The Florida Senate

BILL ANALYSIS AND FISCAL IMPACT STATEMENT

(This document is based on the provisions contained in the legislation as of the latest date listed below.)

Prepared By: The Professional Staff of the Committee on Banking and Insurance

BILL: SB 346

INTRODUCER: Senator Lee

SUBJECT: Florida Insurance Guaranty Association

DATE: February 16, 2014 REVISED:

	ANALYST	STAFF DIRECTOR	REFERENCE	ACTION
1.	Johnson	Knudson	BI	**Pre-meeting**
2.			CM	
3.			AGG	
4.			AP	

I. Summary:

SB 346 revises provisions governing the Florida Insurance Guaranty Association (FIGA), which was created to provide a mechanism for the payment of covered claims, including unearned premiums, of insolvent property and casualty insurance companies. After an insolvency occurs, FIGA is authorized to levy assessments against Florida member insurance companies to pay covered claims. Under current law, FIGA certifies to the Office of Insurance Regulation (OIR) the need for an assessment, and upon approval, the OIR levies an assessment on insurers. Insurers generally remit payment within 30 days of the levy and recoup assessments from policyholders. The bill provides the following changes:

- Requires the OIR to levy assessments directly on policyholders.
- Requires insurers to collect and remit assessments periodically to FIGA. The collection must begin at least 90 days after the certification of the assessment.
- Authorizes FIGA to borrow funds necessary to ensure that its cash flow needs are met in a timely manner to pay covered claims when an assessment is levied.
- Revises assessment calculation by providing a uniform assessment percentage.
- Exempts the regular assessment from the insurance premium tax. Under current law, the emergency assessment is exempt from the insurance premium tax.

II. Present Situation:

Florida Insurance Guaranty Association

Part II of ch. 631, Florida Statutes., governs the operations of the Florida Insurance Guaranty Association (FIGA), a nonprofit corporation, which was created to provide a mechanism for the payment of covered claims, including unearned premiums, of insolvent property and casualty

insurance companies.[1] Property and casualty insurance companies[2] doing business in Florida are required to be a member of FIGA as a condition of their authority to transact insurance.[3] When a property and casualty insurance company becomes insolvent, FIGA is required to assume the claims of the insurer and pay the claims of the company's policyholders, which includes claims on residential and commercial property insurance, automobile insurance, and liability insurance, among others.

The maximum claim amount FIGA will cover is $300,000, but special limits apply to damages to structure and contents on homeowners, condominiums, and homeowners' association claims. For damages to structure and contents on homeowners' claims, FIGA covers an additional $200,000, for a total of $500,000. For condominium and homeowners' association claims, FIGA covers the lesser of policy limits or $100,000 multiplied by the number of units in the association.

FIGA Funding and Assessments

In order to pay the remaining covered claims and maintain the operations of an insolvent insurer, FIGA has several potential funding sources. For example, FIGA receives funds that are available from distributions of the estate of the insolvent insurance company. The Division of Rehabilitation and Liquidation in the Department of Financial Services is responsible for the liquidation of assets of insolvent insurance companies.[4] In addition, FIGA also obtains funds from the liquidation of assets of insolvent insurers domiciled in other states, but having claims in Florida.

After insolvency occurs, FIGA is authorized to levy assessments against Florida member insurance companies under two separate statutory provisions. Under s. 631.57(3)(a), F.S., FIGA is authorized to levy an assessment as necessary for up to 2 percent of an insurer's net written premium for the kind of insurance included in the account for which the assessment is levied. This assessment is known as the "regular assessment." The second assessment is an emergency assessment authorized under s. 631.57(3)(e), F.S., which may be levied only to pay covered claims of an insurer that was rendered insolvent by the effects of a hurricane. At the discretion of FIGA, emergency assessments are payable in 12 monthly installments or in a single payment. The emergency assessment is capped at 2 percent of an insurer's net direct written premiums in Florida for the calendar year preceding the assessment.

The procedure used by FIGA to levy both regular and emergency assessments on member insurance companies and the procedure used by member insurance companies to pass the assessment on to their policyholders are provided in s. 631.57(3), F.S. The procedures are generally the same for regular and emergency assessments:

1. FIGA determines that an assessment is needed to pay claims or administration costs, or to pay bonds issued by FIGA.

[1] Section 631.51, F.S.
[2] Workers' compensation insurance is excluded from FIGA since the Florida Workers' Compensation Insurance Guaranty Association (FWCIGA) pays covered claims under chapter 440, F.S., Florida's Workers' Compensation Law.
[3] Section 631.55(1), F.S.
[4] Typically, insurers are placed into liquidation when the company is insolvent and the goal of liquidation is to dissolve the insurance company. *See* s. 631.061, F.S., for the grounds for liquidation.

