Senate Banking and Insurance Committee 1.23.13

Sen Simmons opened the meeting – there is unanimity and consensus that something that must be done.

We do know that Citizens is not the mkt of last resort and it unfairly competes with private insurers and some believe that that doesn't make any difference but we have a spectrum of opitions to think about.

We can do nothing and let Citizens function as a dual insurer – it causes our state to increase its exposure. One member pointed out to me that that's ok and if Citizens cant pay then Citizens can go to Feds. That we should expect the feds to come down and this legislator sees no problem with that position and I think this idea should be discussed.

We can do a piecemeal approach

Or we can do a comprehensive approach

I think that we need to look at lots of ideas – we need to define Citizens true role as an org of last rsort? Do we give the commissioner the authority to implement Louisiana Citizens approach? Should higher rates apply to rnewals or just new business? We need to define that and what we can accept as a state.

Do we work on a mathematical model to get to the top 20 policy rate? Do we go 50% of the difference between 15% and 20% in terms of a glidepath? What is the "Something" that would cause the market to move?

Private rate bands – do we use these?

Should we allow Citizens to buy term insurance and to purchase reinsurance because if there is an event that it buys reinsurance for only if there is a cataclysmic event so it's better prepared for that storm – poor pun!

We want to make sure that Citizens isn't selling illusory policies and we don't want double catastrophe – first would be the storm and then insureds cant rebuild after an event because they don't have the right coverage.

-Takeouts – do we use the existing format? Do we modify that? Do we amplify or increase upon it?

We have a group of solutions so please think about ways to solve this so we can make sure we have a vibrant market here and at the same time can help redfine the function of citizens. and if not, we will discuss that too.

Robin Westcott: Floridians should go to a competitive insurance state and this can't be accomplished over night and as CFO said, we need to strive to get to a better place so investors get the signal. What I l ike to present to you today is to blunt the shock of a cat.

In every study since Hurriane Andrew, they say that mitigation is the only solution and answer for our state.

We need to centralize and consolidate efforts in this state. That would mean moving the public model to DEM and it m akes sense that this should be moved to folks that do this every day. It centralizes, consolidates and mitigates our homes. We would set up an advisory council that could help us solve some problems in our state with members that work on this every day.

We have no collevitve databse of risk and manytimes folks don't evaluate what their exposure is. Other benefits come with moving the public model. The federal flood model changed this last year and we need to use the model for flood. We control the flood issues in our state and it could be magnificent with our state if we use the model aoppropriately.

We need to re-do our mit credits and we have no match how that is structured in a copany and how they buy reinsurance. We need some sense with the credits and reinsurance and we have no grasp on commercial properties and we have whole gaps in the way mit credits are applied and centralizing that and letting one body control and understand how its done makes sense.

We have a lot of data and we don't kjnow how to collect this data and manipulate the reduction of risks.

We all saw last week that we have the same number of slides and what has changed is our exposure and so different thng have contributed to that and let me give you an example about that. When talking about replacing someone's home its not market value but its what it costs to replace that home on that property. In broward co, the house is at $164k yet it costs over $200k to replace it. If you were to take the microcosm of Citizens and use the $300 million in reinsurance that citizens buys and it only attaches at the 1 in 35 event and you committed it to the coastal acct with its 500k policies and has stayed static and you started to mitigate homes in the coastal acct (average home is a 1700 sq ft home), we could reduce the PML in the coastal acct by 20%. I undertand that what we are doing is getting a btter value in mitigation and mitigating homes saves all ins conusmers money as a whole. There exposure is reduced.

Pociask – American Consumer Institute: let's discuss affordability. Who wins and who loses?

When it comes to affordability and incomes, there is no question these folks have higher incomes. Look at premium or exposure , in every case the income goes up. The difference is South and the other coasts. Some areas have 4 to 16 times the median income of the state. I want to focus on the issue that there are homes we are insuring that we shouldn't.

Homes that are not owner occupied but renter occupied. What we see here is vacant homes and often they are 2nd homes. Let's look at the nature of 2nd homes in the state and I took a band of towns in a coastal area in the southeast and looked at census places with 30, 40, 50 – 60% are vacant. The important fact is that while folks have higher incomes and they pay cash on these homes and these folks can afford the insurance and pay cash for the home and why should we subsidize them.

2nd home buyers have more income but they buy lower value homes. The reality is that if we put $1 milion cap on citzens coverage, that isn't a great screen.

These 2nd homes are not your constituent. In many cases, 50% live more than 300 miles away and many are 500 miles away and many are Foreign homebuyers

National Realtors show the median homeprice of foreign owners pay about $200k in cash.

