

# Florida Property Line Reserving in the Post SB 408 Environment

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# Florida Property Line Reserving in the Post SB 408 Environment

This is not the problem in Florida



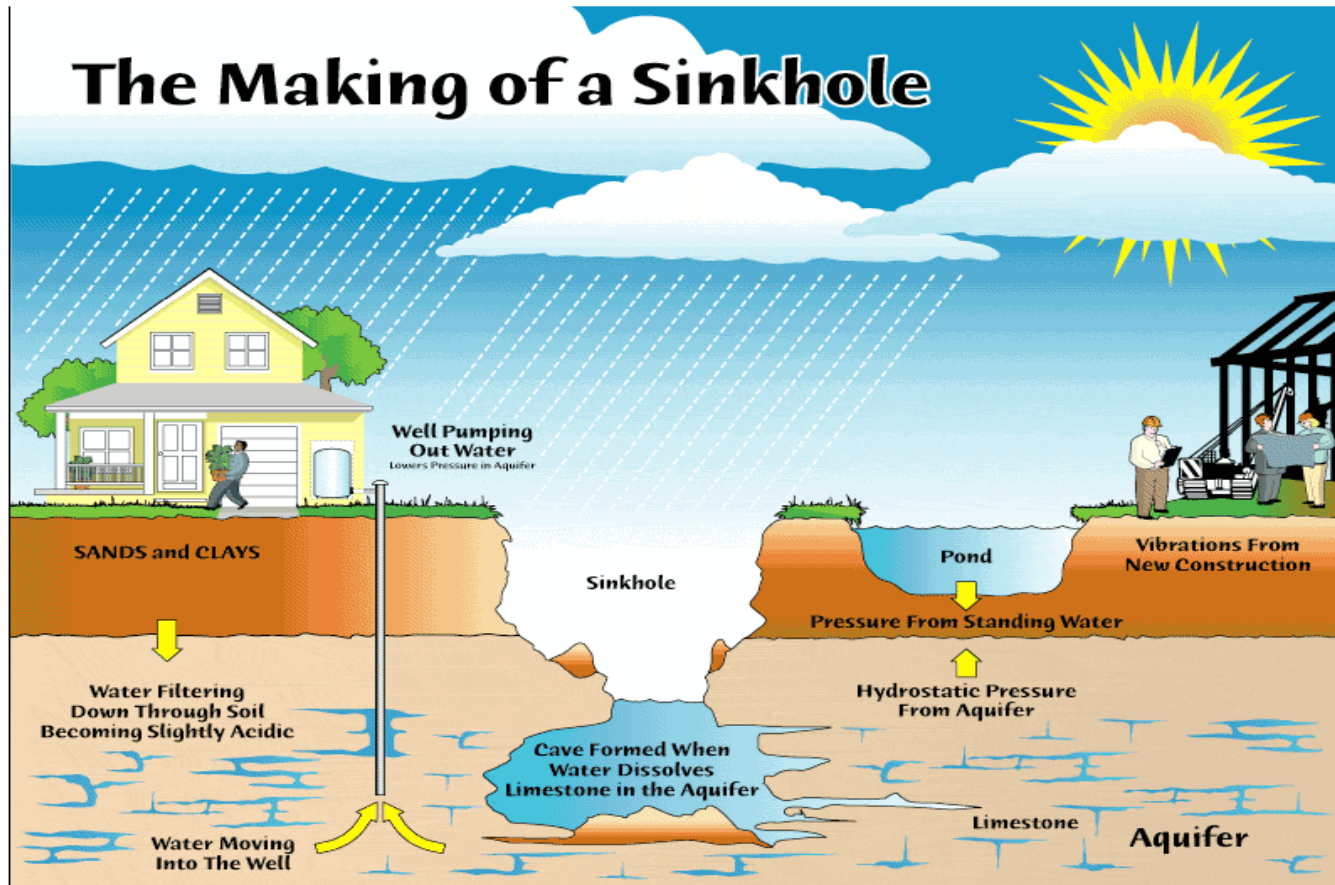
# Definition of Sinkhole Loss

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- “Sinkhole loss” means structural damage to the building, including the foundation, caused by sinkhole activity.
- Historically no definition was provided for structural damage.
- “Sinkhole activity” means settlement or systematic weakening of the earth supporting such property only when such settlement or systematic weakening results from movement or raveling of soils, sediments, or rock materials into subterranean voids created by the effect of water on a limestone or similar rock formation.

