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DATE: April 7, 1997

**HOUSE OF REPRESENTATIVES
COMMITTEE ON
FINANCIAL SERVICES
BILL RESEARCH & ECONOMIC IMPACT STATEMENT**

BILL #: HB 1779

RELATING TO: Insurance

SPONSOR(S): Reps. Lippman, Barreiro, Gay, and Rojas

STATUTE(S) AFFECTED: Chapters 624 and 627, F.S.

COMPANION BILL(S): SB 1744 (s)

ORIGINATING COMMITTEE(S)/COMMITTEE(S) OF REFERENCE:

(1) FINANCIAL SERVICES

(2)

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I. SUMMARY:

Each property and casualty (auto, workers' compensation, liability, etc.) insurance company that writes residential property insurance anywhere in the United States and writes any form of property and casualty insurance in Florida would be required to maintain a Florida residential property insurance market share that matched its Florida market share of all property and casualty insurance. If the insurance company's residential market share did not meet this mandate, the Residential Property and Casualty Joint Underwriting Association (RPCJUA) would assign policies to the company.

The bill would require all property and casualty insurers to write personal lines residential coverage in Florida; the requirement would not apply to an insurer if neither that insurer nor any other insurer that is a member of the same insurer group writes personal lines residential coverage anywhere in the United States.

Each property and casualty insurer subject to the bill would be required to write a share of the personal lines residential market equal to its share of the overall property and casualty market. If it failed to meet this mandate, risks would be assigned to the insurer from the RPCJUA to make up for the shortfall. Refusal to accept assigned risks would be a "willful" violation of the Insurance Code, subject to an administrative fine of up to \$20,000 per violation.

An insurer could petition the Department of Insurance for a temporary waiver of these requirements, but would have the burden of proving that compliance with the requirements would endanger or impair its solvency.

II. SUBSTANTIVE RESEARCH:

A. PRESENT SITUATION:

Depopulation of Residential Property and Casualty Joint Underwriting Association

In response to widespread unavailability of residential property insurance coverage, the Legislature has created insurers of last resort, known as "residual market" insurers. Almost 1 million homes in Florida are insured by one of two residual market entities. A "residual market" entity provides insurance coverage to an applicant who is not able, after a good faith effort, to procure the coverage from a licensed insurance company in the "voluntary," or regular, market.

In Florida, the residual market entities that provide property coverage are statutorily-mandated nonprofit associations of insurance companies. The Residential Property and Casualty Joint Underwriting Association (RPCJUA), was created by statute in 1992 as a result of Hurricane Andrew, and the Florida Windstorm Underwriting Association (FWUA), was created by statute in 1970. The RPCJUA writes full homeowner's policies and other residential policies throughout the state. The FWUA writes policies that cover only losses caused by windstorm, and writes these policies only in certain limited coastal areas; the FWUA writes both residential and non-residential coverage.

As of January 31, 1997, the RPCJUA had 678,809 personal lines policies in force, representing premiums of \$509 million a year, structure exposure of \$53 billion, and contents exposure of \$24 billion. Excluding policies that do not provide windstorm coverage from the calculation, the RPCJUA had 606,949 policies in force, representing \$474 million a year in premium, \$47 billion in structure exposure, and \$21 billion in contents exposure. As of February 14, 1997, the RPCJUA had 2,259 commercial lines policies in force, representing premiums of \$33 million a year, structure exposure of \$11 billion, and contents exposure of \$37 million.

When the premiums and other resources of the RPCJUA are not sufficient to pay claims, assessments are levied against insurers in proportion to their market share. Generally, the assessments must be enough to recoup in one year the entire amount of the deficit. If the deficit is larger than 10% of premium, the deficit is to be recouped over a period of up to 10 years through the issuance of revenue bonds. Single-year assessments and the first year of a multi-year assessment are levied against insurers, who are then able to pass these assessments on to their policyholders; these are referred to as "regular" assessments. The assessments in the out years of a multi-year assessment are not levied on insurers, but are instead collected by insurers from their policyholders; the insurer has no liability, but is instead the collection agent for the residual market entity.

The assessment structure has been a motivation for efforts to reduce the size of the RPCJUA, which at its peak had over 935,000 policies in force, representing over \$66 billion worth of structures. Insurers have often cited the RPCJUA assessment potential as the reason for their decisions to cut back on their presence in the Florida market. In 1995 and 1996, the Legislature created incentives for private sector insurers to take over risks that were insured by the RPCJUA. These incentives primarily consisted of cash rewards and exemptions from RPCJUA deficit assessments. Under the "take-out" plans, an RPCJUA policyholder is offered coverage from a private sector company; the policyholder is free to reject the offer, but, because any offer from a licensed insurer

disqualifies an applicant from eligibility for RPCJUA coverage, the policyholder will not be able to get continued RPCJUA coverage if he rejects the "take-out" offer.

