



Florida's Property and Casualty Insurance System

Rebounding from Hurricanes

A number of factors helped Florida recover from the 2004/2005 hurricanes:

- A **“Battle-Hardened” Emergency Management System**. This has improved over time with each successive disaster.

- **More Effective Enforcement of Updated Building Codes**. Effective enforcement of building codes is essential. After Hurricane Andrew, the State of Florida wisely updated building codes, which proved very effective in strengthening home construction so that newer and retrofitted properties could withstand more intense or prolonged exposure to storms.

- **State-Sponsored Insurance Structures**. As illustrated by the chart to the right, the state has three insurance programs to augment private reinsurance (insurance purchased by insurance companies to help cover their losses) and assure, as well as broaden, availability and affordability of property insurance:

1) **The Florida Hurricane Catastrophe Fund (CAT Fund)** is a tax-exempt, state government trust fund administered by the State Board of Administration, which was created in 1993 as a source of low-cost reinsurance for residential property insurers. As of September 2006, the CAT Fund could pay out \$15 billion backed by state bonding authority. Insurers purchase CAT reinsurance coverage in contracts signed at the beginning of the hurricane season and pay a premium established by the State Board of Administration. The premiums and

private insurance costs paid by the companies are included in their rate bases and passed through to the policyholders. If there are seasons without hurricanes, premiums build up the cash reserve in the CAT. During seasons with hurricanes, the fund is used to partially reimburse property insurers to cover losses they've paid out. The CAT Fund may levy assessments on all property and casualty insurance premiums when bonding authority has been used to cover projected cash shortfalls in the fund.

others who cannot find private property coverage. Citizens Corporation has experienced a disturbing and rapid rate of growth, which is an indication of a severe problem in availability of private coverage. As of August 31, 2006, Citizens had over 1.2 million policies in force with an overall exposure of \$366 billion, up from 775,230 and \$198 billion in 2005. Citizens added 24,555 policies and \$23.3 billion in exposure in August 2006 alone. About 300,000 of the Citizens' policies came about due to the insolvency of Poe Financial Group, which, at the time, was the largest Florida-only insurer. Citizens is backed by state revenue bonds.

3) **The Florida Insurance Guaranty Association (FIGA)**. The state created this non-profit association in 1970 to pay unpaid claims following the insolvency of a property and casualty insurance company.

Factors Contributing to Lack of Availability and Affordability Problem

Natural Factors

- **Florida is hurricane prone**. The state is located in latitudes that expose it more frequently to tropical storms, which begin in tropical zones. One hundred ten (40.3%) of 273 hurricanes making direct hits on the United States from 1854 to 2004 hit Florida. Of the 273 hitting the U.S., 92 were severe storms (categories 3-5) — 35 of those severe storms (38%) hit Florida.

- **Florida is a peninsula**. The Atlantic Ocean, Caribbean Sea, and Gulf of Mexico coastlines wrap almost completely around the Florida land mass and hurricanes are primarily coastline

Dear Fellow Taxpayer,

An unprecedented series of eight catastrophic storms over a 15-month period in 2004 and 2005 caused insured damages in Florida of over \$35 billion—an all-time high for the state—second only to Hurricane Andrew damage in 1992.

Hurricanes are devastating, not only to citizens, but to the economy of Florida as well. Events such as this make it incumbent on the state to assist individuals in recovering and ensure that the state economy rebounds as quickly as possible.

We hope this guide is helpful to you.