2. FIGA certifies the need for an assessment levy to the OIR.
3. The OIR reviews the certification, and if it is sufficient, the OIR issues an order to all insurance companies subject to the FIGA assessment to pay their assessment to FIGA.
4. Regular assessments must be paid by the insurance companies within 30 days of the levy, and emergency assessments can be paid either in one payment at the end of that month, or spread out over 12 months, at the option of FIGA.
5. For both types of assessments, once an insurance company pays the assessment to FIGA, it may begin to recoup the assessment from its policyholders at the policy issuance or renewal.[5]

There have been two instances (1993 and 2006) in the 43-year history of FIGA the assessment has been 4 percent.[6] Insurers pay the assessments upfront and recoup the assessment from policyholders upon issuance or renewal of the policies.

Part II of ch. 631, F.S., provides a limited exception to the assessment. Subject to regulatory approval, an insurer may be exempted from any regular or emergency assessment if an assessment would result in the insurer's financial statement, reflecting an amount of capital or surplus less than the sum required by any jurisdiction in which the insurer is authorized to transact insurance.[7]

Accounting for Assessments

Statutory accounting principles (SAP) govern the preparation of an insurer's annual statement, which is filed with the state regulator, the Office Insurance Regulation. The SAP is characterized as a more conservative approach; it measures the ability to pay claims in the future. In contrast, other users, such as shareholders, bondholders, banks, credit rating agencies, and the Securities and Exchange Commission, may require financial statements that are prepared in accordance with generally accepted accounting principles (GAAP). The GAAP financial statements attempt to match revenues to expenses.[8] The OIR requires insurers to file annual SAP statements and independently audited financial reports.[9]

In some respects, GAAP differs from SAP in the treatment of certain transactions, such as the FIGA assessments. Under both accounting methods, a liability is recognized. However, SAP allows the recognition of an asset for the amount that is likely to be recovered from future premium surcharges for an assessment, which offsets or eliminates the negative effect on statutory surplus. [10] For purposes of GAAP, the assessment recoverable from future premium

[5] If an insurer's book of business is declining during the recoupment period, the assessment factor will be insufficient to recoup the total amount of assessment paid to FIGA. In those circumstances, the insurance company must continue to collect the assessment from policyholders beyond 12 months, until the assessment is recouped in full.
[6] This occurred in 1993 following Hurricane Andrew and in 2006 following Hurricane Wilma and the other storms of the 2004/2005 hurricane seasons.
[7] Section 631.57(4), F.S.
[8] The Financial Accounting Standards Board (FASB) Accounting Standards Codification is the single source of authoritative nongovernmental U.S. Generally Accepted Accounting Principles (GAAP), http://www.fasb.org/jsp/FASB/Page/SectionPage&cid=1176154526495 (last visited February 16, 2014).
[9] Section 624.424, F.S.
[10] *See* Thomas Howell Ferguson P.A., *Accounting for Guaranty Fund Assessments,* memorandum to Sandy Robinson at FIGA, December 3. 2013, (on file with Senate Committee on Banking and Insurance).

writings does not qualify as an asset,[11] resulting in a reduction of retained earnings in the period an assessment is levied. The impact of the assessment on GAAP financial statements is essentially a timing issue; retained earnings are reduced in the year the assessment is paid; however, it is increased the following year as the assessment is recouped from policyholders.

Insurance Premium Tax

Insurance premiums are subject to the insurance premium tax.[12] In Florida, an insurance premium tax of 1.75 percent is imposed on the gross insurance premiums (less reinsurance and returned premiums) of property and casualty insurers. Specified credits, deductions, and exemptions reduce the premium tax liability.

Regular assessments levied by FIGA for insolvencies occurring on or after July 1, 2010, are considered premium for premium tax purposes and thus subject to the premium tax. Emergency assessments levied by FIGA, however, are exempt from the premium tax.

III. Effect of Proposed Changes:

The bill would significantly revise the current regular and emergency assessment process. The bill repeals current law allowing the Florida Insurance Guaranty Association (FIGA) to assess and collect regular and emergency assessments from insurers who later recoup the assessment from their policyholders.

The bill provides that FIGA would determine the necessity and amount of the regular or emergency assessment, and certify the assessment to the OIR. Then, the OIR would levy the assessment directly on policyholders and issue an order to insurers specifying the collection start date and uniform assessment percentage to be collected by insurers from their policyholders over 12 months at policy issuance or renewal. The initial collection start date must be at least 90 days after the FIGA board certifies the need for an assessment. Under the current collection method, an insurer generally remits the regular assessment within 30 days of the levy; however, the emergency assessment may be payable as a single payment or in 12 monthly installments, at FIGA's option. Under current law, assessments are based on each insurer's net direct written premiums in Florida for the calendar year preceding the assessment.

