burden on Florida residents under the proposed risk transfer program for 2022

The results of this analysis illustrates the importance of Citizens' capital structure through its proposed risk transfer program and surplus preservation for Citizens to ensure that state-wide insurance policyholders are not subsidizing Citizens' policyholders through the levying of assessments after an event.

Conclusion

Citizens was established pursuant to 627.351 (6) F.S. to provide certain personal and commercial coverage to qualified risks under circumstances specified in the statute. While Citizens is a governmental entity, it is funded by premiums collected from its policyholders, consistent with the intent of the legislature. Only once in its history has Citizens been the recipient of legislative funds, the intent of which was to reduce the tax burden on Floridians. By optimally managing hurricane risk through efficient strategies, including risk transfer and surplus preservation, Citizens will continue to comply with this statutory intent and not unnecessarily tax Florida residents who are not Citizens policyholders.

Citizens annually evaluates the debt and risk transfer markets in partnership with its financial services team to select the financing and risk transfer options that optimize and strengthen its liquidity position to reduce the probability and amount of assessments on Florida residents. Citizens' enabling Statute and Plan of Operation requires Citizens' Board, under duties and responsibilities, to use its best efforts to procure catastrophe reinsurance at reasonable rates to cover its projected 100-year Probable Maximum Loss ("PML").

Risk transfer has significant financial implications on Citizens, the State of Florida, and ultimately on Florida residents. This white paper was prepared with the intent to impart full awareness, enhance dialogue, and convey the serious statewide consequences of Citizens' risk strategy.

Working with the Board's skillset and leadership, along with the decades of experience brought by Citizens' executive team and advisors, in terms of establishing appropriate financial and business strategies, including the risk transfer program, we can protect not only Citizens' financial position but the state's financial position as well. As discussed in the Board meeting, the staff believes that risk management decisions should serve to protect Citizens' financial position and Florida residents, and not be a way to impact legislative decisions. There are severe potential implications of making decisions that could have significant impacts on Citizens' capital structure and the state's ratings, therefore the resulting assessment risks to Floridians should be socialized with Florida's leadership.

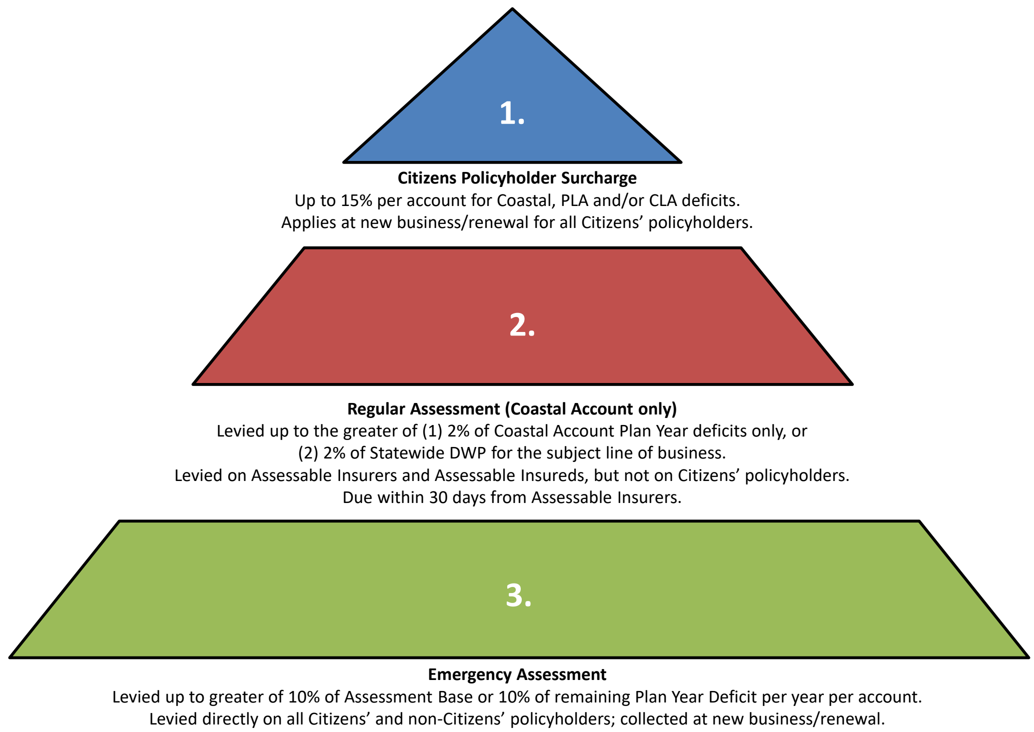
Appendix

Citizens' Financial Team

Citizens' financial team represents the leading specialized insurance-related firms.

