



# Demotech, Inc.

## Demotech Rated Florida Carriers Evolve to Maintain FSRs of A or Better

**Columbus, Ohio, April 2, 2020** – Florida focused carriers, including Citizens Property Insurance Corporation, dominate residential property insurance market share in Florida. Of these, at year-end 2019, Demotech reviewed and rated forty-six of them. As the first to review and rate independent, regional and specialty insurers in 1989, this is not surprising. In 1996, the then Department of Insurance (DOI), Government and Industry Relations Division, asked us to review and rate carriers that would depopulate the Florida Residential Property Casualty Joint Underwriting Authority.

This request was a consequence of a number of insurer insolvencies caused by the damage Hurricane Andrew inflicted on a marketplace that bought too little reinsurance. When the legacy rating agencies were unable or unwilling to assist Floridians, Demotech's team of experienced, credentialed analysts stepped up to fill the void and assist the DOI, legislature, and investors reinvigorate the residential property insurance marketplace. Today, our leadership includes an evaluation of most of the carriers that comprise Florida's residential property insurance landscape.

Although company-focused financial metrics are critical to any review and analysis process, jurisdictional risk and the relative competitive position of an insurer are among other factors explicitly and implicitly utilized to assign a Financial Stability Rating® (FSR). No entity operates in a vacuum and the conditions in every market are intrinsic in corporate operating results. Insurance carriers and the ratings assigned to them are no exception to this holistic reality.

To assess views of jurisdictional risk, our review included *Judicial Hellholes*, a publication of the American Tort Reform Association (ATRA). *Judicial Hellholes* named Florida the number 1 Hellhole in the 2017-2018 report. Their rationale included "The Florida Supreme Court's liability-expanding decisions and barely contained contempt for the lawmaking authority of legislators and the governor has repeatedly led to its inclusion in this report."

The 2018-2019 report had Florida ranked as the number 2 Hellhole. The rationale included "The Florida Supreme Court issued a series of liability-expanding opinions that invalidated civil justice reforms, damaging the state's civil justice system. The high court once again showed contempt for the lawmaking authority of the state legislature and its decisions will have a lasting impact on the state's legal climate. The Florida legislature also failed to address blatant lawsuit abuse and fraud, and plaintiffs' lawyers continued with their usual antics."

In 2019, subsequent to reforms enacted in Florida, ATRA's 2019-2020 rankings noted "A former number 1 Judicial Hellhole, Florida took great strides toward improving its legal climate in 2019. Although there is much work to be done, the election of Governor Ron DeSantis (R) has heralded a sea change in Florida's legal landscape, beginning with the appointment of several new Florida Supreme Court justices. This new court is deferential to legislative efforts to stop lawsuit abuse and poised to correct the course set by the prior activist court."



The residential property insurance market in Florida offers myriad facets on relative competitive position. One consideration of its unique competitive landscape is the existence of Citizens Property Insurance Corporation (Citizens). To paraphrase its website, Citizens was created by the Florida Legislature in August 2002 as a not-for-profit, tax-exempt, government entity. Its mission is to provide insurance protection to Florida policyholders who are entitled to but are unable to find property insurance coverage in the private market.

Today, Citizens reports admitted assets, on a statutory insurance accounting basis, exceeding \$9 billion. Citizens' existence influences the property insurance marketplace in Florida, let alone its unique characteristics; i.e., its rules of engagement include the capability to assess policyholders. Despite references as 'a market of last resort,' its rates are competitive with other carriers, and often lower than the level indicated by actuarial analysis. Other jurisdictions typically price a market of last resort relatively high to the market rather than competitive with the market. It seems clear that the characterization of Citizens as a 'market of last resort' is often incorrect.

Other state specific issues influence our analysis process as does the financial stability of carriers focused on a single jurisdiction. Our Company Classification System characterizes insurers as State Specialists when 90% or more of their direct written premium is associated with a single jurisdiction. Exhibit 1 summarizes a few state specific metrics of carriers in the US that operate and compete by focusing on a single jurisdiction. More observations on State Specialists are summarized and available within Exhibit 1.

