

**Adopted Minutes of August 24, 2005 Meeting of  
Task Force on Long-Term Solutions  
for  
Florida's Hurricane Insurance Market**

The Task Force on Long-Term Solutions for Florida's Hurricane Insurance Market convened its first meeting on Wednesday, August 24, 2005, at 10:00 a.m. in 110 Senate Office Building, Tallahassee, Florida.

Acting Chair **Kevin M. McCarty**, Commissioner, Office of Insurance Regulation, called the meeting to order and recognized a quorum.

In addition to Acting Chair McCarty, attending were the following Task Force members: **Richard Cain**, Vice President, State Farm Insurance Company; **Dave Cobb**, President, Freedom Insurors, Inc.; **Randy Dumm**, Ph.D., Associate Professor of Risk Management and Insurance, Florida State University; **Dan Gilmore**, President, Florida Homebuilders' Association; **George Grawe**, Counsel, Allstate Floridian Insurance Company; **Robert P. Hartwig**, Ph.D., Senior Vice President & Chief Economist, Insurance Information Institute; **Leslie Chapman-Henderson**, President/CEO, Federal Alliance for Safe Homes; **Harold Humphrey**, Vice Chairman, InSource, Inc.; and **James Wurdeman**, President/CEO, Poe Financial Group.

Acting Chair McCarty welcomed members of the Task Force, staff and members of the public who were attending. He noted that the meeting had been called in full compliance with Florida's "Government-in-the-Sunshine Act", Section 286.11, Florida Statutes. Public notice of the meeting had been published, members of the public were invited and were attending, and minutes of the meeting were being taken and would be made available publicly.

1. **Election of Chair and Vice-Chair.** On motion made by Task Force Member George Grawe, Commissioner McCarty was nominated to serve as Chair of the Task Force for the duration of the Task Force's existence through the 2004-2006 legislative biennium. After being seconded, the motion was passed unanimously with Commissioner McCarty abstaining.

On motion made by Chair McCarty, Task Force Member Leslie Chapman-Henderson was nominated to serve as Vice-Chair of the Task Force for the duration of the Task Force's existence through the 2004-2006 legislative biennium. After being seconded, the motion was passed unanimously with Ms. Chapman-Henderson abstaining.

2. **Review of Agenda.** Chair McCarty reviewed the agenda for the meeting which had been published on the website of the Department of Financial Services and made available to all Task Force members.

3. **Government in the Sunshine Overview.** Elizabeth Teegan, Assistant Director of Legal Services for the Department of Financial Services, reviewed the "Government-in-the-Sunshine Act" and the "Public Records Act" with members of the Task Force. She noted that the Task Force was an advisory body to state government and was subject to both Acts. She informed Task Force members that the "Government-in-the-Sunshine Act" required all meetings of the Task Force to be open to the public, publicly noticed in advance and documented by minutes. She observed that "meetings" was a broadly-defined term and included any communications between two or more Task Force members about Task Force business, including phone conversations and e-mail communications. Ms. Teegan informed Task Force members that they could meet in private as long as they did not discuss Task

Force business. She also reviewed the “Public Records Act” that requires all records, including e-mails, regarding Task Force business to be made available for public inspection and copying.

4. **Contents of Task Force Briefing Book and Charge to Task Force.** Chair McCarty reviewed the contents of a briefing materials prepared for the meeting, including the agenda; membership list; copy of an excerpt from Senate Bill 1486 creating the Task Force and charging it with duties and outlining legislative expectations; a summary of CS/SB 1486, Chapter #2005-111, Laws of Florida, identifying numerous changes to Florida’s property insurance laws; the complete text of SB 1486; Final Report and Recommendations of the Joint Select Committee on Hurricane Insurance dated February 25, 2005; “The Property Insurance Market in Florida 2004: The Difference a Decade Makes”, published by the Office of Insurance Regulation in March 2005; “Overview of the Florida Hurricane Risk Market”, a PowerPoint presentation dated August 24, 2005, to be made at the meeting by Ray Spudeck, Senior Research Economist, Office of Insurance Regulation; and “The Insurance Contract”, a PowerPoint presentation dated August 24, 2005, to be made at the meeting by Richard Koon, Senior Management Analyst Supervisor, Office of Insurance Regulation. Chair McCarty noted that these and other materials would be available on the Task Force website. ([www.fldfs.com/hurricaneinsurancetaskforce/](http://www.fldfs.com/hurricaneinsurancetaskforce/))

Chair McCarty reviewed the charge to the Task Force in SB 1486, specifically the need to make recommendations to both the legislative and executive branches about ways to maintain and increase the long-term insurance capacity of the state using both private and public providers. He reviewed the scope of the Task force specified by the legislature and noted that a final report was due no later than April 1, 2006, with interim reports possible. Chair McCarty also noted that the Task Force was to monitor and report on the implementation of extensive legislative action taken in 2005.

