



## **Casualty Loss Reserve Seminar**

Florida Homeowners:  
The 21<sup>st</sup> Century's Version of Whack-A-Mole

**September 16, 2020**

# Agenda

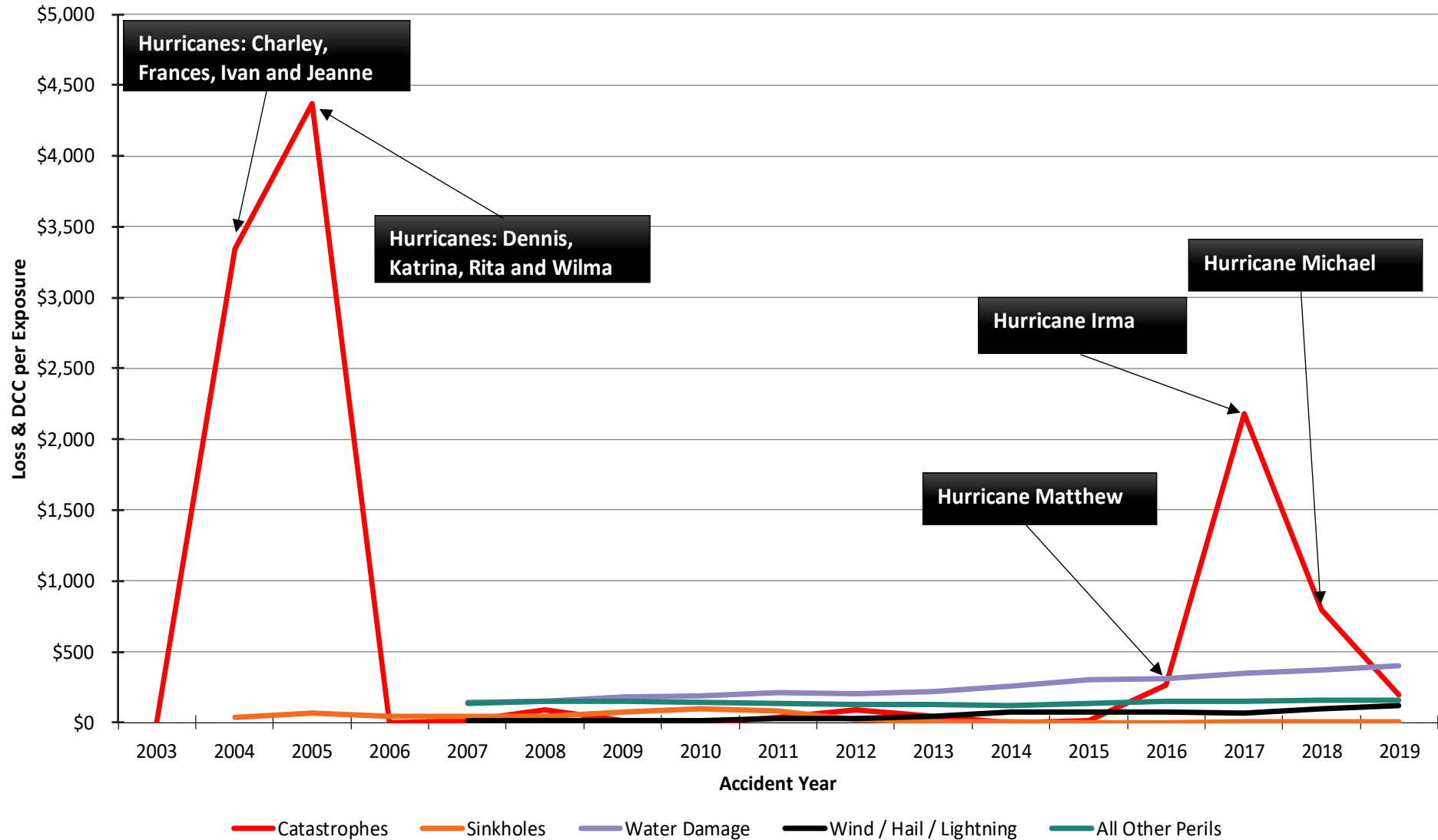
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- “Tail” of Two Eras
- Historical Claim Trends
- Financial Results
  - Balance Sheet
  - Traditional Insurance Risks
  - Profitability
- Questions on Future Profitability
  - Adverse Loss Development
  - Future Loss Cost Trends
  - Impact of AOB Reform

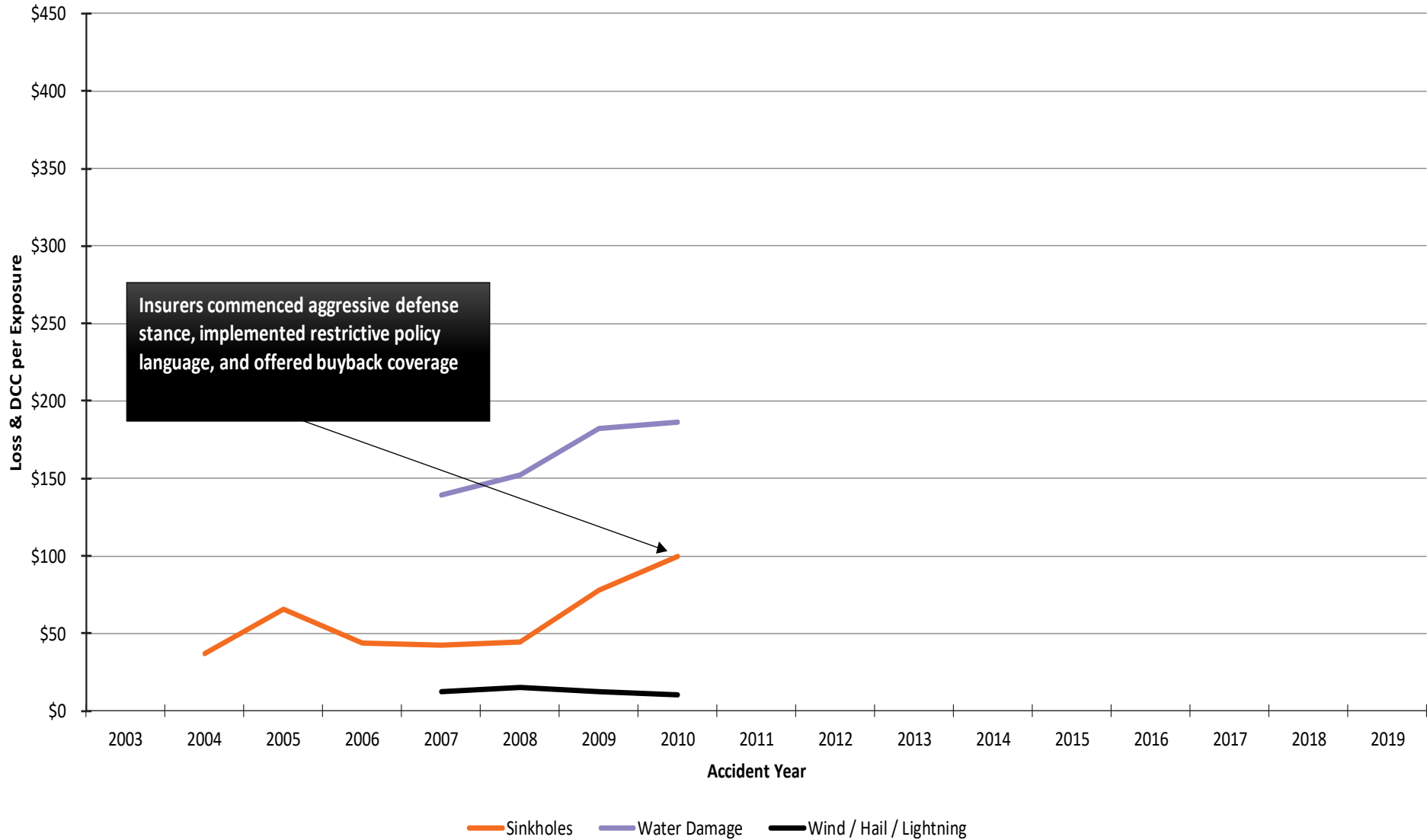
# Sinkhole Era: Historical Claim Trends



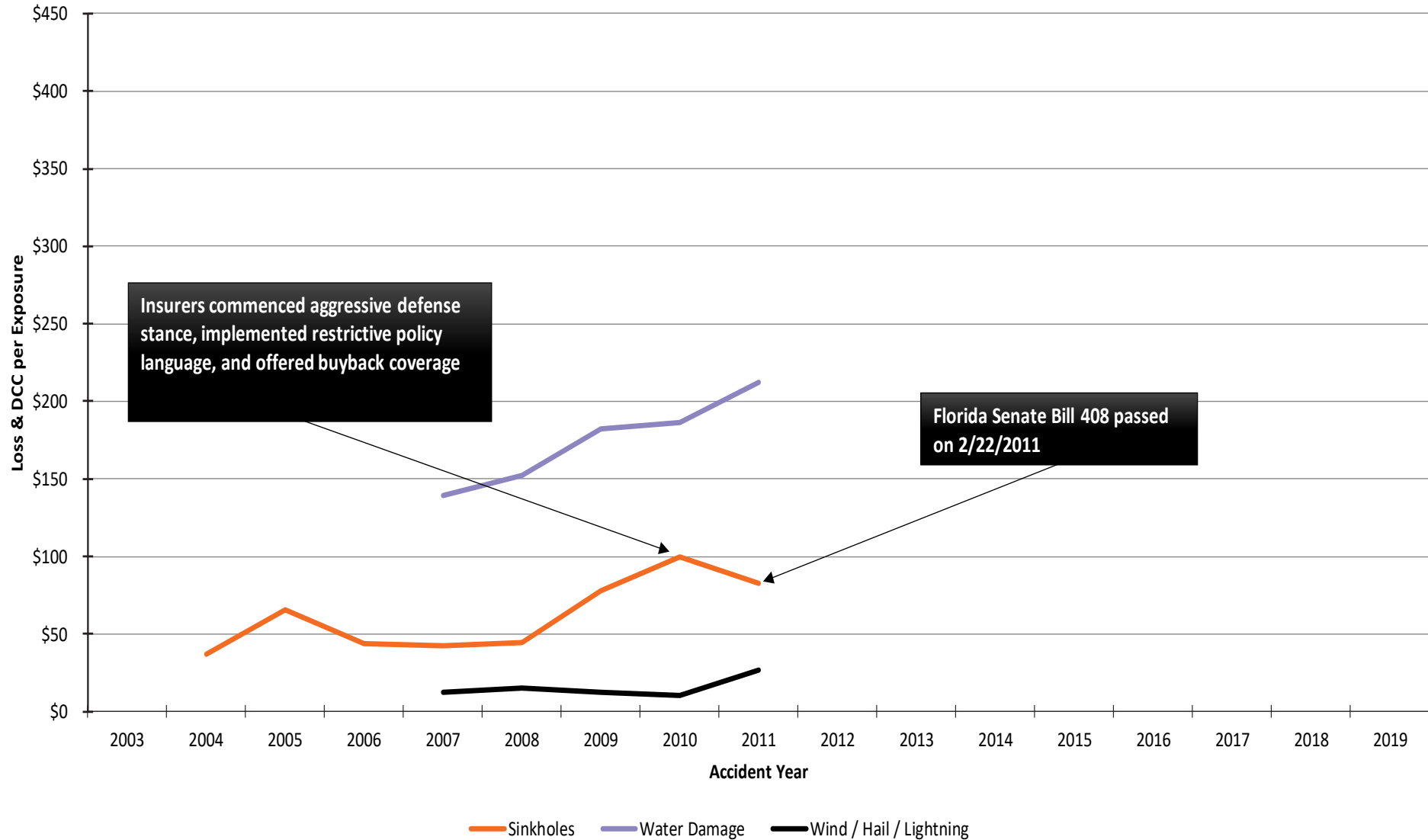
# Loss Cost (Loss & DCC per EHY): By Cause of Loss