- **Raymond James**: Raymond James serves as Citizens' financial and investment advisor. Raymond James is the number one firm nationally in the catastrophe insurance advisory sector and a top 10 municipal bond underwriter. In addition to Citizens, Raymond James' catastrophe insurance advisory clients include: the California Earthquake Authority, the California Wildfire Fund, the Florida Hurricane Catastrophe Fund, the Florida Insurance Guaranty Association, and the Metropolitan Transportation Authority. In addition, Raymond James serves as an underwriter for Louisiana Citizens Property Insurance Corporation, the North Carolina Insurance Underwriting Association, and the Texas Windstorm Insurance Association. Raymond James has served as advisor for the issuance of $4.4 billion of municipal bonds, $5.5 billion of catastrophe bonds, $23 billion of reinsurance, and serves as investment consultant for over $43 billion of assets for all of its clients since 2017.
- **Gallagher Re**: Gallagher Re serves as Citizens reinsurance broker. Gallagher Re recently acquired Willis Re and is one of the largest global reinsurance brokers with over 2,400 employees globally. In 2020, Gallagher Re placed over $19.4 billion in ceded reinsurance for approximately 860 clients in more than 110 countries around the world.
- **Aon and GC Securities**: Aon and GC Securities serve as Citizens' joint structuring agents and joint bookrunners for its catastrophe bond placements. These two firms are the top two catastrophe bond underwriters having served as sole or joint structuring agent or bookrunner for a combined outstanding issuance amount of over $15 billion for Aon and over $12 billion for GC Securities. The use of different firms as catastrophe bond underwriters and reinsurance brokers enables Citizens to achieve the most efficient reinsurance placement and catastrophe bond issuance in order to take advantage of the competitive pricing tension between the two markets.
- **Municipal Bond Senior Managing Underwriters**: Citizens has a senior managing underwriter team comprised of Bank of America / Merrill Lynch, Citigroup, Goldman Sachs, and JPMorgan for its municipal bond transactions that represent the leading municipal bond underwriters in the nation and are the foremost municipal bond underwriters in the catastrophe insurance space. These firms assist Citizens in the issuance of pre-event and post-event municipal bonds.

Citizens' Surcharge and Assessment Authority



The assessment base for emergency assessments represents total premiums of approximately $56 billion compared to Citizens' projected policyholder premiums of approximately $3 billion paid by those who benefit directly from Citizens' coverage. Property and casualty policyholders include approximately 29 lines of coverage including automobile, business property and liability, aircraft, fidelity bonds, surety bonds, warranty, mortgage guaranty, ocean marine, etc.

Insurable Lines Subject to Regular and Emergency Assessments		
Fire	Financial Guaranty	Aircraft (all perils)
Allied Lines	Earthquake	Fidelity
Multiple Peril Crop	Other Liability	Surety
Farmowners Multiple Peril	Products Liability	Burglary and Theft
Homeowners Multiple Peril	Private Passenger Auto No-Fault	Boiler and Machinery
Commercial Mult-Peril (non-liability)	Other Private Passenger Auto Liability	Credit
Commercial Multi-Peril (liability)	Commercial Auto No-Fault	Warranty
Mortgage Guaranty	Other Commercial Auto Liability	Aggregate Write-Ins for Other Lines
Ocean Marine	Private Passenger Auto Physical	
Inland Marine	Commercial Auto Physical	

