THE EVOLUTION OF FLORIDA'S PUBLIC-PRIVATE APPROACH TO PROPERTY INSURANCE

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BEST PRACTICES, BETTER OUTCOMES

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Executive summary

Florida faces a high and growing risk of economic damage from hurricanes and tropical storms. These disasters impose widespread economic costs on households and businesses. They cause substantial property damage that must be repaired, as well as many non-property costs. Insurance is a critical tool to protect residents from such devastating financial losses. These disasters, however, also threaten standard insurance models, making insurance more expensive and, in the extreme, less available.

The cost of property insurance in Florida is among the highest in the country, creating financial burdens for consumers. To address recurring availability and affordability concerns in the private market, Florida has created three state programs to support property insurance markets, all of which are ultimately backed by nearly all state policyholders via policy surcharges ("assessments") that function as post-disaster taxes on a consumer's policy. This includes:

- **Citizens Property Insurance Corporation (Citizens),** a provider of primary insurance,
- **The Florida Hurricane Catastrophe Fund (FHCF)**, a state-backed reinsurance program, and
- **The Florida Insurance Guaranty Association (FIGA)**, which pays the claims of insolvent insurers from the admitted market.

All are at least in part regulated by the Florida Office of Insurance Regulation (OIR), whose Commissioner is appointed jointly by the Governor and Cabinet of statewide elected officials.

Florida's property insurance market has seen several "boom and bust" cycles in the past 30 years. Its homeowners insurance market is anomalous from other places in the U.S. in several ways. There are far fewer national insurers writing policies in the state due to the catastrophic risk. Instead, the Florida market has more regional firms, subsidiaries of national firms that are walled-off from their parent, and a very large share of policies in the public program. Given the policies in Citizens, Florida has a high degree of market concentration. It also sees more insurer churn, with policies backed by less capital on average than in other states.

Florida's market is once again unstable. This is due largely to growing climate risk and continued development in high-risk areas, as well as higher rebuilding costs from recent inflation and supply chain disruptions, all of which has driven up costs for insurers. Insurers have exited the state and those remaining have raised prices commensurate with the higher risk they face. The decline in available and affordable coverage has sent increasing numbers of consumers into Citizens. This program, by its own admission, is not collecting sufficient revenue for the risk.

As noted, when any of the three state programs run deficits, they turn to the bond market to raise the needed cash to pay claims and then repay the debt with assessments on property insurance policies throughout the state. A severe hurricane season could cause massive losses to all three state programs at the same time, but

they manage this risk independently. All three could seek to access the bond market simultaneously, leading to a potential debt clash that could drive down investor interest or drive-up prices or potentially generate claims-paying shortfalls. It could also lead to combined post-storm assessments on policyholders. This situation would make insurance prices even more unaffordable, increasing fiscal stress for the state's households and economy.

Florida will face ongoing policy discussions about the structure of its property insurance market and achieving longer-term stability will require a complementary range of approaches. First, greater investments in risk reduction could attract more insurer capital and stabilize prices. A focus on risk reduction would include investments in protective infrastructure, land use decisions that incorporate consideration of increasing risk, building code upgrades, grants for lower-income households to invest in storm-hardening retrofits, and outreach and education for builders about building standards such as Fortified construction. Second, the information and financial signals to consumers will need to be considered and balanced against affordability challenges. In addition to improved information provision, policymakers and regulators will need to consider the extent of insurance price suppression and subsidization, with consideration of the longer-term consequences and distributional impacts of if or how any subsidies are targeted. Third, a more holistic evaluation of financial risk to the state across the three programs is warranted along with a forward-looking analysis of potential assessment risk to consumers. Finally, the state will face questions about reforming the design of its three state programs in the face of rising risks.

Introduction

Florida faces a high and growing risk of economic damage from hurricanes and tropical storms. Since 2000, Florida has had 36 presidential disaster declarations (not including those related to Covid-19), and in that same time, the National Oceanic and Atmospheric Administration (NOAA) estimates the state experienced 57 "billion-dollar" disasters, with costs from just the last seven years alone exceeding $1 trillion.

Severe storms impose widespread economic costs on households and businesses. These disasters cause substantial property damage that must be repaired, as well as many non-property costs: business interruption and lost income, the need for temporary living or workspaces, the need to clear debris, and adoption of costly coping strategies to deal with a loss in services, such as power or disrupted transportation. Tourism is a key component of Florida's economy, and storms also keep visitors away. For example, Hurricane Irma was estimated to have deterred 1.8 million visitors, with a total economic cost to the state of $2.5 billion.[1] Recovery from severe hurricanes takes many years, and if another storm hits before recovery is complete, the costs can be exponentially worse. In 2004, Floridians were stunned as Hurricanes Frances and Jeanne carved almost identical paths of destruction through the state a mere three weeks apart.

Insurance is a critical tool to protect residents from the devastating financial losses from severe storms. Research has found that households with insurance have fewer unmet needs and financial burdens after hurricanes. In addition, as more households in a community have flood insurance, it has positive spillovers for local economic recovery.[2] Yet disasters also challenge the private insurance sector. These events impose widespread and catastrophic levels of loss that stress risk-pooling mechanisms and require high premiums to support the tremendous capital that must be committed to back their promises. Sometimes premiums can rise beyond what households and businesses are able to pay.

To address recurring availability and affordability concerns in the private market, Florida has created three state programs to support property insurance markets, all of which are ultimately backed by nearly all state policyholders via post-storm policy surcharges ("assessments") that function as taxes on policies:

- Citizens Property Insurance Corporation (Citizens) – A provider of primary insurance.
- Florida Hurricane Catastrophe Fund (FHCF) – A state-backed, mandatory reinsurer for property insurers.
- Florida Insurance Guaranty Association (FIGA) – A state program to discharge claims of insolvent insurers.

Two other institutions regulate aspects of the above programs and all private insurers:

- Florida Office of Insurance Regulation (OIR) – The state agency that enforces, and in some instances, interprets the Florida insurance laws.

- Florida Commission on Hurricane Loss Projection Methodology (Commission) – A body of scientific experts and agency heads that reviews and must accept catastrophe models before they can be employed for calculating residential insurance rates or for regulatory financial analysis.

This report provides an overview of Florida's risk profile and the implications for the private insurance sector, explaining the challenges with insuring disaster risks. It then overviews the private homeowners market, as well as the three state programs, discussing their history and current dynamics. The report ends with a summary of current public policy concerns that will shape the future of Florida's property insurance market.