*Source: Section 627.706 Florida Statute*

# The Making of a Sinkhole



Source: <http://southeastsinkhole.com/>

# Florida Sinkholes

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- **Sinkholes are a common feature of Florida's landscape.**
- **Nationally, property insurance policies typically exclude coverage for —earth movement.**
- **Since 1981 Florida Insurers have been required to offer Sinkhole coverage for an additional premium.**
  - Losses on any structure as well as personal property contents. Contents coverage shall apply only if there is structural damage to the building caused by sinkhole activity.
  - Coverage includes repairing home, stabilizing the underlying land, and foundation repairs.
- **Insurers must provide coverage for catastrophic ground collapse.**

# Sample pictures of Sinkholes



Source: <http://www.nachi.org/sinkholes.htm>

Source: Senate Sinkhole Report

# Example of Claims-Example A





# Example A Claim



# Example A Claim

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- **Example A shows a home which had cosmetic or minor damages to various parts of the house.**
- **There was no sinkhole activity found to exist by the geologist/engineer.**
- **The policyholder disputed the finding and the insurer sued for breach of contract.**
- **Notwithstanding the finding that no sinkhole activity existed, the insurer paid the policyholder \$28,261.18 for cosmetic damage, to avoid paying the costs of litigation.**

# Example of Claims-Example B



# Example of Claims-Example B



# Example B Claim

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**Example B shows a home with cosmetic or minor damages to various parts of the house.**

**Sinkhole activity was found to exist as the cause of the damage to the house by the geologist/engineer in the testing report and the cost was estimated to be \$26,773.52 to repair the house and \$65,000 for grouting to stabilize the foundation (total cost: \$91,773.52).**

**The policyholder's public adjuster estimated the repair and grouting to cost \$145,000, but the house policy limit was \$138,000.**

**The insurer settled the claim for \$120,000 to avoid paying the costs of litigation.**

# Problems with not settling a claim

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- Lack of a definition for structural damage.
- Establishing whether sinkhole activity has caused structural damage is fraught with problems:
  - whether there actually is sinkhole activity underneath the property.
  - structural damage may be caused by a variety of other factors including shrinking/swelling of clay soils, post construction settlement, erosion, tree roots, decompression/erosion of organic materials, faulty construction, and thermal material expansion/contraction (e.g., cement or stucco cracking).
- Many engineers and geologists opine that sinkhole activity cannot be ruled out as a factor in causing damage to the structure.

# Problems with not settling a claim

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- One way attorney provisions in the law
  - An insurer must pay attorney's fees if it loses in court. If the insurer prevails, its fees are not paid by the losing side.
- Bad Faith Law
  - Allows an insured to bring a civil action against an insurer if the insurer: (1) violates a specified statutory provision; or (2) commits a prohibited act, one of which is not attempting in good faith to settle claims when, under the circumstances, the insurer could and should have done so.

# Bad Faith Issues

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Bad faith related to settlement of insurance claims is determined based on the circumstances of each case rather than on a defined standard that is applicable to all situations or behaviors.

With sinkhole claims, the absence of such a standard may lead to increased litigation.



# Review of 2010 Sinkhole Data Call

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- Florida Office of Insurance Regulation (OIR) released on November 8, 2010 a Review of the 2010 Sinkhole Data Call.
- Between 2006 and 2010, the OIR received 24,671 sinkhole claims with losses amounting to \$1.4 B.
- ***Findings***
  - An increase in the occurrence and costs of sinkhole claims.
  - There is an increase in reported sinkholes in the parts of South Florida where sinkholes traditionally have not been an issue.

