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August 9, 2013

The Honorable Jeff Atwater
Chief Financial Officer
Florida Department of Financial Services
The Capitol
Tallahassee, FL 32399-0301

Dear Chief Financial Officer Atwater:

Thank you for your August 7, 2013 letter regarding property insurance rates and reinsurance costs. I appreciate the opportunity to address your concerns. There are several reasons why a significant drop in reinsurance costs has not yet corresponded with a significant drop in property insurance rates.

The Office of Insurance Regulation (Office) has no firm rule on how much reinsurance a company must purchase and is constrained by statute to allow the cost of a purchase that complies with the rating law (a purchase of up to a 1 in 250 year event). The reinsurance needed is a function of how much insurance a company is writing, its exposure to hurricane loss, as well as the availability of other funds such as policyholder surplus, that can be used to pay for potential hurricane losses. An insurance company must evaluate its reinsurance need and purchase accordingly. In a time when reinsurance rates are dropping, an insurance company may choose to purchase more reinsurance. In fact, several Florida property insurance companies are being required by their rating agency to buy more reinsurance than they initially planned to purchase. This is likely to keep rates up and move additional premium and exposure to reinsurers. The additional coverage is added protection to ensure claims are paid in a time of a catastrophic event.

Another issue has to do with timing. There has not been enough time for most insurance companies to reflect any decreases in the reinsurance premiums. Most property reinsurance contracts in Florida have policy periods that run from June 1st to May 31st. Once the insurance company has finalized its reinsurance contracts, the insurance company would then conduct an actuarial review of its loss experience and expenses to determine the appropriate changes that must be made on both a statewide and a territorial level, which can be very time-consuming. Then the insurance company must submit a filing to the Office to reflect these proposed changes. Most insurance companies submit these filing on a "file and use" provision pursuant to the rating law found in Section 627.062, Florida Statutes. The "file and use" provision requires the filing to be submitted at least 90 days prior to its proposed effective date and the proposed change cannot be implemented until the Office approves the filing. Once the insurance company has received approval for the filing, the changes must then be programmed into its system. Florida Statutes requires that an insurance company provide at least 45 days advance written notice of the renewal premium for residential property insurance. Even if the insurance company had the changes pre-

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KEVIN M. McCARTY • COMMISSIONER
200 EAST GAINES STREET • TALLAHASSEE, FLORIDA 32399-0305 • (850) 413-5914 • FAX (850) 488-3334
WEBSITE: WWW.FLOIR.COM • EMAIL: KEVIN.MCCARTY@FLOIR.COM

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programmed into its system, it would be at least 45 days from the date of approval of the filing before the change could be reflected at renewal time to its current policyholders.

While the average reinsurance cost might have decreased this year, not every insurance company will experience a drop in its reinsurance costs. Furthermore, the cost of reinsurance from the Florida Hurricane Catastrophe Fund has actually increased this year. It is important to remember reinsurance costs make up only a portion of the total homeowners premium and a reduction in reinsurance costs does not translate into a one-to-one reduction in premium. For example, in a recent homeowners rate filing, an insurance company received an approximate 19% reduction in reinsurance costs which translated into an indicated 8% reduction in overall premiums.

In addition, many insurance companies have chosen to transition large rate increases over a period of years in order to mitigate the effects on their policyholders, as allowed under Section 627.0629, Florida Statutes. Depending on the size of that residual rate need and current loss experience and expenses, increases in premium may still be warranted despite a decrease in reinsurance costs.

Homeowners insurance companies must make at least one filing to comply with the annual rate filing requirements of Section 627.0645, Florida Statutes. That filing could contain changes to the base rates, a rate certification if the company does not request a rate change with the company actuary's certification that the current rate is actuarially sound and not inadequate, or a request for an exemption due to insufficient premium volume or number of policies. Therefore, companies are expected to make a rate filing within one year from their last filing.

The Office can reject a proposed rate increase if it is not supported in accordance with actuarial standards, or if the proposed rate would violate Florida Statutes or applicable administrative rules adopted as authorized by Florida Statutes. Insurance companies would be expected to reflect any reinsurance costs savings in its rate level indications and the Office has requested in recent filings that insurance companies include the reinsurance costs from the 2013/2014 contracts. Insurance companies that experience a reduction in reinsurance costs could make a full rate filing and reduce rates for policyholders. Insurance companies should do this or certify rates within one calendar year from the last time an annual rate certification or rate filing was made. Some insurers have indicated their intent to reduce rates at least in some territories based on the 2013 reinsurance costs. As stated above, others may purchase more reinsurance rather than reducing rates and the purchase of more reinsurance based on, or up to, a 1 in 250 year event is allowed by the rating law to be included in the premiums.

I agree that it is necessary to provide economic relief to Florida families and the Office will remain vigilant in its review of rate filings in accordance with Florida law to ensure all possibilities for such relief are identified and passed along to consumers.

Sincerely,



Kevin M. McCarty
Commissioner