About 500,000 RPCJUA policies have been selected ("tagged") by insurance companies for removal from the RPCJUA and replacement with private sector coverage; the RPCJUA expects its policy count to soon drop below 500,000 as a result of these take-outs. In addition, on January 14, 1997 the RPCJUA board approved take-out plans for an additional 279,000 personal lines policies and 310 commercial lines policies; these proposals await DOI approval. According to the RPCJUA's modeling firm, the currently-approved depopulation plans will not reduce the JUA's 100-year probable maximum loss (which is \$4.8 billion), because of the relatively few risks taken from the most hazardous areas of the state and the JUA's continued growth in those areas.

The results of depopulation may mask the fact that the RPCJUA is still issuing substantial numbers of new policies. Although the RPCJUA results for January, 1997, showed a net reduction of 27,179 policies, the RPCJUA wrote a total of 37,201 new policies in the period 1/1/97 - 2/5/97.

The "Fair Share" concept

The idea of "linkage," or conditioning an insurer's ability to write one kind of insurance on the amount of another kind of insurance it writes, is not without precedent. Florida law requires residential property insurers to include windstorm coverage in all policies except those written in FWUA-eligible areas. California law requires residential property insurers either to make earthquake coverage available or to participate in the California Earthquake Authority.

The idea of a broader form of linkage, under which an insurer would be required to write a volume of residential property insurance reflective of its overall property and casualty market share, was first formally proposed by the Academic Task Force on Property Insurance, which was created by the 1995 General Appropriations Act. As proposed by the task force, each insurer that writes homeowners' insurance outside of Florida would have to assume its "fair share" of the Florida's homeowners' market in order to continue writing other lines of business. The "fair share" would be determined under a formula that considered the insurer's financial capacity and its non-homeowners' market share. The proposal was not linked to depopulation of the RPCJUA.

The task force recommended "fair share" as an alternative to be implemented only if the other task force recommendations failed to restore a competitive property insurance market in Florida. Other recommendations of the task force included a taxpayer-funded cap on insurance industry losses, reduction of regulatory control over insurers' rates, increased reliance on higher deductibles, and stronger loss prevention programs.

B. EFFECT OF PROPOSED CHANGES:

Each property and casualty (auto, workers' compensation, liability, etc.) insurance company that writes residential property insurance anywhere in the United States would be required to maintain a Florida residential property insurance market share that matched its Florida market share of all property and casualty insurance. If the insurance

company's residential market share did not meet this mandate, the RPCJUA would assign policies to the company.

All property and casualty (P&C) insurers would be required to write personal lines residential coverage in Florida; the requirement would not apply to an insurer if neither that insurer nor any other insurer that is a member of the same insurer group writes personal lines residential coverage anywhere in the United States. "Property and casualty" includes motor vehicle, workers' compensation, commercial and professional liability, and most other forms of insurance except for life or health insurance.

Each P&C insurer subject to the bill would be required to write a share of the personal lines residential market equal to its share of the overall P&C market. If it failed to meet this mandate, risks would be assigned to the insurer to make up for the shortfall.

The bill would require each P&C insurer to make four calculations:

1. "Fair market share" -- the insurer's market share of the entire P&C market for the reporting year.
2. "Actual market share" -- the insurer's market share of the entire personal lines residential property insurance market for the reporting year.
3. "Fair market shortfall" -- the difference between fair market share and actual market share.
4. "Available capacity" -- the difference between the amount of premium an insurer is allowed to write based on its surplus (in general, net premiums may not exceed 4 times surplus and gross premiums may not exceed 10 times surplus) and the amount of premium actually written.

For members of an insurer group, these calculations would be made on a group basis.

If the insurer or group has available capacity and its fair market share exceeds its actual market share, the RPCJUA would assign residential property risks (as selected by the RPCJUA) to the insurer or group to make up the shortfall, up to 90% of the insurer's available capacity.

EXAMPLE: Hypothetical Insurance Co. is a national company with surplus of \$1 billion and countrywide premiums of \$2.5 billion. In Florida, it writes \$325 million a year in P&C premium (most of it private passenger auto) and \$20 million in homeowners' premium. Hypothetical's overall P&C market share is 2.5%, and its homeowners' market share is 1.5%. Its "fair market shortfall" is \$13 million (the amount of homeowners' premiums needed to reach a 2.5% market share).