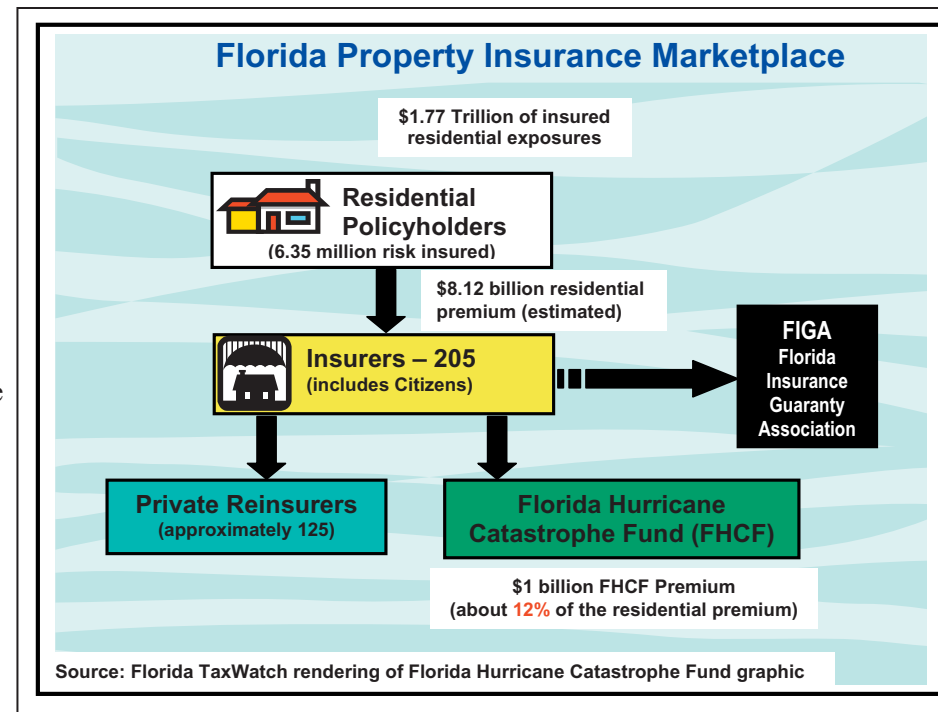
Respectfully,

Michael A. Jennings

Michael A. Jennings
Chairman
Florida TaxWatch

Dominic M. Calabro

Dominic M. Calabro
President & CEO
Florida TaxWatch



2) **The Citizens Property Insurance Corporation (Citizens)** is a state corporation created in 2002 through the merger of the Residential Joint Underwriters Association, which had been in existence since 1993, and the Florida Wind Storm Underwriting Association, established in 1972. Citizens Corporation provides property coverage for homeowners in high-risk (wind) areas and

Natural Factors (cont.)

catastrophes. Most of Florida's population lives in coastal counties.

- **Catastrophic storms are increasing in number and severity.** Four of the strongest (category 5) storms recorded since 1935 occurred in 2004-05 (Katrina, Ivan, Wilma, and Rita).

- **Hurricanes are ruining increasingly more valuable properties.** Due to the combination of a seller's real estate market from 2003-06, appreciating Florida property in general, and sharply increased values for property located in natural wind zones, hurricane damage in Florida is becoming increasingly more expensive. Recent Florida hurricanes Ivan, Charley, Wilma, and Andrew, in particular, were among the most expensive in history.

- **More robust storm forecasting models.** As hurricane forecasting models become more sophisticated and sensitive, as a result of more timely and accurate data, the increasing frequency and cost severity of storms affecting Florida have resulted in grim predictions for the state. Reinsurers rely heavily on these models for assessing risk and determining prices.

Market Factors

- **Greater Reliance on Reinsurance.** Florida property insurance companies rely more heavily on reinsurance, including Florida's CAT Fund, than those in other states. Florida insurers "cede" approximately 50% of private residential insurance premiums to reinsurers, compared to about a third by other U.S. insurers, excluding Florida.

- **"Hard Market" for Reinsurance.** According to the State Board of Administration,

"Pricing at the beginning of calendar 2006 for private sector Florida hurricane risk reinsurance increased 50-70% from the prior year and increased another 50-100% on July 1, 2006."

- **Cost and Rate Pressure on Primary Insurers.** As hurricane models predict risks of loss above those that companies had previously planned for, and as rating agencies demand that insurance companies provide additional capital to cover this increased risk in Florida or face a potentially lowered financial rating, the companies are placed in a quandary. Because there is little or no capital to commit to a market, which has produced nothing but net losses in recent years, the solution can only be to lay off risk. Thus Florida has an availability problem.

Increasing Affordability and Availability of Property Insurance

The 2006 Legislature appropriated more than \$700 million to bail out Citizens Property Insurance, which was running a deficit. The move avoided large assessments to homeowners that otherwise would have been used to make up the shortfall. The Legislature also appropriated \$250 million for house inspections to determine what retrofitting is necessary to better protect those homes and reduce future storm losses.

As of this writing, the Legislature is considering reforms to the property and casualty market in Florida. These reforms include ideas to better align the true cost and price of insurance, allow insurers to reinsure a higher percentage of their losses, provide more capital to expand the CAT Fund, and provide greater incentives to encourage property owners to hurricane-harden their properties.



Mission

To provide the citizens of Florida and public officials with high quality, independent research and education on government revenues, expenditures, taxation, public policies and programs and to increase the productivity and accountability of Florida Government.

Values

Integrity
Productivity
Accountability
Independence
Quality Research

Florida TaxWatch
106 N. Bronough Street
Tallahassee, FL 32301
850/222-5052

© Copyright Florida TaxWatch
November 2006

To become a member of Florida TaxWatch, please phone or visit our website at www.FloridaTaxWatch.org

Taxpayer's Guide to

Florida's Property and Casualty Insurance System