Florida's risk profile and the challenge for insurance markets

Disaster risk in Florida

Florida, with 1,350 miles of coastline,[i] has the highest coastal storm risk in the country, and over 50% of the insured hurricane risk in the United States. Since 1980, NOAA estimates that Florida has had 32 tropical storms causing more than $1 billion in damages, leading to total costs of between $300 billion and $360 billion. Storm impacts can also be "streaky" — shortly after 10 straight years with no hurricane landfalls, a third of those storms have occurred in the last five years. Major Hurricanes Ian in 2022 and Idalia in 2023 were the most recent and damaging, with Hurricane Ian in 2022 the third-most costly hurricane in the U.S., causing roughly $65 billion in insured losses.[3]

Hurricane and storm risks are projected to continue increasing in Florida as the planet warms. Climate change is projected to increase rates of hurricane intensification,[4,5] increase the frequency of "stalling" the forward movement of storms,[6] and slow down their dispersion after landfall[7] — all of which lead to greater levels of damage. Recent research also indicates that the likelihood of two storms occurring in quick succession has increased and is projected to increase further as warming continues.[8] Sea-level rise will allow storm surge to push farther inland — and Florida accounts for roughly half of the U.S. population exposed to sea-level rise this century.[9]

Florida also has had some of the highest rates of growth in flood-prone areas nationally. Between 2001 and 2019, Florida was the state with the highest number of new residential properties built in the floodplain. In absolute terms, this was 47% of all new floodplain housing nationally, but since most of Florida's developable land is in the floodplain, it is not the highest relative amount of development.[10] Census data indicate a long-term trend of increasing population in the state; indeed, Florida has been a fast-growing state in recent years.[11] While the growth rate in population has slowed from the rates of the 1970s and 1980s, it has remained positive and larger than the

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[i] This estimate is from the U.S. Census (https://www2.census.gov/library/publications/2010/compendia/statab/130ed/tables/11s0360.pdf). NOAA has a detailed mapping of the state including islands, sounds, and bays (https://coast.noaa.gov/data/docs/states/shorelines.pdf) and estimates over 8,000 miles of tidal shoreline.

U.S. average, and Florida is still one of the fastest-growing states in the country. Between 2021 and 2022, the Census estimates the state's population grew by 1.9% and the estimated population as of July, 2023 was 22.6 million. Building permits for new private single housing units have trended upward since the spring of 2009, following their decline between 2006 and 2008, but have roughly stabilized since 2021.[12]

Storms cause far less damage to construction that is built to withstand high winds or floodwaters. The Insurance Institute for Building and Home Safety (IBHS) has developed a comprehensive hurricane building standard, "IBHS Fortified," that dramatically reduces wind losses. Images have shown complete destruction in a neighborhood from a hurricane, with only Fortified homes left standing, as if immune to the storm. Alabama, a leader in Fortified construction, has over 36,000 Fortified homes as of January 2023, despite having a housing stock that is one-quarter the number of Florida's,[ii] while Florida only has 129.

That said, in its most recent ranking in 2021, IBHS ranked Florida as having the strongest building code among Gulf and Atlantic states. Florida's statewide building code is indexed to "wind speed design" contours and "wind-borne debris" regions and does incorporate several elements of Fortified construction. Strong building codes keep residents safer and reduce uninsured losses. Stronger homes have also been found to improve home values.[13,14] Fortified homes also obtain lower insurance prices, often through a flat discount based on loss history and approved by state regulators. While Fortified adds a modest amount to the costs of building, in places with severe weather, it is cost-effective, saving more in future damages than is spent in the upfront costs.

Beyond its building code, the state has begun taking steps to improve resilience to growing flood and storm risks. Much of this has been led by communities, through investments in risk reduction, such as Miami, which has been rewarded for its efforts with lower flood insurance prices through a program within the National Flood Insurance Program. In addition, there are collaborative efforts, such as the Southeast Florida Climate Change Compact, established in 2009, or the Resilient305 initative in Miami-Dade County. Florida's Water Management Districts have also been making significant resilience investments. The state has also recently been taking steps to improve resilience. In 2019, the governor appointed the first Chief Resilience Officer. Other statewide efforts include the Florida Resilient Coastlines program, which offers both grants and technical assistance to evaluate local flooding and erosion risks and the Statewide Flood Vulnerability and Sea Level Rise Assessment to identify the areas of highest risk, the data of which is publicly available for planning purposes. The state also established the Florida Flood Hub at the University of South Florida College of Marine Science to link research and practice around flood risk management. That said, Swiss Re estimates that increased population growth, coupled to growing hurricane risk, has driven up losses in Florida. They note that mitigation efforts are only partially offsetting increases in expected losses — growth and concentration in insured values are dominating trends.[3]

[ii] The housing stock comparison is based on the 2022 U.S. Census Report, but the comparative sizes of the two states' housing stock have been fairly consistent for the past decade. See https://www.census.gov/quickfacts/fact/table/AL,FL/PST045222.

Challenges with insuring catastrophes

Insurance is fundamentally about risk pooling and diversification. When independent risks are assumed together, and individual risks are not too extreme, losses become more predictable, uncertainty is reduced, and the probable maximum loss per unit of risk declines. In this environment, insurance companies may price policies with confidence. The mathematics become less kind when many properties are likely to experience large losses at the same time.

While non-catastrophe property insurance losses, such as kitchen fires and appliance leaks, are stable from year-to-year, disaster-related losses are not. Instead, catastrophe losses may be low for many years and then incredibly high. After Hurricane Andrew in 1992, insurers paid out more in claims than the sum total of the previous 10 years of homeowners premiums.[15] Losses then remained moderate until the multiple-storm years of 2004 and 2005 caused several insurer failures, after which Florida enjoyed a decade of minimal losses.

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Severe losses, particularly multiple events in quick succession, can put insurers out of business. Elevated hurricane activity in recent years has contributed to 10 insolvencies since 2019 in Florida.[16] Insurers know disasters threaten their solvency, so they purchase reinsurance (insurance for insurance companies) up to their estimated probable maximum losses from individual events as well as for their season loss totals and then hold substantial reserves to pay their reinsurance "retentions" in each storm. They might also transfer some risk to the financial markets. These approaches, while necessary, raise costs, which are passed on to the policyholder in rates that are often regulated by state agencies on a "cost-plus" basis. Florida faces some of the highest insurance costs in the nation because both the amount of exposed property, particularly along the coasts, and the annual probability of storms are severe. The state has also struggled with other drivers of higher claims payments, such as inflation in construction costs as well as legal and fraud concerns.