5. **Market Overview by Ray Spudeck.** Ray Spudeck, Senior Research Economist, Office of Insurance Regulation, briefed the Task Force on Florida’s hurricane risk market to provide an overall context for the work of the Task Force. Mr. Spudeck noted that the hurricane risk poses a unique challenge to Florida’s property insurance market. He reviewed the definition of “catastrophic risk”, a function of frequency, severity and correlation of disasters, and the substantial “risk of ruin” to suppliers of capital that take the risk. He reviewed the global market for catastrophic risk and observed that hurricanes are not the only natural source of such risk. These risks are considered insurable in some cases and not in other cases. A steady demand for catastrophic insured losses exists in the US but peaks have occurred recently in 2001, 2004 and other years that greatly increased the demand for risk capital.

Insuring catastrophic risk involves the property/casualty and reinsurance industry, alternative private market capital sources and federal, state and local government enterprises. Insurers include catastrophic risk as part of their core business. They have a finite and slowly growing national capital base, supplemented by reinsurance in amounts that are cyclical. In 2003, global property reinsurance premiums totaled an estimated \$53 billion. Global “surpluses” of insurers available for property/casualty risks of all types have ranged from an aggregate of approximately \$200 billion in 1994 to approximately \$375 billion in 2004. These “surpluses” are the “capital” available to absorb losses.

Alternative capital markets have grown since catastrophe securities were created in 1995. Institutional and hedge fund investment demand is strong, currently exceeding supply. Other attempts to create alternative capital markets with options and futures have not yet been economically successful.

Public insurance markets also have grown with beach plans, catastrophe funds and authorities in California, Florida and Hawaii, and other residual markets.

Florida's hurricane risk appears to be increasing because of an active multi-decadal cycle beginning in 1995, imprecise measurement and identification methodologies, stronger storms, more limited insurance coverage, aging and more intensive construction and other factors. The state's private insurance property market has decreased from 251 companies and 5.5 million policies in force in 2000 to 184 companies and 4.99 million policies in force in 2004. The combined loss ratio experience of Florida's 13 largest underwriting groups changed substantially in 2004 to close to 350% from an average of between 50% and 60% over the previous decade.

Issues identified by Mr. Spudeck included the multi-year nature of catastrophe risk with current year accounting and reserving not geared to these events. Unlike the US, most other developed countries permit tax-deferred catastrophic reserves. US Congressman Mark Foley has introduced HR 2668 to permit such reserves in the US. Many countries also have a national risk fund or pool.

Florida's Citizens Property Insurance Corporation and Hurricane Catastrophe Fund are unique residual markets that play an important role in Florida's insurance market.

In summary, Mr. Spudeck made the following points:

- Florida's hurricanes are one of the many global catastrophic risks in the market
- Traditional capital has not kept up with demand, especially in Florida
- Alternative markets have not grown to meet the demands
- Accounting and tax policies do not suit catastrophic risk requirements
- Other bodies have developed national plans to respond to catastrophic risk
- Citizens Property Insurance Corporation is a dominant footprint in the market
- Exposure load for the Florida Hurricane Catastrophe Fund is growing steadily.

Members of the Task Force then asked Mr. Spudeck questions with emphasis on ways to attract new capital to the catastrophic risk market, education of the consumer on risks covered by insurance and mitigation activities, the importance of adequate catastrophic protection to the economic health of the state and related matters. Mr. Spudeck noted that the most important coverage issues relate primarily to the "risk of ruin" caused by major catastrophes, such as Category 4 and 5 hurricanes, and that such major events are very difficult to forecast and, by definition, very severe in their potential consequences. With the "risk of ruin" of major disasters, underwriters and others can do their jobs well and still lose everything.

