STATE OF THE FLORIDA HOMEOWNERS MARKET

The Long-Term View: December 31, 2018

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About Today’s Presenter

• Derek Freihaut, FCAS, MAAA
• Principal and Consulting Actuary
• Bloomington, Illinois
Characteristics: Medical Professional Liability

• Complex coverage
• Protracted claims lifecycle: long-tailed exposure
  – Reporting lags
  – Settlement lags
• Reserve volatility and uncertainty
• High IBNR-to-case ratios especially for current coverage years
• Aggressive plaintiffs’ attorneys
• Previous availability and affordability challenges
• Heavy reliance on reinsurance
• Regulatory hurdles: rate filings
Characteristics: Florida Homeowners

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  - Settlement lags
- Reserve volatility and uncertainty
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 Agenda

• Historical Claim Trends

• Financial Results
  – Balance Sheet
  – Traditional Insurance Risks
  – Profitability

• Questions on Future Profitability
  – Adverse Loss Development
  – Future Loss Cost Trends
  – Impact of AOB Reform

• Rate Activity
Analysis Segmentation
Data

- Loss and defense & cost containment expenses (DCC) combined
- Gross of ceded reinsurance
- Includes all homeowners and dwelling fire policy forms
- Excludes
  - Commercial business
  - Claims closed without payment (loss or DCC) – CNPs
    - Impact ability to recognize loss drivers
    - Ratio of CNPs to reported claims have changed
  - Catastrophe claims (except where noted)
  - Sinkhole claims (except where noted)
Considerations

• No geographic bifurcation – Tri-Counties area vs. remainder
• Aggregated by accident year – not closure year
  – Includes provision for unreported claims
  – Includes provision for incurred but not reported (IBNR) reserves
  – Improves determination of underlying trends
  – May conceal shifts in reporting and settlement lags
• Representative cross section of Florida experience
  – Mix of large and small carriers with various geographic concentrations
  – Relative trends and directional changes more important than absolute indications
Considerations

• Wind/hail/lightning claims proxy for AOB roofing claims
  – Indications also impacted by increase in weather events
  – Long-term and short-term trends can be misleading
Historical Claim Trends
Insurers commenced aggressive defense stance, implemented restrictive policy language, and offered buyback coverage.
Loss Cost: By Cause of Loss (ex-Catastrophes)

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Florida Senate Bill 408 passed on 2/22/2011.
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What is AOB?

• AOB is not a type of claim, rather a mechanism with which to report and address claims.
• AOB allows the insured to permit outside parties, such as contractors, to request payment from their insurance companies on their behalf.
• AOB’s goal is to streamline the claims process for homeowners and create a better overall customer experience.
• However, some contractors with an AOB in hand have made claims for much higher values than expected.
• Attorneys associated with AOB claims have also increased costs through more claims going to litigation.
• Studies by the OIR and by Citizens have shown a large disparity in claims based on whether or not an AOB is involved. This along with tremendous growth in claims using AOB have led to higher losses and higher rates.
• Upon the AOB, the assignee takes on rights of insured
• Under Florida’s prior one-way attorney fee statute, policyholders suing their insurer over a claim dispute could recover their attorney’s fees if the insurer is shown to have underpaid the claim, by any amount.
• Insurance Commissioner David Altmaier:
  – “We believe that the major incentive to the abuse that we have seen over the past few years is the one-way attorney fee statute,” Altmaier told a Senate committee in early April of 2017. “We are concerned that any reform that doesn’t meaningfully address the one-way attorney fee statute will fall very short of being effective.”
Assignment of Benefits: Water Damage
Water Damage: Loss Cost

Accident Year

Ultimate Loss Cost

$0

$50

$100

$150

$200

$250

$300

$350

$400


Accident Year

Ultimate Loss Cost
Water Damage: Loss Cost

Accident Year

Ultimate Loss Cost
Exponential Fit (Trend = 8.8%)
Water Damage: Loss Cost

Accident Year

Ultimate Loss Cost
Exponential Fit (Trend = 8.8%)
Exponential Fit (Trend = 7.3%)


$0 $50 $100 $150 $200 $250 $300 $350 $400


Accident Year

Ultimate Loss Cost
Exponential Fit (Trend = 8.8%)
Exponential Fit (Trend = 7.3%)
Water Damage: Severity

Accident Year

Ultimate Severity

Water Damage: Severity

![Graph showing the increase in water damage severity over time with exponential fits for trends of 4.6% and 6.1%.]
Water Damage: Frequency