Florida's insurance market: Where are we and how did we get here?

Property owners in the United States must secure coverage for hurricane and storm winds, typically through a standard homeowners policy, and separately purchase insurance for flood damage associated with the storm. Flood insurance has long been provided by a federal program (the National Flood Insurance Program or NFIP), supplemented by a limited private market. Wind coverage is usually provided by the private market, but when that coverage is not available or too expensive, residents in Florida can also turn to Citizens. Whether public or

private, wind or flood, insurers have recently faced growing losses nationally and in Florida, leading to cutbacks in coverage and price hikes that have amplified stress for consumers.

Florida's property insurance market has seen several "boom and bust" cycles in the past 30 years. Hurricane Andrew, in 1992, marked a turning point. Following the devastating storm, insurers began cancelling and non-renewing policies, reducing the number of new policies written, and limiting coverage terms. For instance, the storm ushered in "hurricane deductibles," now common, which place a larger share of hurricane losses on the policyholder. Hurricane Andrew demonstrated that insurers had not sufficiently appreciated the damage potential of major hurricanes or their exposure concentration, leading to shock at the high losses and the discovery of poor adherence to building codes.[17]

Florida again faced challenges in its property insurance market following the hurricane losses of 2004 and 2005. This time, multiple storms in a season rather than the "big one" stressed insurer finances and led to insolvencies and shortages of coverage. The Task Force on Long-Term Solutions for Florida's Hurricane Insurance Market was established, which met and submitted a report for the state.[18] The task force noted that the potential size of economic losses from an extreme hurricane season in Florida exceeds what can be covered by the private market and the public programs. This echoed the findings of a 1993 report that also noted that covering catastrophic hurricane risk in Florida would require a national intervention combined with substantial focus on hazard mitigation. Both of these — a federal role and a greater need to reduce risks — are ongoing policy issues for the state.

In response to previous market turmoil, Florida has created three public-sector institutions to complement its two regulatory bodies. Citizens provides homeowners insurance (on either a multi-peril or wind-only basis) to those unable to affordably find it in the private market. The FHCF is the only state-run hurricane reinsurance program. And as in other states, the guaranty association (FIGA) covers the claims of insolvent insurers. Each of these are discussed in turn after consideration of current dynamics in the private homeowners market.

Homeowners market

Homeowners insurance, which is required by lenders and federal mortgage guarantors, protects policyholders against a range of losses, which typically include burglary, hail, fire, wind, and tornadoes. Coverage for some perils experienced in disasters may be limited. Policies typically exclude flood damage, and may also only cover certain damages, such as sewer back-ups or mold, if policyholders have elected to add that additional coverage. All homeowners insurance policies have a deductible — the amount the policyholder must pay before the insurer pays in a given claim. In Florida, deductibles are usually much higher for hurricanes, though they do apply on a calendar-year rather than per-claim basis.

As of mid-2023, Florida had about 6.4 million homeowners insurance policies (including dwelling fire, mobile home, and tenant and condominium unit owners). After Andrew, many national brand-name insurers began to rethink the Florida market and reduce exposures in Florida and coastal areas more specifically. To preserve their branding and agency relationships, those that stayed created Florida-specific "pup" firms that were walled-off from the parent company — the parent could let the pup go insolvent and limit its Florida losses. In addition, the void in capacity was filled by new companies operating only in Florida (and sometimes a few Southeastern states), referred to as Florida-specialist insurers. These firms tended to be smaller and less diversified, relying heavily on reinsurance. As of June 2023, Florida-specialist insurers represented 54% of the market (up from only 22% in 2004) and Florida-only subsidiaries of national brands represented 15% of the market (down from 35% in 2004). The state program, Citizens, covered 16% of the market.

Florida's market is also anomalous from other states by other metrics. Given the large number of policies in Citizens, Florida has a high degree of market concentration compared to other states, even coastal states. It also sees more insurer "churn" — many insurers operating in Florida fail to build substantial market share.[14] The Florida insurance market is also capitalized less robustly than any other state, with the lowest level of policyholder surplus.[19]

Undercapitalization may be a growing problem. Homeowners insurers establish loss reserves to cover claims. These are estimates of the cost and must be re-evaluated as claims are actually paid. In recent years, Florida loss reserve estimates have consistently been substantially too low. In 2022, claims (inclusive of storm claims) were $224 million more than originally estimated, and two years afterward were $772 million more than originally estimated.[20]

Demotech, Inc. has been the primary ratings agency for Florida-specialist homeowners insurers. The agency has required that insurers have reinsurance protection to cover a single hurricane estimated (by credible catastrophe models) as a one-in-130-year event, as well as two hurricanes in one year, with the first at the one-in-100-year probability of occurrence interval and the second at a one-in-50-year interval.[iii] Research has found, however, that Demotech ratings are much higher than would be given by other traditional rating companies for the same firms and that firms rated by Demotech, likely because they have focused on the niche of rating smaller companies in high-risk states, tend to have riskier liabilities, operate in higher risk areas, be under-diversified, smaller in size, have concentrated reinsurance relationships, and have higher leverage and lower risk based capital ratios.[21]