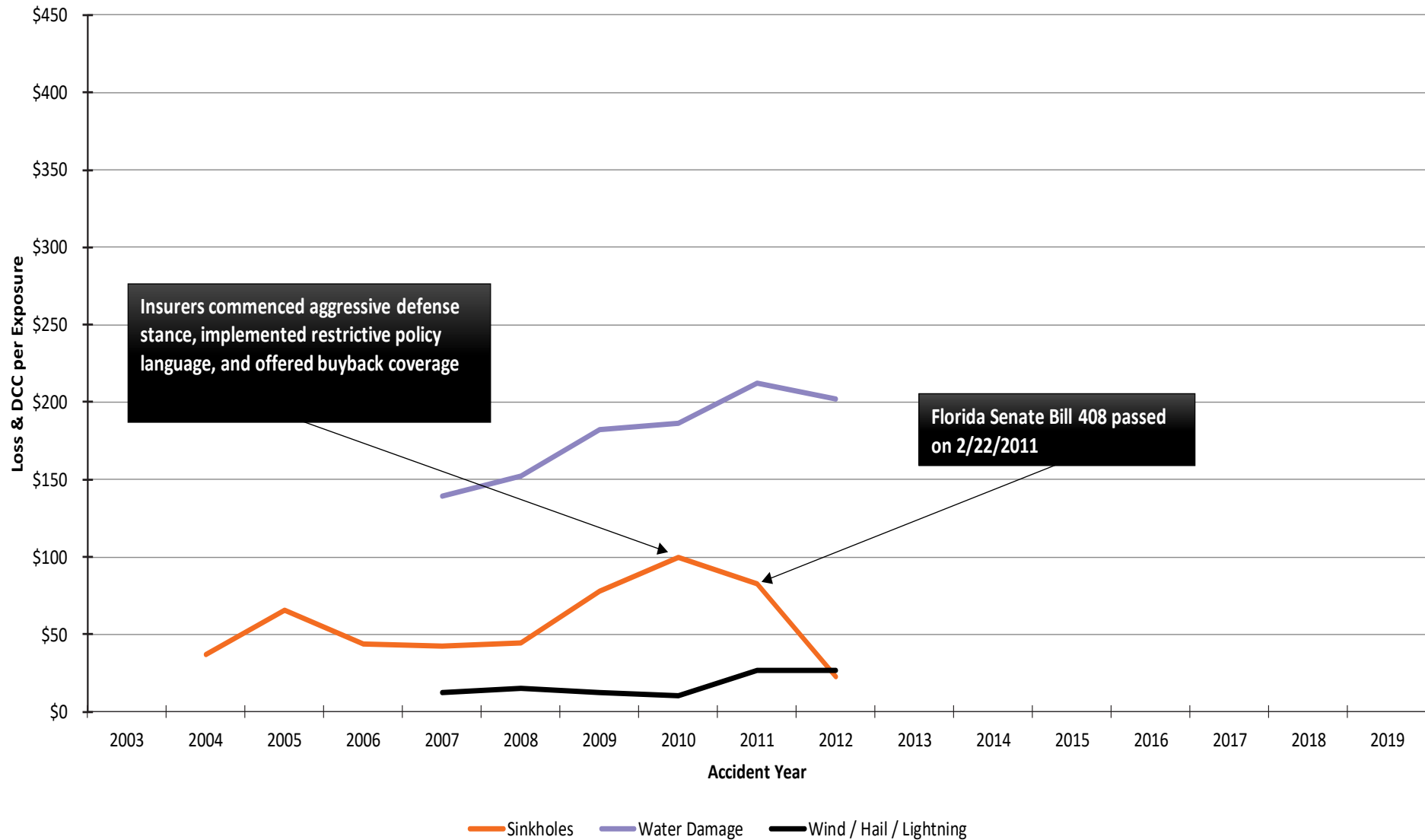
# Loss Cost: By Cause of Loss (ex-Catastrophes)



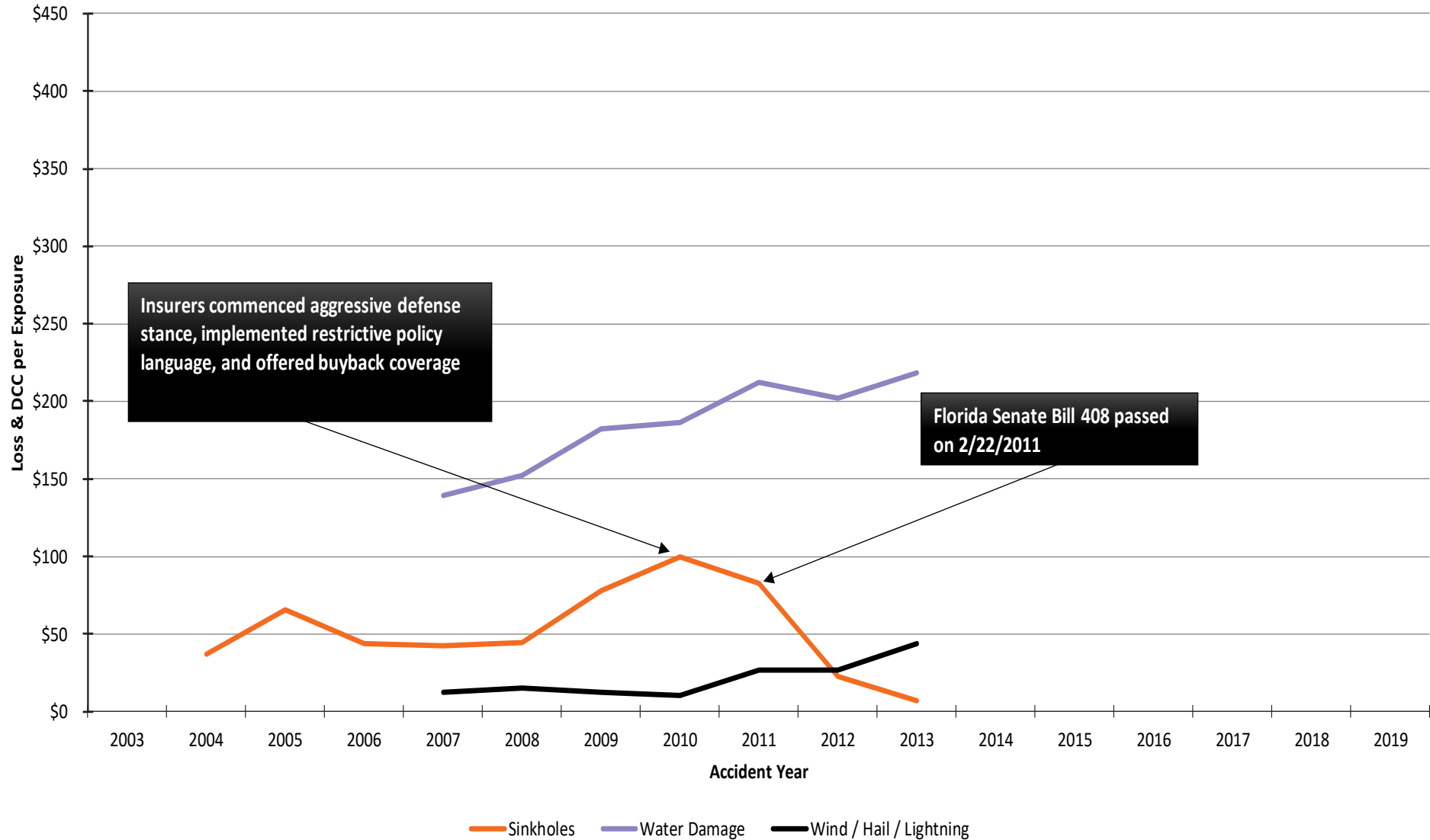
# Loss Cost: By Cause of Loss (ex-Catastrophes)



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# Sinkhole Era: Financial Results



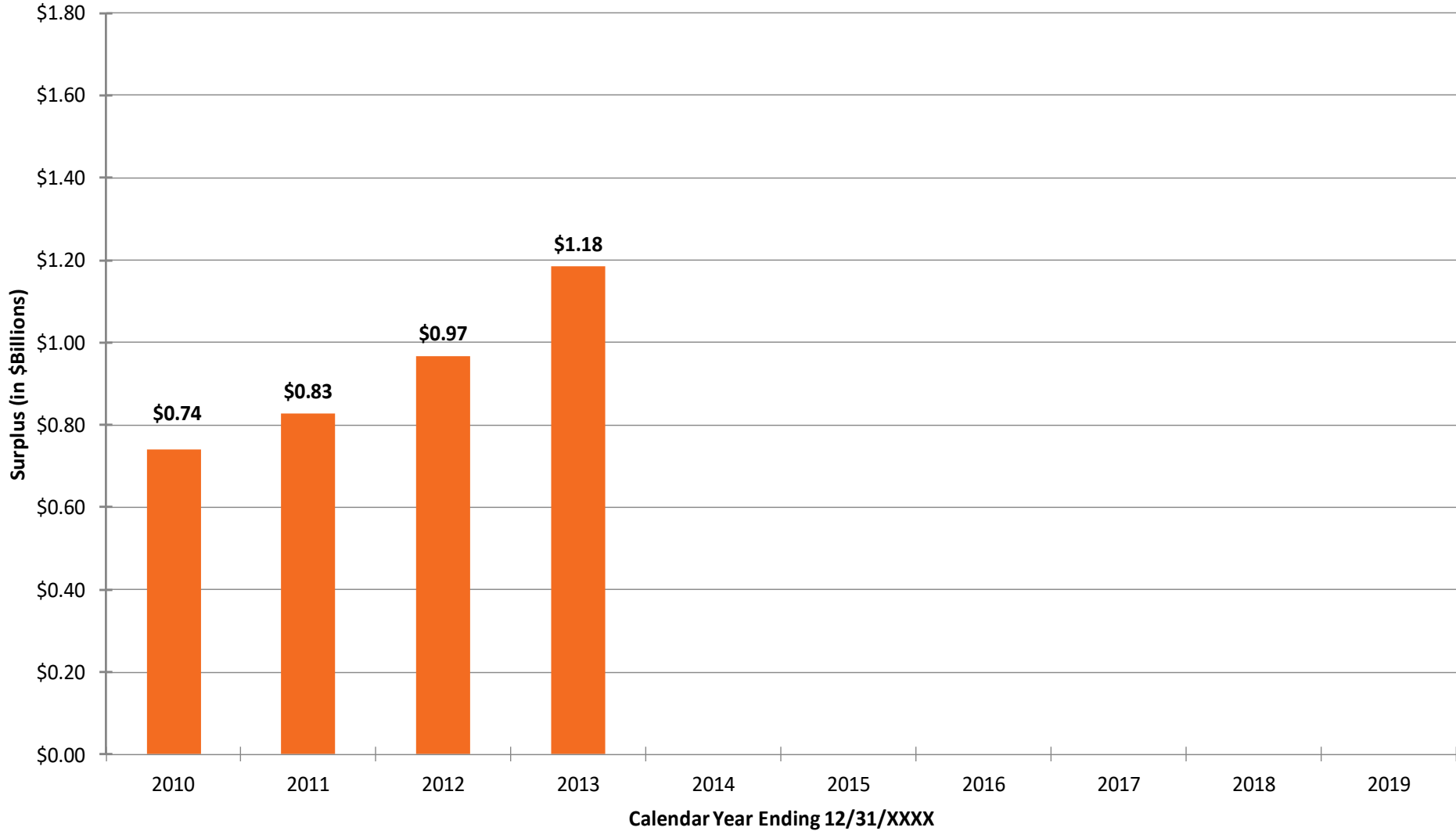
# Balance Sheet

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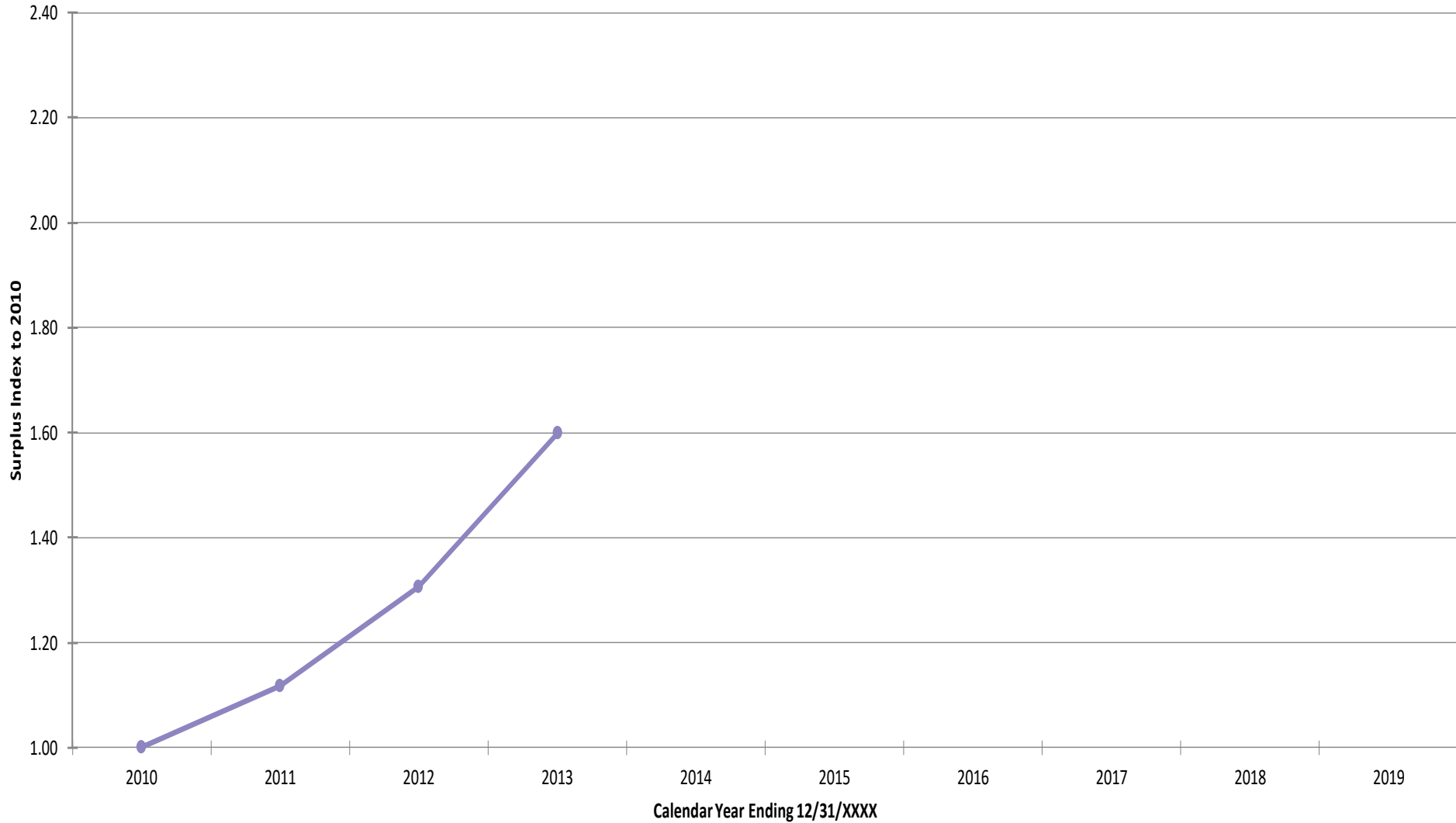
- Calendar years 2010 through 2019
- Presented for a sample of Florida-domiciled homeowners insurance companies
  - Majority of premium associated with FL HMP annual statement line
  - Generally, more than 10 years of experience for the group