In addition to qualitative factors influencing ratings, during the recent past insurers focused on Florida endured an onslaught of weather related activity. The following list is applicable:

- 2016 Tropical Storm Colin
- 2016 Hurricane Hermione
- 2016 Tropical Storm Julia
- 2016 Hurricane Matthew
  
- 2017 Tropical Storm Cindy
- 2017 Tropical Storm Emily
- 2017 Hurricane Harvey (rainfall)
- 2017 Hurricane Irma
- 2017 Tropical Storm Phillip
  
- 2018 Tropical Storm Alberto
- 2018 Tropical Storm Gordon
- 2018 Hurricane Florence
- 2018 Hurricane Michael
  
- 2019 Tropical Storm Chantel
- 2019 Hurricane Dorian
- 2019 Tropical Storm Erin
- 2019 Tropical Storm Nestor
- 2019 Tropical Storm Olga



Our view of Florida’s current residential property insurance marketplace is that the numerous financial and market based criteria that affect Florida residential property insurance have never been more difficult for carriers to navigate since we first rated Florida focused carriers in 1996. The marketplace as well as carrier-specific financial metrics drove the need to consider downgrades. A list of issues beyond those referenced above is included as Exhibit 2.

Jurisdictional and weather-related challenges are two obvious issues facing the Sunshine State. A substantial increase in reinsurance costs during 2019, another likely increase in the cost of reinsurance in 2020, plus the cost of the Rapid Cash Buildup Program of the Florida Hurricane Catastrophe Fund are others. As a long-term, informed observer of jurisdictions prone to natural catastrophes, Demotech recognizes that operating losses over the past several years are the reality, in spite of the courageous legislative reforms enacted in 2019.

Our analysis of year-end 2019 financial statements began immediately after our review of September 30, 2019 financial statements, about Thanksgiving of 2019. At that time, although we asked certain insurers to provide projections of their year-end 2019 financials, we asked two questions, implicitly or explicitly, of each Florida focused insurer that we reviewed:

‘Given

1. the lingering impact of the judicial activism of the past
  2. the litany of named weather events
  3. increases in the cost of reinsurance, and
  4. the specter of additional increases in the cost of reinsurance in 2020,
- will you continue to be focused on residential property insurance in Florida?’

‘If so, based upon the conditions in the marketplace and the operating results that will emanate from those conditions, how will you revise your business model, or otherwise position your company, to combat more of those same conditions in the future?’

Carrier responses included documentation of their jurisdictional diversification, voluntary runoff, marketing existing books of business to other carriers, merging affiliates, or securing assistance to answer our questions and avoid a downgrade. The list below includes carriers downgraded, those affirmed due to a pending merger, affiliates impacted by a review of a Florida focused carrier, as well as those re-committed to being a Florida focused State Specialist:

- |                             |   |
|-----------------------------|---|
| 1. Anchor P&C Ins Co        | Assigned an FSR of M                            |
| 2. Anchor Specialty Ins Co  | FSR of A – Acquired by insurer with FSR of A    |
| 3. Omega Ins Co             | FSR of A – Merged into an insurer with FSR of A |
| 4. Tower Hill Select Ins Co | FSR of A – Merged into an insurer with FSR of A |
| 5. Cypress TX Ins Co        | FSR of A – Merged into an insurer with FSR of A |
| 6. Access Home Ins Co       | FSR of A – Merged into an insurer with FSR of A |
| 7. Prepared Ins Co          | FSR of A – Merged into an insurer with FSR of A |



Other carriers aggressively enhanced the capability of their business models to respond to the anticipated continuation of jurisdictional and weather-related challenges, the substantial increase in reinsurance costs during 2019, the likely increase in the cost of reinsurance in 2020, and the cost of the Rapid Cash Buildup Program of the Florida Hurricane Catastrophe Fund. They were:

8. Centauri Specialty Ins Co	FSR of A, Business model enhanced
9. Centauri National Ins Co	FSR of A, Business model enhanced
10. Safepoint Ins Co	FSR of A, Business model enhanced
11. Gulfstream P&C Ins Co	FSR of A, Business model enhanced
12. Avatar P&C Ins Co	FSR of A, Business model enhanced
13. Capitol Preferred Ins Co	FSR of A, Business model enhanced
14. Security First Ins Co	FSR of A, Business model enhanced
15. Tower Hill Signature Ins Co	FSR of A, Business model enhanced
16. Cypress P&C Ins Co	FSR of A, Business model enhanced

The management teams of these carriers have fought the conditions in the most difficult operating jurisdiction in the country to a draw. They have addressed the needs of policyholders, investigated and settled claims, paid their employees, producers, and reinsurers, met with us, negotiated with reinsurers for their 2020 programs, and filed timely financial statements in an orderly manner.