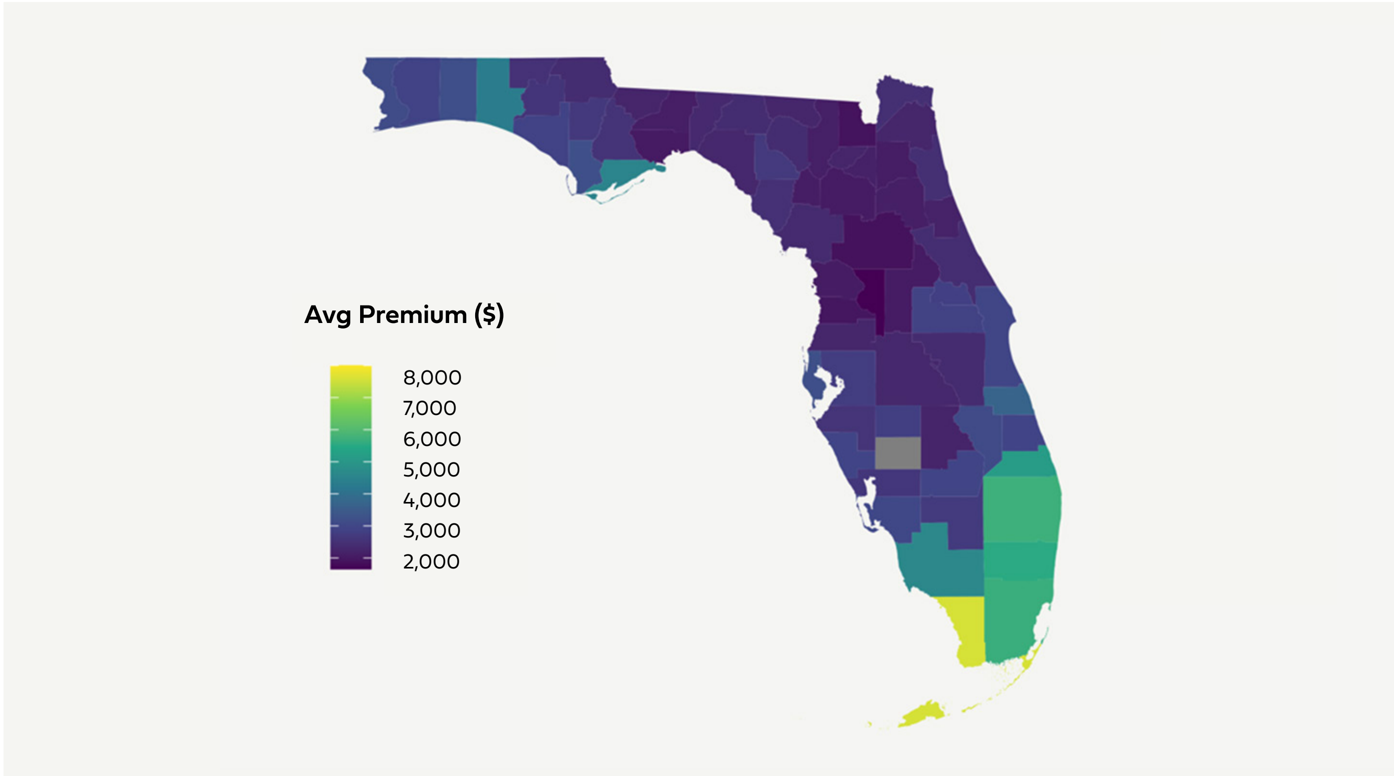
Most Florida insurers have limited protection beyond the required levels, indicating that a more severe season (or succession thereof) could create fiscal hardship for firms. In 2022, Demotech alerted 16 Florida insurers that

[iii] Notably, these intervals do not imply regular cycles over which insurers could simply build reserves — in other words, insurers must prepare for the extreme events each year because they could happen in any year, and even in successive years like 2004-2005.

they could face downgrades. Downgrades would limit their ability to provide insurance to those with a mortgage guaranteed by Fannie Mae or Freddie Mac, since these "government sponsored enterprises," or GSEs, will only accept insurance from highly rated insurers. Instead of addressing the growing risk indicated by Demotech, Florida legislators focused on finding another rating agency that would provide high ratings despite the fragility of the insurers. A year later, however, Demotech had not downgraded any of the firms still actively underwriting, although one became insolvent.

The costs of homeowners insurance in Florida are among the highest in the country, and they have been growing in recent years. The cost of coverage grew 16% between 2021 and 2022 alone, and was up 45% between 2017 and 2022.[22] Within the state, commensurate with the higher disaster risk, premiums are greatest in South Florida, as shown in Figure 1.

Figure 1: Average Annual Homeowners Insurance Premiums by County, 2023



Source: Data from the Florida Office of Insurance Regulation

[iv] Calculations by authors based on QUASR data.

Homeowners insurance rates have recently increased for several reasons. We have discussed the high and growing risk of storms and hurricanes, coupled with the relentless increase in exposed property values, especially near the coast. Florida's residential property insurance market database shows that structure insured values increased 42% statewide from (mid-year) 2019-2023.[iv] In Miami-Dade County, the increase was 52%.

Another concern voiced by insurers the past few years has been litigation expenses, particularly tied to fraud, although there is very little data or research differentiating frivolous versus meritorious lawsuits, causally identifying underlying drivers, or comparing the costs and benefits of proposed legal reforms.[23] The industry concern has been that laws intended to protect consumers were being exploited. "Assignment of benefits" allows a policyholder to transfer insurance benefits to a third-party, such as a contractor. Intended to allow more knowledgeable contractors to assist with insurer negotiations on behalf of a client, there has been concern in Florida that it opened the door to potential fraud. In addition, there has been concern by insurers that attorney fees were driven upward by Florida's "one-way" provision forcing the insurer to pay both sides' attorney fees, a provision designed for consumer protection when engaging with deeper-pocketed insurers. The Florida legislature adopted various reforms between 2019 and 2023 to help lower expenses on insurers. A 2022 investigation of the state legislature reported that Florida opened almost 15% of homeowners claims nationwide but had almost 71% of the homeowners lawsuits.[v] The report also found that only about 8% of total closed claims in 2022 were litigated, with those claims clustered in a few counties, and that litigation was more likely when insurers may not have been acting in good faith, such as taking a long time to close a claim. These lawsuits only cost insurers roughly 3.5% of total paid premiums that year.[24] The report also stated that concern about contingency fee multipliers that allow juries to award more to plaintiff attorneys when they think the case merits it were only used a handful of times.

The costs of homeowners insurance in Florida are among the highest in the country, and they have been growing in recent years.

Apart from litigation, the costs to rebuild have increased due to high inflation beginning in mid-2021, as well as supply chain disruptions. Construction costs grew rapidly after 2020 due to the combined impacts of inflation and scarcity in some building materials. The construction industry also lost workers, putting upward pressure on wages. This has led to increases in insurance prices across the country, including Florida. Inflation rates in the U.S. declined through the spring of 2023, however, and have been relatively flat since then, which should ease this cost pressure.