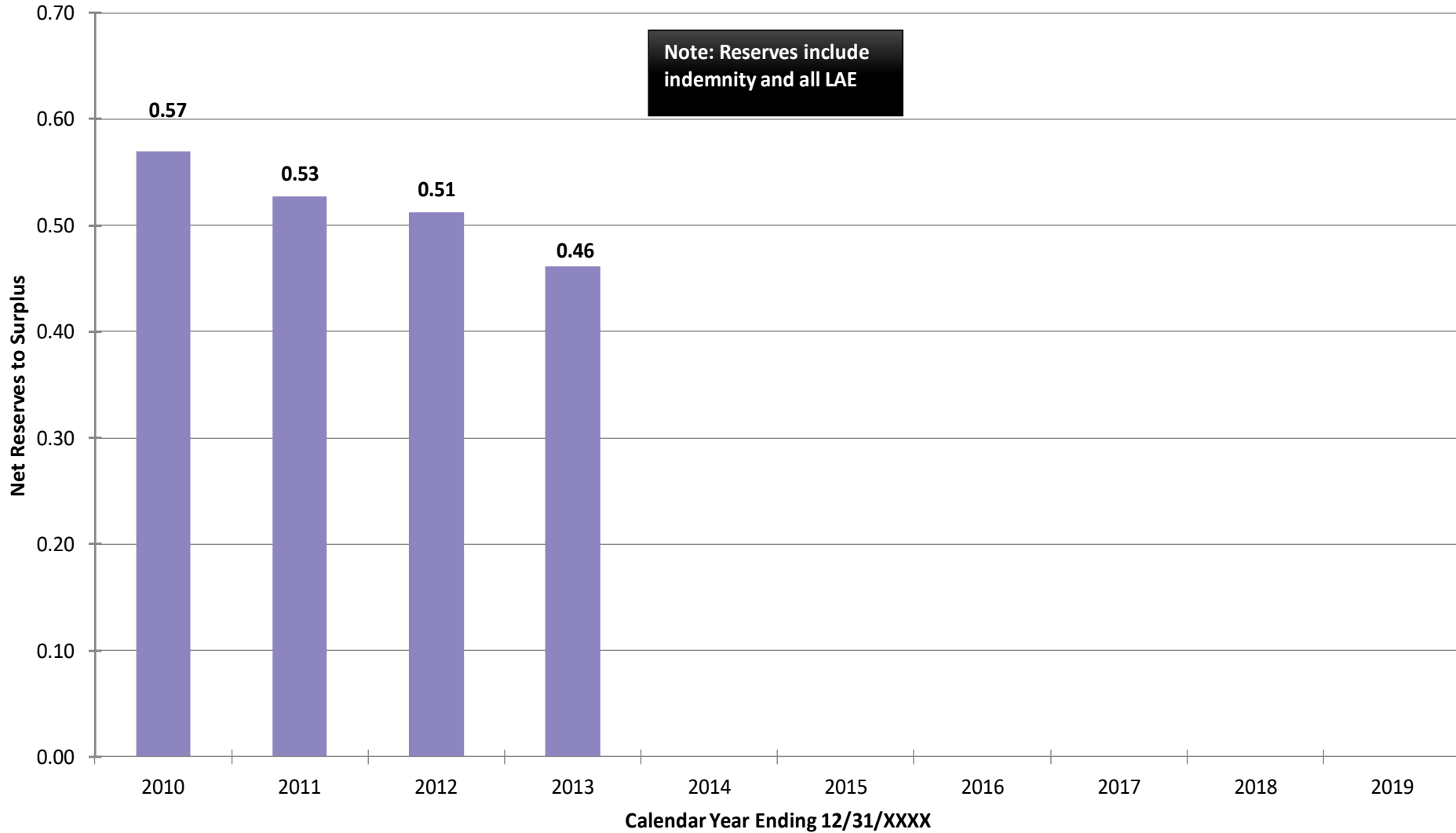
# Surplus



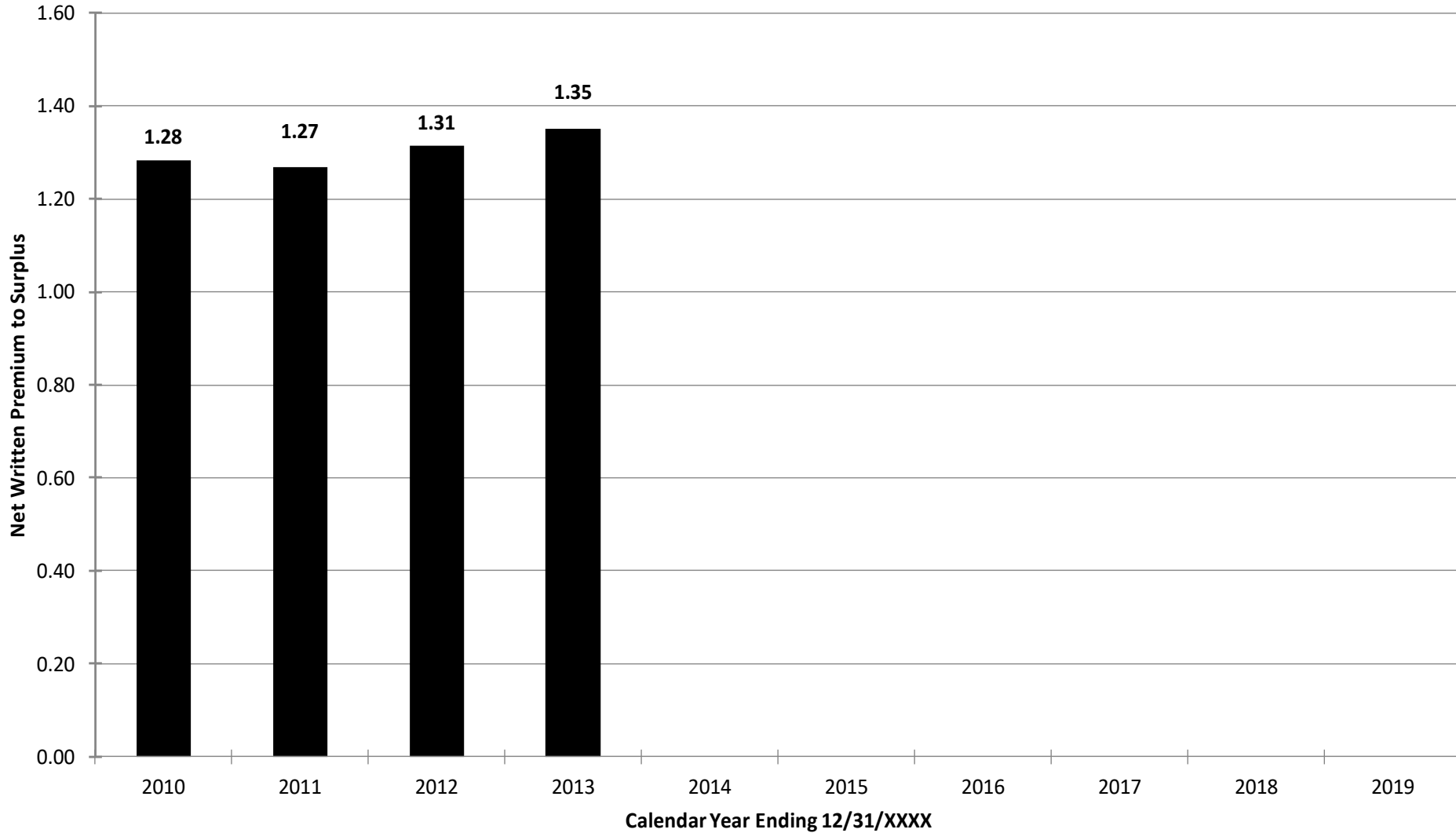
# Surplus: Relative to 2010



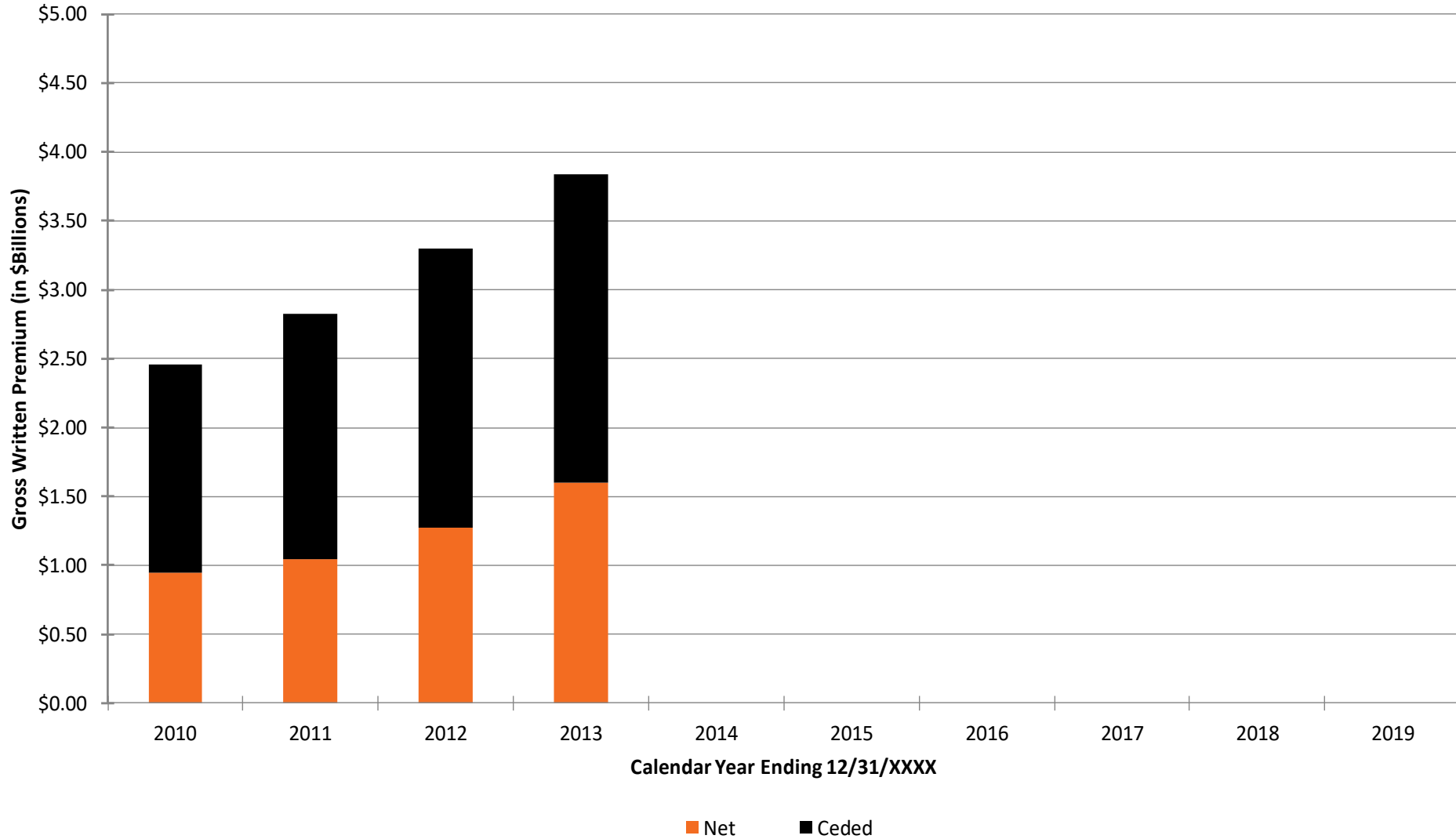
# Net Reserves to Surplus



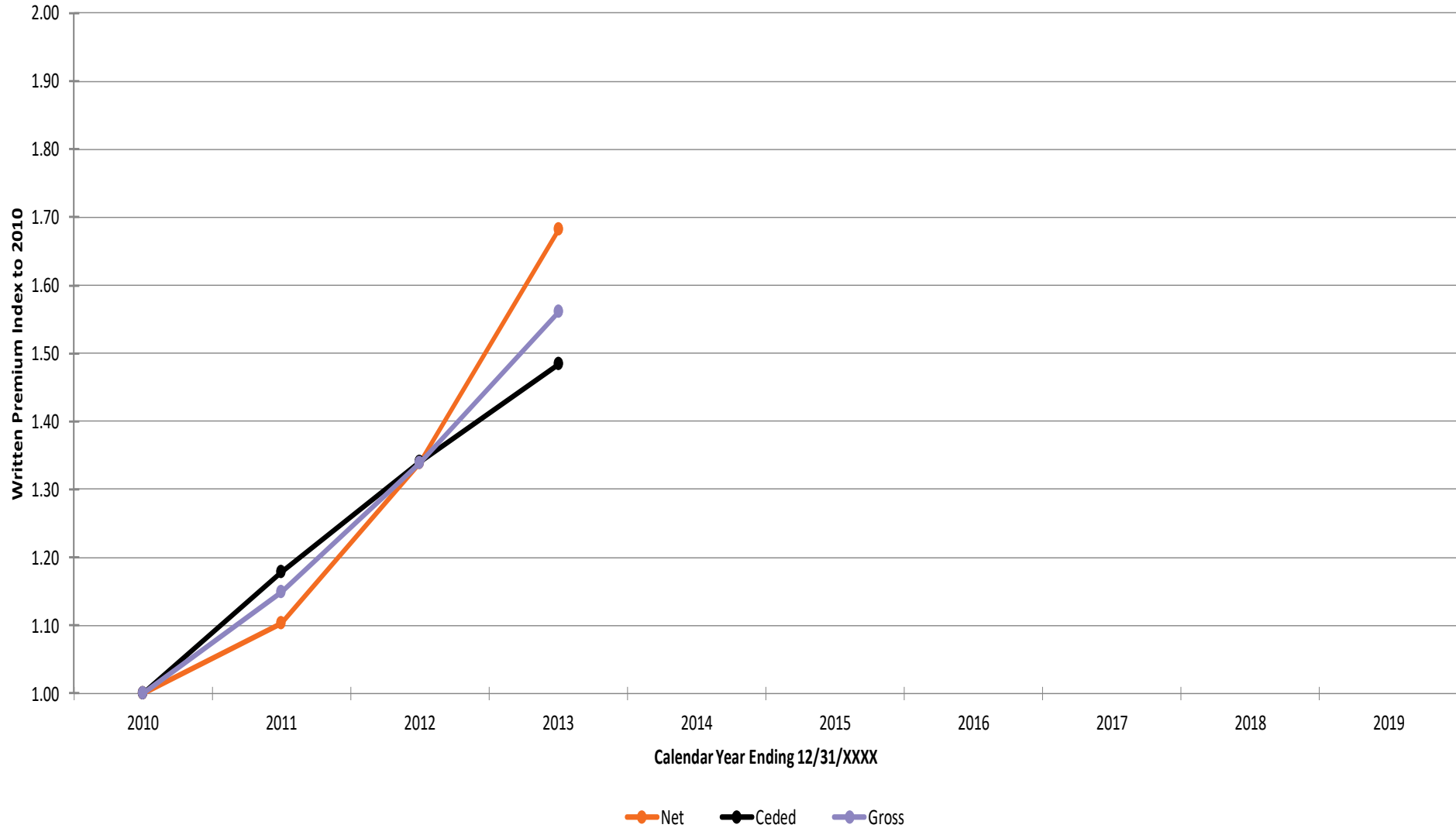
# Net Written Premium to Surplus



# Gross Written Premium by Component



# Gross Written Premium: Relative to 2010





# The Sinkhole Litigation Problem

## **Data from the Office of insurance Regulation showed:**

- Total sinkhole claims increased from 2,360 in 2006 to 7,245 in 2009.
- Total sinkhole losses for closed and open claims combined increased from \$209 million in 2006 to \$406 million in 2009.
- Total losses for open and closed claims exceeded \$1.4 billion over the 4-year period.
- Data from Citizens showed the number of sinkhole claims doubled between 2005 and 2009.

# What Caused the Increase in Sinkhole Claims?

- The Director of the Office of the Florida Geological Survey told the Florida Senate staff that there was no geological explanation for the significant increase in sinkhole claims being reported to insurers.
- According to a Florida Senate staff analysis, representatives from OIR and representatives of insurers believed that a major driving force for the significant increase in sinkhole claims is the fact that many policyholders file such claims because they can keep the cash proceeds from the claim instead of repairing the structure or remediating the land.

# Legislative Response to the Sinkhole Litigation Problem

In response to the litigation crisis, Florida has enacted statutes to limit abusive sinkhole claims. Reforms enacted in 2006 and 2011 include:

(1) Coverage for “catastrophic ground cover collapse” and “sinkhole loss” require that there be **structural damage** to the covered building. See §§ 627.706(2)(a), 627.706(2)(j), Fla. Stat.

- “Structural damage” was not initially defined in statute so there was litigation over the term’s meaning and different courts could find different definitions. In 2011, “structural damage” was defined to create five distinct types of damage that constitute structural damage. See § 627.706(1)(k), Fla. Stat.
- The definitions are similar to definitions in the Florida Building Code.
- In order for the policyholder to obtain policy benefits for sinkhole loss, the insured structure must sustain structural damage that is caused by sinkhole activity. The definitions reduced litigation over what constitutes “structural damage.”

