

**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 1274

INTRODUCER: Senator Latvala

SUBJECT: Sinkhole Insurance

DATE: February 8, 2016

REVISED: \_\_\_\_\_

|    | ANALYST | STAFF DIRECTOR | REFERENCE | ACTION             |
|----|---------|----------------|-----------|--------------------|
| 1. | Knudson | Knudson        | BI        | <b>Pre-meeting</b> |
| 2. |         |                | AGG       |                    |
| 3. |         |                | FP        |                    |

---

**I. Summary:**

SB 1274 creates s. 627.7151, F.S., which allows insurers to offer a new type of sinkhole insurance coverage. This sinkhole coverage would, as under current law, only provide coverage for “sinkhole loss” which is defined in statute as structural damage to the covered building, including the foundation, caused by sinkhole activity. The new form of coverage differs from existing coverage in that it is exempt from the following statutory requirements:

- Standards for the investigation and payment of a sinkhole loss claim in s. 627.707, F.S.;
- Standards for sinkhole testing by professional engineers and professional geologists in s. 627.7072, F.S.;
- Standards for sinkhole testing reports in s. 627.7073, F.S.; and
- Neutral evaluation standards in s. 627.7074, F.S.

Regarding the sinkhole coverage created by s. 627.7151, F.S., the bill:

- Establishes surplus requirements for insurers that solely transact the form of residential property insurance for sinkholes that is created by the bill.
- Specifies that an authorized insurer may issue the coverage, but is not required to do so. If offered, such coverage may only provide personal lines residential property insurance for sinkhole loss to the structure or the contents of personal property.
- Requires the inclusion of coverage for additional living expenses.
- Requires that any loss under personal property or contents coverage that is repaired or replaced be adjusted only on the basis of replacement costs up to the policy limits, thus prohibiting adjustment based on actual cash value.
- Provides that any limitations on sinkhole coverage or policy limits, including, but not limited to deductibles, must be prominently noted on the policy declarations page or face page.
- Allows insurers, until October 1, 2019, to use rates for sinkhole coverage that are not subject to the filing and review requirements of s. 627.062(2)(a) and (f), F.S.

- Allows surplus lines agents, until July 1, 2020, to export coverage to eligible surplus lines insurers without obtaining three declinations from admitted insurers.
- Prohibits Citizens Property Insurance Corporation from writing or renewing such coverage after July 1, 2018.
- Requires the Florida Commission on Hurricane Loss Projection Methodology to review sinkhole loss models and develop standards by July 1, 2018.

The bill is effective upon becoming a law.

## II. Present Situation:

### Insurance for Sinkholes and Catastrophic Ground Cover Collapse

A sinkhole is defined in Florida law as a landform created by subsidence of soil, sediment, or rock as underlying strata are dissolved by groundwater.<sup>1</sup> Sinkholes occur in certain parts of Florida due to the unique geological structure of the land. Sinkholes are geographic features formed by movement of rock or sediment into voids created by the dissolution of water-soluble rock. This type of subsidence formation may be aggravated and accelerated by urbanization and suburbanization, by water usage and changes in weather patterns.

Since 1981, insurers offering property coverage in Florida have been required by law to provide coverage for property damage from sinkholes.<sup>2</sup> In 2007, Florida law was amended to require insurers in Florida to cover only catastrophic ground cover collapse, rather than all sinkhole loss, in the base property insurance policy.<sup>3</sup> Catastrophic ground cover collapse is more severe than sinkhole loss. Catastrophic ground cover collapse means geological activity that results in all the following:

1. The abrupt collapse of the ground cover;
2. A depression in the ground cover clearly visible to the naked eye;
3. Structural damage to the covered building, including the foundation; and
4. The insured structure being condemned and ordered to be vacated by the governmental agency authorized by law to issue such an order for that structure.<sup>4</sup>

Insurers must also offer policyholders, for an appropriate additional premium, sinkhole loss coverage covering any structure, including personal property contents.<sup>5</sup> Such coverage is subject to the insurer's approved underwriting and insurability guidelines. At a minimum, sinkhole loss coverage includes repairing the covered building, repairing the foundation, and stabilizing the underlying land. All property insurers can restrict catastrophic ground cover collapse and sinkhole loss coverage to the property's principal building. However, by law, Citizens Property Insurance Corporation (Citizens)<sup>6</sup> sinkhole loss coverage does not cover sinkhole losses to

---

<sup>1</sup> Section 627.706(2)(b), F.S.