# FOIR Report Result 1 – Statewide Results

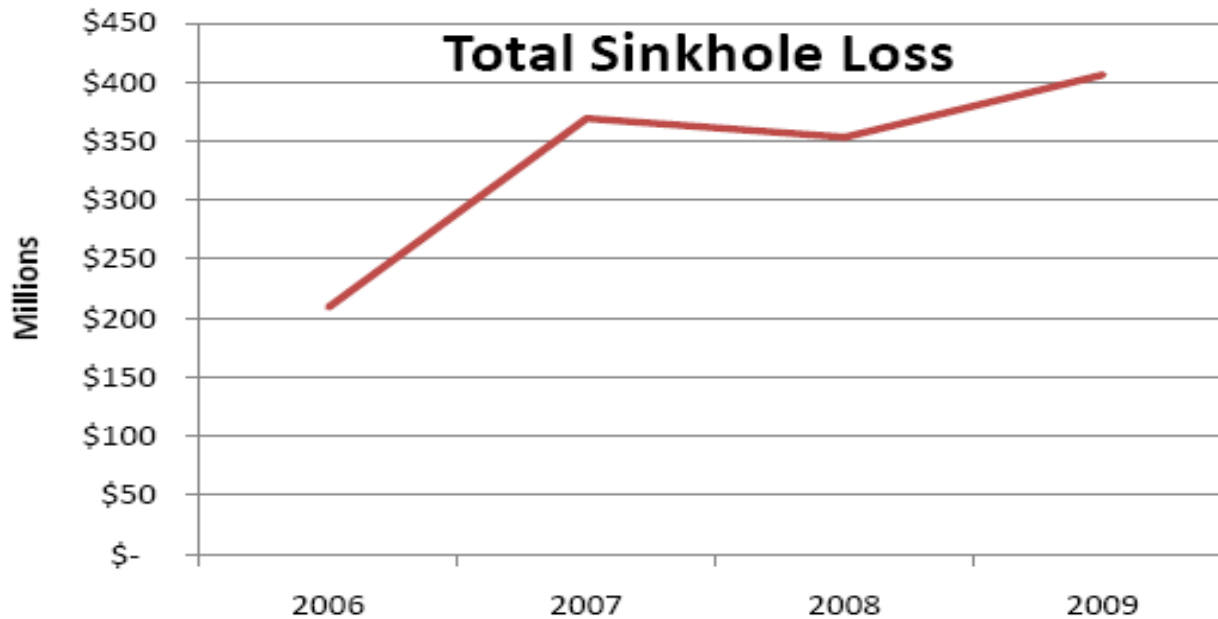
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- Total sinkhole costs (indemnity + expense) increased from \$209 million in 2006 to \$406 million in 2009.
- Total claim count increases from 2,360 in 2006 to 7,245 in 2009
- % share -- Structure Loss (54%), Land Loss (27%) and Engineering Expense (12%).

# FOIR Report Result 1 – Statewide Results

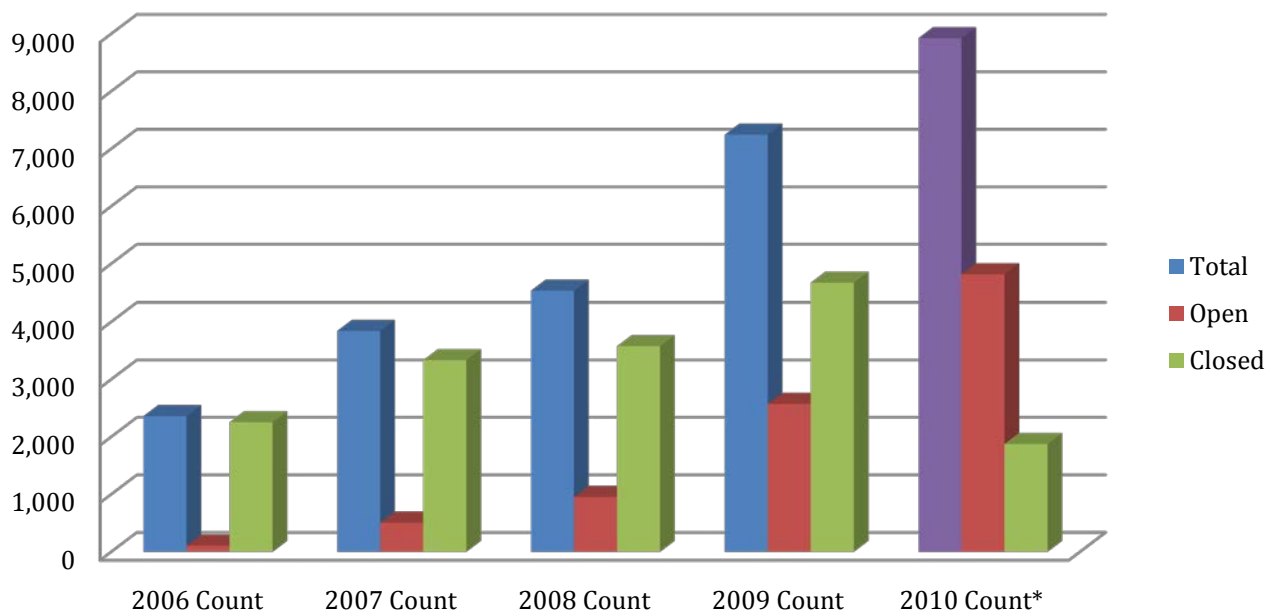
	Closed Claims	Total Expense	Expense Per Claim	Total Indemnity	Indemnity Per Claim
2006	2,254	\$ 28,347,486	\$ 12,577	\$ 163,876,153	\$ 72,705
2007	3,334	\$ 42,190,576	\$ 12,655	\$ 263,003,683	\$ 78,885
2008	3,577	\$ 37,784,992	\$ 10,563	\$ 225,229,165	\$ 62,966
2009	4,671	\$ 41,870,403	\$ 8,964	\$ 220,270,928	\$ 47,157
2010	1,876	\$ 11,779,436	\$ 6,279	\$ 34,767,071	\$ 18,533
<b>Total</b>	<b>15,712</b>	<b>\$ 161,972,893</b>		<b>\$ 907,147,000</b>	
	Open Claims	Total Expense	Expense Per Claim	Total Indemnity	Indemnity Per Claim
2006	106	\$ 3,312,887	\$ 31,254	\$ 13,650,675	\$ 128,780
2007	508	\$ 11,372,170	\$ 22,386	\$ 52,279,347	\$ 102,912
2008	954	\$ 17,862,248	\$ 18,724	\$ 72,474,973	\$ 75,970
2009	2,574	\$ 29,525,972	\$ 11,471	\$ 114,626,167	\$ 44,532
2010	4,817	\$ 21,093,635	\$ 4,379	\$ 49,386,061	\$ 10,252
<b>Total</b>	<b>8,959</b>	<b>\$ 83,166,912</b>		<b>\$ 302,417,223</b>	
<b>Grand Total</b>	<b>24,671</b>	<b>\$ 245,139,805</b>		<b>\$ 1,209,564,223</b>	