The bill would give Hypothetical three options:

1. It could write new homeowners' business voluntarily in an amount sufficient to raise its homeowners' market share to 2.5%.
2. It could cancel or nonrenew enough private passenger auto business to reduce its overall P&C market share to 1.5%.

3. It could be assigned policies from the RPCJUA with a total premium of \$13 million.

Since Hypothetical's "available capacity" as defined by the bill is over \$1 billion, policies covering the full amount of the shortfall could be assigned.

Each refusal to accept an assignment would constitute a "willful" violation of the Insurance Code, subject to an administrative fine of up to \$20,000 per violation or \$100,000 for all violations growing out of the same action.

If an insurer can prove that the assignments impair or endanger its solvency, the insurer can apply to the DOI for a temporary deferment or revision of the assignments, and the insurer would have the burden of proving the endangerment or impairment of its solvency.

The DOI would have broad rulemaking authority to implement these requirements, including authority to "adopt any reasonable methods to accomplish the essential purpose of this section, which is to depopulate the association [RPCJUA] of personal lines residential risks by requiring insurers to underwrite their fair market share with respect to such risks."

C. APPLICATION OF PRINCIPLES:

1. Less Government:

a. Does the bill create, increase or reduce, either directly or indirectly:

(1) any authority to make rules or adjudicate disputes?

Yes. The bill requires the Department of Insurance to adopt rules to implement the bill, which may include "any reasonable methods" to accomplish depopulation of the RPCJUA.

(2) any new responsibilities, obligations or work for other governmental or private organizations or individuals?

Yes. The bill would require a property and casualty insurer to write a certain amount of residential property insurance or accept policies assigned to it by the RPCJUA.

(3) any entitlement to a government service or benefit?

No.

b. If an agency or program is eliminated or reduced:

(1) what responsibilities, costs and powers are passed on to another program, agency, level of government, or private entity?

Not applicable.

(2) what is the cost of such responsibility at the new level/agency?

Not applicable.

(3) how is the new agency accountable to the people governed?

Not applicable.

2. Lower Taxes:

a. Does the bill increase anyone's taxes?

No.

b. Does the bill require or authorize an increase in any fees?

No.

c. Does the bill reduce total taxes, both rates and revenues?

No.

d. Does the bill reduce total fees, both rates and revenues?

No.

e. Does the bill authorize any fee or tax increase by any local government?

No.

3. Personal Responsibility:

a. Does the bill reduce or eliminate an entitlement to government services or subsidy?

No.

- b. Do the beneficiaries of the legislation directly pay any portion of the cost of implementation and operation?

Not applicable.

4. Individual Freedom:

- a. Does the bill increase the allowable options of individuals or private organizations/associations to conduct their own affairs?

No. The bill reduces the ability of insurance companies to decide how much residential property exposure they can sustain, and requires insurance companies to accept policies assigned to them by the RPCJUA.

- b. Does the bill prohibit, or create new government interference with, any presently lawful activity?

Yes. Although the Insurance Code currently contains restrictions on insurance companies' ability to terminate policies, there are no current statutory provisions that would require an insurance company to write a specified amount of business or to accept specific applicants or risks.

5. Family Empowerment:

- a. If the bill purports to provide services to families or children:

- (1) Who evaluates the family's needs?

Not applicable.

- (2) Who makes the decisions?

Not applicable.

- (3) Are private alternatives permitted?

Not applicable.

- (4) Are families required to participate in a program?

Not applicable.

(5) Are families penalized for not participating in a program?

Not applicable.

b. Does the bill directly affect the legal rights and obligations between family members?

Not applicable.

c. If the bill creates or changes a program providing services to families or children, in which of the following does the bill vest control of the program, either through direct participation or appointment authority:

(1) parents and guardians?

Not applicable.

(2) service providers?

Not applicable.

(3) government employees/agencies?

Not applicable.

D. SECTION-BY-SECTION RESEARCH:

Section 1 creates s. 624.4015, F.S., relating to requirements for writing personal lines residential coverage. The bill would require any authorized property and casualty insurer to write personal lines residential coverage if the insurer, or any member of an insurer group that includes the insurer, writes personal lines residential coverage anywhere in the United States.

Section 2 creates s. 627.3516, F.S., relating to the "fair share" plan. This section would impose the specific requirements described in "Effects of Proposed Changes," above.