# Legislative Response to the Sinkhole Litigation Problem

(2) Section 627.706, Florida Statutes, requires insurers to provide coverage for a “catastrophic ground cover collapse” and must make available coverage for a “sinkhole loss” for an additional premium.

- Insurers may restrict catastrophic ground cover collapse and sinkhole loss coverage to the **covered** building as defined in the insurance policy, rather than any building. *See* §§ 627.706(2)(a), 627.706(2)(j), Fla. Stat.
- Additional living expense coverage is only available pursuant to a sinkhole loss if there is structural damage to the covered building. *See* § 627.706(2)(j), Fla. Stat.

# Legislative Response to the Sinkhole Litigation Problem

(3) Section 627.7074, Florida Statutes, creates a neutral evaluation process through the Department of Financial Services.

- Either party may request neutral evaluation. *See* § 627.7074(4), Fla. Stat.
- A neutral evaluator receives testimony and evidence from the claimant and the insurer. *See* § 627.7074(5), Fla. Stat.
- Neutral evaluation must determine causation, all methods of stabilization and repair, and the costs for stabilization and all repairs. *See* § 627.7074(2), Fla. Stat.
- The neutral evaluator recommendation is not binding. The neutral evaluator’s written recommendation, oral testimony, and full report shall be admitted in any action relating to the claim or to the cause of action giving rise to the claim. *See* § 627.7074(13), Fla. Stat.
- If the insurer complies with the recommendation of the neutral evaluator, the insurer is not liable for certain “bad faith” damages related to a claim for a sinkhole loss and is not liable for “one way” attorney’s fees unless the policyholder obtains a judgment that is more favorable than the recommendation of the neutral evaluator. *See* § 627.7074(15), Fla. Stat.
- Insurers can continue to use the appraisal process in the insurance policy. *See* § 627.7074(3), Fla. Stat.

# Legislative Response to the Sinkhole Litigation Problem

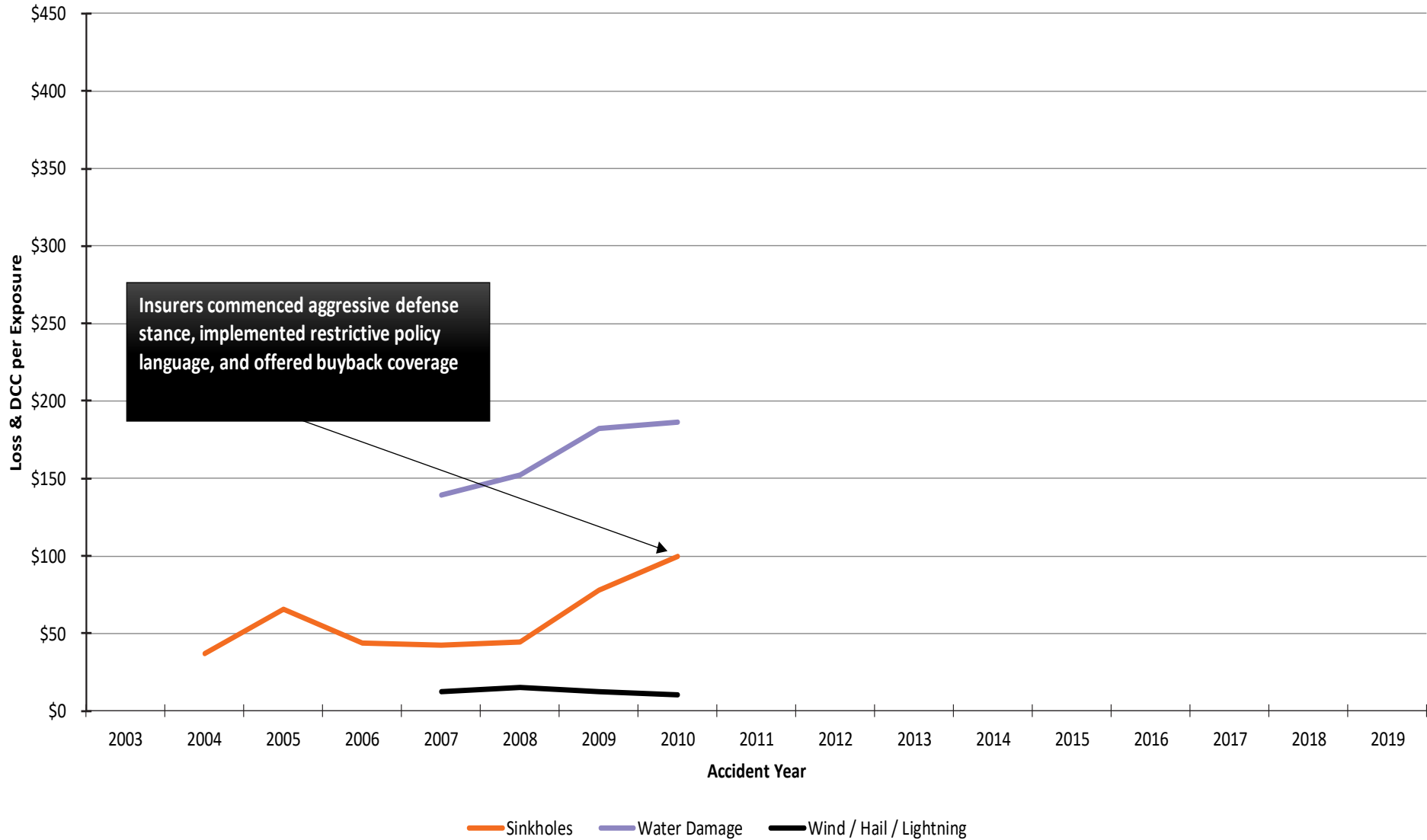
(4) Section 627.707(5), Fla. Stat., provides that if a covered building suffers a sinkhole loss or catastrophic ground cover collapse, the insured must repair such damage. If repairs cannot be completed within policy limits, the insurer has the option to either pay to complete the recommended repairs or tender policy limits.

(5) Section 627.707(5)(f), Florida Statutes, prohibits the policyholder from accepting a rebate from a person performing sinkhole repairs.