Why not more downgrades? At year-end 2019, our scorecard reads as follows: one downgrade, one acquisition by a carrier with an FSR of A, five mergers into carriers with FSRs of A, and an additional nine enhancements of carrier business models - a total of sixteen substantive responses to the observations we shared with carriers at year-end 2019.

Carriers willing to sustain an FSR at the A level have demonstrated how they will fulfill their commitments to Floridians through a revised or enhanced business model. The insurers took action to enhance their capability to address the needs of homeowners knowing that they operate in the most complicated marketplace in the country.

Although Florida may be a geographical peninsula, it is an island when one considers the impact of previous judicial rulings, private sector reinsurance costs, and the additional cost of what was to be a post-event assessment FHCF. These factors plus the 800-pound gorilla known as Citizens Property Insurance Corporation create the singularity of the residential property insurance market.

Some observers commenting on the Florida market have it wrong. They base their naïve comments on public financial information only, rather than the confidential information that we review on a regular basis. In contrast, we receive and review this information shared in the strictest of confidentiality. Here is a partial list of items requested, received, and reviewed in the past:

- Managing general agency contract and financial statements, when necessary
- Holding company financial statements, when necessary
- Actuarial reports and documents containing appreciably more detail than the actuarial opinion letter, which is a public document
- Independent audits
- Anticipated operating results in the form of pro forma financials in a prescribed format



- Claims adjusting details and reports
- Litigation services
- Asset and investment management contracts
- Disaster recovery plan
- Catastrophe response plans
- Catastrophe modelling output
- A preliminary review of horizontal and vertical reinsurance programs
- A final review of horizontal and vertical reinsurance programs
- Review of rate level indications
- Personal financial statements of key financial supporters.

On-site meetings with key reinsurers located in London or Bermuda supplement company-specific information. We also have held on-site meetings at the Company's location or our own. Our analysis team has education and professionalism to supplement their experience. Barry Koestler, CFA, Chief Ratings Officer, Bob Warren, CPA (Inactive), CPCU, Client Services Manager, Sharon Romano Petrelli, CPCU, AIAF, CCP, ARC, Vice President and co-founder, and myself, an ACAS, MAAA, MBA, possess collectively 150 years of P&C insurance experience, and we review more than publicly available insurance financial statements.

Patrick White, Lighthouse Insurance Corporation, responded by saying: 'Florida-only carriers will need to make significant changes to their business plans, or see meaningful change in the state's judicial and legal environment, to operate profitably in that market.'

Since 1996, Demotech has been part of Florida's solution to its residential property insurance crisis. This high-level history was prepared prior to espousing a suggestion to address the myriad challenges facing Florida focused carriers.

In the mid-1990s, stakeholders had a common interest in recreating an insurance marketplace. As the consensus solution emerged, all stakeholders had been heard, albeit none secured 100% of what they requested. Our independent, third party evaluations resulting in assignment of FSRs have evolved to permit us to address the requirements of the secondary mortgage marketplace, agent's errors and omissions insurers, and premium finance requirements. Demotech assisted the stakeholders in Florida re-vitalize the most complicated, dynamic, catastrophe prone market in the United States. What changed to cause this same jurisdiction to be declared a Hellhole?

From our perspective, two changes are subtle yet pervasive. Over time, an insurance ecosystem designed to mitigate the financial impact of natural disasters was revised on an ad hoc basis. Second, the insurance ecosystem was never designed to address or mitigate man-made disasters such as the judicial precedents created by AOB, Sebo, Johnson, and Joyce.

Part of the solution is returning to a process where all voices are valued and heard. The Federal Association for Insurance Reform (FAIR) lives the perspective that created the marketplace that survived the storms of 2004, 2005, and Irma, Michael and Matthew. FAIR focuses on common language and an understanding of the issues.



FAIR is about balance. Long-term public policy is best when all stakeholders have a place at the table. Demotech agrees with this tenet. Decisions should not be made because one voice is shouting louder than the rest; but rather, better decisions are made by a choir of voices reading and singing one hymn from the same page, in the proper key.

Financial ratings are necessary but not sufficient. Ratings are a scorecard on what has occurred in the past, and whether or not it is likely to continue into the future. You might think of financial operating results as a lagging indicator of the conditions in the marketplace. One should view the aggregate impact of public policy as the proximate cause of conditions in a marketplace.