# FOIR Report Result 1 - Statewide Results



# FOIR Report Result 1 – Statewide Results

## Annual Sinkhole Claims



*\*For 2010, only about  $\frac{3}{4}$  claims are represented because the data was received in the latter half of 2010. This is the projected value.*

# FOIR Report Result 5 – Regional Level Analysis- Miami-Dade & Broward County increase



Miami-Dade & Broward combined claim count share changes from 2.9% to 4.2% --- this is statistically significant because this area is generally not subject to sinkhole activity.

# FOIR Report Result 2 - Types of Claims

1. Collapse Sinkholes
2. Subsidence Sinkholes
3. Clay Shrinkage

Type of Claim	Closed Claims Reported	Percentage	Average Payment of Closed Claims
Sink Hole (Subsidence)	8,744	56.7%	\$ 140,094
Other	6,288	39.8%	\$ 102,319
Clay Shrinkage	472	2.4%	\$ 124,933
Sink Hole (Catastrophic Ground Cover Collapse)	118	1.1%	\$ 149,491

Average payment per claim are roughly the same for **Collapse** sinkhole and **subsidence** sinkhole.

# FOIR Report Result 4 – Testing Procedures

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- The two major components of the testing procedure were the inspection and the engineering report.
- Total of the two almost tripled in 2009 compared with 2006.
- But the average have been fairly steady.
- Minimum payment for engineering expense over the sample period was \$25, maximum payment was \$93,628.
- Data indicates companies must routinely expend extensive and costly testing procedures to adjust a sinkhole claim.



# FOIR Report Result 4 – Testing Procedures

	Claims Reported	Inspection	Engineering	Total	Per Claim
2006	2,360	\$ 2,335,465	\$ 18,077,444	\$ 20,412,909	\$8,649.54
2007	3,842	\$ 4,429,641	\$ 31,303,561	\$ 35,733,202	\$9,300.68
2008	4,531	\$ 3,745,527	\$ 35,294,972	\$ 39,040,499	\$8,616.31
2009	7,244	\$ 3,770,980	\$ 54,211,121	\$ 57,982,101	\$8,004.16

# Florida Senate Sinkhole Report

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➤ A Florida Senate Interim Report identified that sinkhole claims could threaten the solvency of domestic insurers and have a significant destabilizing effect on an already fragile market.

## Other Findings:

➤ **There** is no geological explanation for such a significant increase in the number of sinkhole claims reported to insurance carriers over the last several years.