Loss Analysis Tables

	Coastal Account			
	Initial Event (2022)		Subsequent Event (2022)	
($ in Millions)	Base Case: No New Risk Transfer Purchased in 2022	Alternative: Budgeted Risk Transfer Purchase for 2022	Base Case: No New Risk Transfer Purchased in 2022	Alternative: Budgeted Risk Transfer Purchase for 2022
Sources				
Surplus Available	**$3,208**	**$3,037**		
FHCF Coverage	$1,770	$1,770		
Private Risk Transfer	$625	$2,492		
Total Claims-Paying Resources	***$5,604***	***$7,300***		
1-50 Year Loss Uses				
Gross Losses and LAE	**$3,833**	**$3,833**	**$3,833**	**$3,833**
Surplus Used	$2,003	$1,133	$1,206	$1,904
FHCF Coverage	$1,770	$1,770	$0	$0
Private Risk Transfer	$60	$930	$565	$1,562
Citizens' Policyholder Surcharge	$0	$0	$126	$126
Regular Assessments	$0	$0	$1,094	$241
Emergency Assessments over 1-Year	$0	$0	$843	$0
Emergency Assessment % over 1-Year	0.00%	0.00%	1.51%	0.00%
Surplus Used as a % of Surplus Available	**62%**	**37%**	**38%**	**63%**
Surplus Remaining for Subsequent Events (2022)	**$1,206**	**$1,904**	**$0**	**$0**
Investment Income on Remaining Surplus (1.9%)	*$23*	*$36*	*$0*	*$0*
Citizens Policyholders Surcharges (CPS)	**$0**	**$0**	**$126**	**$126**
Total Assessments on Florida Policyholders (RA + EA)	**$0**	**$0**	**$1,937**	**$241**
Total Surcharges & Assessments (CPS + RA + EA)	**$0**	**$0**	**$2,063**	**$366**
1-100 Year Loss Uses				
Gross Losses and LAE	**$6,216**	**$6,216**	**$6,216**	**$6,216**
Surplus Used	$3,208	$1,953	$0	$1,084
FHCF Coverage	$1,770	$1,770	$0	$0
Private Risk Transfer	$625	$2,492	$0	$0
Citizens' Policyholder Surcharge	$126	$0	$0	$126
Regular Assessments	$486	$0	$607	$1,094
Emergency Assessments over 1-Year	$0	$0	$5,589	$3,912
Emergency Assessment % over 1-Year	0.00%	0.00%	10.00%	7.00%
Unfunded Liability Funded by Emergency Assessments in 2023	$0	$0	$19	$0
Surplus Used as a % of Surplus Available	**100%**	**64%**	**0%**	**0%**
Surplus Remaining for Subsequent Events (2022)	**$0**	**$1,084**	**$0**	**$0**
Investment Income on Remaining Surplus (1.9%)	*$0*	*$21*	*$0*	*$0*
Citizens Policyholders Surcharges (CPS)	**$126**	**$0**	**$0**	**$126**
Total Assessments on Florida Policyholders (RA + EA)	**$486**	**$0**	**$6,197**	**$5,006**
Total Surcharges & Assessments (CPS + RA + EA)	**$612**	**$0**	**$6,197**	**$5,132**

The maximum Citizens' policyholder surcharge able to be levied is 15% of direct written premium per account.
The maximum regular assessment able to be levied for the Coastal Account is 2% of state-wide assessable direct written premium less Citizens' direct written premium.
The maximum emergency assessment able to be levied is 10% of state-wide assessable direct written premium per account as a one-time assessment or can be funded with post-event bonds with a maximum maturity of 30-years. Levying the emergency assessment as a one-time assessment will have a timing delay based on calculating the assessment rate, OIR approval of the assessment rate, OIR issuing the assessment order, and then the insurance companies including the assessment rate in their billing programs.

