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 1454

INTRODUCER: Senator Brandes

SUBJECT: Florida Hurricane Catastrophe Fund

DATE: February 19, 2018 REVISED:

	ANALYST	STAFF DIRECTOR	REFERENCE	ACTION
1.	Matiyow	Knudson	BI	**Favorable**
2.			AGG	
3.			AP	

I. Summary:

SB 1454 eliminates the cash build-up factor for the Florida Hurricane Catastrophe Fund (FHCF). The cash build-up factor is collected in addition to premiums paid to the FHCF by policyholders of residential property insurance with coverage for losses from wind. The current cash build-up factor is 25 percent of the FHCF premium.

II. Present Situation:

The Florida Hurricane Catastrophe Fund (FHCF)

The FHCF is a tax-exempt[1] fund created in 1993[2] after Hurricane Andrew[3] as a form of mandatory reinsurance for residential property insurers. The FHCF is administered by the State Board of Administration (SBA)[4] and is a tax-exempt source of reimbursement to property insurers for a selected percentage (45, 75, or 90 percent)[5] of hurricane losses above the insurer's retention (deductible). The FHCF provides insurers an additional source of reinsurance that is less expensive than what is available in the private market, enabling insurers to generally write more residential property insurance in the state than would otherwise be written. Because of the low cost of coverage from the FHCF, the fund acts to lower residential property insurance premiums for consumers.

[1] s. 215.555(1)(f), F.S.
[2] ch. 93-409, L.O.F.
[3] https://www.nhc.noaa.gov/1992andrew.html (last viewed February 17, 2018).
[4] https://www.sbafla.com/fsb/ (last viewed February 17, 2018).
[5] s. 215.555(2)(e), F.S.

FHCF Mandatory Coverage

All insurers admitted to do business in this state writing residential property insurance that includes wind coverage must buy reimbursement coverage (reinsurance) on their residential property exposure through the FHCF. The FHCF is authorized by statute to sell $17 billion of mandatory layer coverage.[6] Each insurer that purchases coverage may receive up to its proportional share of the $17 billion mandatory layer of coverage based upon the insurer's share of the actual premium paid for the contract year, multiplied by the claims paying capacity of the fund. For example, if an insurer paid 10 percent of the total premium paid in a contract-year, then that insurer would be eligible to receive up to 10 percent of the mandatory layer of coverage ($1.7 billion of the $17 billion mandatory layer). Each insurer may select a reimbursement contract wherein the FHCF promises to reimburse the insurer for 45 percent, 75 percent, or 90 percent of covered losses, plus 5 percent of loss adjustment expenses.[7]

Insurers that experience multiple hurricanes causing loss during the contract year may receive reimbursement from the FHCF for losses that exceed the applicable retention. The insurer's full retention is applied to each hurricane causing the two largest losses for that insurer. For each other covered event resulting in losses, the insurer's retention is only one-third of the full retention. To access the FHCF an insurer must have incurred losses above the retention levels calculated and set by statute.[8] When faced with a multi-storm season, insurers must reach their full retention levels on the two largest storms of the season. The retention level is then reduced to one-third the normal amount for any other storms that season.

FHCF Premiums

The FHCF must charge insurers the actuarially indicated premium[9] for the coverage provided, based on hurricane loss projection models found acceptable by the Florida Commission on Hurricane Loss Projection Methodology.[10] The actuarially indicated premium is an amount that is adequate to pay current and future obligations and expenses of the fund. In practice, each insurer pays the FHCF annual reimbursement premiums that are proportionate to each insurer's share of the FHCF's risk exposure. The cost of FHCF coverage is generally lower than the cost of private reinsurance because the fund is a tax-exempt non-profit corporation and does not charge a risk load as it relates to overhead and operating expenses incurred by other private insurers.[11]

Cash Build-up Factor

The premium charged by the FHCF includes an additional 25 percent cash build-up factor. The Legislature enacted the cash build-up factor in 2009[12] when the cash balance of the fund was

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[6] s. 215.555(4)(c)1., F.S.
[7] s. 215.555(4)(b), F.S.
[8] s. 215.555(2)(e), F.S.
[9] s. 215.555(2)(a), F.S.
[10] https://www.sbafla.com/method/ (last viewed February 17, 2018).
[11] https://www.sbafla.com/fhcf/Portals/FHCF/Content/Reports/Annual/20170606_FHCF_2016_AnnualReport_A.pdf?ver=2017-07-06-085215-943 (last viewed February 17, 2018).
[12] ch. 2009-87, L.O.F.

approximately $4.564 billion[13] and, due to optional layer options available at that time, the single season obligations of the FHCF was around $28 billion. The factor was phased in over a 5-year period beginning with 5 percent in the 2009-2010 contract year and increasing by 5 percent each contact year until capped at the current 25 percent level that it has been at since the 2013-2014 contract year. The cash build-up factor premium for the current (2017-2018) contract year is calculated to be $222,405,534.[14] The following chart details the growth in the FHCF balance in recent years.