Recent operating results were adversely impacted by the storms of the past several years, increased reinsurance costs, an extended period of judicial activism, and other factors. The impact of COVID-19 is unknown at this time. Yet, despite all of this, the boards and management teams of dozens of residential property insurers employing tens of thousands of employees, appointing tens of thousands of agents, insuring the property of millions of Floridians have said “Demotech, we will do whatever it takes to be part of Florida’s residential property insurance solution.”

Demotech rated carriers revised their business models, re-evaluated the financial consequences of supporting the most complex, dynamic, catastrophe prone jurisdiction in the world, or otherwise affirmed their willingness to continue to write business in Florida.

Exhibit 1, the supplement on State Specialists, lays to rest the belief that the problem with the Florida residential property insurance marketplace is the number of Florida focused insurers and minimal number of national carriers. From coast to coast, virtually every state is well represented by State Specialists. Furthermore, the State Specialists in Florida have similar financial metrics to the State Specialists in other jurisdictions.

Demotech actively reviews more than 400 insurers countrywide. We work with State Specialists in every jurisdiction. We assure you that jurisdictional diversification, voluntary runoff, marketing existing books of business to other carriers, merging affiliates, or otherwise securing assistance to avoid a downgrade rarely occurs outside of the Sunshine State. The challenges facing Florida focused insurers is the operating environment that has emerged in Florida.

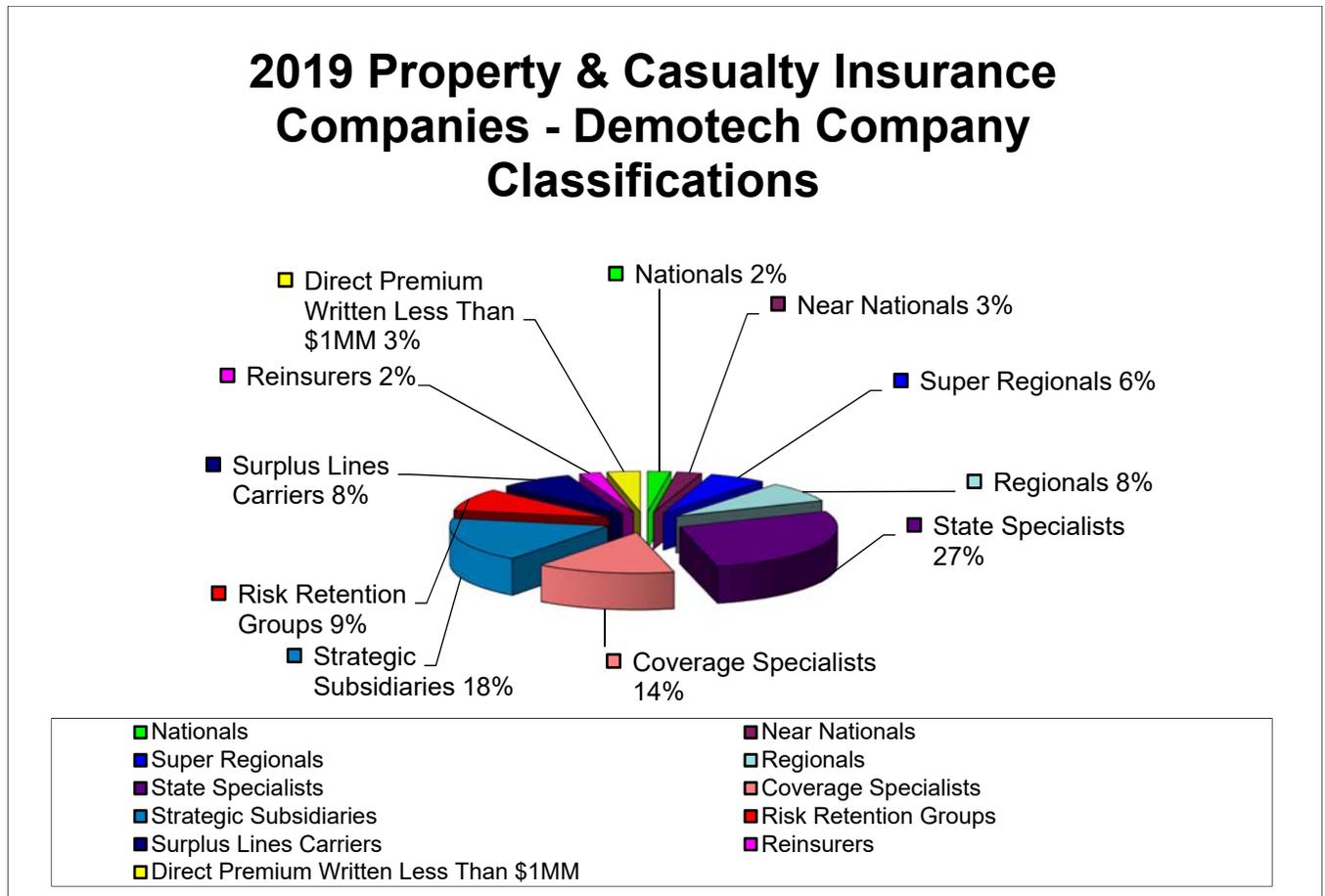
Ayn Rand, the author and philosopher, noted “*The hardest thing to explain is the glaringly evident which everybody has decided not to see.*” From our perspective, the glaringly evident is that conditions in the current residential property insurance market in Florida need to be re-evaluated and, when necessary, re-positioned to focus on the overwhelming majority of Floridians who purchase and procure insurance coverage yet never have a claim. Then and only then will an ecosystem designed to protect Floridians from natural disasters be able to protect Floridians from the rigors of the most complicated, dynamic insurance marketplace in the US.