<sup>2</sup> Ch. 1981-280, Laws of Fla.

<sup>3</sup> Section 30, Ch. 2007-1, Laws of Fla.

<sup>4</sup> Section 627.706(2)(a), F.S.

<sup>5</sup>Section 627.706, F.S.

<sup>6</sup> Citizens Property Insurance Corporation is a state-created, not-for-profit, tax-exempt governmental entity whose public purpose is to provide property insurance coverage to those unable to find affordable coverage in the voluntary admitted market. It is not a private insurance company.

appurtenant structures, driveways, sidewalks, decks, or patios. Furthermore, insurers can require an inspection of the property before providing sinkhole loss coverage.

For sinkhole loss coverage in residential property insurance, current law allows insurers to include a deductible that applies only to sinkhole loss in the following amounts: 1 percent, 2 percent, 5 percent, or 10 percent of policy dwelling limits. The insurer has the option to choose which sinkhole loss deductible is offered to policyholders and currently, most insurers, including Citizens, offer policyholders only a 10 percent sinkhole loss deductible.

Substantial changes to Florida's sinkhole law occurred in 2005, 2006, and 2011.<sup>7</sup> In 2011, the Legislature reviewed the sinkhole law and enacted comprehensive reforms addressing all areas of the law. Data collected by the Office of Insurance Regulation (OIR) in 2010, before the reforms were enacted, showed a significant increase in the number and cost of sinkhole claims from 2006 to 2010.<sup>8</sup> These increases impacted the financial stability of property insurers in Florida, including Citizens, and were used by insurers to justify property insurance rate increases.

### **2011 Sinkhole Insurance Reforms**

The sinkhole reforms enacted in 2011 were in response to the increasing number and cost of sinkhole claims. The goal of the reforms was to keep sinkhole loss insurance available to homeowners while providing more certainty in sinkhole claims for homeowners and insurers in terms of coverage, costs, repairs, and exposure. The bill enacted numerous revisions and clarifications to ss. 627.706-627.7074, F.S., governing sinkhole and catastrophic ground cover collapse insurance.

#### ***Definition of Sinkhole Loss***

The legislative reforms revised the definition of "sinkhole loss," primarily by creating a statutory definition of "structural damage." A sinkhole loss is defined in statute as structural damage to the covered building, including the foundation, caused by sinkhole activity. The 2011 legislative reforms created a detailed definition of "structural damage" for purposes of determining whether a sinkhole loss has occurred. The definition specifies five distinct types of damage that constitute structural damage. Each type of damage is tied to standards contained in the Florida Building Code or used in the construction industry. Accordingly, in order for the policyholder to obtain policy benefits for sinkhole loss, the insured structure must sustain structural damage as defined by the bill that is caused by sinkhole activity.

#### ***Investigation and Payment of Sinkhole Claims***

The 2011 legislative sinkhole reforms substantially revised the statutory process for investigating and paying sinkhole claims in s. 627.707, F.S. The process requires the insurer to determine whether the building has incurred structural damage that has been caused by sinkhole activity.<sup>9</sup>

---

<sup>7</sup> chs. 2005-111, 2006-12, and 2011-39, Laws of Fla.

<sup>8</sup> *Report on Review of the 2010 Sinkhole Data Call by the Office of Insurance Regulation*, Nov. 8, 2010, [http://www.flor.com/siteDocuments/Sinkholes/2010\\_Sinkhole\\_Data\\_Call\\_Report.pdf](http://www.flor.com/siteDocuments/Sinkholes/2010_Sinkhole_Data_Call_Report.pdf) (last visited Feb. 5, 2016).

<sup>9</sup> Section 627.707(1), F.S.