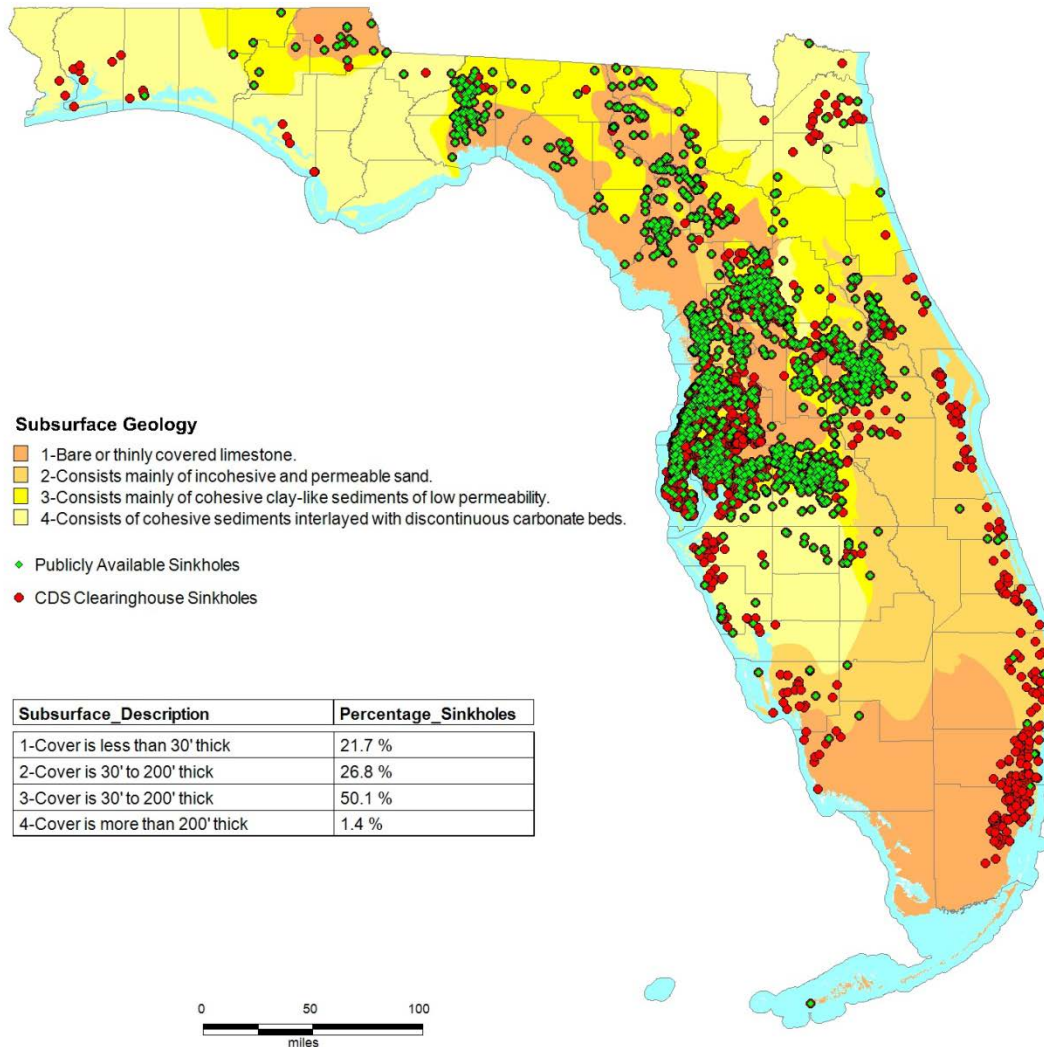
➤ In practice, claims are often paid without a demonstration that the structural damage is caused by sinkhole activity.

# Florida Senate Sinkhole Report

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- Citizens reports that in 2005, only 3% had public adjuster involvement, but by 2009, 25% represented by public adjusters. The number of public adjusters increase 330% between FY 03-04 and FY 08-09, growing from 678 to 2,914; Aggressive advertising and solicitation campaigns used by public adjusting firms.
- Moral hazard on the part of the insured, such as when the insured accepts payment for a sinkhole loss and does not make proper repairs. People are incentivized to file such claims because they can keep the cash proceeds.

# Subsurface Geology and Sinkholes State of Florida



Source: CDS Business Mapping and its RiskMeter Online service

- RiskMeter's sinkhole database and its sinkhole clearinghouse contain more than 12,000 sinkholes information not available from public sources.