## Exhibit 1

### Information on State Specialists

In our Company Classification System, a State Specialist is a carrier that writes 90% or more of its direct written premium dollar volume in one state. The 704 State Specialists represent 27.4% of the 2,569 insurers writing P&C insurance and reporting data to the National Association of Insurance Commissioners.



- Exhibit 1A State Specialists Counts by State
- Exhibit 1B State Specialists Aggregate Direct Written Premium by State
- Exhibit 1C State Specialists Average Direct Premium Written by State
- Exhibit 1D State Specialists Average Policyholders' Surplus

Exhibit 1A  
**State Specialists**  
**Counts by State**

State	Number of State Specialists
TX	90
FL	70
NY	66
CA	48
NJ	46
PA	36
MA	30
WI	25
IL	22
MI	22
LA	20
GA	17
AZ	16
HI	13
MN	13
NC	13
OK	11
NM	10
WV	10
VA	9
AL	7
AR	7
ID	7
KS	7
MS	7
MO	7
NV	6
TN	6
IN	5
KY	5
OH	5
CO	4
SD	4
UT	4
AK	3
CT	3
IA	3
ME	3
MD	3
MT	3
ND	3
OR	3
SC	3
DE	2
RI	2
WA	2
DC	1
NE	1
NH	1
VT	0
WY	0
704	

States with more State Specialists than Florida: 1  
States with fewer State Specialists than Florida: 49

Exhibit 1B  
**State Specialists**  
**Aggregate Direct Premium Written by State**

State	Number of State Specialists	Direct Premium Written in State of Specialty (\$000s)
TX	90	20,848,127
CA	48	19,750,033
FL	70	12,123,491
NJ	46	8,129,760
MI	22	5,304,055
MA	30	4,182,929
NY	66	3,395,167
LA	20	1,881,523
GA	17	1,776,544
TN	6	1,634,774
KY	5	1,362,262
NC	13	1,321,966
IN	5	1,057,543
AL	7	903,133
OR	3	813,629
CO	4	729,639
OK	11	679,489
PA	36	619,731
ID	7	615,452
HI	13	601,530
IL	22	572,373
WI	25	565,702
AR	7	564,223
MS	7	542,309
MO	7	533,098
VA	9	461,493
UT	4	407,712
WV	10	397,595
AZ	16	345,374
WA	2	322,925
OH	5	295,319
MD	3	288,130
DE	2	249,383
SC	3	223,929
ND	3	214,232
MT	3	208,734
ME	3	206,493
MN	13	126,815
RI	2	126,694
KS	7	119,715
NM	10	99,858
AK	3	67,682
SD	4	53,393
CT	3	48,281
NV	6	40,525
NE	1	37,819
NH	1	24,189
IA	3	21,115
DC	1	3,218
VT	0	0
WY	0	0
	704	94,899,102

States where State Specialists write more aggregate DPW than Florida State Specialists: 2  
States where State Specialists write less aggregate DPW than Florida State Specialists: 48