Coverage for sinkhole loss is not available if structural damage is not present or sinkhole activity is not the cause of structural damage. This process is as follows:

- Initial Inspection and Structural Damage Determination – Upon receipt of a claim for sinkhole loss, the insurer must inspect the policyholder’s premises to determine if there has been structural damage which may be the result of sinkhole activity.<sup>10</sup> This inspection will often require the insurer to retain a professional engineer to evaluate whether the insured building has incurred structural damage as defined by statute.
- Sinkhole Testing – The insurer is required to engage a professional engineer or professional geologist to conduct sinkhole testing pursuant to s. 627.7072, F.S., if the insurer confirms that structural damage exists and is either unable to identify a valid cause of the structural damage or discovers that the structural damage is consistent with sinkhole loss.<sup>11</sup> If coverage is excluded under the policy even if sinkhole loss is confirmed, then the insurer is not required to conduct sinkhole testing.<sup>12</sup>
- Notice to the Policyholder – The insurer must provide written notice to the policyholder detailing what the insurer has determined to be the cause of damage (if the determination has been made) and a statement of the circumstances under which the insurer must conduct sinkhole testing.<sup>13</sup> The policyholder must also be notified of his or her right to demand sinkhole testing and the circumstances under which the policyholder may incur costs associated with testing.<sup>14</sup>
- Authorization to Deny Sinkhole Claim – An insurer may deny a claim upon a determination that there is no sinkhole loss.<sup>15</sup>
- Policyholder Demand for Sinkhole Testing – The policyholder may demand sinkhole testing in writing within 60 days after receiving a claim denial if the insurer denied the claim without performing sinkhole testing and coverage would be available<sup>16</sup> if a sinkhole loss is confirmed.<sup>17</sup> However, a policyholder requesting such testing must pay the insurer 50 percent of the sinkhole testing costs up to \$2,500.<sup>18</sup> If the requested testing confirms a sinkhole loss the insurer must reimburse the testing costs to the policyholder.<sup>19</sup>
- Payment of Sinkhole Claims – If a sinkhole loss is verified, the insurer must pay to stabilize the land and building and repair the foundation in accordance with the recommendation of the professional engineer retained by the insurer.<sup>20</sup> Payment for other repairs to the structure and contents are governed by the insurance policy. The insurer may limit payment to the actual cash value of the sinkhole loss not including below-ground repair techniques until the policyholder enters into a contract for the performance of building stabilization repairs.<sup>21</sup> The contract for below-ground repairs must be made in accordance with the recommendations set

---

<sup>10</sup> See *id.*

<sup>11</sup> Section 627.707(2), F.S.

<sup>12</sup> See *id.*

<sup>13</sup> Section 627.707(3), F.S.

<sup>14</sup> See *id.*

<sup>15</sup> Section 627.707(4)(a), F.S.

<sup>16</sup> The claim denial was not issued due to policy conditions or exclusions of coverage and instead was based the failure of the loss to meet the definition of sinkhole loss.

<sup>17</sup> Section 627.707(4)(b), F.S.

<sup>18</sup> Section 627.707(4)(b)2., F.S.

<sup>19</sup> Section 627.707(4)(b)3., F.S.

<sup>20</sup> Section 627.707(5), F.S.

<sup>21</sup> Section 627.707(5)(a), F.S.

forth in the insurer's sinkhole report issued pursuant to s. 627.7073, F.S.,<sup>22</sup> and entered into within 90 days after the policyholder receives notice that the insurer has confirmed coverage for sinkhole loss.<sup>23</sup> The time period is tolled if either party invokes neutral evaluation. If repairs cannot be completed within policy limits, the insurer may either pay to complete the recommended repairs or tender policy limits without a reduction for repair expenses already incurred.<sup>24</sup>

### ***Other Revisions***

The 2011 bill authorized insurers to restrict catastrophic ground cover collapse and sinkhole loss coverage to the principal building as defined in the insurance policy. The bill also allows an insurer to require a property inspection prior to issuing sinkhole loss coverage. The bill clarified that additional living expense coverage is only available pursuant to a sinkhole loss if there is structural damage to the covered building.