Finally, a "hard" reinsurance market (cycle of sustained price increases and capacity restrictions) began in 2020 for many of the same reasons: growing catastrophe exposure, assessments of increased risk from climate change, and higher costs of rebuilding. When the reinsurance market turns, the business costs of Florida-specialist insurers rise because most insurers in Florida have relatively low re-

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[v] Report online at: https://www.floir.com/docs-sf/default-source/property-and-casualty/other-property-casualty-reports/january-2024-pclr.pdf?sfvrsn=d8c92a4f_4.

tained capital (surplus) and are highly reliant on reinsurance capital to back their risk exposure. OIR reported that for the 2023-2024 year, insurers saw reinsurance costs increase from the previous year roughly 27%.[25]

These stresses have led to not only higher prices and declining availability, but even insolvencies – 10 property insurers since 2019. To deal with the growing risk, in 2022, the property insurer stability unit was created in the OIR to provide enhanced monitoring of insurers that may be in financial trouble. Between January and June, 18 firms were referred to this unit, and two of those were deemed to need enhanced monitoring.[20]

Numerous firms that remain solvent are also leaving the state. While many national carriers left Florida years ago, many others have recently followed suit. Exits include national firms, such as Farmers and Lexington Insurance, an AIG subsidiary, as well as more regional and local insurers including Progressive and Wilshire. These exits put increasing stress on the state's residual market, Citizens.

Citizens Property Insurance Corporation

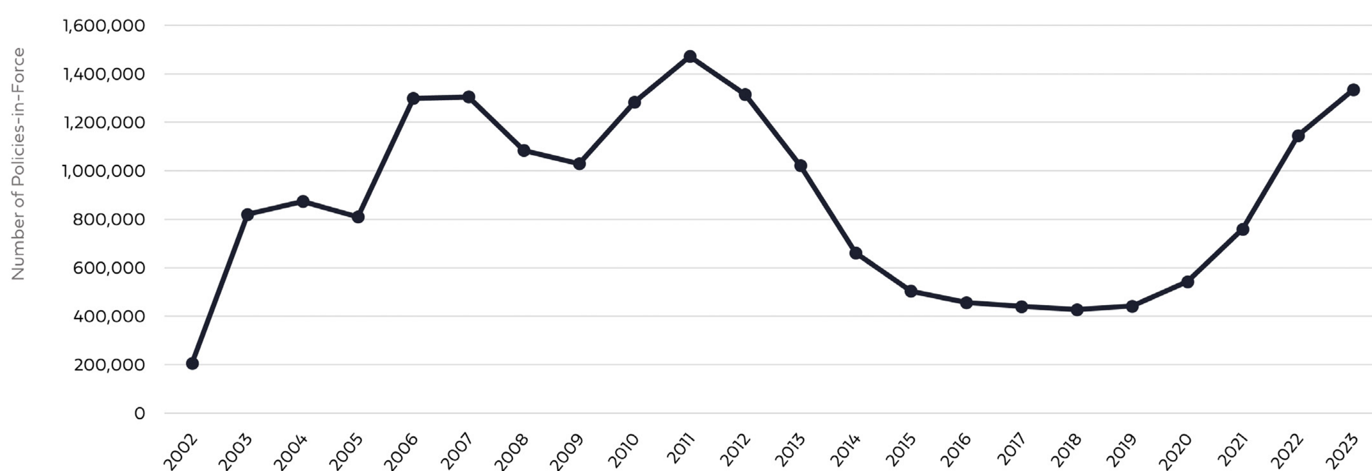
Citizens is a not-for-profit government entity created by the Florida legislature in 2002 (through the merger of two prior entities) to provide property insurance to residents of Florida unable to find affordable coverage in the private market. Property owners are eligible to purchase a Citizens policy if they cannot find coverage or can only find a private-market policy that costs at least 20% more than comparable coverage from Citizens. The program offers both wind-only and multi-peril policies for both residential and commercial structures.

Private insurers must collect sufficient premium revenue to cover losses. Citizens, however, is only partially funded through premium payments. It does not fully reinsure its risk, and, therefore, severe loss years could exhaust its surplus. Deficits are funded through post-disaster bonds, which are paid back using proceeds from assessments on policyholders. Citizens would first assess its own policyholders up to 15% of premium. If this surcharge is insufficient, Citizens would then levy an emergency assessment of up to 10% per year on all assessable lines of premium written in the state, including Citizens policyholders. This generally includes all premium except for workers' compensation, medical malpractice, and flood. This means that hurricane losses for Citizens policyholders would be shared across many households not impacted by the storm and on policy lines not related to homeowner damage, such as business and auto policies.

Unlike "residual" insurers in other states, Citizens has for periods of time looked more like an alternative insurance market featuring subsidized premiums rather than a market-of-last-resort. After the devastating 2004 and 2005 hurricane season, the state legislature took steps to make Citizens more attractive. In 2007, the state legislature's House Bill 1A (HB1A) decreased rates for Citizens and froze them for two years (while also forcing rate rollbacks onto private insurers and expanding the coverage of the FHCF). Eligibility requirements for the program were re-

laxed. Prior to HB1A, a policyholder had to be rejected in the private market or show that admitted insurers were charging 25% more or higher than Citizens to be eligible for Citizens coverage. HB1A removed from the Citizens eligibility requirement that a policyholder must be rejected by the private admitted insurance market. After the passage of HB1A, the minimum premium difference requirement for Citizens eligibility was reduced from 25% to 15%. Offered coverage limits were also increased up to $2 million in some sublines. Citizens grew rapidly, peaking in 2011 with over 1.47 million policies, as seen in Figure 2.