**6. Insurance Contract Coverage Presentation by Richard Koon.** Richard Koon, Management Analyst Supervisor, Office of Insurance Regulation, provided a presentation of insurance contract coverage issues. Mr. Koon reviewed definitions of "appropriate insurance coverage" and actual coverage offered by insurers under various forms. He summarized coverage under Forms HO-1 (Basic Coverage), HO-2 (Broad Coverage), HO-3 (Special Coverage), HO-4 (Tenants), HO-5 (Comprehensive), HO-6 (Unit Owners), and HO-8 (Modified).

Mr. Koon noted reductions and other changes in coverage reflected in hurricane coverage endorsements to written insurance contracts since Hurricane Andrew in 1992, including caps on replacement costs, inflation guards, construction materials exclusions, treatment of appurtenant structures, limits on additional living expenses, limits on screen pool enclosures and mold coverage,

the 50% rule and tie-ins with changes in building codes and replacement costs, sinkholes, calendar year deductions, tree and other debris removal, landscaping exclusions and other consumer-driven issues.

He reviewed coverage issues under SB 1486, including a coverage checklist now prescribed by statute and related matters.

After reviewing these issues, Mr. Koon summarized his view that a major issue to be addressed by the Task Force was a clear definition of "appropriate" insurance coverage and possible variations in coverage because of consumer and company choices.

Members of the Task Force asked Mr. Koon to clarify various coverage matters and identified issues to be addressed at future Task Force meetings, outlined subsequently in these minutes.

**7. Presentation on Industry Perspective of Florida Hurricane Market by Steve Goldberg.** Steve Goldberg, Chief Actuary, Benfield Group, a reinsurance intermediary, provided a presentation on industry's perspective of the Florida hurricane market. Mr. Goldberg distributed written copies of his statement, dated August 24, 2005.

Mr. Goldberg noted that Benfield Group places a substantial share of the dollars of reinsurance capacity at risk in Florida into global reinsurance markets and has administered the Florida Hurricane Catastrophe Fund since the Fund's inception.

Mr. Goldberg offered a meteorological perspective on the frequency and severity of hurricanes in Florida and perspective on how we got to where we are today, including the need for sustained profitability for any business, including insurance; the inability of investors to tolerate consistent losses in an insurer's major operations; limited available capital; expectations of ruinous losses arising from future storms; 11 years of recouped losses since Hurricane Andrew followed by 6 weeks of major losses in 2004; Florida's need for large amounts of capital in the future because of its growth; and the need to provide capital with a reasonable rate of return, combined with strengthened building codes, wise land use policies and increased mitigation. He noted that building codes had improved in recent years and catastrophe modeling was maturing.

Mr. Goldberg discussed six strategic principles he believes should be used to evaluate possible solutions: recognize the true costs of coverage by eliminating price controls; focus regulator effort on solvency by realistically appraising new capital; end unfair subsidization (of properties insured by Citizens Property Insurance Corporation); realize the weaknesses of accounting for financially catastrophic events; continue to make the most of the tax status of the Florida Hurricane Catastrophe Fund; and nurture a spirit of cooperation and trust among stakeholders.

**8. Issues for Future Attention by the Task Force.** Chair McCarty facilitated a discussion of presentations made during the meeting and identification of issues for future attention by the Task Force. During the discussion, and through written submission to staff, members of the Task Force identified the following action items. (*Editorial note: Statutory charges are included for clarity*)

**I. Trends in the Florida Insurance Market:**

1. Estimate the profitability over time of property insurance in Florida.
2. Provide a review of loss data by policy form number.
3. Recreate the current state loss exceedence curve for hurricane risk, and compare to past years, including presentations from catastrophe modeling firms.

4. From Task Force member questionnaires:
  - a. A focused analysis of the Mobile Home Insurance Market.
  - b. A study of the affordability and availability of property insurance for low-income homeowners.