### ***Results of 2011 Sinkhole Insurance Reforms***

The first complete year the reforms were in effect was 2012.<sup>25</sup> No data has been collected on an industry-wide basis on the number of claims, claim severity, or claim costs since the reforms were enacted, so their impact on sinkhole claims and costs on an industry-wide basis is unknown. However, Citizens performed a sinkhole study in 2012 to compute the impact of the 2011 reforms on their policies.<sup>26</sup> This study looked at actual sinkhole claim files from Citizens and readjusted the losses and expenses associated with the claims as if the 2011 reforms had been in effect. The actuarial analysis which accompanied the study projected the 2011 reforms would reduce Citizens' expected incurred sinkhole losses for 2013 by almost 55 percent. In Citizens' rate filing for 2014,<sup>27</sup> their actuary projected Citizens' sinkhole losses would decrease by over 52 percent relative to what they would have been without the 2011 reforms. The actuary further noted, however, that even with the projected reduction in sinkhole losses, Citizens still has a significant rate deficiency in the sinkhole area. In fact, in 2012, Citizens earned almost \$57 million in sinkhole premium but paid almost \$227 million in sinkhole losses and expenses.

According to data accompanying Citizens 2016 rate filing,<sup>28</sup> in 2014, new sinkhole claim volume was down 68 percent from 2013. This continued a trend of annual reductions in the number of sinkhole claims filed with the corporation. In 2011, over 4,500 sinkhole claims were reported to Citizens. In 2012, that number decreased to approximately 3,100 claims and in 2013 the total

---

<sup>22</sup> Section 627.707(5), F.S.

<sup>23</sup> Section 627.707(5)(b), F.S.

<sup>24</sup> Section 627.707(5), F.S.

<sup>25</sup> The reforms were effective on May 17, 2011, when the bill (CS/CS/CS/SB 408) was signed by the Governor.

<sup>26</sup> *Citizens Property Insurance Corporation Senate Bill 408 Sinkhole Analysis*, prepared by Insurance Services Office, dated Jul. 19, 2012, and presented at Citizens' Board of Governors Meeting on Jul. 27, 2012, [https://www.citizensfla.com/documents/20702/643634/07AH\\_Citizens\\_SB408\\_Sinkhole\\_Analysis.pdf/a26f62af-b142-4b5c-aed2-35821603c1a0](https://www.citizensfla.com/documents/20702/643634/07AH_Citizens_SB408_Sinkhole_Analysis.pdf/a26f62af-b142-4b5c-aed2-35821603c1a0) (last visited Feb. 5, 2016).

<sup>27</sup> Citizens Property Insurance Company, *2014 Rate Kit*, pg. 4, <https://www.citizensfla.com/documents/20702/124817/2014+Rate+Kit.pdf/7564c271-8e83-427d-8cb4-ca41b67a2e57> (last visited Feb. 5, 2016).

<sup>28</sup> Citizens Property Insurance Company, *2016 Rate Kit*, pg. 10, <https://www.citizensfla.com/documents/20702/30286/2016+Rate+Hearing+Kit/479c1ab7-f120-47ca-a158-6f908ff36d1a> (last visited Feb. 5, 2016).

claims received was approximately 1,200.<sup>29</sup> Total incurred losses and allocated loss adjustment expenses have dropped substantially from approximately \$537 million in 2011 to approximately \$83 million in 2014.<sup>30</sup>

### **Standards for Sinkhole Testing and Sinkhole Reports**

Section 627.7072, F.S., requires sinkhole testing to be performed by a professional engineer and a professional geologist. The tests performed must be sufficient for the professional geologist and professional engineer to determine the presence of a sinkhole loss or other cause of damage. The tests must also enable the professional engineer to make recommendations regarding necessary building stabilization and foundation repair.

Upon the completion of sinkhole testing, the professional engineer or professional geologist must issue a report and certification to the insurer and the policyholder pursuant to the requirements of s. 627.7073, F.S. The report must detail the testing performed, whether structural damage is present, whether sinkhole activity is the cause of the damage, and any recommendations for stabilizing the land and building and making foundation repairs. The findings and recommendations of the insurer's professional engineer are presumed to be correct. If an insurer pays a claim for sinkhole loss, the insurer must file a copy of the report and certification and other required documentation with the county clerk of court. Once building stabilization or foundation repairs are complete for a verified sinkhole loss, the engineer responsible for monitoring repairs must issue a report to the policyholder detailing the repairs performed and certify that the repairs were performed properly. The report must also be filed with the county clerk of court.