Contract Year[15]	**FHCF Balance[16]**	**Maximum FHCF Statutory Obligation[17]**
2009-2010	$4.5 billion	$27.8 billion
2010-2011	$5.9 billion	$23.1 billion
2011-2012	$7.2 billion	$18.8 billion
2012-2013	$8.5 billion	$18.4 billion
2013-2014	$9.8 billion	$17.0 billion
2014-2015	$11.0 billion	$17.0 billion
2015-2016	$12.7 billion	$17.0 billion
2016-2017	$13.8 billion	$17.0 billion

The FHCF balance as of December 31, 2017, was $14.9 billion. When taking into account expected 2018 premiums that include the cash build up factor, minus approximately $2 billion in projected claims payments for losses due to Hurricane Irma in 2017, the projected fund balance on December 31, 2018, is expected to be approximately $14.1 billion.[18]

FHCF Bonding and Assessment Authority

When the moneys in the FHCF are or will be insufficient to cover losses, the law[19] authorizes the FHCF to issue revenue bonds funded by emergency assessments on all lines of insurance except medical malpractice and workers compensation.[20] Emergency assessments may be levied up to 6 percent of premium for losses attributable to any one contract year, and up to 10 percent of premium for aggregate losses from multiple years. The FHCF's broad-based assessment authority is one of the reasons the FHCF was able to obtain an exemption from federal taxation from the Internal Revenue Service as an integral part of state government.[21]

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[13] https://www.sbafla.com/fhcf/Portals/FHCF/Content/Reports/Annual/20100413_SBA_CATF_Annual_Report.pdf?ver=2016-06-08-121914-787 (last viewed February 17, 2018).
[14] https://www.sbafla.com/fhcf/Portals/fhcf/Content/AdvisoryCouncil/2017/20170323_FINAL_2017_RatemakingFormulaReport.pdf (last viewed February 17, 2018).
[15] https://www.sbafla.com/fhcf/Portals/FHCF/Content/Reports/Annual/20170606_FHCF_2016_AnnualReport_A.pdf?ver=2017-07-06-085215-943 (last viewed February 17, 2018).
[16] Totals include the collection of premium including the cash buildup factor and investment income.
[17] https://www.sbafla.com/fhcf/Portals/FHCF/Content/Reports/Annual/20170606_FHCF_2016_AnnualReport_A.pdf?ver=2017-07-06-085215-943 (last viewed February 17, 2018).
[18] Email from FHCF staff on February 19, 2018 (on file with the Committee on Banking and Insurance).
[19] s. 215.555(6), F.S.
[20] s. 215.555(6)(b), F.S.
[21] The U.S. Internal Revenue Service has, by a Private Letter Ruling, authorized the FHCF to issue tax-exempt bonds. The initial ruling was granted on March 27, 1998, for 5 years until June 30, 2003. On May 28, 2008, the Internal Revenue Service issued a private letter ruling holding that the prior exemption, which was to expire on June 30, 2008, could continue to be relied upon on a permanent basis (on file with the Committee on Banking and Insurance).

III. Effect of Proposed Changes:

The bill eliminates the cash build-up factor for the Florida Hurricane Catastrophe Fund. The cash build-up factor premium for the current (2017-2018) contract year is calculated to be $222,405,534. Eliminating the cash build-up factor will reduce the premiums paid by insurers for FHCF coverage.

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:

If the reduction in FHCF premiums paid by insurers is factored into rates, and not used to purchase additional reinsurance, residential property insurance policyholders with coverage for wind will see an average reduction in their overall insurance premium of approximately 2 percent.[22]

C. Government Sector Impact:

None.

VI. Technical Deficiencies:

None.

VII. Related Issues:

The bill is effective upon becoming law, however, the FHCF has already begun executing contracts with insurers for the 2018-2019 hurricane season. Insurers made their purchasing decisions with the inclusion of the cash buildup factor. It is possible had insurers known the cash

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[22] Report by the FHCF "Potential Impact of Changes to the Florida Hurricane Catastrophe Fund Maximum Limit and Cash Build-Up Factor" December 27, 2017 (on file with the Committee on Banking and Insurance).

build up factor was being phased out some might have contracted differently for their FHCF coverages. Application of the bill to the 2019-2020 contact year would resolve this issue.

VIII. Statutes Affected:

This bill substantially amends the following sections of the Florida Statutes: 215.555, 627.062 and 627.351.

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.