Canadian and Europeans represent 1/3 – 31% are foreign and the one million means almost nothing.

90% are paid by cash. We have a group of folks who are buying cash and Citizens is subsidizing. The folks that pay, the 76% who pay are paying into this and who is benefiting? These folks tend to have higher wealth and the other element is that these are 2nd hmes, foreign homes, and out of state and the result is the support going to folks that are not your constituents.

The national flood insurance program said no more subsidies for 2nd properties so we should consider that here. Part of the answer is to get capital back here. We need a keepout policy and we should renew for just primary homes for folks that live, work in the state and get to risk based pricing.

Lowering the million may work and if they take on new policies then take them on a the right rate and it's a good way to stop Citizens from growing and it provides a last resort opportunity. We need rate bands and compete with excess and surplus lines providers. We need to have them to be self sufficient.

I ike the point abou tmitigationh but if we don't have risk based pricing – you can't discount something that is already a negative number.

Jay Neal: We were formed 2 years ago and one of the observations we made was that we needed long term policy in place – we need balance.

Simmons: who are your members?
Neal: anyone in Florida can join – policyholders, construction, real estate, trial attorneys, defense bar

One of things we should avoid is the civil war rhetoric – coastal v inland, north v south and when we focus on this the media picks it up and we belive citizens should come down in size when that process is in place lets not put the policyholder in the cross hairs. We should focus on reducing the costs for those removing policies vs constantly talking about increasing rates. Out of state CEOs talk about the regulatory environment and the political

Neal : we need consumer groups and industry groups standing together

Recommendations to downsize citizens:

Current takeout letter – the policyholder doesn't talk about rate and that is impediment for those wanting to come out
We have used diminished policy coverages to get folks to come out but we must use the threat of assessment as a reason for folks to come out – its 4 times as expensive and in additional years I have a theory

If you look at where we would be at 1:100 event, you will see we will pay 5% every year for 30 years after a 100 year event. If I

Further restrictions on coverage A values to do a study to make sure the property values are there in the private market.

When we talk about the glidepath and the cost curve – if you lower the cost of the indicated rates you can decrease the glidepath.

1- mitigation and look at how to get those pre FBC
2- claims costs drive rates and there re two particular areas – we have these abusive assignment of benefits and we should get rid of abuses of chipped tile – we have tendency to fight fraud and others to get hurt
3- Citizens and the cat fund – we took time to get in the pickle we re in and what we think – we hear all the time that the cat fund can't pay its bills. Estimated bonding is $1.5 billion – what we have is a timing problem

Sen Detert you asked why rates are so high? I don't want to knock

We endorse the FIGA reforms as well

Don Brown: You have received a plethora of ideas and we encourage you to take a look at the detail and I will summarize the recommendations. I don't want the volume of the words to disguise a simple truth. Florida does not have an insurance problem – we have a hurricane problem. FL concentrated exposure is greater than any gulf coasts state. FL has half of the hurricane exposure in the entire nation. This is fundamental. We can't afford to self insure all of this exposure. We need to transfer it globally. There are two strategies to manage this hurricane this risk. You can finance that risk with debt or private capital. If you choose to transfer capital then you will payfor that. If post event debt, then hurricane taxes after the storm. AIF is very nervous about this unfunded liability. We request that you give careful attn that Citizens policyholders represent 23% of the market and great deference is paid in the past and approximately 77% are NOT insured by Citizens. This 77% plus local governmental entities who buy insurance, auto owners, etc will pay this tax. There is not a single person on this committee that has a majority of Citizens in their districts. We have focused too much on Citizens policyholders to the detriment of the non-Citizens policyholder

Is the ultimate the goal to provide insurance with real risk transfer or provide self insurance ? Each idea should be measured with the answer to this question. Rely much less on the retention of risk. The status quo is not an option but the status quo is what prompted Howard Troxler to say we have the worst of the worst and we wil sock it to everyone on the back end. We are subject on hurricane taxes. We have a scenario that says pay me now and pay me later. We rely on public debt vs capital. The cat fund should be rightsized and reduce mandatory layer. WE sould reduce the co-pay and we should increase the retention by $8 billion. We should allow companies to buy coverage that they use to replace the cat fund coverage.

AIF's platform was presented that discusses mandating folks to not be sent to Citizens if they have an offer. Higher standards for audit, etc at Citizens; adopt an assessment protection surcharge and use the proceeds of this for real risk transfer; improve FMAP to help find coverage in private market; and raise rates so that those in the coastal areas and give consideration

At times we become so confident in our ability that we believe that we are so smart we can suspend the l aws of common sense. AIF and it always welcomes the ideas to further reform the market.