### **Neutral Evaluation**

Neutral evaluation is an alternative procedure in s. 627.7074, F.S., for the resolution of disputed sinkhole insurance claims for which a sinkhole testing report<sup>31</sup> has been issued. The neutral evaluator must have sufficient professional training and credentials to render opinions as to causation, and if applicable, the recommended method of repair and the estimated cost of such repairs.<sup>32</sup> Neutral evaluation is nonbinding, but the insurer and policyholder must participate if either party requests it.<sup>33</sup> At a minimum, neutral evaluation must determine the cause of the loss, all methods of stabilization and repair both above and below ground, the costs for stabilization

---

<sup>29</sup> Citizens Property Insurance Company, *Citizens Property Insurance Corporation Actuarial & Underwriting Committee Recommended Rate Filing Executive Summary*, Jun. 23, 2015, at pg. 5, [https://www.citizensfla.com/documents/20702/27059/02\\_2016\\_Annual\\_Recommended\\_Rate\\_Filing\\_Exec\\_Summary.pdf/57019cdf-e272-4307-b78e-620883395be0](https://www.citizensfla.com/documents/20702/27059/02_2016_Annual_Recommended_Rate_Filing_Exec_Summary.pdf/57019cdf-e272-4307-b78e-620883395be0) (last visited Feb. 5, 2016).

<sup>30</sup> Citizens Property Insurance Corporation, *2016 Rate Hearing*, pg. 19, <https://www.citizensfla.com/documents/20702/30286/2016+Rate+Hearing+Kit/479c1ab7-f120-47ca-a158-6f908ff36d1a> (last visited Feb. 5, 2016).

<sup>31</sup> Section 627.7073, F.S., contains the statutory standards for a sinkhole report. A sinkhole report must be based on tests performed by a professional engineer and professional geologist that, as required by s. 627.7072, F.S., are sufficient to determine the presence or absence of sinkhole loss and allow the professional engineer to make recommendations regarding necessary building stabilization and foundation repair. The sinkhole report must contain the opinion of the professional engineer or professional geologist as to whether a sinkhole loss is present, and if so, the recommendation of the professional engineer of methods for stabilizing the land and repairing the foundation.

<sup>32</sup> See s. 627.7074(1)(a), F.S., and s. 627.7074(11), F.S.

<sup>33</sup> Section 627.7074(4), F.S.

and all repairs, and the information necessary to issue a report of the neutral evaluator's findings and recommendations.<sup>34</sup>

Neutral evaluation is an informal process in which formal rules of evidence and procedure need not be observed.<sup>35</sup> The insurer or the policyholder request neutral evaluation by sending written notice to the Department of Financial Services (DFS).<sup>36</sup> The DFS then provides a list of certified neutral evaluators to the parties who have 14 days to select a neutral evaluator.<sup>37</sup> If the parties cannot agree to a neutral evaluator, the department makes the selection. Once a neutral evaluator is selected, within 14 days he or she must notify the policyholder and the insurer of the date, time, and place of the neutral evaluation conference.<sup>38</sup>

Once a neutral evaluator has been selected by the parties or appointed by the DFS, the insurer submits the sinkhole testing report to the neutral evaluator and the policyholder submits all reports initiated by the policyholder or an agent of the policyholder that either confirm sinkhole loss or dispute the results of another report.<sup>39</sup> The neutral evaluator must be allowed reasonable access to the interior and exterior of the insured structures to be evaluated.<sup>40</sup> At the conclusion of neutral evaluation, the neutral evaluator must prepare a report describing all matters that are the subject of neutral evaluation, including whether a sinkhole loss has occurred, and, if so, the estimated costs of stabilizing the land and any covered building and other appropriate repairs.<sup>41</sup> The recommendation of the neutral evaluator and his or her testimony must be admitted in any litigation relating to the insurance claim.<sup>42</sup> If the insurer timely complies with the recommendation of the neutral evaluator, the insurer is not liable for extra-contractual damages related to issues determined under neutral evaluation.<sup>43</sup>

### **Surplus Requirements**

To transact insurance in Florida, insurers must apply for a certificate of authority and meet certain surplus requirements. For a new domestic insurer that transacts residential property insurance and is:

- Not a wholly owned subsidiary of an insurer domiciled in any other state, the surplus requirement is at least \$15 million.
- A wholly owned subsidiary of an insurer domiciled in any other state, the requirement is at least \$50 million.