	PLA			
	Initial Event (2022)		Subsequent Event (2022)	
($ in Millions)	Base Case: No New Risk Transfer Purchased in 2022	Alternative: Budgeted Risk Transfer Purchase for 2022	Base Case: No New Risk Transfer Purchased in 2022	Alternative: Budgeted Risk Transfer Purchase for 2022
Sources				
Surplus Available	**$1,835**	**$1,671**		
FHCF Coverage	$2,714	$2,714		
Private Risk Transfer	$435	$1,987		
Total Claims-Paying Resources	***$4,984***	***$6,372***		
1-50 Year Loss Uses				
Gross Losses and LAE	**$3,715**	**$3,715**	**$3,715**	**$3,715**
Surplus Used	$1,593	$1,357	$242	$314
FHCF Coverage	$2,122	$2,122	$591	$591
Private Risk Transfer	$0	$236	$435	$1,751
Citizens' Policyholder Surcharge	$0	$0	$321	$321
Emergency Assessments over 1-Year	$0	$0	$2,126	$738
Emergency Assessment % over 1-Year	0.00%	0.00%	3.80%	1.32%
Surplus Used as a % of Surplus Available	**87%**	**81%**	**13%**	**19%**
Surplus Remaining for Subsequent Events (2022)	**$242**	**$314**	**$0**	**$0**
Investment Income on Remaining Surplus (1.9%)	*$5*	*$6*	*$0*	*$0*
Citizens Policyholders Surcharges (CPS)	**$0**	**$0**	**$321**	**$321**
Total Assessments on Florida Policyholders (EA)	**$0**	**$0**	**$2,126**	**$738**
Total Surcharges & Assessments (CPS + EA)	**$0**	**$0**	**$2,447**	**$1,059**
1-100 Year Loss Uses				
Gross Losses and LAE	**$6,271**	**$6,271**	**$6,271**	**$6,271**
Surplus Used	$1,835	$1,570	$0	$101
FHCF Coverage	$2,714	$2,714	$0	$0
Private Risk Transfer	$435	$1,987	$0	$0
Citizens' Policyholder Surcharge	$321	$0	$0	$321
Emergency Assessments over 1-Year	$966	$0	$4,624	$5,589
Emergency Assessment % over 1-Year	1.73%	0.00%	8.27%	10.00%
Unfunded Liability Funded by Emergency Assessments in 2023	$0	$0	$1,647	$259
Surplus Used as a % of Surplus Available	**100%**	**94%**	**0%**	**0%**
Surplus Remaining for Subsequent Events (2022)	**$0**	**$101**	**$0**	**$0**
Investment Income on Remaining Surplus (1.9%)	*$0*	*$2*	*$0*	*$0*
Citizens Policyholders Surcharges (CPS)	**$321**	**$0**	**$0**	**$321**
Total Assessments on Florida Policyholders (EA)	**$966**	**$0**	**$4,624**	**$5,589**
Total Surcharges & Assessments (CPS + EA)	**$1,287**	**$0**	**$4,624**	**$5,911**

The maximum Citizens' policyholder surcharge able to be levied is 15% of direct written premium per account.
The maximum emergency assessment able to be levied is 10% of state-wide assessable direct written premium per account as a one-time assessment or can be funded with post-event bonds with a maximum maturity of 30-years. Levying the emergency assessment as a one-time assessment will have a timing delay based on calculating the assessment rate, OIR approval of the assessment rate, OIR issuing the assessment order, and then the insurance companies including the assessment rate in their billing programs.

To: Tim Cerio, General Counsel

Date: January 11, 2022

From: Jimmy Kutter, Senior Counsel, Corporate Legal Counsel

Re: Best Efforts to Procure Catastrophe Reinsurance

Best Efforts to Procure Catastrophe Reinsurance

Citizens' Plan of Operation and enabling statute establish that Citizens must use "best efforts" to procure catastrophe reinsurance at reasonable rates to cover its projected 100-year maximum probable loss.[1] This memorandum addresses the meaning of this "best efforts" requirement under Florida law.

A. Recommendations/Conclusions.

- An examination of the plain language and surrounding provisions provides persuasive evidence that "best efforts" requires diligent pursuit of catastrophe reinsurance by Citizens.
- Where two courts have interpreted similar statutory language requiring that condominium associations use "best efforts" to procure insurance coverage for the condominium, their analyses reflect that the duty of best efforts requires the obligor to exercise substantial efforts in procuring insurance specified in the provision, subject to the recognition that successful procurement is not guaranteed due to market forces beyond the obligor's control.
- While courts interpreting the requirements of a contractual "best efforts" provision may differ by circumstance or jurisdiction, the obligation will at a minimum be construed as equal to the duty of good faith, as that is an implied duty recognized by Florida in every contract. However, the phrase is commonly interpreted as more extensive than a mere obligation of good faith.

B. Analysis

Citizens' Plan of Operation requires that the Board use its "best efforts" to procure catastrophe reinsurance at reasonable rates, as follows:

> The Board shall use its best efforts to procure catastrophe reinsurance at reasonable rates to cover its projected 100-year probable maximum loss, as determined by the Board, from reinsurers determined to be qualified by the Board.[2]

This provision implements a mandatory requirement specified in Citizens' enabling statute, which provides as follows:

> (c) The corporation's plan of operation:
>
> . . .
>
> 9. Must provide that the corporation make its best efforts to procure catastrophe reinsurance at reasonable rates, to cover its projected 100-year probable maximum loss as determined by the board of governors. If catastrophe reinsurance is not available at reasonable rates, the corporation need not purchase it, but the corporation shall include the costs of

[1] Citizens' Plan of Operation, Section 7(C); Section 627.351(6)(c)9., Florida Statutes

[2] Citizens' Plan of Operation, Section 7(C)

reinsurance to cover its projected 100-year probable maximum loss in its rate calculations even if it does not purchase catastrophe reinsurance.[3]

The phrase "best efforts" is not defined within Citizens' Plan of Operation or enabling statute. However, an examination of the plain language and surrounding provisions of the statute supports two conclusions.