# Assignment of Benefits Era: Historical Claim Trends

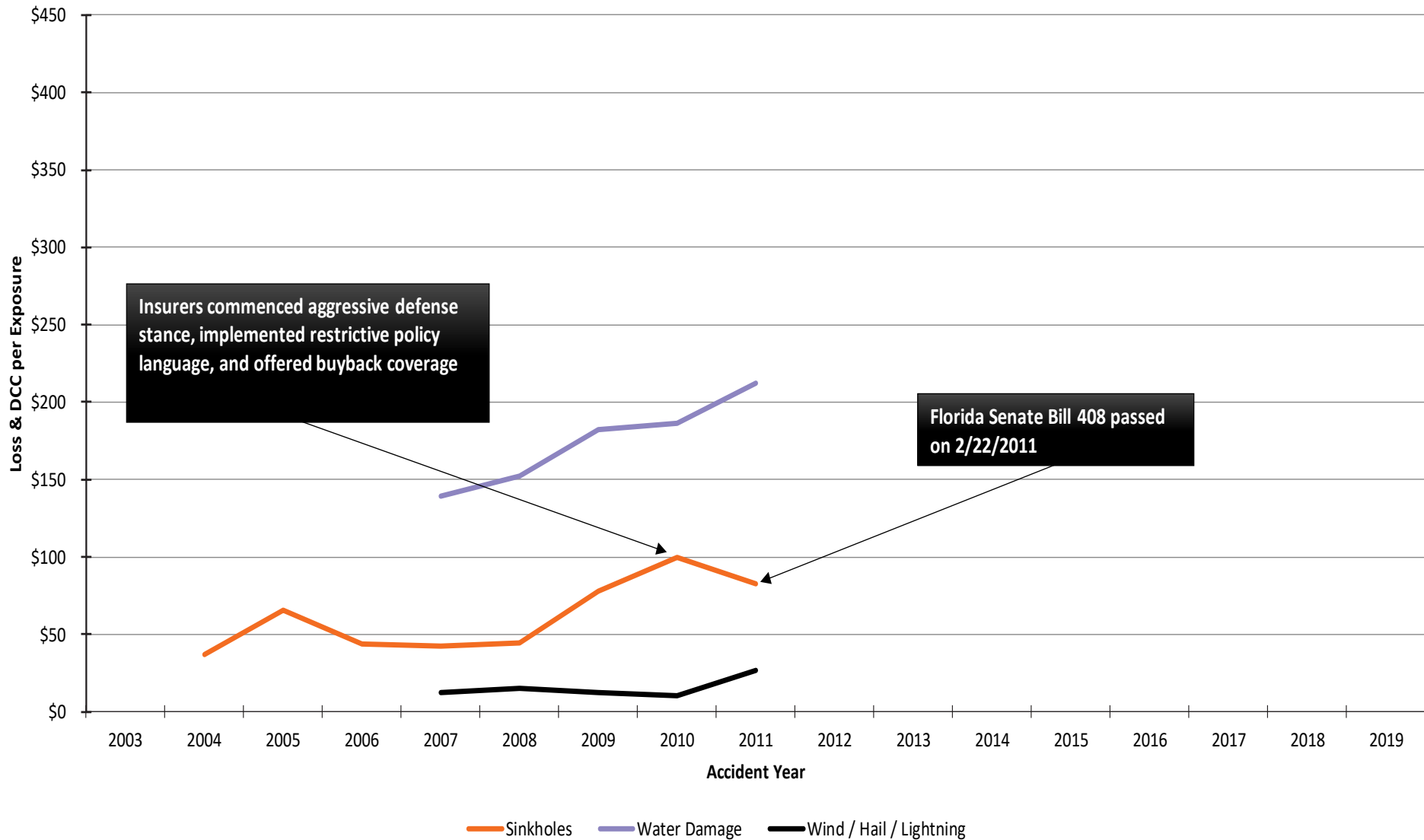


# Loss Cost: By Cause of Loss (ex-Catastrophes)

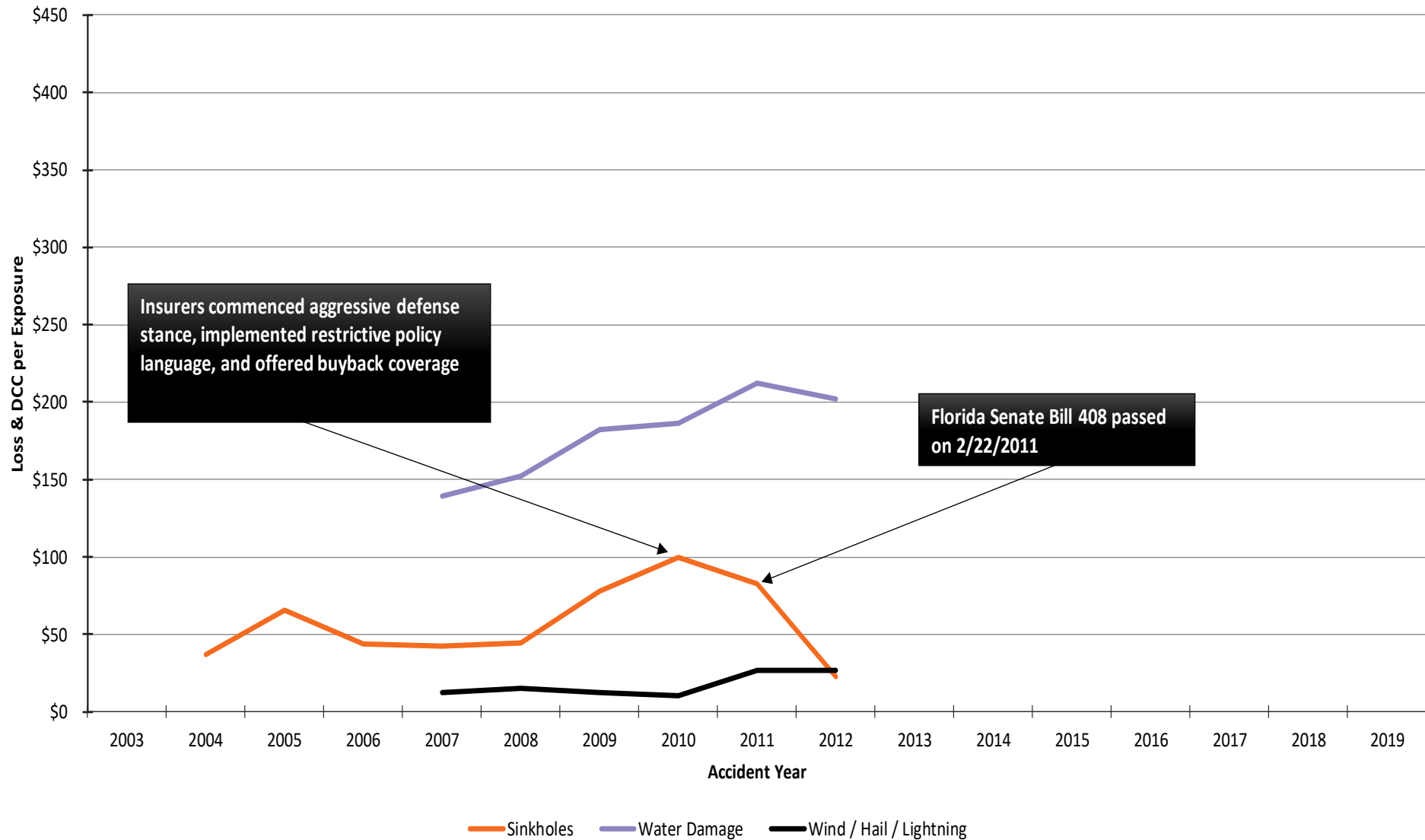




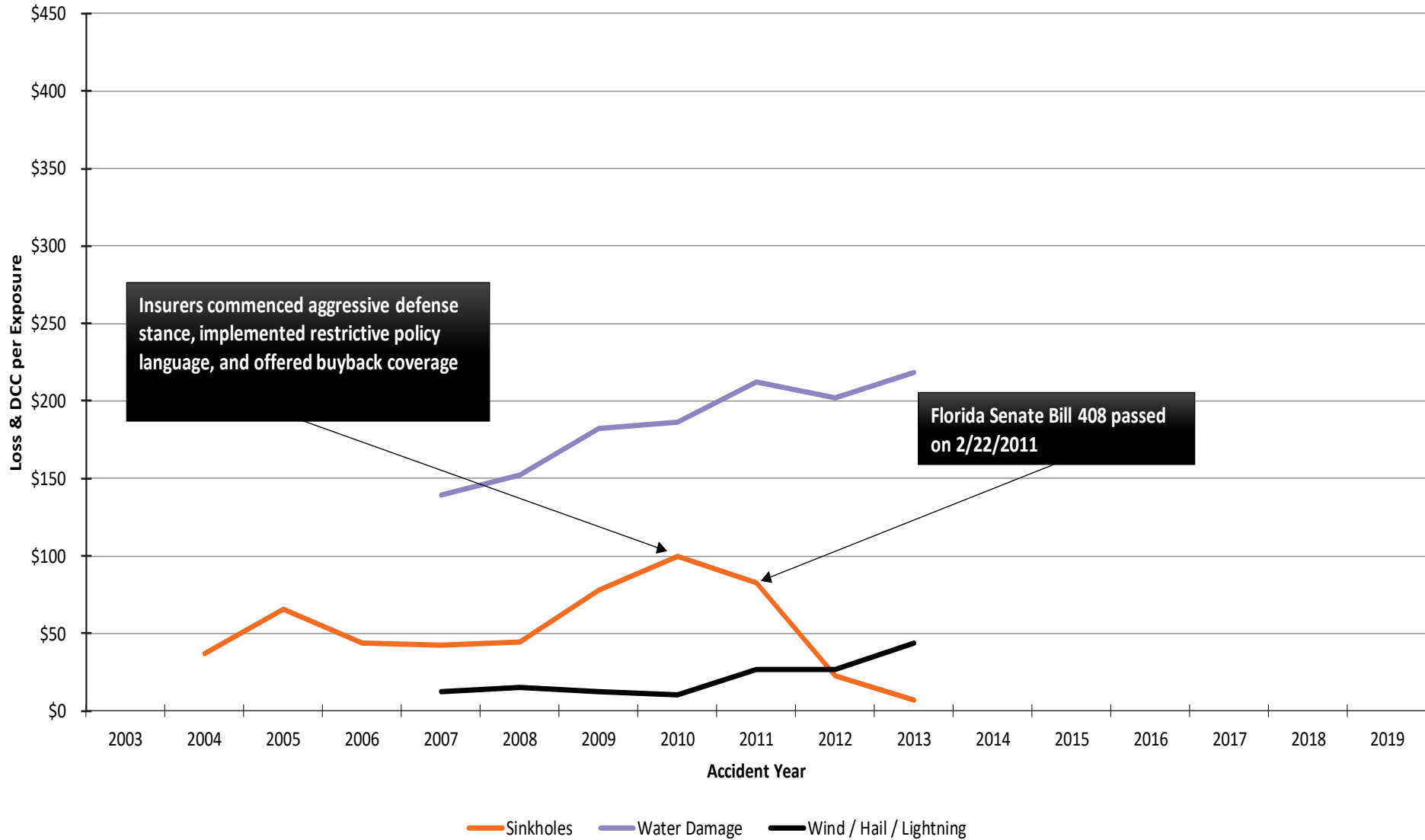
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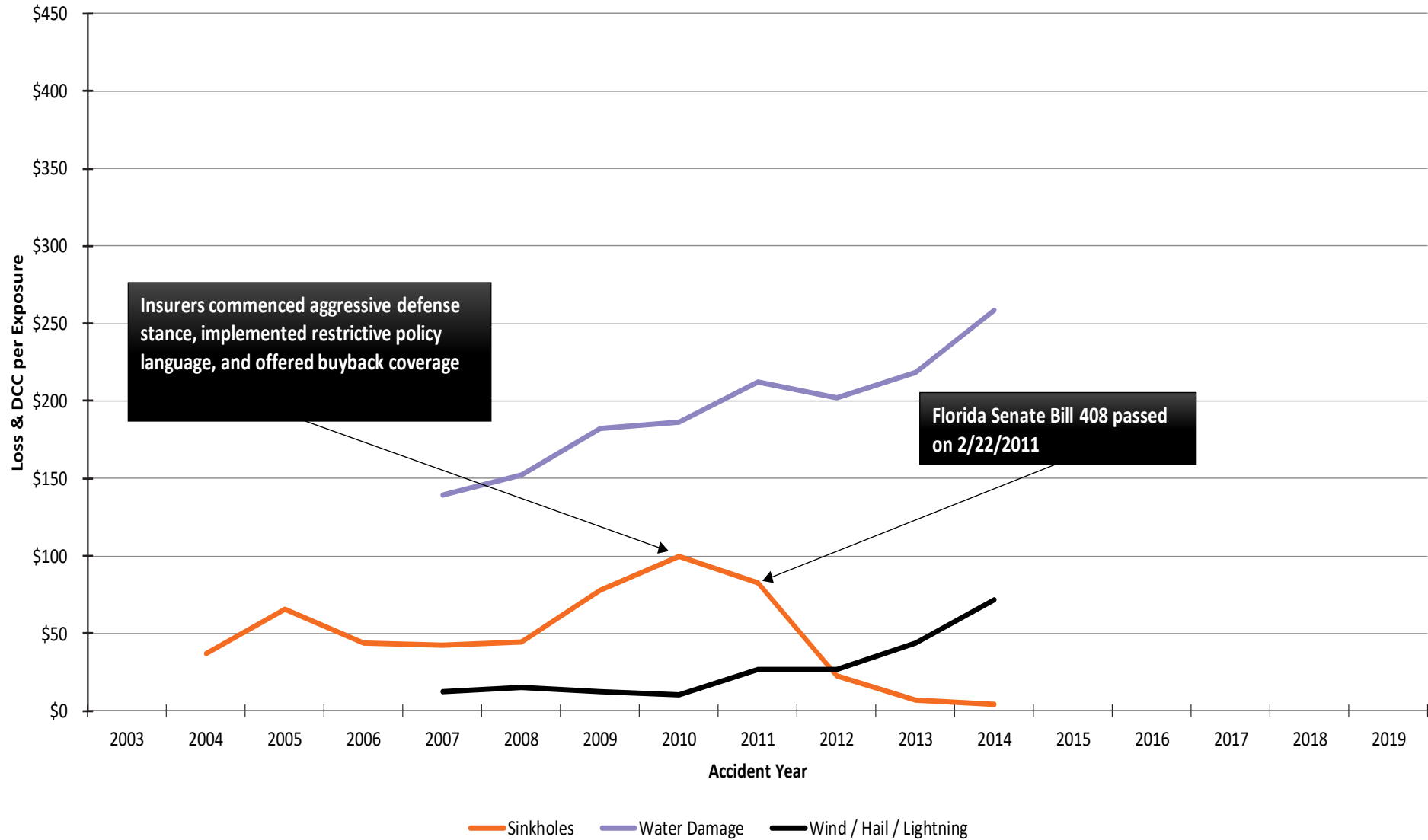
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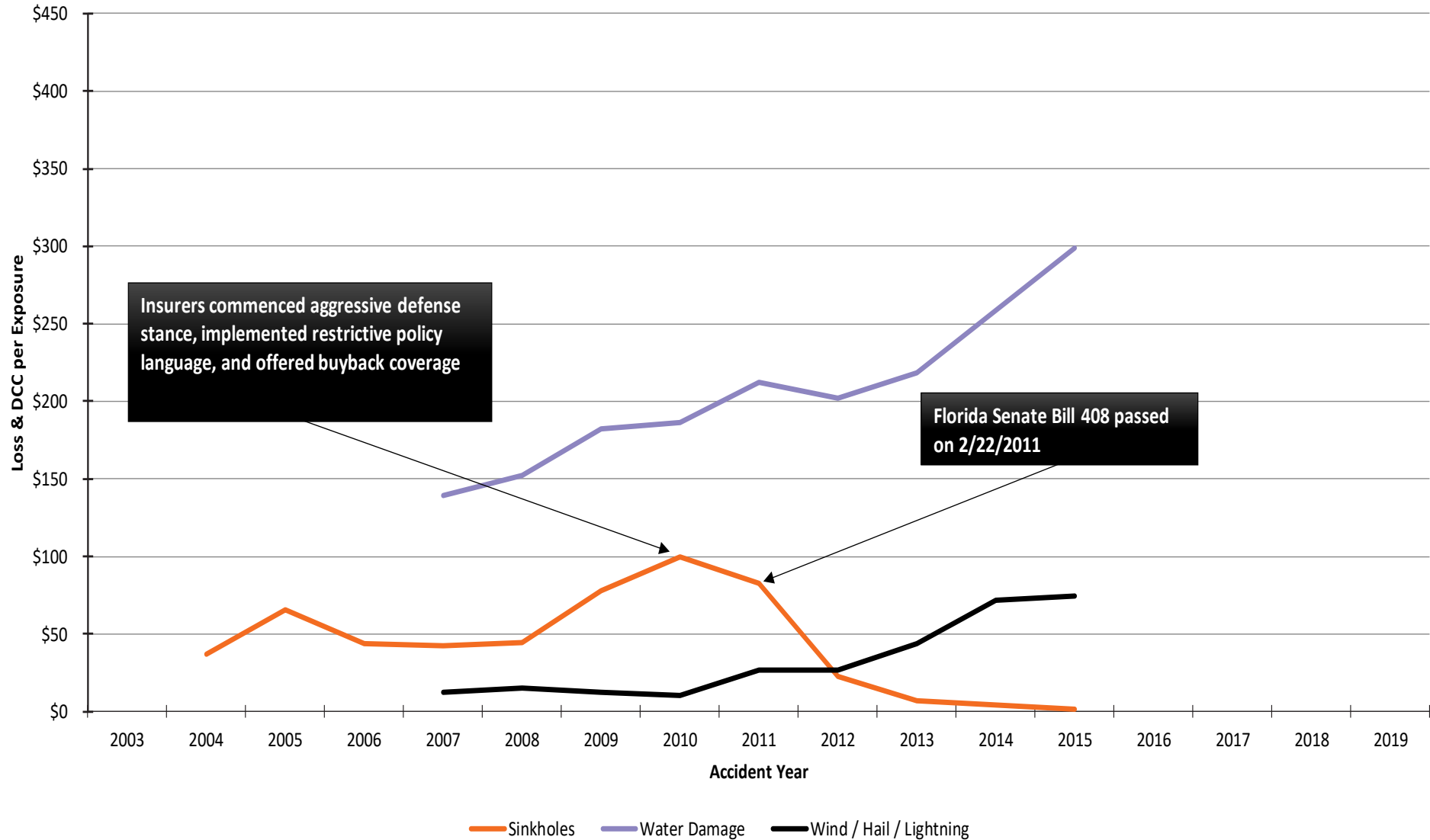