![Graph showing the frequency of water damage over the years from 2007 to 2018. The frequency increases gradually from 0.0% in 2007 to around 2.5% in 2018. The graph includes an orange line indicating the ultimate frequency over the years.](image-url)

Accident Year

Ultimate Frequency
Water Damage: Frequency

Accident Year

Ultimate Frequency

Exponential Fit (Trend = 4.3%)
Water Damage: Frequency

- 0.0%
- 0.5%
- 1.0%
- 1.5%
- 2.0%
- 2.5%

2007 to 2018 Accident Year

Ultimate Frequency

Exponential Fit (Trend = 4.3%)

Pinnacle Actuarial Resources, Inc.
By-Segment Comparison
By-Segment Comparison: Frequency/Claim Distr.
Aggregate Non-CAT: Loss Cost

Accident Year

Ultimate Loss Cost

Exponential Fit (Trend = 8.6%)

Exponential Fit (Trend = 5.8%)
Aggregate Non-CAT Non-Sinkhole: Loss Cost

Accident Year

Ultimate Loss Cost
Exponential Fit (Trend = 9.4%)
Exponential Fit (Trend = 5.8%)
Financial Results
Balance Sheet

• Calendar years 2009 through 2018
• Presented for a sample of Florida-domiciled homeowners insurance companies
  – Majority of premium associated with FL HMP annual statement line
  – Generally, more than 10 years of experience for the group
Surplus

Calendar Year Ending 12/31/XXXX

Amounts in $Billions

2009 $0.82
2010 $0.82
2011 $0.88
2012 $1.02
2013 $1.28
2014 $1.64
2015 $1.83
2016 $1.89
2017 $1.86
2018 $1.88
Surplus: Relative to 2009

Calendar Year Ending 12/31/XXXX
Change in Surplus

2012 - 2014: $955.8M

2016 - 2018: $48.1M
Traditional Insurance Risks

- Reserve Risk
- Pricing Risk
- Investment Risk
- Reinsurance Risk
Net Reserves to Surplus

Calendar Year Ending 12/31/XXXX

Note: Reserves include indemnity and all LAE.
Assets by Class

Calendar Year Ending 12/31/XXXX

Amounts in $Billions

Note: Totals tie to cash and invested assets, subtotals line in annual statement.
Assets by Class

Calendar Year Ending 12/31/XXXX

Bonds
Equities
Cash & Short Term
Other

Legend:
- Bonds
- Equities
- Cash & Short Term
- Other
Gross Written Premium by Component

Calendar Year Ending 12/31/XXXX

Amounts in $Billions

<table>
<thead>
<tr>
<th>Year</th>
<th>Net</th>
<th>Ceded</th>
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<tbody>
<tr>
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<td>$1.00</td>
<td>$2.00</td>
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<tr>
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<td>$2.00</td>
<td>$1.00</td>
</tr>
<tr>
<td>2012</td>
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</tr>
<tr>
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<td>$3.00</td>
<td>$0.00</td>
</tr>
<tr>
<td>2014</td>
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</tr>
<tr>
<td>2018</td>
<td>$5.50</td>
<td>$0.00</td>
</tr>
</tbody>
</table>
Gross Written Premium: Relative to 2009

Calendar Year Ending 12/31/XXXX

Net Ceded Gross
On a calendar year basis, measured by two key ratios:

**Combined Ratio =** \( \frac{\text{Losses} + \text{U/W Expenses} + \text{PH Dividends}}{\text{Premium}} \)

**Operating Ratio =** \( \frac{\text{Losses} + \text{U/W Expenses} + \text{PH Dividends} - \text{Investment Gain}}{\text{Premium}} \)
Calendar Year Net Loss & LAE Ratio

Note: Ratio to net earned premium. Development ratio is calculated assuming that the A&O development is immaterial.
Calendar Year Net Loss & LAE Ratio

Note: Ratio to net earned premium
Underwriting Expense Ratio

Note: Ratio to net written premium

Calendar Year Ending 12/31/XXXX

2009 47.6%
2010 40.9%
2011 40.1%
2012 37.0%
2013 33.0%
2014 32.6%
2015 34.9%
2016 36.3%
2017 34.8%
2018 33.2%
Loss & LAE Ratio + Underwriting Expense Ratio

Calendar Year Ending 12/31/XXXX

- 2009: 119.4%
- 2010: 116.4%
- 2011: 105.1%
- 2012: 95.0%
- 2013: 80.6%
- 2014: 86.8%
- 2015: 104.1%
- 2016: 105.0%
- 2017: 102.9%
- 2018: 102.9%
Combined Ratio