Figure 2: Policies-in-Force in Florida Citizens by Year



Source: Data from Florida Citizens

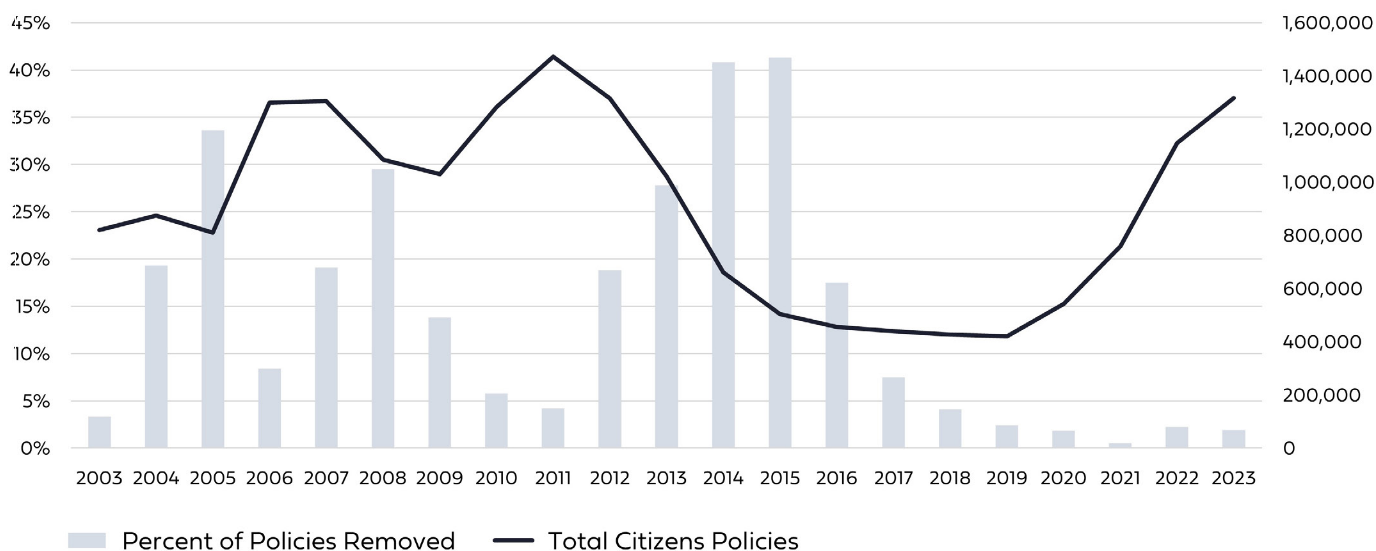
A new Governor's Cabinet became concerned about the fiscal impact on Citizens of swelling policy counts and several steps were taken to reduce Citizens' exposure. Programs were launched or repurposed to reduce ("de-populate") the policies held by Citizens, moving policies back to the private market.[19] Private insurers apply to OIR and, once approved, can make offers to Citizens policyholders. As seen in Figure 3 below, depopulation peaked in 2014-15, a time of steady non-catastrophe losses and falling reinsurance costs, with over 40% of policies removed in 2015. Citizens reached a low of about 427,000 policies in 2018. Rising costs on insurers the last half decade caused depopulation to virtually cease and remain low, even after initial positive signs from the series of litigation reforms in 2019-2022.[vi]

Consumer advocates remain wary of the takeout process. After a firm "tags" (selects to remove) a Citizens policy, the policyholder receives a mail notice containing one or more offers from private insurers — which could be at much higher premiums. If the policyholder does not respond by the deadline, they are automatically transferred

[vi] The fall of 2023 saw renewed depopulation activity, prompting some analysts to speculate that reforms are finally leading to new capital that can support takeouts.

to the lowest-premium offer among private insurers. The new firm might not only be more expensive, but less stable financially. Half of the carriers over the last two decades that have assumed Citizens' policies have become insolvent, passing costs back to the state and its taxpayers.

Figure 3: Total Policies and Policies Removed Through Depopulation in Florida Citizens



Source: Data from Florida Citizens

Citizens has grown rapidly again since 2019 as reinsurance and capital costs have ratcheted upward each year, increasing the number of policies in the state program by over 200% since 2019. When prices become too high, or coverage becomes scarce in the private market, residents turn to Citizens. In addition, when property insurers become insolvent, Citizens is often flooded with their customers, despite the best efforts of OIR to negotiate block transfers to better-capitalized insurers. As of spring 2023, Citizens' market share for homeowners was almost 19%, and for condo owner policies it was almost 11%.[20] Once again, Citizens is now the largest insurer in the state.

Citizens has requested price increases, both to cover its own increasing reinsurance costs and to "catch up" given its historically inadequate rate levels. Private insurers are discouraged from large rate hikes by public hearings, documentation requirements, and their own customers and agents. In contrast, Citizens faces a hard "glide path" cap on individual renewal policy increases of 10% per year (though recent reforms phase in a cap change to 15% over five years). Moreover, OIR has interpreted the law to require Citizens to actively suppress new business rates to approximately the same rate level to avoid being "unfairly discriminatory." In a press release associated with a June 2023 request for rate increases, the President/CEO of Citizens noted that "being able to charge actuarially sound rates is critical to market recovery and promoting depopulation" and that right now, "Citizens' rates are artificially low, which throws off the private market and distorts competition." Citizens' actuaries, as required by the

same law, calculate sound rate levels that are juxtaposed with the capped rate requests. The press release noted that Citizens' rates were on average almost 60% below actuarially sound levels. The FLOIR denied this request for price increases and Citizens made another, smaller, request this past fall, which was approved. Citizens was thus able to increase rates for primary residences an average of 12.3% at the end of 2023.

Storm risks, reinsurance costs, and litigation tend to all be highest in the same regions of Florida, so it is not surprising that Citizens' policyholders are concentrated in some counties. Palm Beach, Broward, and Miami-Dade Counties in 2022 represented 44% of all Citizens' policies in the state, with a significant share also in the Tampa Bay counties.

Florida Hurricane Catastrophe Fund

Florida is the only state with its own public hurricane reinsurance program. The Florida Hurricane Catastrophe Fund (FHCF) provides "reimbursements" to private insurers and Citizens, which by law are treated as reinsurance coverage by OIR. It is a tax-exempt trust fund that was created in 1993 following Hurricane Andrew to provide a "layer" of stable coverage that is priced with less volatility than cyclical private reinsurance markets. Its rates are set using an actuarial blend of outputs from all models accepted by the Commission in the previous year but calibrated to only the "average annual loss" from those models, with no "multiple" or "risk load" for the cost of reinsurance capital. The premium that insurers pay for coverage from the FHCF is lower than the private market due to its rate formula, but also because the FHCF pays no taxes, has relatively low operating costs, and does not pay profits to investors.