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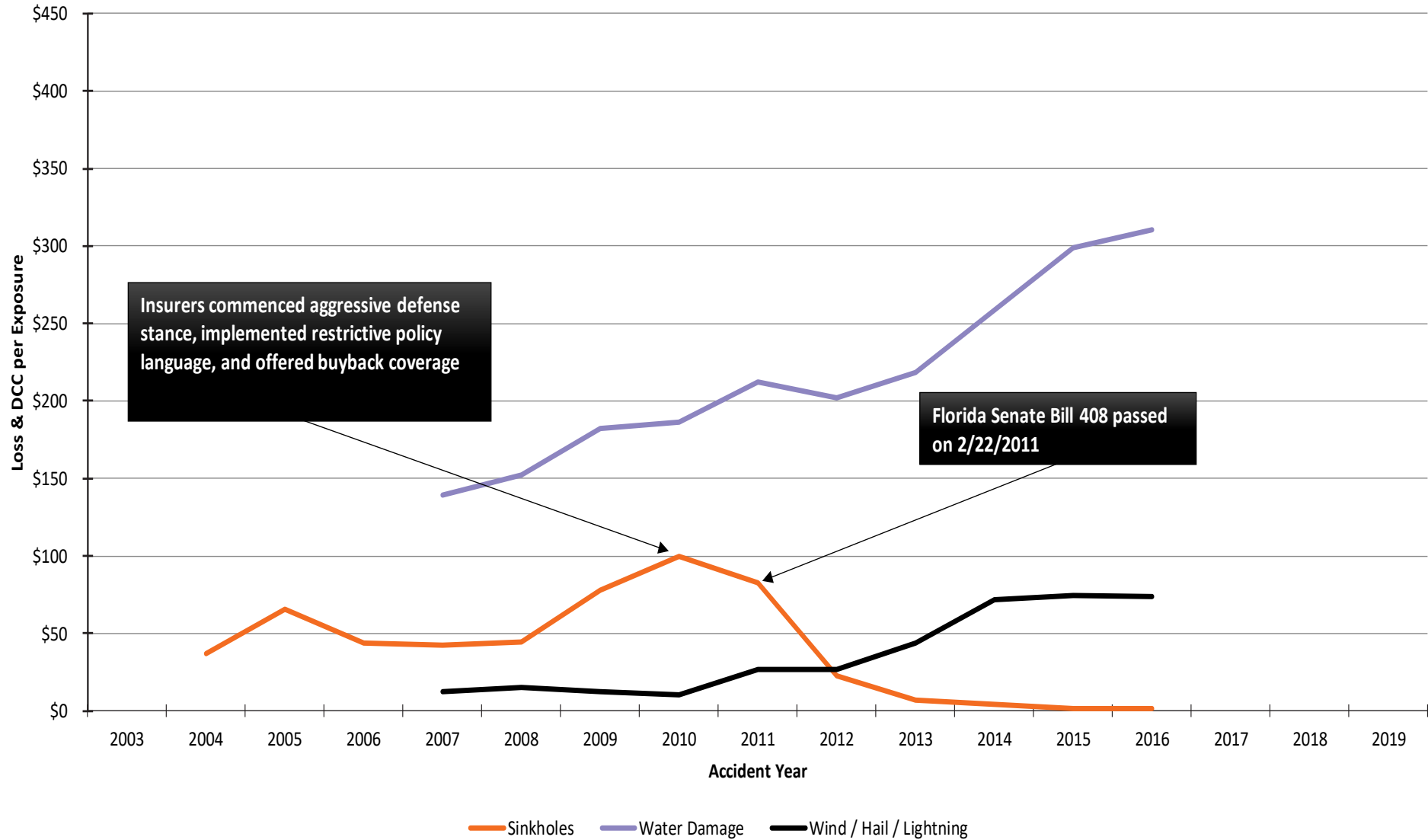
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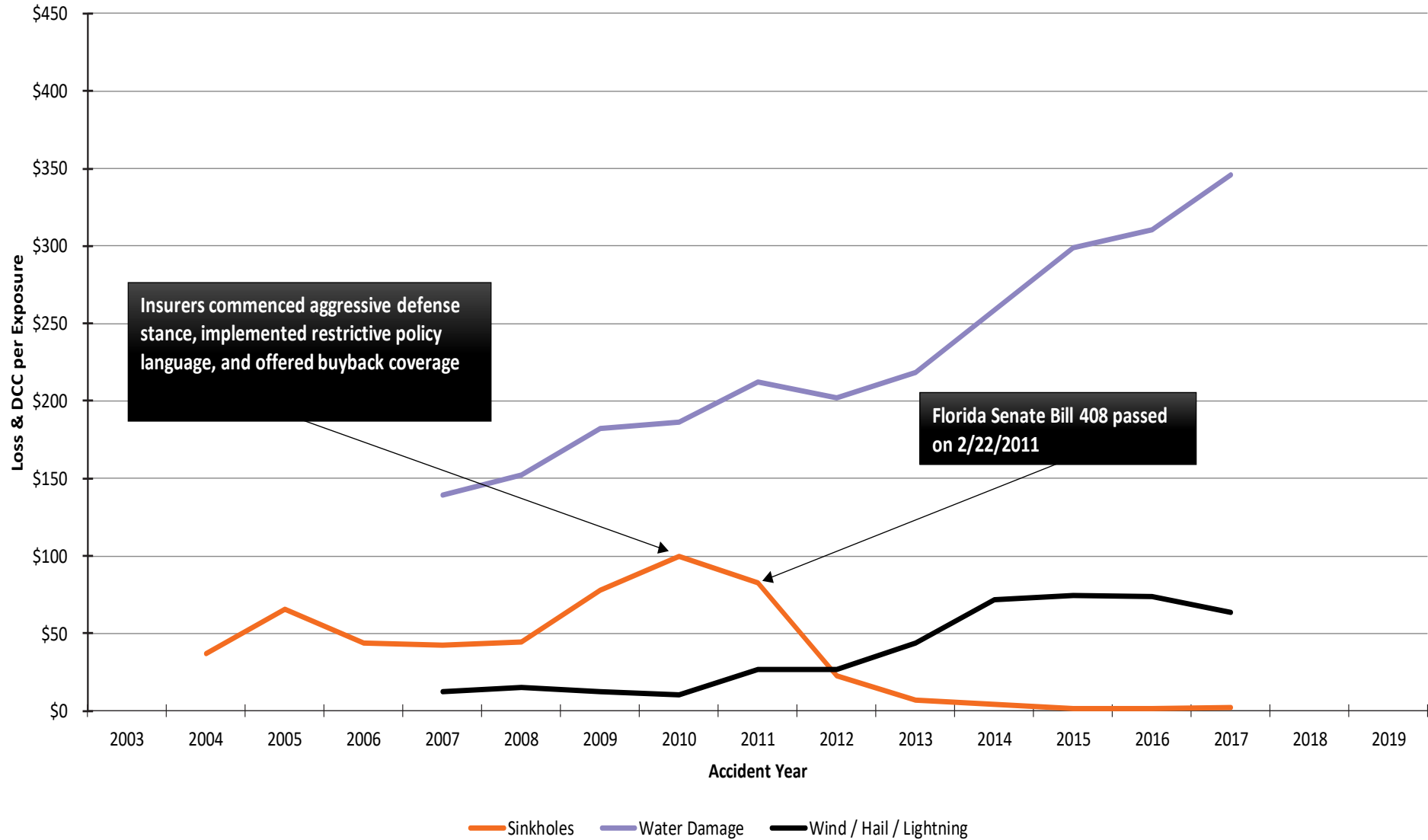
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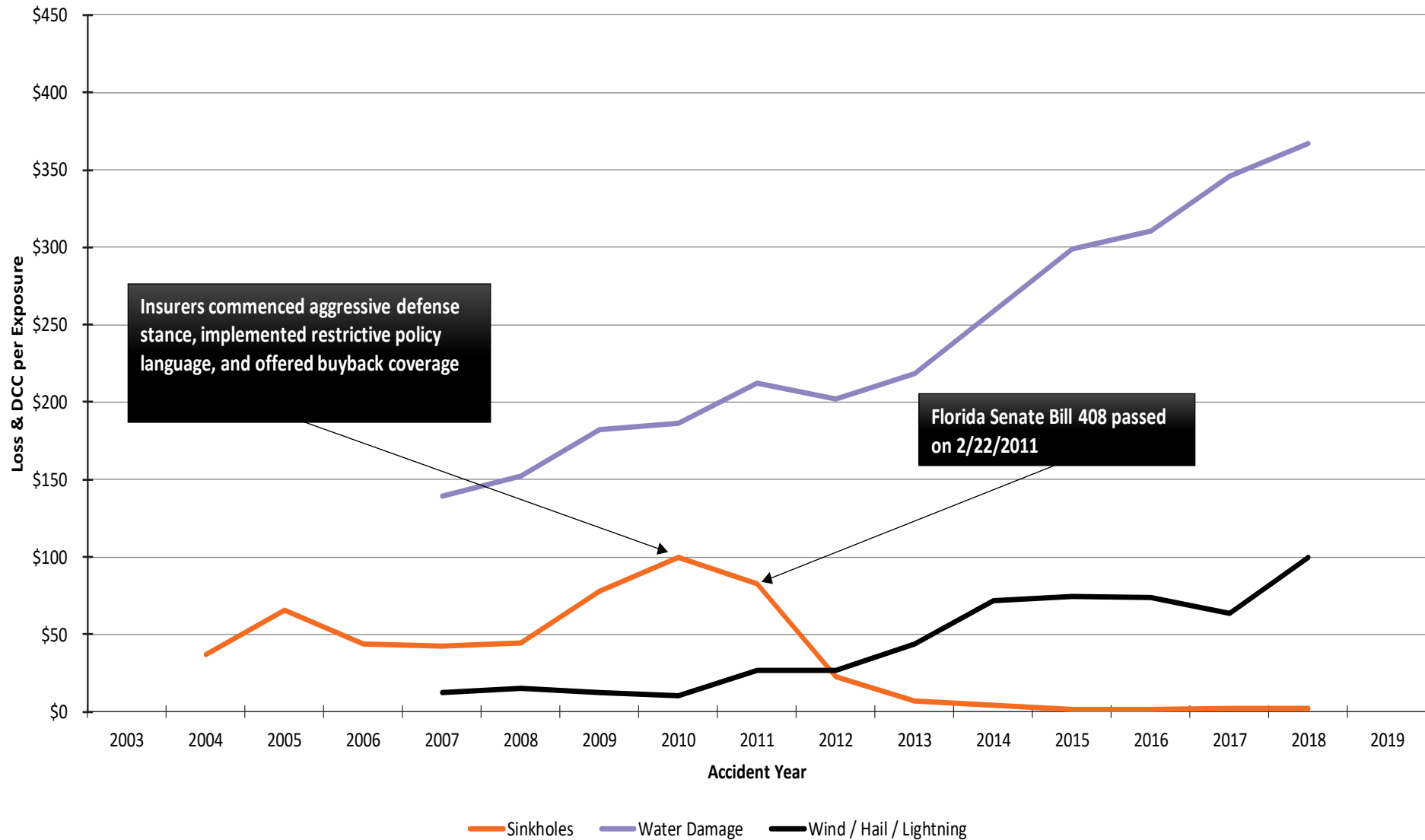
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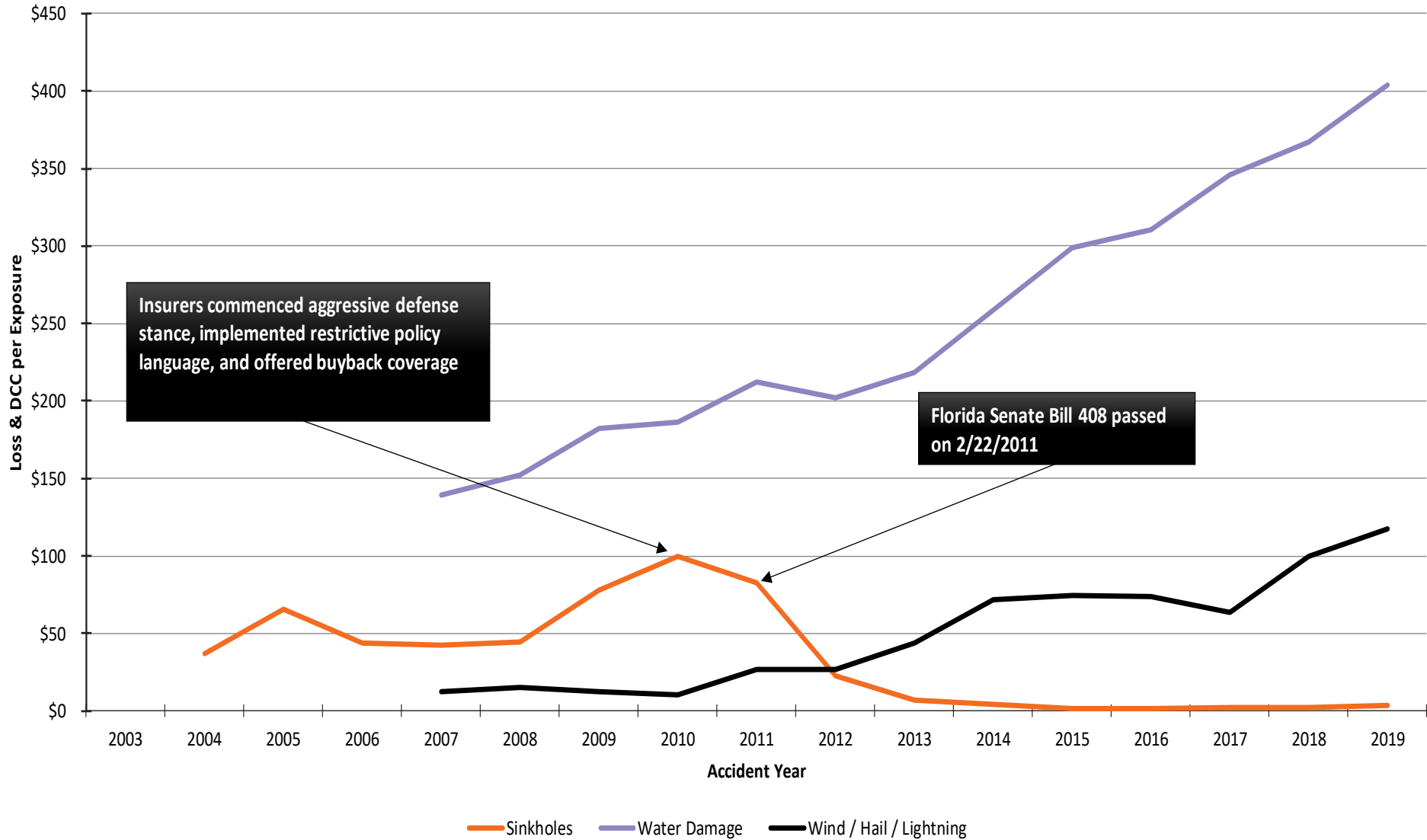