First, this provision requires that Citizens pursue catastrophic reinsurance at reasonable rates to cover its projected 100-year probable maximum loss. If Citizens construed this provision as providing full discretion in determining whether to pursue catastrophic reinsurance, that interpretation would not reflect the legislative word choice of "must" and "best efforts" for this provision. Other provisions within the same subsection use the word "may" to indicate that Citizens has discretion. "The legislative use of different terms in different portions of the same statute is strong evidence that different meanings were intended."[4] Further, the fact that the statute requires Citizens to include the cost of reinsurance to cover its projected 100-year probable maximum loss in its rates (even if not purchased), coupled with the provision that only provides that Citizens need not purchase such reinsurance if it is "not available at reasonable rates" is persuasive evidence that the legislature intends to require a diligent pursuit of catastrophe reinsurance by Citizens at reasonable rates.

Second, an examination of other requirements within the same statutory subsection supports the conclusion that "best efforts" is used in recognition that certain factors are beyond Citizens' control. Most other provisions within the same subsection use a more absolute "must" and relate to matters that are more fully within Citizens' control. For instance, other provisions with a more absolute "must" relate to adoption of certain coverage forms, adoption of a quota share program, and operating subject to the supervision and approval of a board of governors.[5]

Where two courts have interpreted a similar "best efforts" provision in condominium law, their analyses reflect that "best efforts" requires substantial efforts in procuring the insurance specified in the provision, subject to the recognition that successful procurement is not guaranteed due to market forces beyond the obligor's control. In both cases, the statutory provision at issue requires that the condominium association use "best efforts to obtain and maintain adequate insurance to protect the association" as further specified in the statute. [6]

In Roberts v. Nine Island Ave. Condo Ass'n, the Third District Court of Appeal affirms the trial court's determination that the condominium association had not violated its obligation under the statute when it failed to secure coverage for the condominium's marina.[7] The court reasons that even if coverage for the marina was contemplated as part of the best efforts requirement – of which the court was skeptical – the plaintiffs offered no evidence that the association had failed to seek coverage, or that coverage was available. Rather, the only evidence on record was that insurance had been maintained until coverage was

[3] Section 627.351(6)(c)9., Florida Statutes. The first sentence of subsection 9. has remained unchanged since Citizens was established in 2002. The second sentence was added effective July 1, 2021 pursuant to Chapter 2021-77, Laws of Florida (2021).
[4] State v. Mark Marks, P.A., 698 So. 2d 533, 541 (Fla. 1997)(citing Department of Professional Regulation v. Durrani, 455 So.2d 515, 218 (Fla. 1st DCA 1984)).
[5] Section 627.351(6)(c)1., Florida Statutes; Section 627.351(6)(c)2., Florida Statutes; Section 627.351(6)(c)4., Florida Statutes.
[6] Section 718.111, Florida Statutes (2005).
[7] Roberts v. Nine Island Ave. Condo. Ass'n, Inc., 126 So. 3d 286, 290 (Fla. 3d DCA 2011)

nonrenewed by the insurer, and that the only available insurer, the "'state sponsored' insurer of last resort", had advised the association that there was "no way of getting insurance" for the marina because of its age.[8]

In Citizens Prop. Ins. Corp. v. River Manor Condo Ass'n, the Fourth District Court of Appeal rejects that the condominium statute's "best efforts" requirement for certain coverages overrides an exclusion for such coverages within the insurance policy, notwithstanding other more general insurance policy language requiring compliance with Florida law.[9] When rejecting this conclusion, the court in part reasons that the best efforts requirement for coverage was "implicitly recognizing that market forces may in some instance prevent this objective from being achieved".[10] However, in rejecting the condominium association's argument that the statute should be read to override the coverage exclusion, the court notes that the statute could not be read that way because then the provision requiring the association to use its best efforts

> …would be meaningless, as the association would not have to use any effort—let alone its "best efforts"—to obtain it. The association, in violation of its statutory obligation, could in fact expend "no effort" and secure the coverage by legislative fiat any time an insurer elected to issue a policy.[11]

Although these cases do not create a bright line regarding how much effort one must exert to meet the duty to exert best efforts, they reflect that the duty to exert best efforts does not equal a duty to achieve a result. The ability to achieve a result may be limited by forces outside of the control of the obligor. However, they also clearly reflect that a level of "diligence" is required.