Section 3 provides that the bill would take effect October 1, 1997.

III. FISCAL RESEARCH & ECONOMIC IMPACT STATEMENT:

A. FISCAL IMPACT ON STATE AGENCIES/STATE FUNDS:

1. Non-recurring Effects:

None.

2. Recurring Effects:

None.

3. Long Run Effects Other Than Normal Growth:

None.

4. Total Revenues and Expenditures:

None.

B. FISCAL IMPACT ON LOCAL GOVERNMENTS AS A WHOLE:

1. Non-recurring Effects:

None.

2. Recurring Effects:

None.

3. Long Run Effects Other Than Normal Growth:

None.

C. DIRECT ECONOMIC IMPACT ON PRIVATE SECTOR:

1. Direct Private Sector Costs:

The bill could negatively impact the solvency of insurance companies in several ways. Although the Insurance Code generally allows a property and casualty insurer to write net premiums equal to 4 times its surplus, ratios of 2-to-1 or 2½-to-1 are generally considered prudent. Requiring an insurer to maintain a higher ratio could weaken its solvency and lower its claims-paying-ability ratings.

Solvency of an insurer could also be affected if the policies assigned to it by the RPCJUA contained a high proportion of particularly hazardous risks. Unlike typical assigned risk programs, there is no provision in the bill allowing an insurer to charge different rates to assigned risks than to risks it accepted voluntarily.

The bill could create shortages in forms of insurance other than residential property insurance, if some insurers choose to reduce their property and casualty market share rather than increase their residential market share, or if some insurers choose to leave the state entirely rather than accept assigned risks.

2. Direct Private Sector Benefits:

To the extent that the bill facilitates depopulation of the RPCJUA, it reduces the potential for RPCJUA deficit assessments on insurance companies and their policyholders.

3. Effects on Competition, Private Enterprise and Employment Markets:

The mandates of the bill could disproportionately affect insurers that have relatively low premium structures for residential coverage. If two insurers have comparable rates for non-property P&C, significant differences in property rates, and identical property exposures, the insurer with low property rates could show a shortfall while the insurer with high property rates does not; the result would be that one insurer would be subject to the mandates while the other insurer (which is presumably stronger financially because of its higher rate structure) would not.

D. FISCAL COMMENTS:

IV. CONSEQUENCES OF ARTICLE VII, SECTION 18 OF THE FLORIDA CONSTITUTION:

A. APPLICABILITY OF THE MANDATES PROVISION:

This bill does not require counties or municipalities to spend funds or to take an action requiring the expenditure of funds.

B. REDUCTION OF REVENUE RAISING AUTHORITY:

This bill does not reduce the authority that municipalities or counties have to raise revenues in the aggregate.

C. REDUCTION OF STATE TAX SHARED WITH COUNTIES AND MUNICIPALITIES:

This bill does not reduce the percentage of a state tax shared with counties or municipalities.

V. COMMENTS:

VI. AMENDMENTS OR COMMITTEE SUBSTITUTE CHANGES:

A "strike everything" amendment has been filed that would retain the substance of the bill and:

clarify that assignments of policies from the RPCJUA would begin in May, 1998.

provide for a phase-in of the assigned risk plan, such that assignments in 1998 would equal one-fourth of the 1997 shortfall, assignments in 1999 would equal one-third of the 1998 shortfall, assignments in 2000 would equal one-half of the 1999 shortfall, and subsequent assignments would equal 100% of the prior year's shortfall.

require that insurers issue policies to assigned risks at approved rates and on substantially similar terms as the insurer uses for voluntary risks, and require that the insurer guarantee at least 4 years of coverage (the initial term plus 3 renewals) to the assigned risks.

suspend operation of the assigned risk plan during any year in which the policy count of the RPCJUA drops below 250,000.

add new authority for depopulation to the RPCJUA law. When the policy count of the RPCJUA exceeds 249,000, the RPCJUA would be required to make packages of take-out policies available to all insurers; if the policy count a year later still exceeded 249,000, the RPCJUA would be allowed to offer to one or more insurers on a competitive bid basis the opportunity to take RPCJUA policies with the RPCJUA retaining liability as a reinsurer. It is not clear whether the RPCJUA would receive premium from the take-out company to support its reinsurance obligations. These provisions would supersede other statutory provisions relating to RPCJUA take-out plans.

VII. SIGNATURES:

COMMITTEE ON FINANCIAL SERVICES:

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