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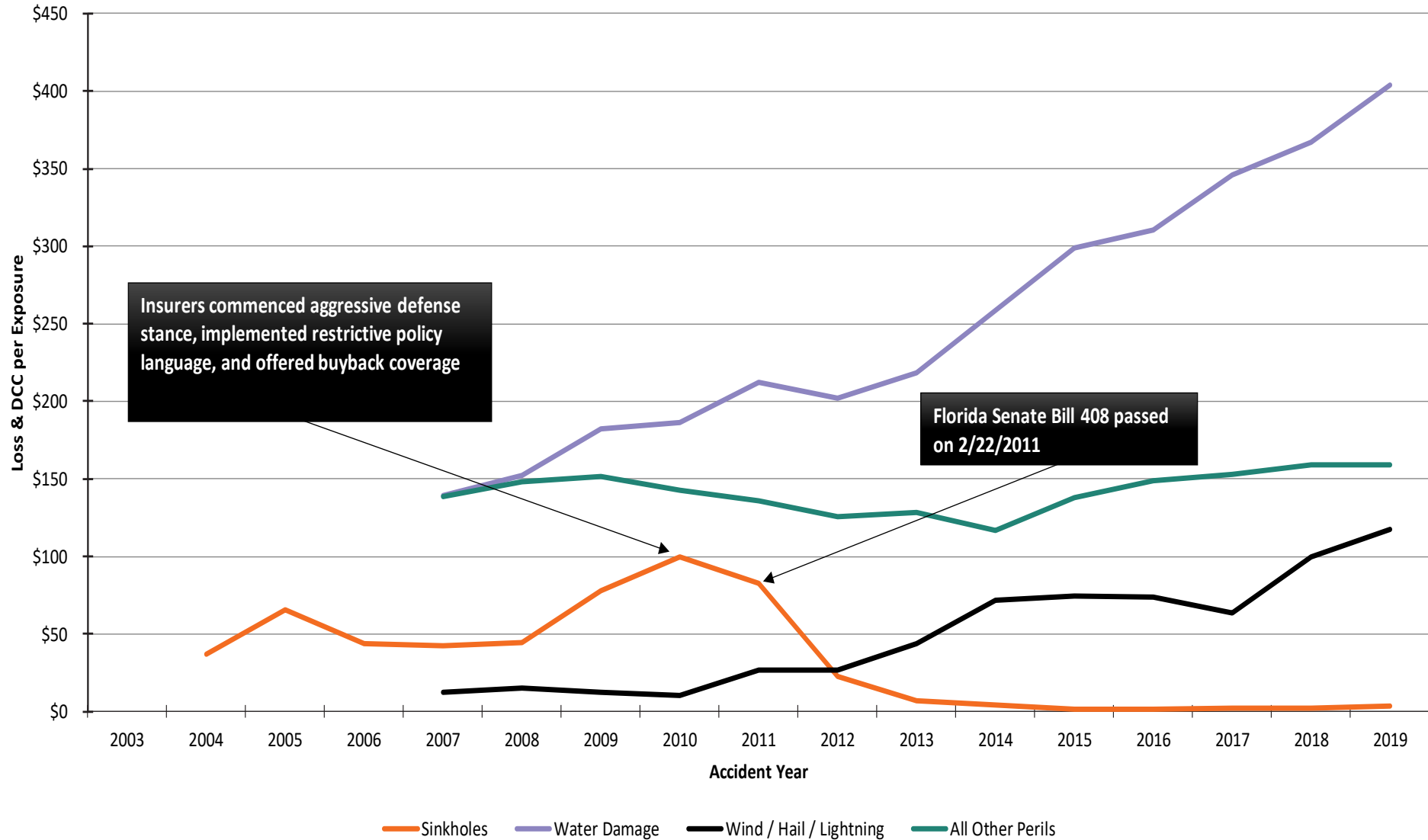




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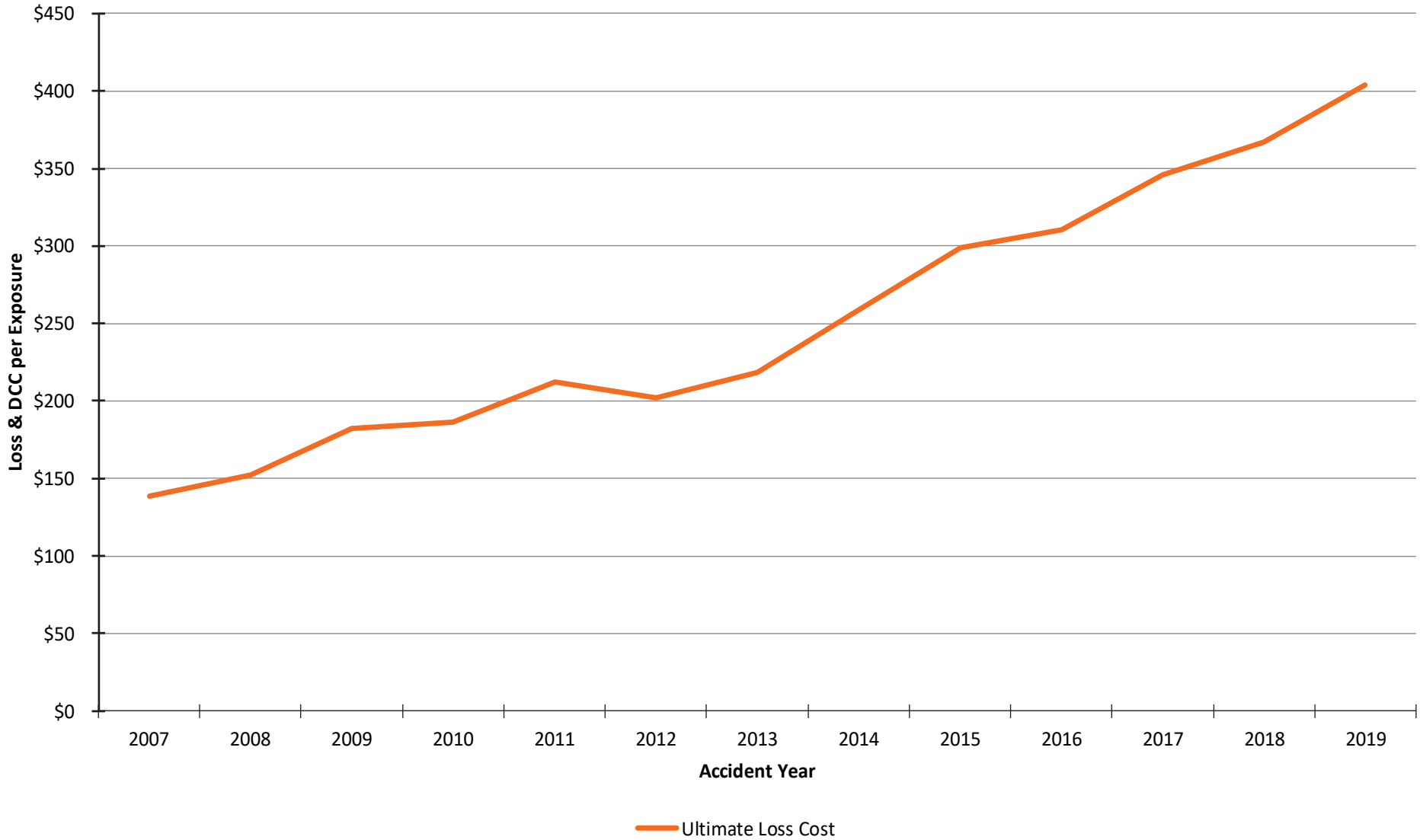
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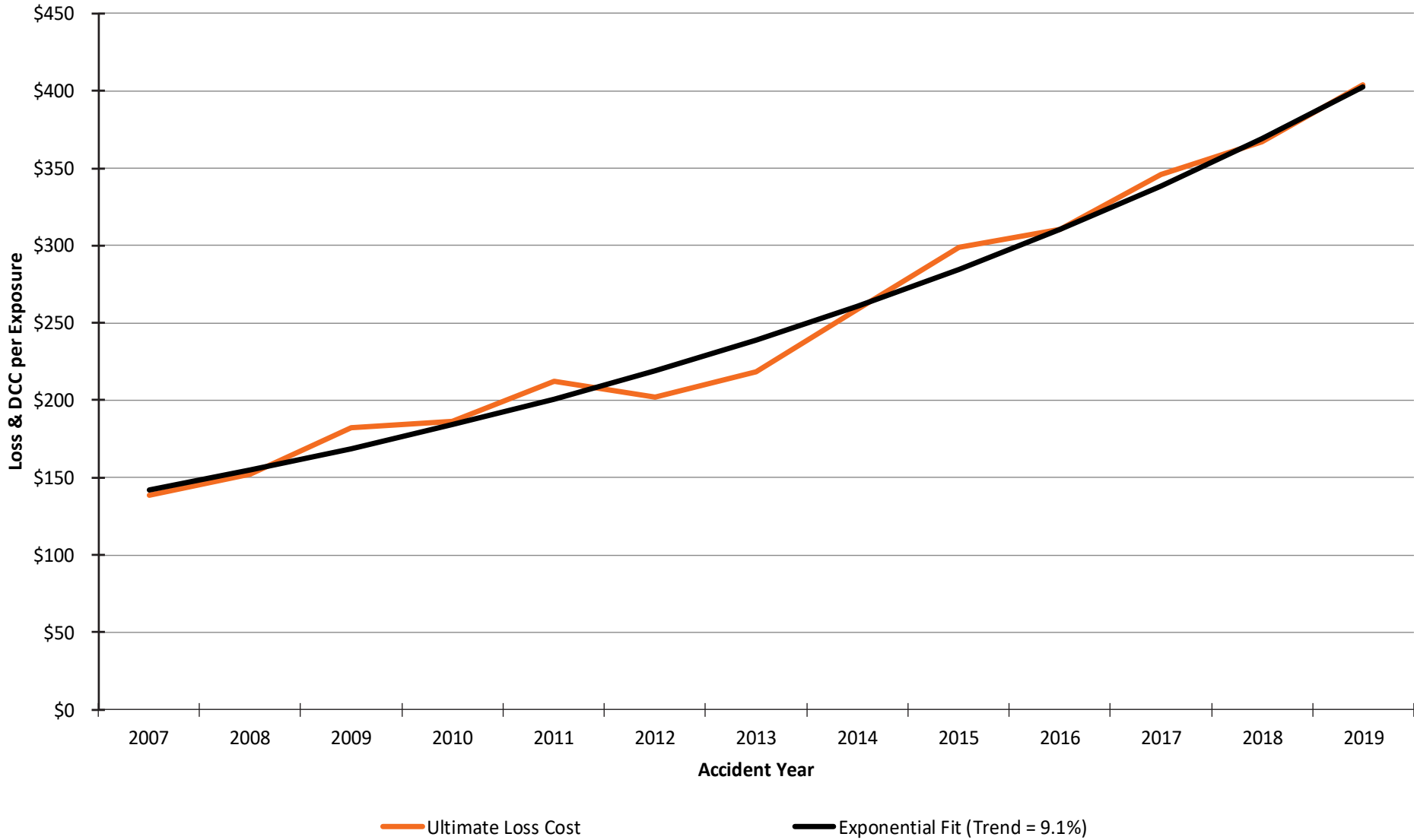
# Assignment of Benefits: Water Damage