## **II. Market Capacity Issues:**

1. Estimate the impact of assessments by Citizen's on private insurer profitability, cash flow, and ratings.
2. Review accounting and tax law rules to facilitate catastrophic coverage, especially HR 2668 (Rep. Foley) and the NAIC Catastrophe Reserve Plan.
3. Analyze the attendant effect of sinkhole risk on the private property insurance market.
4. Estimate the necessary capital needed to support the homeowners' market moving forward.
5. Review developments in the financial markets regarding alternative risk transfer financing mechanisms.
6. Address any systemic effects of insolvencies and how that affects both available additional capital and FIGA.
7. From SB 1486:
  - a. Investigate whether this state currently has sufficient hurricane insurance capacity to ensure the continuation of a healthy, competitive marketplace, taking into consideration both private-sector resources and public-sector resources.
  - b. Identify the future demands on this state's hurricane insurance capacity, taking into account population growth, coastal growth, and anticipated future hurricane activity.
  - c. Investigate whether the Florida Hurricane Catastrophe Fund fulfilled its purpose of creating additional insurance capacity sufficient to ameliorate the current dangers to the state's economy and to the public health, safety, and welfare in its response to the 2004 hurricane season.
  - d. Determine the extent to which the growth in Citizens Property Insurance Corporation is attributable to insufficient insurance capacity.
  - e. Determine the extent to which the growth trends of Citizens Property Insurance Corporation create long-term problems for property owners, buyers, and sellers in this state and for other persons and businesses that depend on a viable market.
8. From Task Force Member questionnaires:
  - a. Consider the ramifications of higher hurricane deductibles.

## **III. Issues involving the Regulatory Structure:**

1. Review key aspects of the currently mandated regulatory process, including especially the rating process.
2. From S.B. 1486:
  - a. Monitor the implementation of hurricane insurance-related legislation enacted during the 2005 Regular Session and shall make such additional recommendations, as it deems appropriate for further legislative action during the 2004-2006 legislative biennium.

## **IV. Issues Regarding the Insurance Contract:**

1. Clarify the relationship between building codes and insurance coverage.
2. Further address ordinance and law coverage.
3. Discuss clarity in policy coverage regarding replacement coverage.
4. Review the concept of personal disaster savings accounts held by consumers.
5. Address simplified disclosure for consumers.

## V. Mitigation Issues:

1. Evaluate the efficacy of building codes and how well jurisdictions enforce them.
2. From Task Force Member questionnaires:
  - a. Mitigation case studies.
  - b. Address exceptions to the Building Code.
  - c. Address the cost of disaster resistant construction techniques.
  - d. Discuss the potential for builder/realtor disclosure regarding the method of construction and types of mitigation at time of construction or resale.

## VI. Issues Regarding Citizens Property Insurance Corporation

1. Review Citizens' rating process and reinsurance provisions.
2. Review the degree of subsidization, if any, in Citizen's rate structure.
3. From Task Force Member questionnaires:

Conduct a review of the current and historical performance of "take-out" companies, including the volume of business and financial condition.
4. From S.B. 1486: Study the operation and role of Citizens Property Insurance Corporation, including:
  - a. How to ensure that the corporation operates as an insurer of last resort which does not compete with insurers in the voluntary market, but which charges rates that are not excessive, inadequate, or unfairly discriminatory;
  - b. Whether the bonuses paid by the corporation to carriers taking policies out of the corporation provide a cost-effective means of reducing the potential liability of the corporation;
  - c. Whether the "Consumer Choice" law should be repealed or amended to ensure that the corporation serves as the insurer of last resort;
  - d. Whether coverage amounts should be limited;
  - e. Whether the corporation has hired an adequate level of permanent claims and adjusting staff in addition to outsourcing its claims-adjusting functions to independent adjusting firms;
  - f. The effect of reducing or expanding the areas that are eligible for coverage in the high-risk, wind-only account;
  - g. Whether the corporation should purchase reinsurance or take other actions that reduce the potential for debt financing and deficit assessments; and
  - h. An evaluation of the infrastructure and administration of the corporation and how to improve customer service, claims handling, and communication and the exchange of information with agents of policyholders of the corporation.

Chair McCarty noted that these and other issues would be addressed at future meetings of the Task Force.

**9. Public Testimony.** Chair McCarty asked members of the public who were attending the meeting if any of them wished to offer testimony. Hearing no request, he moved to the next item on the agenda.

**10. Meeting Schedule.** Chair McCarty announced the next meeting of the Task Force on September 28, 2005, in Room 110 Senate Office Building, Tallahassee, Florida, beginning at 10 a.m.

Hearing no request to consider additional business, Chair McCarty adjourned the meeting at 2:30 p.m.