Under current law, the surplus requirements for existing insurers are different than the requirements for new insurers. For property and casualty insurers, the requirement is \$4 million, except for property and casualty insurers authorized to underwrite any line of residential property insurance. For residential property insurers not holding a certificate of authority before July 1,

---

<sup>34</sup> Section 627.7074(2), F.S.

<sup>35</sup> Section 627.7074(5), F.S.

<sup>36</sup> Section 627.7074(4), F.S.

<sup>37</sup> Section 627.7074(7), F.S.

<sup>38</sup> See *id.*

<sup>39</sup> See section 627.7074(2) and (5), F.S.

<sup>40</sup> Section 627.7074(5), F.S.

<sup>41</sup> Section 627.7074(12), F.S.

<sup>42</sup> Section 627.7074(13), F.S.

<sup>43</sup> Section 627.7074(15), F.S.

2011, the requirement is \$15 million. For residential property insurers holding a certificate of authority before July 1, 2011, and until June 30, 2016, \$5 million; on or after July 1, 2016, and until June 30, 2021, \$10 million; on or after July 1, 2021, \$15 million.

### **Rate Filings for Property, Casualty, and Surety Insurance**

The rating requirements for property, casualty, and surety insurance are located in part I of ch. 627, F.S., entitled the “Rating Law,” and apply to property, casualty, and surety insurance. The law states that the rates for all classes to which part I applies “shall not be excessive, inadequate, or unfairly discriminatory.”<sup>44</sup> The Office of Insurance Regulation (OIR) has the responsibility to review and approve or disapprove rates charged by insurance companies to ensure compliance with the rate standards.

Section 627.062(2)(a), F.S., describes the filing process and time frames that must be followed by all insurers subject to its provisions. Generally, insurers may choose to submit their rate to the OIR pursuant to either the “file and use” method or the “use and file” method. Under “file and use,” the insurer submits its proposed rate to the OIR at least 90 days before the rate’s effective date but does not implement the rate until it is approved. Under “use and file,” the insurer may implement the rate before filing for approval, but must submit the filing within 30 days of the rate’s effective date. Under “use and file,” if a portion of the rate is subsequently found to be excessive, the insurer must refund to policyholders the portion of the rate that is excessive.

The OIR applies the following factors in determining whether a rate is excessive, inadequate, or unfairly discriminatory:

- Past and prospective loss experience in Florida and in other jurisdictions;
- Past and prospective expenses;
- Degree of competition to insure the risk;
- Investment income reasonably expected by the insurer;
- Reasonableness of the judgment reflected in the filing;
- Dividends, savings, or unabsorbed premium deposits returned to Florida insureds;
- Adequacy of loss reserves;
- Cost of reinsurance;
- Trend factors, including those for actual losses per insured unit;
- Catastrophe and conflagration hazards, when applicable;
- Projected hurricane losses, if applicable;
- A reasonable margin for underwriting profit and contingencies;
- Cost of medical services, when applicable; and
- Other relevant factors impacting frequency and severity of claims or expenses.

### **Florida Commission on Hurricane Loss Projection Methodology**

In 1995 the Legislature established the Florida Commission on Hurricane Loss Projection Methodology (Commission) to serve as an independent body within the State Board of Administration.<sup>45</sup> The Commission is comprised of 12 members. Members include experts in

---

<sup>44</sup> Section 627.062(1), F.S.

<sup>45</sup> The Commission is created in s. 627.0628, F.S. This statute also provides the composition and duties of the Commission.

insurance finance, statistics, computer system design, structural engineering, and meteorology who are full-time faculty members in the State University System, three actuaries, the Executive Director of Citizens, the senior employee responsible for Florida Hurricane Catastrophe Fund operations, the Insurance Consumer Advocate, and the Director of Emergency Management. The Commission sets standards for hurricane loss projection methodology and examines the methods employed in proprietary hurricane loss models used by private insurers in setting property insurance rates to determine whether they meet the Commission's standards.

The Commission adopts findings on the accuracy or reliability of the methods, standards, principles, models and other means used to project hurricane losses. Only hurricane loss models or methods the Commission deems accurate or reliable can be used by insurers in rate filings to estimate hurricane losses used to set property insurance rates.