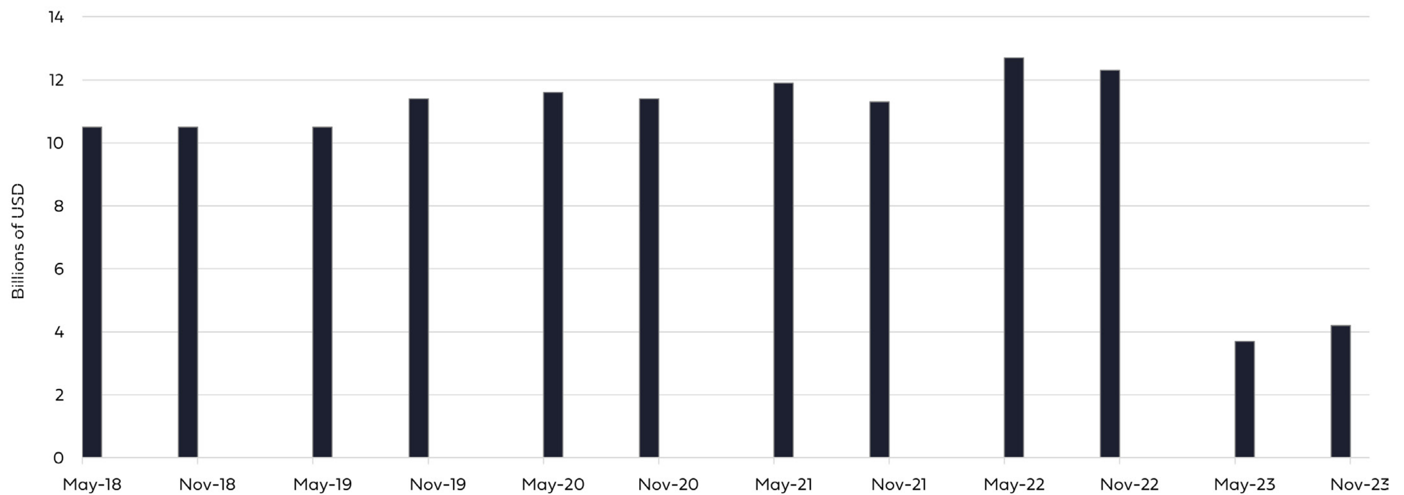
Participation is mandatory, but property insurers can choose to purchase 90%, 75%, or 45% reimbursement levels for subject losses. Due to a recent hard reinsurance market, FHCF has seen an increase in the average coverage level chosen by insurers, which for 2023 was relatively high, at 87.4%. FHCF only covers hurricanes, not tropical or unnamed storms, and only excess of a per-storm retention — but the coverage is in aggregate for a season and not subject to "reinstatement" for an additional premium, unlike typical private reinsurance. Therefore, private reinsurance programs must work around FHCF by using "inuring" coverage that allows FHCF to pay first, with private reinsurance providing coverage for second and subsequent events should the FHCF layer be exhausted mid-season. Overall, use of FHCF typically lowers the total reinsurance cost for private insurers, but can also create complications that result in private insurers spending up to half of their total reinsurance budgets on coverage that operates below the retention of FHCF.

Due to a recent hard reinsurance market, FHCF has seen an increase in the average coverage level chosen by insurers, which for 2023 was relatively high, at 87.4%.

When FHCF must pay claims from insurers after a storm, it first draws from its fund, which is built up from premium revenues and investment income. As with Citizens, a season deficit causes FHCF to issue (usually tax-exempt) bonds and repay those bonds with assessments. The assessment lines and percentages authorized differ somewhat for Citizens, FHCF, and FIGA. FHCF faces a 6% maximum levy in a single season and 10% across multiple seasons, but the base is similar to Citizens' "emergency" 10% assessment base, covering nearly all lines and all regions. The state authorizes FHCF to issue debt for terms up to 30 years, and it must publicly estimate its bonding capacity in May and October of each year. Sometimes, FHCF also borrows money in advance of storm seasons for liquidity purposes, but this debt is typically not tax-exempt.

FHCF is only obligated to pay claims that it can meet through its reserves, bonding, and assessments. Hurricane Ian in 2022 resulted in an ultimate FHCF estimated loss of $10 billion, of which $3.35 billion has been paid as of year-end 2023. This event, plus continuing payments from Hurricanes Irma and Michael of over $9 billion, has caused its fund balance to drop substantially from 2022 through 2023, as seen in Figure 4, such that a near-future extreme event could wipe out all reserves. For the current contract year, which runs from June 2023 through May 2024, the FHCF maximum potential liability is $17 billion. This amount is set by law and has not changed in several years. It has total liquid resources of roughly $7.7 billion ($4.2 billion in reserves plus $3.5 billion in pre-event bonds). To meet the $17 billion, therefore, FHCF would have to issue $9.3 billion in post-event debt. If FHCF is unable to finance its losses in the private bond market, it is not obligated to pay. Over the years, FHCF has purchased reinsurance for itself when markets were favorable, but the growing cost has led FHCF to forego purchasing reinsurance for the past several contract years.

Figure 4: Florida Hurricane Catastrophe Fund Balance



Source: Data from Claims-Paying Capacity Estimates prepared for the Florida Hurricane Catastrophe Fund

Florida Insurance Guaranty Association

Florida also has the Florida Insurance Guaranty Association, created by the state legislature in 1970 to cover the claims of insolvent insurers operating in the admitted market. (The claims of insolvent "excess and surplus" lines insurers are not covered by FIGA.) It pays those claims from investment income and the assets of the liquidated companies. This, however, is rarely sufficient since the company was declared insolvent. When needed, FIGA must turn to debt markets to pay its unfunded claims, as it did recently in the summer of 2023. To repay the debt, like Citizens and FHCF, FIGA levies assessments (approved by the OIR) on member insurers. To lessen the cash outlay on private insurers, these assessments can be designated "emergency," such that the insurers collect and remit from policyholders monthly rather than paying the entire assessment up front and "recouping" it from policyholders via a special rate filing. Since 2019, FIGA's property lines account has had to cover claims from 10 insolvent insurers with over 440,000 policies, ultimately costing FIGA roughly $1.6 billion.[26]

In the face of recent insolvencies, Florida regulators have been accused of turning a blind eye to risky insurer practices, such as those of United Property & Casualty (UPC), which went bankrupt in 2023 and passed nearly all its losses onto FIGA — after which FIGA levied a multi-year assessment ultimately borne by consumers. Some reporting suggested that UPC underpaid consumers in need and ignored growing risk, while paying executives and shareholders millions of dollars in dividends. The firm may have not reserved sufficient capital and regulators had failed to intervene, despite the firm receiving a disproportionate share of complaints.[27]

National Flood Insurance Program

Over 93% of all flood insurance policies written in Florida are from the federal National Flood Insurance Program.

Standard homeowners insurance policies do not provide coverage for flood damage. As such, those at risk of flooding must purchase an additional flood policy. Lack of private availability for such coverage led to the 1968 creation of a federal program, the National Flood Insurance Program (NFIP), now housed in the Federal Emergency Management Agency (FEMA). Communities that join the NFIP adopt minimum development regulations governing the floodplain, defined as geographical areas with at least a 1% annual chance of flooding. Their residents (whether located in the regulatory floodplain or not) then become eligible to purchase flood insurance policies through the program. Single-family and two- to four-dwelling residences can purchase up to $250,000 of building coverage and $100,000 of contents coverage. Nonresidential policyholders can insure both structure and contents up to $500,000 each.