Exhibit 1C  
**State Specialists**  
**Average Direct Premium Written per State Specialist**

State	Number of State Specialists	Average Direct Premium Written in State of Specialty (\$000s)
CA	48	411,459
TN	6	272,462
KY	5	272,452
OR	3	271,210
MI	22	241,093
TX	90	231,646
IN	5	211,509
CO	4	182,410
NJ	46	176,734
<b>FL</b>	<b>70</b>	<b>173,193</b>
WA	2	161,463
MA	30	139,431
AL	7	129,019
DE	2	124,691
GA	17	104,503
UT	4	101,928
NC	13	101,690
MD	3	96,043
LA	20	94,076
ID	7	87,922
AR	7	80,603
MS	7	77,473
MO	7	76,157
SC	3	74,643
ND	3	71,411
MT	3	69,578
ME	3	68,831
RI	2	63,347
OK	11	61,772
OH	5	59,064
NY	66	51,442
VA	9	51,277
HI	13	46,272
WV	10	39,760
NE	1	37,819
IL	22	26,017
NH	1	24,189
WI	25	22,628
AK	3	22,561
AZ	16	21,586
PA	36	17,215
KS	7	17,102
CT	3	16,094
SD	4	13,348
NM	10	9,986
MN	13	9,755
IA	3	7,038
NV	6	6,754
DC	1	3,218
VT	0	N/A
WY	0	N/A
	704	134,800

States with higher average DPW per State Specialist than Florida: 9

States with lower average DPW per State Specialist than Florida: 41

## Exhibit 1D

**State Specialists****Average Policyholders' Surplus per State Specialist**

State	Number of State Specialists	Average Policyholders Surplus of a State Specialist (\$000s)
DE	2	2,070,047
OR	3	858,657
CA	48	484,743
TN	6	449,568
MD	3	395,560
KY	5	369,656
CO	4	357,814
UT	4	267,614
AR	7	237,758
NJ	46	208,167
MT	3	185,652
IN	5	178,642
MA	30	158,115
AL	7	154,305
ME	3	150,236
MI	22	149,219
AZ	16	145,686
WA	2	119,030
NC	13	107,638
RI	2	102,306
MO	7	93,181
LA	20	91,947
TX	90	90,990
OK	11	90,706
OH	5	90,473
ID	7	89,351
ND	3	86,353
<b>FL</b>	<b>70</b>	<b>73,176</b>
HI	13	71,242
NY	66	70,560
MS	7	64,223
GA	17	53,462
IL	22	52,938
PA	36	46,066
NV	6	40,628
VA	9	39,652
WI	25	29,975
SC	3	28,000
KS	7	27,298
WV	10	24,959
NM	10	23,618
AK	3	20,009
CT	3	15,739
IA	3	13,396
MN	13	12,016
SD	4	10,465
NE	1	6,052
NH	1	3,703
DC	1	1,670
VT	0	N/A
WY	0	N/A
	704	134,954

States with higher average PHS per State Specialist than Florida: 27

States with lower average PHS per State Specialist than Florida: 23



## Exhibit 2

- Insurer investor capital appears to be exiting rather than entering Florida
- Holding company debt, once infused to support growth, strengthen loss and loss adjustment expense reserves without diminution of surplus, or otherwise support the implementation of business models, is at burdensome levels given the operating results of carriers that had to address the natural disasters of 2016 through 2019.
- Although carriers can “true up” reinsurance costs through filings with the State of Florida Office of Insurance Regulation, the financial impact of paying higher reinsurance costs is short-term and the financial impact of “true up” is long-term. With timing being critical, the timing mismatch adversely impacts carriers, given the other conditions.
- The cumulative impact of carrier acceptance of rate revisions at a percentage change that eliminates the time, effort and expense for a hearing and decision, i.e., less than 15%, has had a cumulative impact over the past several years.
- Demotech requires carriers to book adequate loss and loss adjustment expense reserves. In an operating environment characterized by stability of claims procedures, protocols and practices, unblemished by judicial decisions that revise claim settlement paradigm, this can be in place. However, an AOB decision, Sebo, Johnson, Joyce and other cases revised the claim settlement landscape. Insurers and the actuaries they depend on were on their heels.
- The revised rules of engagement for claims settlement had undue impact due to the natural disasters of 2016, 2017, 2018, and 2019.