# Legislative Intent for SB 408 Related to Sinkholes

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- Declared there is a compelling State interest to maintain a viable and orderly private sector market for property insurance.
- Declared losses associated with sinkhole claims adversely affect the public health, safety and welfare of Florida and its citizens.
- Uses the term “clarify” which will allow insurers to argue some of the changes are retroactive.

# Legislative Intent for SB 408 Related to Sinkholes

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- Reduce the number and cost of sinkhole claims and disputes;
- Increase the reliance on scientific or technical determination related to sinkhole claims;
- Ensure repairs are made in accordance with scientific and technical determinations and insurance claims payments.

# SB 408-Time Limits for Claim and Statute of Limitations

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- Hurricane or windstorm claim must be filed within 3 years from when hurricane makes landfall or date of windstorm. (Covers reopen and supplemental claims)
- Sinkholes must be filed within 2 years after policyholder knew or should have known about sinkhole losses.
- Bill also enacted 5 year statute of limitations for bringing an action for the breach of a property insurance contract that runs from date of loss.

# SB 408-Sinkhole and Catastrophic Ground Cover Collapse Insurance

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- Must provide coverage for a catastrophe ground cover collapse.
- Bill restricts catastrophic ground cover collapse and sinkhole loss coverage to the principal building as defined in policy.
- Allows insurer to require a property inspection prior to issuing sinkhole coverage.
- Clarifies additional living expenses is only available if structural damage to covered building.



# Sinkhole and Catastrophic Ground Cover Collapse Insurance (continued)

- Creates a statutory definition of structural damage. Each is tied to the Florida Building Code.
  - Interior floor displacement or deflection in excess of variance allowed in code. Becomes a safety hazard defined in Code.
  - Foundation displacement or deflection is excess of variances allowed in code.
  - Damage results in listing, leaning, or buckling of exterior load bearing walls in excess of variance in code.
  - Damage that causes any portion of building to be in imminent danger of collapse because of ground movement or instability.
  - Damage that qualifies as substantial structural damage as defined in the Florida Building Code.

# Investigation of Sinkhole Claims

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- Creates a new process for the investigation of a sinkhole claim.
  - Determine if building has incurred structural damage and that;
  - Damage is caused by sinkhole activity
- Initial Inspection and Structural Damage Determination.
- Sinkhole Testing initiated by the insurer.
- Notice to policyholder (no change).
- Authorization to Deny Sinkhole Claim.
- Policyholder Demand for sinkhole testing.

# Payment of Sinkhole Claims

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- Insurer may limit payment to the ACV of the sinkhole loss not including below ground repair until the policyholder enters into a contract for the performance of building stabilization repairs.
- Requires for below ground repairs to commence within 90 days and must follow engineers report. All repairs must be completed within 12 months.
- Repairs must be made according to professional engineer's report and if cannot within policy limits then insurer has option to either complete repairs or tender policy limits.

# Payment of Sinkhole Claims

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- Allows an insurer to non-renew a policy if it has paid policy limits.
- Sinkhole loss payment may not include attorneys' fees or PA fees if insurer pays the claim in compliance with the neutral evaluators recommendations.

# SB 408 Impact on Public Adjusters

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- Bill limits PA fees related to reopen or supplemental claims to a max of 20% of a reopen or supplemental claim.
- Bill limits PA fees to a max of 20% of an insurance claim payment made more than 1 year from date of a state of emergency by the governor.
- PA fees on policy issued by Citizens may not exceed 10% of the additional amount actually paid in excess of amount originally offered by Citizens.
- PA's are prohibited from making deceptive or misleading advertisements or solicitations. New section governs activity of PA's.

# SB 408-Neutral Evaluation of Disputed Sinkhole Claims

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- Does not invalidate an insurance policy's appraisal.
- Can disqualify a neutral evaluator for cause based on professional relationships.
- Requires admission of neutral evaluator's oral testimony and full report in any action or litigation.
- The actions of the insurer in neutral evaluation are not a confession or admission of a liability.
- Deems neutral evaluators as agents of DFS and grants them immunity from suits.

