

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 Commerce and Tourism

BILL: CS/SB 940

INTRODUCER: Banking and Insurance Committee and Senator Bradley

SUBJECT: Title Insurance

DATE: January 22, 2016

REVISED: _____

	ANALYST	STAFF DIRECTOR	REFERENCE	ACTION
1.	<u>Billmeier</u>	<u>Knudson</u>	<u>BI</u>	<u>Fav/CS</u>
2.	<u>Little</u>	<u>McKay</u>	<u>CM</u>	<u>Pre-meeting</u>
3.	_____	_____	<u>FP</u>	_____

Please see Section IX. for Additional Information:

COMMITTEE SUBSTITUTE - Substantial Changes

I. Summary:

CS/SB 940 changes the unearned premium reserve requirement for title insurers that are members of an insurance holding company system having \$1 billion or more in surplus as to policyholders. However, such title insurers must have a financial strength rating of “superior,” “excellent,” “exceptional,” or an equivalent rating by a rating agency acceptable to the Office of Insurance Regulation. Such insurers must also have a reserve of a minimum of 6.5 percent of the total of (1) direct premiums written and (2) premiums for reinsurance assumed, with certain adjustments. Currently, only title insurers with a surplus of \$50 million or more as to policyholders can use that formula to calculate required unearned premium reserve.

The bill removes the requirement that a title insurer that transfers its domicile to Florida release its unearned premium under the laws of its previous domicile state. The bill requires the title insurer to release the unearned premium reserve over 20 years at a rate not to exceed the following formula:

- 35 percent of the initial sum during the year following the year the premium was written or assumed;
- 15 percent during each year of the next succeeding 2 years;
- 10 percent during the next succeeding year;
- 3 percent during each of the next succeeding 3 years;
- 2 percent during each of the next succeeding 3 years; and
- 1 percent during each of the next succeeding 10 years.

II. Present Situation:

Title insurance is (1) insurance of owners of real property or others having an interest in real property or contractual interest derived therefrom, or liens or encumbrances on real property, against loss by encumbrance, or defective titles, or invalidity, or adverse claim to title; or (2) insurance of owners and secured parties of the existence, attachment, perfection, and priority of security interests in personal property under the Uniform Commercial Code.¹ Title insurance serves to indemnify the insured against financial loss caused by defects in the title arising out of events that occurred before the date of the policy.²

Title insurance agents and agencies are licensed and regulated by the Department of Financial Services (DFS), while title insurance companies are licensed and regulated by the Office of Insurance Regulation (OIR).

Title Insurance Reserve Requirements

Insurance companies must maintain cash or liquid assets on hand to pay claims and satisfy other liabilities. These are called reserves. A title insurer must maintain two types of reserves. First, a title insurer must maintain reserves sufficient to pay all of its unpaid losses.³ In addition, a title insurer must maintain a guaranty fund or unearned premium reserve to be used for reinsurance in the event the insurer becomes insolvent.⁴

Since 2014,⁵ Florida has implemented different unearned premium reserve requirements depending on whether a title insurer has \$50 million or more in surplus.⁶ For title insurers with less than \$50 million in surplus, the unearned premium reserve must consist of at least the sum of:

- A reserve with respect to unearned premiums for policies written or title liability assumed in reinsurance before July 1, 1999, equal to the reserve established on June 30, 1999, for those unearned premiums. For domestic title insurers, such amounts shall be calculated in accordance with provisions of law of this state in effect at the time the associated premiums were written or assumed and as amended prior to July 1, 1999.⁷
- A total amount equal to 30 cents for each \$1,000 of net retained liability⁸ for policies written or title liability assumed in reinsurance on or after July 1, 1999.⁹
- An additional amount, if deemed necessary by a qualified actuary.¹⁰

¹ See s. 624.608, F.S.

² See *Lawyers Title Insurance Co. Inc. v. Novastar Mortgage, Inc.*, 862 So.2d 793, 797 (Fla. 4th DCA 2003).

³ See ss. 625.041, 625.111, F.S.

⁴ See s. 625.111, F.S.

⁵ The reserve requirements were changed by 2014-132, L.O.F.

⁶ The capital and surplus of an insurance company are sometimes referred to as surplus as regards to policyholders or policyholders' surplus. Policyholders' surplus is equal to net admitted assets, or admitted assets minus liabilities. See s. 627.778(2), F.S.

⁷ See s. 625.111(1)(a), F.S.

⁸ "Net retained liability" means the "total liability retained by a title insurer for a single risk, after taking into account the deduction for ceded liability, if any." s. 625.111(6)(b), F.S.

⁹ See s. 625.111(1)(b), F.S.

¹⁰ See s. 625.111(1)(d), F.S.

For title insurance with \$50 million or more in surplus, the unearned premium reserve must be the sum of:

- A minimum of 6.5 percent of the total of (1) direct premiums written and (2) premiums for reinsurance assumed, plus other income, less premiums for reinsurance ceded as displayed in Schedule P of the title insurer's most recent annual statement filed with the OIR.¹¹
- An additional amount, if deemed necessary by a qualified actuary.¹²

According to the OIR, the changes to the reserve requirements made Florida “a more attractive place for title companies.” A large title company moved to Florida after the change in reserve requirements.¹³

Releasing Unearned Premium Reserve

Section 625.111, F.S., sets the following schedule for release of reserves. Once the reserve money is released, it is available for use by the title insurer. For policies written before July 1, 1999, an insurer must release:

- 30 percent of the initial aggregate sum during 1999;
- 15 percent during calendar year 2000;
- 10 percent during each of calendar years 2001 and 2002;
- 5 percent during each of calendar years 2003 and 2004;
- 3 percent during each of calendar years 2005 and 2006;
- 2 percent during each of calendar years 2007-2013; and
- 1 percent during each of calendar years 2014-2018.¹⁴