Florida also has a small but growing private flood insurance market. This market began by providing excess coverage above the NFIP caps and "wraparound" policies, covering items that are excluded by NFIP, but now

multiple private firms offer full coverage. The OIR reports that as of 2022, there were 107,825 private flood insurance policies across Florida. By comparison, as of the end of 2023 there were 1.65 million NFIP policies in Florida. Recent (2022) legislation requires policyholders with coverage from Citizens to also secure a flood policy from the NFIP or a private provider, phased in over three years by descending tiers of insured value. This is designed to minimize disagreements after storms as to whether the damage was caused by wind or water and limit incentives to report claims with uncertain causes to Citizens.

Interdependencies and research challenges

A "big one" or "big season" could simultaneously cause severe losses across all three Florida insurance programs. If the three programs face deficits simultaneously, they would all seek to access the bond market at the same time, leading to a potential debt clash. It is uncertain in this situation if all three programs could find sufficient capacity and/or if it would drive up prices. Insufficient investor interest would create pressure on the state to back the programs and ensure their ability to pay claims. If the programs all do secure needed debt, it would then lead to "stacked" policyholder assessments on consumers. This could add further financial stress at a moment when many households will already be struggling with the financial shock of a severe storm.

In a severe hurricane year, all three Florida insurance programs could face high losses, causing them to access the bond market simultaneously. This could potentially create a debt clash and compounding consumer assessments.

Unfortunately, to date there is no unifying stress test that gives policymakers comprehensive data about the impact of extreme events or seasons on the entire property insurance system of Florida. Citizens, in its public board documents and reinsurance market submissions, measures its own risk carefully, as does the FHCF in its rate formula and bonding capacity reports. But Citizens' estimates assume full payment from FHCF, and do not consider an event that would send both institutions to the bond market at the same time or result in a delay in reimbursement. FHCF, for its part, carefully estimates bonding capacity, but again, these estimates do not presume that Citizens and FIGA may be competing for funds in debt markets.

The most difficult assessment probability to estimate is that of FIGA, because each insurer's financials and reinsurance structures are largely private, and it is both difficult and dangerous to opine on exactly what events would cause insolvency. OIR sees considerable data, including confidential stress tests from each private insurer, but is restricted regarding public, identifiable release of findings. It evaluates these test data, methods, and results in a "pass/fail" mode, either approving an insurer's reinsurance program or demanding changes.

Conclusion: Policy options

Florida's property insurance market has seen booms (soft markets, with low prices and abundant coverage) and busts (hard markets, with high prices, limited coverage, nonrenewals, and frequent insolvencies) since 1992. Right now, Florida is experiencing the hardest market since the wake of Hurricane Andrew. Private market availability is shrinking, and prices are higher than the rest of the country, yet still inadequate to cover the risk. Some drivers of current challenges are slowly being corrected. The state has adopted numerous legal reforms. Inflation has abated since its peak in 2022. But private capital will flow to the Florida market only if and as reinsurers re-price risk and stabilize their offerings, given the combination of escalating severe storm risk and continued exposure growth in high-risk areas.

This turmoil has exacerbated the stress on the three public sector programs and challenged the faculties of their regulators. Citizens is once again a preferred market for many residents, but its size now threatens its own fiscal position. Citizens has made multiple public statements that its rates are far from sufficient for the risk. Florida policymakers and regulators face difficult tradeoffs. Will the state continue to subsidize risk, or even double down by allowing more high-value homes and commercial properties into Citizens? This would maintain lower insurance prices for residents in the near-term, but it could also invite a future fiscal crisis. Or will rates be allowed to approach levels commensurate to the risk, particularly for new customers? This would stabilize the finances of Citizens, allowing it to better protect the state's taxpayers from future losses. But risk-based pricing would also force residents to pay higher rates, threatening housing budgets and, therefore, real estate and mortgage markets. As none of the state programs are means-tested, impacts will be disproportionally borne by lower-income households and communities unless the state adopts new policies to target actuarial subsidies to those most in need.

Private insurer rates are tightly regulated, but even so, must reflect market-clearing costs of capital, most of which is provided by reinsurance. FHCF's participation in the reinsurance needs of its customers could be re-targeted and updated to reflect current conditions. While the state legislature has passed several temporary programs to relieve short-term stress using optional FHCF layers, the basic retention of FHCF has inflated on an exposure-driven formula since 2010. This is even as private insurers spend an increasing amount of policyholder premiums to secure reinsurance coverage below the FHCF retention. FHCF's rates are approved by the executive branch but its retention is set by statute, so a combined effort to modify the FHCF layer and recalibrate its rates to appropriately reflect the risk could allow private insurers to send fewer dollars offshore and encourage them to provide more coverage as their capital position and cost structures improve. FHCF's contracted actuaries could work with OIR actuaries to find the changes that will show the highest "bang for the buck" in the form of lower rates for homeowners while maintaining stability and bond market access of the FHCF.

Underscoring the other market problems is that the state's three insurance programs — Citizens, FHCF and FIGA—are all managed financially independently, when their losses are indeed correlated. This creates an unmanaged fiscal risk for the state, which would be unable to pay all claims if the three programs could not obtain

the needed debt financing. In addition, it means a risk of assessments from all three programs hitting Florida policyholders simultaneously, further driving up the costs of insurance, which is already among the highest in the country. This could have negative spillover economic consequences to housing markets, mortgage markets, and local economies. A deeper analysis of these risks is warranted.

Finally, a cornerstone of reforms to addressing current market problems should be for the state to invest in transformative levels of risk reduction. As risks of claims payouts are lowered, it could attract more insurer capital and stabilize prices. This approach would require several changes. Programs to upgrade buildings to better withstand hurricanes (such as the Fortified standard by IBHS) would be key. This means building code upgrades, grants to help those who cannot afford such measures, training programs for builders and contractors to ensure sufficient capacity to undertake the work, outreach and education on the benefits of the standard, and requirements for insurers to support the process through Fortified endorsements and pricing commensurate with the lower risk. Beyond this, though, risk reduction will also require improved land use and siting decisions that are adequately reflective of growing risk. And finally, it requires the state and local communities to continue to expand public sector investments in risk reduction. Some local governments, like Miami, have already been investing in such measures and there are multiple federal grants available to share costs.

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