Calendar Year Ending 12/31/XXXX

2009: 119.4%
2010: 116.4%
2011: 105.1%
2012: 95.0%
2013: 80.6%
2014: 79.8%
2015: 86.8%
2016: 104.1%
2017: 105.0%
2018: 102.9%
Investment Gain

Calendar Year Ending 12/31/XXXX

Net Investment Income Earned
Net Realized Capital Gain/Loss

Note: Ratio to net earned premium


Net Investment Income Earned: 2.5% in 2009, 3.0% in 2010, 2.5% in 2011, 2.0% in 2012, 1.5% in 2013, 1.0% in 2014, 0.5% in 2015, 0.0% in 2016, 0.5% in 2017, 1.0% in 2018
Net Realized Capital Gain/Loss: 0.5% in 2009, 1.0% in 2010, 1.5% in 2011, 2.0% in 2012, 2.5% in 2013, 3.0% in 2014, 3.5% in 2015, 4.0% in 2016, 3.5% in 2017, 3.0% in 2018
Investment Gain

Note: Ratio to net earned premium

Calendar Year Ending 12/31/YYYY

2009: 5.4%
2010: 5.8%
2011: 3.6%
2012: 3.3%
2013: 2.2%
2014: 2.6%
2015: 2.9%
2016: 3.3%
2017: 3.9%
2018: 3.5%
Operating Ratio = Combined - Investment Gain

Calendar Year Ending 12/31/XXXX


114.0% 110.6% 101.5% 91.6% 78.4% 77.2% 83.9% 100.8% 101.1% 99.4%
Several Questions Determine Likelihood for Future Profitability

• Will adverse loss development continue to increase?

• How will future loss cost trends affect profitability?

• Will AOB reform be impactful?
Percentage Increases in Net Ultimate Loss & DCC Estimates through 12/31/2018

Calendar Year Ending 12/31/XXXX

One-Year Development Ratio  Two-Year Development Ratio

Note: Includes indemnity and DCC; excludes A&O
IBNR-to-Case Ratio: Current Accident Year

Calendar Year Ending 12/31/XXXX

AY 2013 reserves evaluated at 12/31/2013
AY 2018 reserves evaluated at 12/31/2018

2009 108.7% 2010 124.1% 2011 132.5% 2012 178.4% 2013 196.7% 2014 195.1% 2015 128.7% 2016 129.1% 2017 151.9% 2018 189.8%
IBNR-to-Case Ratio: Prior Accident Years

Calendar Year Ending 12/31/XXXX

AYs 2012 & prior reserves evaluated at 12/31/2013

AYs 2017 & prior reserves evaluated at 12/31/2018

2009: 182.4%
2010: 132.1%
2011: 97.8%
2012: 82.5%
2013: 103.9%
2014: 121.9%
2015: 119.4%
2016: 88.4%
2017: 103.4%
2018: 111.6%
IBNR-to-Case Ratio: Calendar Year

AYs 2013 & prior reserves evaluated at 12/31/2013

AYs 2018 & prior reserves evaluated at 12/31/2018

<table>
<thead>
<tr>
<th>Calendar Year</th>
<th>IBNR-to-Case Ratio</th>
</tr>
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<tbody>
<tr>
<td>2009</td>
<td>126.6%</td>
</tr>
<tr>
<td>2010</td>
<td>127.0%</td>
</tr>
<tr>
<td>2011</td>
<td>114.0%</td>
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<tr>
<td>2012</td>
<td>126.1%</td>
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<td>2013</td>
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<td>2014</td>
<td>161.2%</td>
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<tr>
<td>2015</td>
<td>125.2%</td>
</tr>
<tr>
<td>2016</td>
<td>113.3%</td>
</tr>
<tr>
<td>2017</td>
<td>132.3%</td>
</tr>
<tr>
<td>2018</td>
<td>149.7%</td>
</tr>
</tbody>
</table>
IBNR-to-Case Ratio: Current Accident Year (adj)

Calendar Year Ending 12/31/XXXX

AY 2013 reserves evaluated at 12/31/2013
AY 2018 reserves evaluated at 12/31/2018

Note: Adjusted to remove large anticipated S&S recovery
IBNR-to-Case Ratio: Prior Accident Years (adj)

AYs 2012 & prior reserves evaluated at 12/31/2013

AYs 2017 & prior reserves evaluated at 12/31/2018

Note: Adjusted to remove large anticipated S&S recovery
IBNR-to-Case Ratio: Calendar Year (adjusted)

AYs 2013 & prior reserves evaluated at 12/31/2013

AYs 2018 & prior reserves evaluated at 12/31/2018

Note: Adjusted to remove large anticipated S&S recovery

Calendar Year Ending 12/31/XXXX


109.5% 116.3% 103.1% 116.9% 142.5% 164.0% 135.6% 147.6% 164.0% 178.9%
Several Questions Determine Likelihood for Future Profitability

• Will adverse loss development continue to increase?