For policies written on or after July 1, 1999, an insurer must release:

- 30 percent of the initial sum during calendar year next succeeding the year the premium was written
- 15 percent during the next succeeding year;
- 10 percent during each of the next succeeding 2 years;
- 5 percent during each of the next succeeding 2 years;
- 3 percent during each of the next succeeding 2 years;
- 2 percent during each of the next succeeding 7 years; and
- 1 percent during each of the next succeeding 5 years.¹⁵

For companies with more than \$50 million in surplus, the title insurer must release 35 percent of the initial sum during the year following the year the premium was written or assumed, with one quarter of that amount being released on March 31, June 30, September 30, and December 31 of such year.¹⁶ Thereafter, the title insurer must release, on the same quarterly basis:

- 15 percent during each year of the next succeeding 2 years;
- 10 percent during the next succeeding year;

¹¹ See s. 625.111(1)(c), F.S.

¹² See s. 625.111(1)(d), F.S.

¹³ See <http://www.floir.com/pressreleases/viewmediarelease.aspx?id=2086> (last accessed January 18, 2016).

¹⁴ See s. 625.111(2)(a), F.S.

¹⁵ See s. 625.111(2)(b), F.S.

¹⁶ See s. 625.111(2)(c), F.S.

- 3 percent during each of the next succeeding 3 years;
- 2 percent during each of the next succeeding 3 years; and
- 1 percent during each of the next succeeding 10 years.¹⁷

Reserve Requirement When a Title Insurer Moves to Florida

A title insurer organized under the laws of another state that transfers its domicile to Florida has the same unearned premium reserve requirement as set by the laws of the title insurer's former state of domicile. The reserve is released according to the requirements of law in effect in the former state at the time of domicile. For business written after January 1, 2014, the title insurer must add to and set aside in the statutory or unearned premium reserve the appropriate amount as determined by the company's surplus.¹⁸

Rating Agencies

Rating agencies issue financial strength ratings for insurance companies. The opinions of rating agencies such as Standard & Poor's, Moody's Investors Service, Fitch Ratings, A.M. Best Company, and Demotech may be used in some instances by the OIR.¹⁹ These ratings are an attempt by the rating agencies to judge whether an insurance company can survive an economic downturn or meet policy obligations.²⁰ The A.M. Best Company ratings range from "A+" to "D."²¹ A rating of A- or higher by A.M. Best Company is considered "superior" or "excellent" under that company's rating system.²² An "A" rating by Demotech is considered "exceptional" under the Demotech rating system. The OIR is not involved in the rating of insurance companies by outside entities.

III. Effect of Proposed Changes:

This bill allows title insurers that are members of an insurance holding company system having \$1 billion or more in surplus as to policyholders and a "superior," "excellent," "exceptional," or equivalent financial strength rating, as determined by a rating agency acceptable to the OIR, to set unearned premium reserve in the same manner as companies with \$50 million in surplus. This unearned premium reserve requirement will give smaller insurers access to additional capital if they are members of larger holding companies.

The bill removes the requirement that a title insurer that transfers its domicile to Florida must release its unearned premium under the laws of its previous domicile state. Instead, the bill requires the title insurer to release the unearned premium reserve over 20 years at a rate not to exceed the following formula:

¹⁷ *Id.*

¹⁸ *See* s. 625.111(3), F.S.

¹⁹ *See* s. 624.610(3)(e), F.S.

²⁰ *See* http://www.demotech.com/fsr_definitions.asp and <http://www.ambest.com/ratings/guide.pdf> (last accessed January 18, 2016).

²¹ *Id.*

²² *Id.*

- 35 percent of the initial sum during the year following the year the premium was written or assumed, with one quarter of that amount being released on March 31, June 30, September 30, and December 31 of such year; 15 percent during each year of the next succeeding 2 years;
- 10 percent during the next succeeding year;
- 3 percent during each of the next succeeding 3 years;
- 2 percent during each of the next succeeding 3 years; and
- 1 percent during each of the next succeeding 10 years.

This could result in a quicker release schedule if Florida's release schedule is quicker than other states'. A quicker release of unearned premium reserve could increase a title insurer's surplus above \$50 million and allow it to use different reserve requirements. However, the quicker release of reserve could cause less unearned premium to be available to pay claims if a title insurer transfers its domicile to Florida and subsequently becomes insolvent.²³

This bill takes effect July 1, 2016.

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:

This bill could allow some title insurers to have access to additional capital due to different reserve requirements and more favorable release schedules.

C. Government Sector Impact:

The OIR does not anticipate a fiscal impact on the agency due to this bill.

²³ See Department of Financial Services *SB 940 Bill Analysis* (December 15, 2015)(on file with the Senate Committee on Banking and Insurance).

VI. Technical Deficiencies:

None.

VII. Related Issues:

None.

VIII. Statutes Affected:

This bill substantially amends section 625.111 of the Florida Statutes.

IX. Additional Information:

- A. **Committee Substitute – Statement of Substantial Changes:**
(Summarizing differences between the Committee Substitute and the prior version of the bill.)

CS by Banking and Insurance on January 11, 2016:

The CS allows a title insurer that is a member of an insurance holding company system that has \$1 billion or more in surplus and a superior, excellent, exceptional or equivalent financial strength rating from a rating agency acceptable to the OIR to have different reserve requirements from companies with less than \$50 million in surplus. The original bill only applied to companies with a specified rating by the A.M. Best Company. The CS allows companies to use different rating agencies if the agency is acceptable to the OIR.

- B. **Amendments:**

None.