# Florida Senate Bill 408

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- Other Changes Adopted in SB 408

# Surplus Requirements

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- New Insurer surplus requirement is \$15 million (from \$5 million)
- Existing insurers:
  - \$5 million until June 30, 2016;
  - \$10 million July 1, 2016 to June 30, 2021; and
  - after July 1, 2021 surplus of \$15 million



# Insurance Capital Build-Up Incentive Program

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- Allows for renegotiation of terms of a surplus note issued before January 1, 2011.
- If Insurer agrees to accelerate by at least 5 years then company exempt from premium to surplus ratios required by statute.
- If Insurer agrees to accelerate by less than 5 years then OIR may revise premium to surplus ratio requirement subject to minimum of 1 to 1 for net and 3 to 1 for gross.

# SB 408-Replacement Cost Coverage

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- For Dwelling, Insurer must initially pay actual cash value, minus the deductible. Subsequently, insurer must pay any amounts necessary to perform repairs as work is performed.
- For personal property insurer must offer two options:
  - Insurer pays full replacement costs without holdback of depreciation, regardless of whether or not the insured replaces the property.
  - Insurer limits the initial payment to the actual cash value and to receive full replacement the insured must provide receipts for the replaced property. Insurer must provide a credit or discount for this option with clear notice of payment prior to policy being bound.

# Notice of Cancellation

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- Reduced from 180 days to 120 days the notice of cancellation for policies with insurer for at least 5 years.
- Non-renewal of a policy that covers both home and motor vehicle allows for 90 days cancellation notice.
- 45 days cancellation required for a Citizens policy assumed by a “Take-Out” carrier.
- Early cancellation is allowed after 45 days notice if the OIR finds that it is necessary to protect the best interests of the public or policyholders. OIR may base its decision on the financial condition of Company, lack of adequate reinsurance coverage for hurricane risk or other relevant factors.

# Notice of change in Policy Terms

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- Allows insurers to renew a policy under different policy terms by providing a written notice of “Change in Policy Terms” instead of a written “Notice of Non-Renewal”.

# Citizens Property Insurance Corporation

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- Renames the “high risk” account the “coastal” account.
- Citizens may not assess until full Citizens policyholder surcharge has been levied. Also the levied must be collected upon cancellation, termination, or renewal of an existing policy and on new policies issued within 12 months after the surcharge is levied.
- Citizens must get a signed acknowledgement of potential surcharge and that the surcharge could be as high as 45% of premium.

# Citizens Property Insurance Corporation (continued)

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- On policies including coverage for sinkhole must exclude coverage for losses to appurtenant structures, sidewalks, decks, or patios caused by sinkhole activity.
- Citizens is required to hire a consultant to determine cost benefit of outsourcing policy issuance and service functions to private service carriers. Report due July 1, 2012 and implementation plan by January 1, 2013.
- Bill also provided for changes regarding Board governance issues on conflict of interests for Board members.

# Florida Hurricane Catastrophe Fund (Effective June 1, 2011)

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- Requires Cat Fund to provide reimbursement for all incurred losses, including amounts paid as fees on behalf of policyholders.
- Exceptions:
  - Losses for fair rental value, loss of rents or business interruption losses
  - Losses under liability coverage
  - Losses by any other peril other than covered event such as theft, fire, flood, or rising water
  - Voluntary expansion of coverage such as waived deductible
  - HO or Condo loss assessments
  - Bad faith awards
  - Amounts in excess of coverage limit

# What was left out-What needs to be done

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# Florida Homeowners

## *Total Less Catastrophes* **Incurred Losses (000s)**

Accident Year	@15 Months	@27 Months	@39 Months	@51 Months	@63 Months
2005	134,401	150,695	157,789	159,844	160,609
2006	144,880	174,700	182,371	187,001	187,726
2007	338,320	395,109	421,681	430,984	
2008	327,473	380,307	396,704		
2009	273,185	329,580			
2010	399,736				

Citizens Property Insurance Company

# Florida Homeowners

## Total Less Cat Homeowners LDFs

Accident Year	15 to 27 Months	27 to 39 Months	39 to 51 Months	51 to 63 Months
2005	1.1212	1.0471	1.0130	1.0048
2006	1.2058	1.0439	1.0254	1.0039
2007	1.1679	1.0673	1.0221	
2008	1.1613	1.0431		
2009	1.2064			
Selected	1.1725	1.0503	1.0202	1.0043

### Unexpected Loss Development Factors

# Florida Homeowners

## *Non- Catastrophe Wind* Incurred Losses (000s)

Accident Year	@15 Months	@27 Months	@39 Months	@51 Months	@63 Months
2005	7,018	7,137	7,190	7,352	6,664
2006	3,631	4,006	4,321	4,379	4,512
2007	4,714	5,181	5,752	5,663	
2008	4,390	4,875	5,320		
2009	5,026	5,286			
2010	3,433				