• How will future loss cost trends affect profitability?

• Will AOB reform be impactful?
Aggregate Non-CAT Non-Sinkhole: Loss Cost

Accident Year: 2007 to 2018

Ultimate Loss Cost
Exponential Fit (Trend = 9.4%)
Exponential Fit (Trend = 5.8%)

- Ultimate Loss Cost
- Exponential Fit (Trend = 9.4%)
- Exponential Fit (Trend = 5.8%)
Several Questions Determine Likelihood for Future Profitability

• Will adverse loss development continue to increase?

• How will future loss cost trends affect profitability?

• Will AOB reform be impactful?
How Companies Have Addressed AOB Issue

• AOB issues are sometimes compared to problems with fraudulent sinkhole claims
  – Sinkhole problem was addressed from four directions – Pricing, Underwriting, Policy Language, Legislative
  – AOB is not a specific exposure that can be as readily addressed via pricing and underwriting
    • Rates in most affected territories are going up
  – Focus has been on policy language, policyholder education (“Call Citizens First”), and a legislative fix
  – More solutions are being attempted
    • Limits
    • Managed repair programs
AOB Legislative Updates - 2019

- AOB legislation passed in 2019 (HB 7065)
  - Define “assignment agreement” and establish requirements
  - Prohibit certain fees
  - Transfer pre-lawsuit duties under the insurance contract to the assignee
  - Require each insurer to report specified data on claims paid in the prior year under assignment agreements by Jan. 30, 2022, and each year thereafter
  - Allow an insurer to make available a policy prohibiting assignment
  - Revise Florida’s one-way attorney fee statute to incorporate an attorney fee structure in determining the fee amount awarded in suits by an assignee against an insurer
  - Require service providers to give an insurer and the consumer prior written notice of at least 10 business days before filing suit on a claim
Loss Cost: By Cause of Loss (ex-Catastrophes)

Insurers commenced aggressive defense stance, implemented restrictive policy language, and offered buyback coverage.
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Florida Senate Bill 408 passed on 2/22/2011.
...what’s next?
AOB Legislative Updates – 2019 cont.

• Leading AOB lawyer put out video days after legislation passed urging vendors to submit AOB claims before 7/1 effective date of legislation

• Lawmakers added provision to another bill moving attorney fee structure changes to be effective date the bill was signed by the governor (5/24)
Rate Activity
Rate Activity

• Reinsurance costs had been coming down in recent years
• October 2013 letter from CFO Atwater
  – “Why have rates not come down?”
• Through 2015 rates were generally declining
  – Loss trends that had improved began deteriorating
  – Some indications remained negative despite positive loss trends due to decreasing reinsurance costs
  – As reinsurance costs leveled off and water losses drove up loss trends rates have been increasing
• In 2019 reinsurance costs began increasing more materially
  – Reinsurance costs up 10% to 20%
  – Over 20 “Limited Reinsurance/Financial Cost” filings thus far in 2019
• Pressure on insurers to reflect rate impact from AOB legislation
  – Citizens was required to reflect the AOB legislation in rate filing
    • Citizens showed a material impact due to legislation but has a large concentration of business in South Florida where AOB claims were more prevalent
  – Other insurers not required by legislation to explicitly reflect HB 7065 in rate filings
All Perils: Approved Change by Effective Date

Graph showing the percentage changes from 2014 to 2019.
All Other Perils: Approved Change by Effective Date
All Other: Loss Trend (retro) by Effective Date
All Other: Loss Trend (pro) by Effective Date

The chart shows the loss trend by effective date for All Other categories. The data points fluctuate significantly from year to year, with some years showing a decrease and others showing an increase. The trend line indicates overall variability, with no clear upward or downward trend over the years 2014 to 2019.
Questions
Join Us for the Next APEX Webinar

Thursday, December 19  
2:00 p.m. ET  
Registration is Open  

Three Perspectives on Peer Review
Final Notes

• We’d like your feedback and suggestions
  • Please complete our survey

• For copies of this APEX presentation
  • Visit the Resource Knowledge Center at Pinnacleactuaries.com
Thank You for Your Time and Attention

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