### **III. Effect of Proposed Changes:**

SB 1274 creates s. 627.7151, F.S., which allows insurers to offer a new type of sinkhole insurance coverage. This sinkhole coverage would, as under current law, only provide coverage for "sinkhole loss" which is defined in statute as structural damage to the covered building, including the foundation, caused by sinkhole activity. An authorized insurer may issue the coverage, but is not required to do so. If offered, such coverage may only provide personal lines residential property insurance for sinkhole loss to the structure or the contents of personal property. Losses under personal property or contents coverage must be adjusted only on the basis of replacement costs up to the policy limits, thus prohibiting adjustment based on actual cash value. The insurance must also include coverage for additional living expenses.

The new form of coverage differs from existing coverage in that it is exempt from the following statutory requirements:

- Standards for the investigation and payment of a sinkhole loss claim in s. 627.707, F.S.;
- Standards for sinkhole testing by professional engineers and professional geologists in s. 627.7072, F.S.;
- Standards for sinkhole testing reports in s. 627.7073, F.S.; and
- Neutral evaluation standards in s. 627.7074, F.S.

Regarding the sinkhole coverage created by s. 627.7151, F.S., the bill provides that any limitations on sinkhole coverage or policy limits, including, but not limited to deductibles, must be prominently noted on the policy declarations page or face page.

The bill reduces the surplus as to policyholder requirements for insurers that only transact sinkhole insurance for personal lines residential property pursuant to s. 627.7151, F.S. For a new domestic insurer the bill lowers the surplus requirement to \$2.5 million. For an existing domestic insurer, the requirement is reduced to \$1.5 million.

The bill allows insurers to develop rates for the new version of sinkhole insurance created by the bill under the full rate review process provided for in s. 627.062, F.S. Alternatively, the bill allows the use of rates developed by an alternative option if the rate filing is submitted to the OIR before October 1, 2019. Under the alternative option created by the bill, a rate filing for the sinkhole coverage created by the bill is exempt from the filing and review requirements of

s. 627.062(2)(a) and (f), F.S. Instead, the insurer makes an informational filing. In the informational filing, the insurer must notify the OIR of any change to its sinkhole insurance rates, including the average statewide percentage change in rates, no later than 30 days after the effective date of the change in rates. Insurers that utilize this option must maintain actual data regarding its sinkhole insurance rates for 2 years after the effective date of those rates.

Regardless of the rate filing method used, a rate still cannot be excessive, inadequate, or unfairly discriminatory. The insurer writing the sinkhole insurance is responsible for ensuring the rate charged meets this requirement. The bill allows the OIR to examine an insurer's documentation supporting a rate to verify the rate meets the requirement with the insurer paying for the examination. During an examination, the OIR uses the rate factors and standards in current law that apply to property, casualty and surety insurance rates filed with the OIR to determine whether the sinkhole insurance rate charged is excessive, inadequate, or unfairly discriminatory. Additionally, the insurer must notify the OIR within 30 days of a rate change for sinkhole insurance that was originally set by this method. Setting sinkhole rates using this method is similar to what is allowed in current law for rates for flood insurance and certain types of commercial lines risks under s. 627.062(3)(d), F.S.

The bill expands the duties of the Commission on Hurricane Loss Projection Methodology. It requires the Commission to adopt, by July 1, 2018, actuarial methods, principles, standards, models, or output ranges for sinkhole loss to be used in setting rates for personal lines residential sinkhole coverage.

The bill also requires the OIR to consider projected sinkhole losses from models or methods found to be acceptable or reliable by the Commission or a straight average of the model results for a rate filing that includes sinkhole coverage. To support a sinkhole insurance rate, for those filed with and approved by the OIR before use, the bill allows sinkhole losses to be projected by a sinkhole loss model found acceptable or reliable by the Commission. For sinkhole rates not filed with or approved by the OIR, if the OIR examines the rate after use, it will consider whether the insurer's sinkhole rates were set based on sinkhole losses projected by a Commission approved model.