Simmons : we will not hold it against you that you sat on this side of the dias.

Brandes: Shortest presen with the best ideas. Currently the statute allow insurers to enter into quota share and allow folks to share risks of a policy . At the last meeting CEOs wanted to enter these risk share agreements. The law is difficult so I want to allow some additional flexibility to enter risk sharing agreements and in the best interest of our constituents. It allows us to contract on an agreeable amt of the risk share. There is no reason that an insurer could take 20% of that property and let Citizens retain a part of it and let Citizens handle/administer the risk. It allows private insurers to take a share of the risk. Reduce and not overpay claims and flexibility in the process and there would be companies who would share.

Nicholson: He discussed prices spiking and gave his issues with his "deficit." Cash is good and bonding is bad. We want to fund the cat fund with cash and we can't depend on financial markets. Someone says you can estimate the capacity – we do but its still a guess. We have seen no more bond insurance for muni bonds and that reduced our investor base by half and makes it difficult to raise money. We should look at two years and we need to look at 12 months tho. Our ability to come thru is important . Don Brown reiterated the legislation we tried to pass llast year. We need to move in the right directin. The cat fund is the back bone of the prop insurance system.

One thing you should kjnow is that a cat 5 is verystrong. One thing with a cat 5 hurricane there is total destruction and that is what you will see with a cat 5 event. We would be called upon to do our bonding fast and that's why its important .

Mitigation – pre event and post event. There is a lot of inflation in claims brought about in post event basis and we have got to get a way to manage claims issues.

David Christian, FL Chamber: They provided a letter that lays out details of their position. Since 2008 the Chamber has hosted the premier insurance summit where we discussed:

Curtail Citizens
Support the Citizens clearinghouse
Foster stable insurance market and right size the cat fund
Attract new capital to FL
Attack cost drivers to reduce fraud and abuse

Sen Ring: You pose an interesting question but you didn't answer it. What would happen if we didn't have the money in 04/05 storms to pay the cat fund.

Nicholdson: the law says we are only obligated what we can raise. Private insurers paid $27 billion and we paid $13.3 billion. My gut feel that 75 to 80% of the co's would have gone under. FIGA would have assessed as well and if we can't bond then FIGA cant bond. We were only able in 2007 to bond $3 billion according to estimates. It would have been a big problem with hat in hand. We were working with federal govt to get federal backstop and we didn't need it but we didn't have an event to make us believable.

Detert: I have mentioned previously that rates are too high and then we are the explainers and why we need to get used to it – maybe they are jealous of our marketshare and can we make a living in the insurance bz? Are we just conning them? I want to know how do our rates compre to neighboring states and how do we compare to CA? it must be expensive there too? Are we better or worse off? Cost of CA insurance and we have Citizen and we are keeping it.

Simmons will get that for next committee meeting.

Steve P: when you artificially sets the market and Citizens comes in underpriced, it's the manipulation of the market price. You have Citizens and the private sector reducing beneifts and increased the price. If Citizens goes awy then we need to explain.

Westcott: it goes back to exposure – we do have cat risk that is disguisable in any other coastal state, when CA is discussed, earthquake isn't required. Inequities when other experience and what requts are. Absolutley that it's a fair question – there was disparity between my slide and a slide by Gilway – I used the rates Citizens requested – the glidepath has moved us forward and there is some disagreement on how we get there.

Belinda Miller: discussed that she would get the comparison numbers

Margolis: discussed how we circulated lots of money after a storm and it worked. The bonding worked and we paid the claims and we got a lot of money in the economy and the state prospered. I can't be negative on that and I have asked for those numbers post Andrew. There are issues we should look at and it is proper to say that only one home insured by Citizens. It would be appropriate that there should be a rating for homes that are pre-buiding code that isn't mitigated. When there is a way to say the construction is vulnerable. You mitigate or pay a larger fee. We need not say, "you have the biggest problem so you should pay more." The best way is to not pay commissions – we shouldn't pay it. I am not sure what commissions are and if you don't pay them, then boy these brokers would find another market.

Montford: asked about 2nd homes

Posciask: there are a number of places on the coast that are not owner occupied. It suggests they are 2nd homes.

Montford: when you look at average household income its difficult todo that these are not FL residents

Posciask: Realtors surveyed and looked at transactions that took place – essentially they look at transactions and look at average costs. Floridans are a backstop to these homes that have owners out of state and out of the country.