# Florida Homeowners

## Non- Catastrophe Wind LDFs

Accident Year	15 to 27 Months	27 to 39 Months	39 to 51 Months	51 to 63 Months
2005	1.0169	1.0075	1.0225	0.9064
2006	1.1033	1.0787	1.0134	1.0304
2007	1.0990	1.1103	.9844	
2008	1.1105	1.0912		
2009	1.0519			
Selected	1.0912	1.0812	1.0180	1.0000

# Florida Homeowners

## *All Other Perils* Incurred Losses

Accident Year	@15 Months	@27 Months	@39 Months	@51 Months	@63 Months
2005	96,835	107,451	111,423	112,257	112,777
2006	106,275	117,244	120,517	122,118	122,608
2007	261,179	285,059	291,041	292,136	
2008	261,854	289,213	293,139		
2009	210,528	233,364			
2010	268,187				

Excludes non-catastrophe wind and sinkhole losses

# Florida Homeowners

## All Other Perils LDFs

Accident Year	15 to 27 Months	27 to 39 Months	39 to 51 Months	51 to 63 Months
2005	1.1096	1.0370	1.0075	1.0046
2006	1.1032	1.0279	1.0133	1.0040
2007	1.0914	1.0210	1.0038	
2008	1.1045	1.0136		
2009	1.1085			
Selected	1.1034	1.0249	1.0082	1.0043

# Florida Homeowners

## *Sinkhole*

### **Incurred Losses (000s)**

Accident Year	@15 Months	@27 Months	@39 Months	@51 Months	@63 Months
2005	30,548	36,107	39,175	40,235	41,169
2006	34,974	53,449	57,533	60,504	60,605
2007	72,427	104,870	124,887	133,184	
2008	61,229	86,218	98,245		
2009	57,632	90,930			
2010	128,117				

Citizens Property Insurance Company

# Florida Homeowners

## Sinkhole Losses as a Percent of Total less Cat Incurred Losses

Accident Year	@15 Months	@27 Months	@39 Months	@51 Months	@63 Months
2005	22.7%	24.0%	24.8%	25.2%	25.6%
2006	24.1%	30.6%	31.5%	32.4%	32.3%
2007	21.4%	26.5%	29.6%	30.9%	
2008	18.7%	22.7%	24.8%		
2009	21.1%	27.1%			
2010	<b>32.1%</b>				



# Florida Homeowners

## Homeowner Sinkhole LDFs

Accident Year	15 to 27 Months	27 to 39 Months	39 to 51 Months	51 to 63 Months
2005	1.1820	1.0850	1.0271	<b>1.0232</b>
2006	1.5282	1.0764	<b>1.0516</b>	1.0017
2007	1.4479	<b>1.1909</b>	1.0664	
2008	1.4081	1.1395		
2009	1.5778			
Selected	1.4905	1.1652	1.0590	1.0124

### Unexpected Loss Development Factors

# Florida Homeowners

## Summary of Loss Development Factors

Accident Year	Total ex Cat Losses	Non- Cat Wind	All Other Perils	Sinkhole Claims	Combined Basis
2005	1.0000	1.0000	1.0000	1.0000	1.0000
2006	1.0000	1.0000	1.0000	1.0000	1.0000
2007	1.0043	1.0000	1.0043	1.0124	1.0067
2008	1.0202	1.1080	1.0082	1.0590	1.0221
2009	1.0503	1.0812	1.0249	<b>1.1652</b>	1.0645
2010	1.1725	1.0912	1.1034	<b>1.4905</b>	1.2274

# Florida Homeowners

## Summary of Ultimate Losses (000s)

Accident Year	Total ex Cat Losses	Non- Cat Wind	All Other Perils	Sinkhole Claims	Combined Basis
2005	160,609	6,664	112,777	41,169	160,610
2006	187,726	4,512	122,608	60,605	187,725
2007	432,837	5,663	293,392	134,835	433,890
2008	406,458	5,895	296,814	105,332	408,041
2009	<b>354,669</b>	6,332	242,173	113,594	<b>362,099</b>
2010	<b>504,369</b>	4,488	307,088	238,554	<b>550,130</b>

## Thank You for Your Attention

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N. Terry Godbold, ACAS, MAAA, FCA

Christopher Carlson, FCAS, MAAA

James Graganella, President Capitol Preferred