The bill retains the current caps on assessments of 2 percent for the regular assessment and 2 percent for the emergency assessment per year. The bill provides that regular assessments are not premium and are not subject to the premium tax. Under current law, regular assessments are not subject to fees or commissions and the emergency assessment is not subject to the premium tax, any fees, or commissions.

The bill authorizes FIGA to borrow funds necessary to ensure that cash flows are adequate to pay claims when regular and emergency assessments are levied on policyholders and collected by insurers.

---

[11] Asset recognition is measured based on projected future premium collections or policy surcharges from in-force policies, excluding expected renewals of short-duration contracts, which would disqualify the assessment future recoverable as an asset.
[12] Section 624.509, F.S.

IV. Constitutional Issues:

A. Municipality/County Mandates Restrictions:

None.

B. Public Records/Open Meetings Issues:

None.

C. Trust Funds Restrictions:

None.

V. Fiscal Impact Statement:

A. Tax/Fee Issues:

If FIGA borrows funds, it will incur additional financing costs, which could increase the amount of assessments levied on policyholders.

B. Private Sector Impact:

The bill provides that the FIGA regular assessment collected by insurers would no longer be subject to the insurance premium tax.

Advocates of the bill contend that the current assessment mechanism poses a threat to the solvency of property insurers doing business in Florida after a storm. Advocates also state that the bill spreads out the timing of the collection of the funds and reduces the risk of insolvency by reducing the total amount an insurance company would have to pay FIGA within 30 days.

The bill provides a uniform percentage assessment for policyholders. Advocates of the bill state that the current assessment method is unfair to policyholders because the assessment amount paid by each company is based on the company's market share in the year immediately preceding the assessment. Advocates note that policyholders of companies with decreasing market share pay more in assessments than policyholders of companies with increasing market share, and policyholders of newly formed companies pay nothing.

The impact of assessments on GAAP financial statements, specifically retained earnings, is addressed by allowing insurers to collect assessments directly from policyholders. This new method eliminates the liability of the insurer; therefore, the assessment is not reported in the financial statements.

Under the bill, FIGA would no longer have access to assessments within 30 days after written notice of a levy because the bill requires assessments to be collected from policyholders over a 12 month period. However, the bill authorizes FIGA to borrow

funds necessary to pay covered claims. Sources of financing include letters of credit, lines of credit, bank loans, or post-event bonding.

The financial adviser for FIGA evaluated liquidity options.[13] Lines of credit can be potentially available up to $150-$200 million. Lines of credit fees have two annual fee components: a facility fee paid quarterly in arrears and a drawdown fee paid monthly or quarterly in arrears. For a $100 million line of credit, the annual facility fee is 0.60-1.00 percent ($600,000-$1 million annually) with an annual interest rate, if drawn, of 3.00-4.00 percent ($3-$4 million annually or $250,000-$333,333 monthly). The upfront cost of issuance for a $200 million bank loan would be approximately $200,000 and the interest rate would be approximately 2.50-3.00 percent ($5-$6 million annually). The upfront cost of issuance for a $200 million public offering is approximately $500,000 and the interest rate would be approximately 2.25-3.2 percent ($4.5-$6.5 million annually). The financial advisor notes that, under current law, the regular assessment provides up to $340 million in 30 days and the credit markets cannot provide this capacity, but the current assessment mechanism provides a capital structure, which is efficient, tested, and proven.

C. Government Sector Impact:

According to the OIR, it has no access to policyholder information, no mechanism to collect funds and no ability to apply assessments so collected to individual policyholder accounts. The OIR suggests that current statute, which provides that the OIR levy assessments on insurers, who are subject to regulation by the OIR, remain.[14]

The bill provides that the FIGA regular assessment is no longer subject to the insurance premium tax. The fiscal impact is indeterminate at this time.

VI. Technical Deficiencies:

None.

VII. Related Issues:

None.

VIII. Statutes Affected:

This bill substantially amends the following section of the Florida Statutes: 631.57.

[13] Raymond James and Associates, *Cash Balance and Liquidity Options,* memorandum to Sandy Robinson at FIGA (December 11, 2013) (on file with Senate Committee on Banking and Insurance).
[14] Office of Insurance Regulation, *Analysis of SB 346* (January 19, 2014) (on file with Senate Committee on Banking and Insurance).

IX. Additional Information:

A. Committee Substitute – Statement of Changes:

(Summarizing differences between the Committee Substitute and the prior version of the bill.)

None.

B. Amendments:

None.

This Senate Bill Analysis does not reflect the intent or official position of the bill's introducer or the Florida Senate.