Other courts have analyzed the duty to exert best efforts in contracts. These courts have indicated that the duty is context-specific. In First Nat. Bank of Lake Park v. Gay, the Fourth District Court of Appeal reasons that "the definition of 'best efforts' may vary depending upon the factual circumstances surrounding the transaction and the intent of the parties in entering into the transaction."[12] The court rejects that the trial court erred in refusing a requested jury instruction that best efforts "requires the party owing the duty to take all action and do all things necessary to consummate the transaction completed by the agreement."[13] The case involved a lease provision that obligated the lessor to exercise best efforts to induce a tenant to end the lease early, and the court concludes that interpretation of the term is a proper question for the jury. The court remands the case for other reasons.[14]

In a special concurrence, Judge Farmer reasons that it was problematic for the trial court to not give any jury instruction on the meaning of "best efforts".[15] Judge Farmer asserts that "although deceptively simple and ostensibly clear, the usual contractual term, best efforts, has little common meaning among lawyers, if

[8] *Id.* at 290.
[9] Citizens Prop. Ins. Corp. v. River Manor Condo. Ass'n, Inc., 125 So. 3d 846 (Fla. 4th DCA 2013)
[10] *Id.* at 852.
[11] *Id*. at 851.
[12] First Nat. Bank of Lake Park v. Gay, 694 So. 2d 784, 788 (Fla. 4th DCA 1997); *see also* Ashokan Water Services, Inc. v. New Start, LLC, 11 Misc. 3d 686, 692, 807 N.Y.S.2d 550, 556 (Civ. Ct. 2006)(reasoning that "'Best efforts' can only be defined contextually."); Is This Really the Best We Can Do? American Courts' Irrational Efforts Clause Jurisprudence and How We Can Start to Fix It, 109 Geo. L.J. 665, 673 (2021)(stating that "a party's obligations under a "best efforts" clause are unsettled, fluid, and highly fact-dependent.")
[13] *Id.* at 787.
[14] *Id.* at 788.
[15] *Id.* at 789.

this case is any guide."[16] Judge Farmer acknowledges that there is a range of interpretations of the term, including a US District Court, District of Puerto Rico opinion concluding that the clause is satisfied by mere positive steps, and a US Bankruptcy Court, West District of Kentucky opinion reasoning that "it certainly imposes a legal duty of performance more demanding that mere competence or due diligence."[17] Judge Farmer asserts that the latter view is more consistent with his own.

While the exact requirements of a contractual "best efforts" may differ by circumstance or jurisdiction, the obligation will at a minimum be construed to be equal to the general contractual duty of good faith, as that is an implied duty recognized by Florida in every contract.[18] However, as Judge Farmer references in First Nat. Bank of Lake Park v. Gay, the term is commonly interpreted as more extensive than a mere obligation of good faith.[19] Interpretations are context specific and may vary across jurisdiction, but two common approaches are to interpret "best efforts" as imposing an additional requirement of diligence, or more extensive efforts than good faith subject to reasonableness.[20]

[16] *Id.* at 790.
[17] *Id.* at 790-791.
[18] *See, e.g.,* County of Brevard v. Miorelli Eng'g, Inc., 703 So. 2d 1049, 1050 (Fla. 1997)
[19] *See* First Nat. Bank of Lake Park v. Gay, 694 So. 2d 784, 788 (Fla. 4th DCA 1997); *see, also,* E. Allan Farnsworth, On Trying to Keep One's Promises: The Duty of Best Efforts in Contract Law), 46 U. Pitt. L. Rev. 1 (1984)(citing cases such as the seminal New York decision, Bloor v. Falstaff Brewing Corp., 601 F.2d 609, 610 (2d Cir. 1979); Van Valkenburgh, Nooger & Neville, Inc. v. Hayden Pub. Co., 30 N.Y.2d 34, 42, 281 N.E.2d 142, 143 (1972)); Is This Really the Best We Can Do? American Courts' Irrational Efforts Clause Jurisprudence and How We Can Start to Fix It, 109 Geo. L.J. 665, 675-677 (2021)(citing cases such as W. Geophysical Co. of Am., Inc. v. Bolt Associates, Inc., 584 F.2d 1164, 1166 (2d Cir. 1978))
[20] *See* Is This Really the Best We Can Do? American Courts' Irrational Efforts Clause Jurisprudence and How We Can Start to Fix It, 109 Geo. L.J. 665, 675-677 (2021)