Currently, no insurance coverage is eligible for export to a surplus lines insurer unless it meets certain conditions. One condition is that an agent has sought coverage from and received three documented rejections from authorized insurers currently writing the same type of coverage. Until July 1, 2020, the bill allows this new sinkhole coverage for personal lines residential property to be written by a surplus lines insurer without the agent obtaining three declinations for insurance from Florida licensed sinkhole insurers. This provision tracks the same language in place for flood insurance regarding surplus lines insurers. However, the other requirements governing the exporting of coverage to the surplus lines continue to apply.

Citizens, just like all other property insurers, already must include catastrophic ground cover collapse coverage in all of its policies; The bill reiterates this requirement. The bill, however, requires that Citizens must stop providing coverage for the peril of sinkhole after July 1, 2018. The bill is unclear whether the prohibition is against sinkhole insurance as allowed under this bill, or all sinkhole insurance, including that subject to ss. 627.707-627.7074, F.S. The requirement that Citizens cease renewing such coverage and allowance to continue writing

catastrophic ground cover collapse indicate that the intent is to prohibit Citizens from writing any sinkhole coverage. Citizens is a residual market insurer more commonly referred to as the insurer of last resort. At the end of 2015,<sup>46</sup> Citizens insured 115,374 sinkhole loss policies<sup>47</sup> at a total insured value in excess of \$30 billion dollars.<sup>48</sup> Should the private market be unwilling or unable to insure all of these policies within 2 years many policyholders who currently have sinkhole loss coverage could be left with no options to obtain coverage.

The Florida Insurance Code covers a comprehensive array of property insurance measures related to forms, contracts, trade practice, market conduct, rates, consumer protections, solvency and other regulatory matters. The bill provides that with respect to the regulation of sinkhole coverage written in this state by authorized insurers, the provisions in the bill supersedes any other provision of the Florida Insurance Code in the event of a conflict. Because this broadly supersedes the entire Insurance Code, the effect of the bill on insurance regulation is unknown.

In addition to other requirements in the bill, insurers providing sinkhole coverage are to notify the OIR at least 30 days before writing sinkhole insurance in this state. They also must file a plan of operation and financial projections or revisions to such plan, as applicable, with the OIR.

The bill is effective upon becoming a law.

#### **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:**

None.

##### **B. Private Sector Impact:**

The economic impact on the private sector is unknown. The creation of a new form of sinkhole insurance that is not subject to existing statutory requirements for the

<sup>46</sup> Citizens Policy Inforce data for Sinkhole coverage as of Dec. 31, 2015. (On file with the Banking and Insurance Committee).

<sup>47</sup> Does not include policies tagged for takeout.

<sup>48</sup> As of Dec. 31, 2015 Citizens Total Insured Value for Sinkhole loss was \$30,384,365,886.

investigation and payment of sinkhole loss claims, standards for sinkhole testing and reports, and neutral evaluation may drive up the cost of coverage for homeowners. If insurers offering this new sinkhole insurance raise deductibles and initiate limits on coverage (sub-limits), policyholders may have lower premiums. However, if a policyholder experienced a sinkhole, the costs to the policyholder would be higher.

Not allowing Citizens to offer sinkhole coverage after July 1, 2018, could leave many policyholders who currently have sinkhole loss coverage without any coverage should the private market be unwilling or unable to offer them such coverage. Additionally, removing \$30 billion dollars in insured value for sinkhole coverage from Citizens total exposure would help reduce the risk that Citizens would need to levy assessments on the private market, should Citizens not have enough capital to pay all claims.

**C. Government Sector Impact:**

There is an indeterminate impact to the Florida Commission on Hurricane Loss Projection Methodology. By July 1, 2018, the Commission must adopt actuarial methods, principles, standards, models, or output ranges for sinkhole loss to be used in setting rates for personal lines residential sinkhole coverage.

**VI. Technical Deficiencies:**

Line 252-254: Citizens already must offer catastrophic groundcover collapse with all its policies.

Line 255-259: The Hurricane Catastrophe Fund already cannot cover losses from sinkholes.

**VII. Related Issues:**

None.

**VIII. Statutes Affected:**

This bill substantially amends the following sections of the Florida Statutes: 624.407, 624.408, 627.062 and 627.0628

This bill creates section 627.7151 of the Florida Statutes.

**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.