Montford: if we used $200 mil in mitigation we could reduce the policies by 20%

Westcott: if you mitigated homes in coastal acct – 70% of these homes have no protection. If yu provide that opening protection yu reduce the risk of loss. If yu took the $300 million on reinsurance and invest in those homes, and strengthen them then you could reduce the loss by 20%. That is functional when you think of that means 20% less assessment risk and exposure melts away. When you get exposure down rates do come down.

Lee: You work for SBA right? When you are here advocating cash is good or bonding is bad – are you reflecting your opnion or opinon of SBA?

Nicholson: the SBA- our advisory council and cabinet aides and principals and I hope it reflects their sentiment and its not like they don't know what I am saying . I have been told to reduce the size of the cat fund.

Lee: we could be reasonably be assured that its their perspective as well.

Nicholson: I would not want

Lee 1 in 100 ?

Nicholson: $50billion for the cat fund. And Barry gilway reported 1:45.

Lee: that would include our exposure in citizens?

Nicholson: citizens included?

Lee: how much is that?

Nicholson: citizens is 32% of exposure in the cat fund.. the top of the cat fund is $32B or so PML and realize that some co's its 1:100 and others have 1:20

Lee: if I said the cat fund obligation was $35 b range and citzens is $15 b range, would that unreasonable?

Nicholson: citizens is unique to their book since they are concentrated vs ours which is spread out

Lee: Absent that info – I think in perfect world we'd ike to see the $50 b in ciitzensin the cat fund be absorbed in the private sector – we don't have th e luxury. Our challenge is to figure out how to work our way out of it over time and there will be untenable rate shock in the market if we wean ourselves over the cat fund exposure.

Lee: American is built on debt and if you pull debt out of it, if we are gonna have $50 b in exposure are we better off having that exposure in the cat fund or being the direct writer of ins policies with all of the infrastructure and we still end up with the PML and the obligation and we are ins bz and the financier. There is a $50 billion hole and if you had to pick one vehicle, which one would you pick?

Nicholson: I don't have answer

Lee: that's ok

Nicholson: too much debt is bad and its not that we can't issue bonds. we won't have a problem with $2 billion in bonds. its $10b illion plus – you will have one premium for cash and $17 b limit.

Lee: with this big number exposure, what global opportunities exists for you to sell off the exposure to lower your obligations and cede that somewhere else? Is there a mechanism?

Nicholson: my observation is that when we look at reins, we take capacity off the private reins industry which would cause our prices to go up and its easiest to take some limit off the top. Cat bonds are not as expensive and the basis risk may not pay the claim – the risk is riskier – its not something we can count on reliably and it will be higher priced. And if yu buy an indemnity product, it will cause problems. These options are not viable.

Lee: its'worth having a conversation with the gov and cfo , etc and I know you and rep brown talk about reducing the size of the cat fund and there is a good argument to be made that if we findourselves here we are in the private sector market in two places and just strikes me the less tenable of that is when you are the ins co and there is a much better argument to be made is we need to be a financiaing mechanism that is stable enough to attract the capital at reinsrunce rates athat are regulated vs what happens in china as a mechanism to create greater stability. We try to work our way out of this problem – we are never gonna be able to give companies actuarial sound rates over night. In the interim are we going to be an ins co, a bank or both!

Richter: Detert talked about CA premiums. That's not the question – the most expensive policy is a policy that cant pay its claims. Ring asked Nicholson – what would have happened? Cash would have kicked in, etc and companies would have been insolvent and then claims would have gone unpaid. The medicine with these two sick children – citizens and the cat fund. Richter said I can't make a loan unless I have the capital. There are only three ways to lower premiums – share risk, mitigate the fraud and the home, expand the market and bring in capital for competition. We have got to take the medicine (we have taken it in doses) but there is a reasonable way and a shared risk. Clearinghouse may work and not to pay commissions? To stand still and not take some action and we will be hit with a hurricane. Bonding is ok , cash is a lot better. Jack – the projections for bonding have gone from $3 b to $13 billion.

Clemmons: FL Chamber: you had a survey what a 3% increase would mean and 73% of respondents wold pay a 3% increase. Posciask: clemmons asked who posciask is

Hays: I will not share my opinions: Nicholson: dangerously overexposed? And Nicholson said not as bad

Hays: if the 1:100 pml hits the next year we'd have prem increases and you didn't say if we ha another storm and you'll be barebotomed?

Nicholson: our coverage is aggregate so if we run out of money in the first storm, we are out of money

Simmons: the staff will meet and bring us a list of solutions for us to consider. Thank you for your time and we are adjourned.