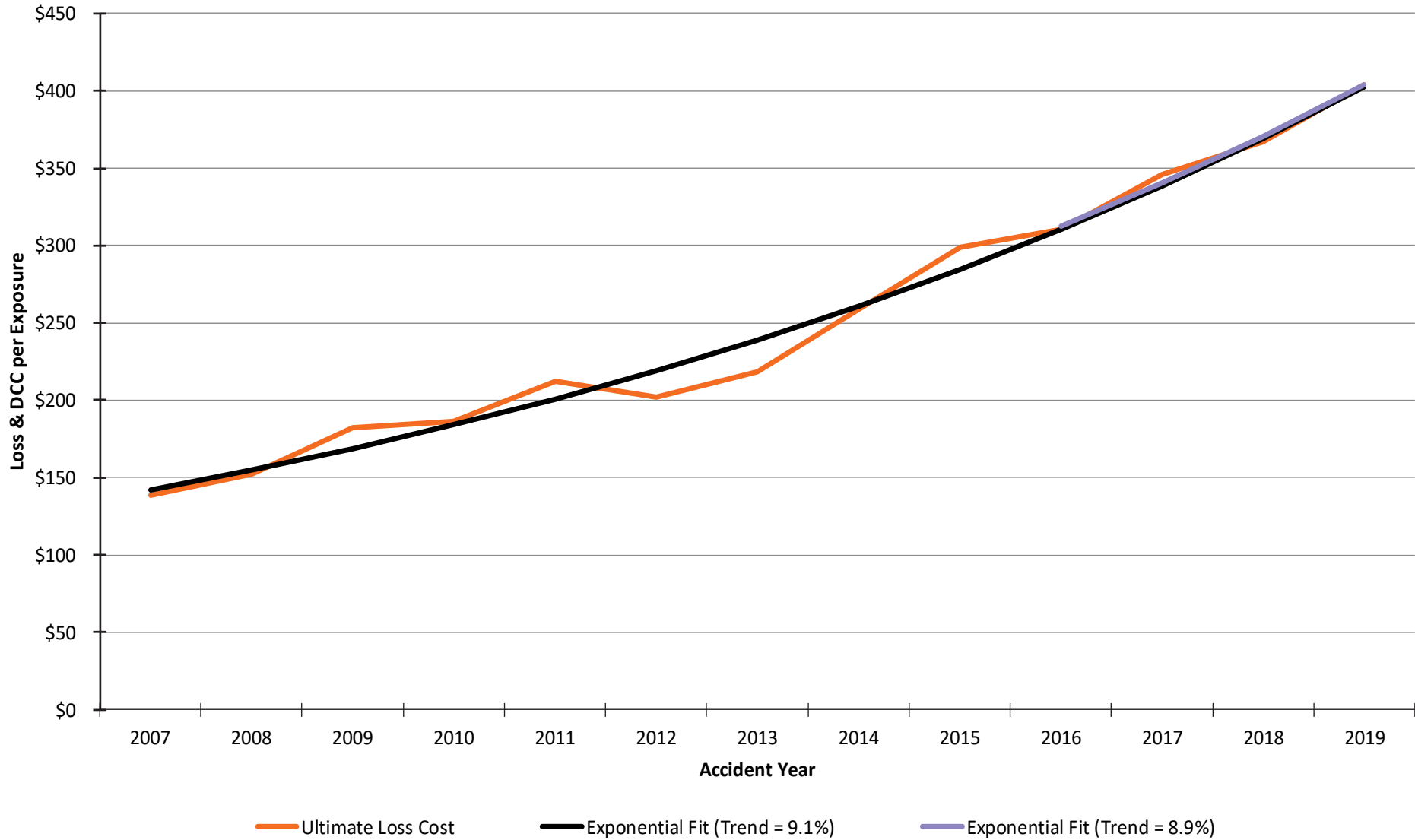
# Water Damage: Loss Cost



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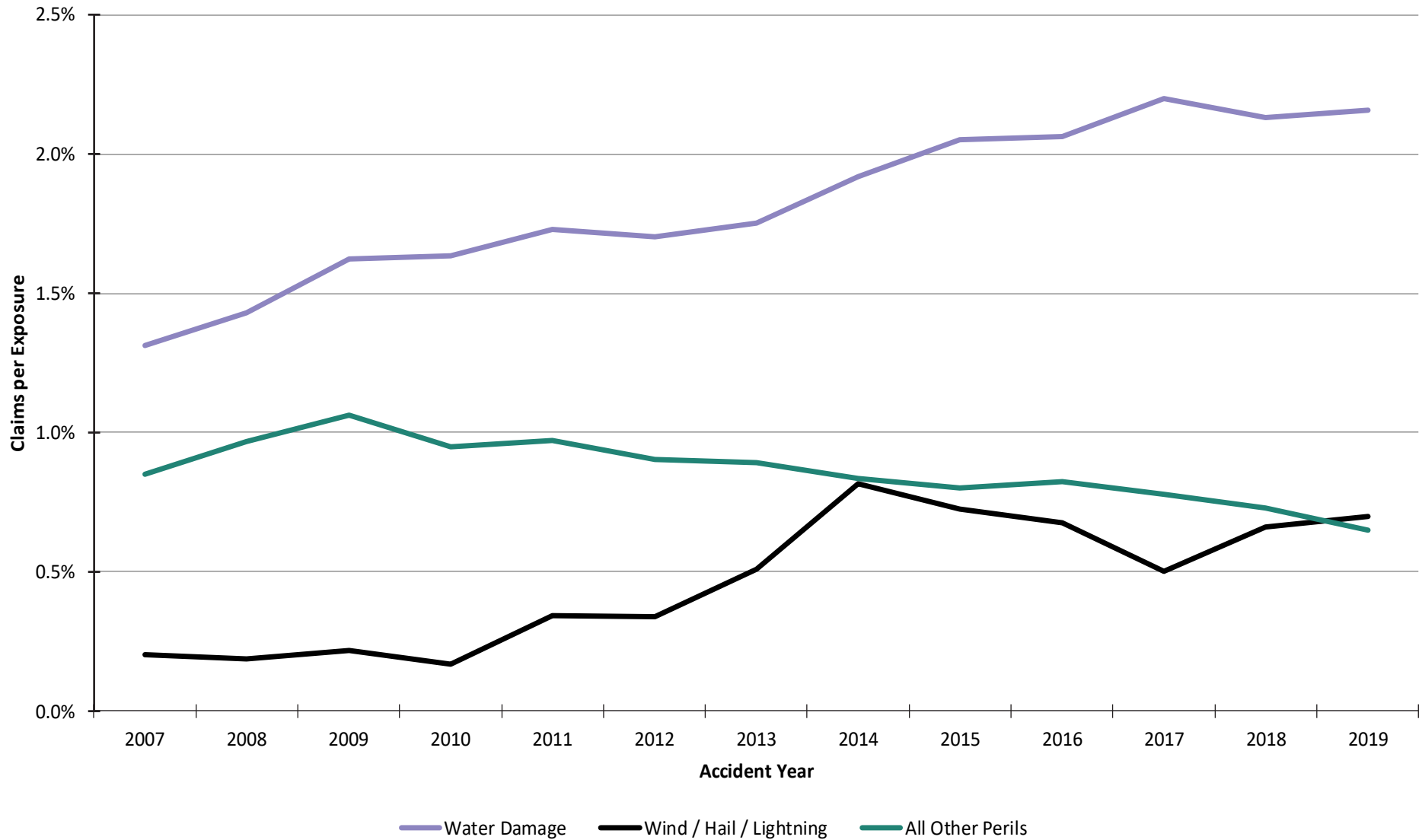
# Water Damage: Loss Cost



# By-Segment Comparison

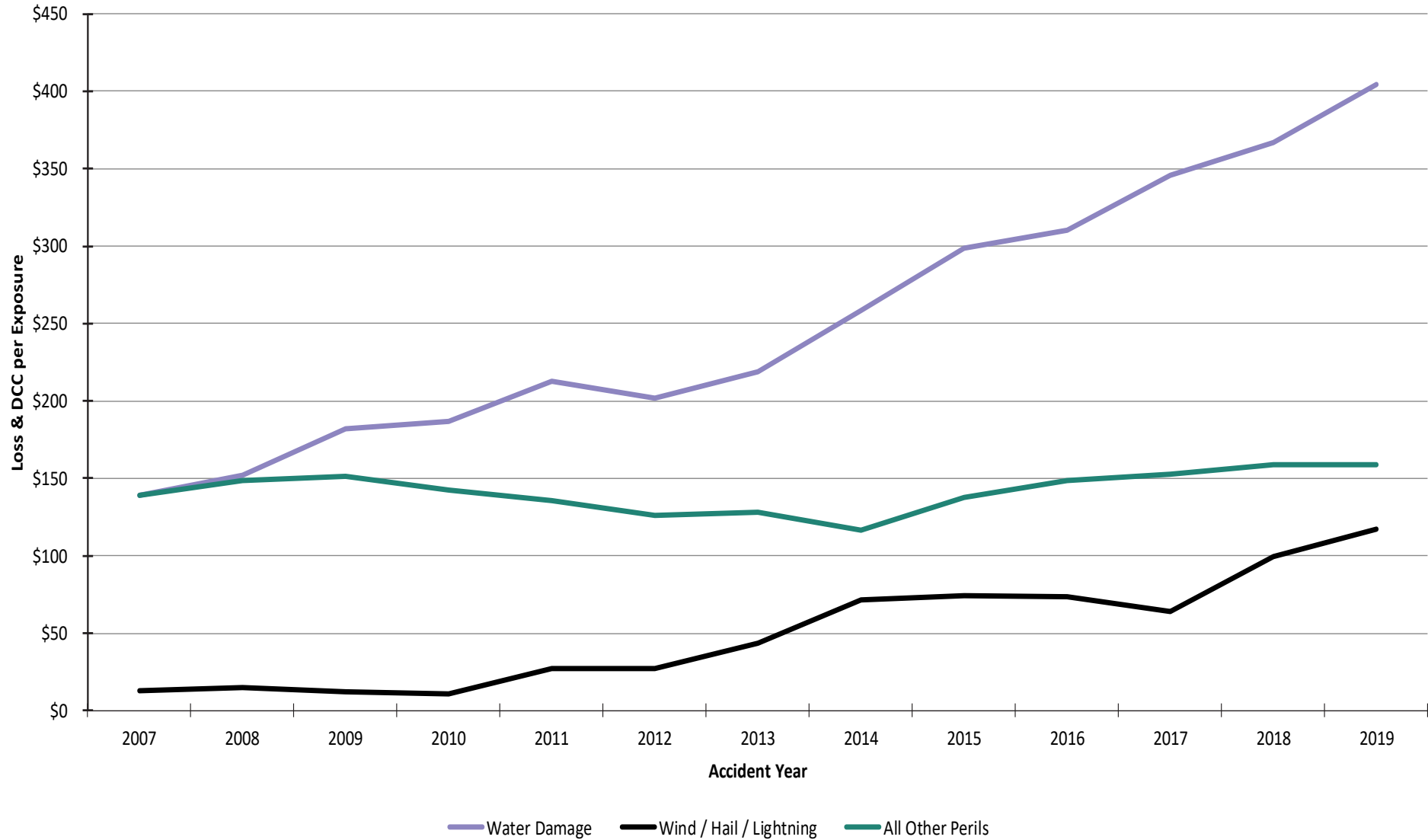


# By-Segment Comparison: Frequency/Claim Distr.

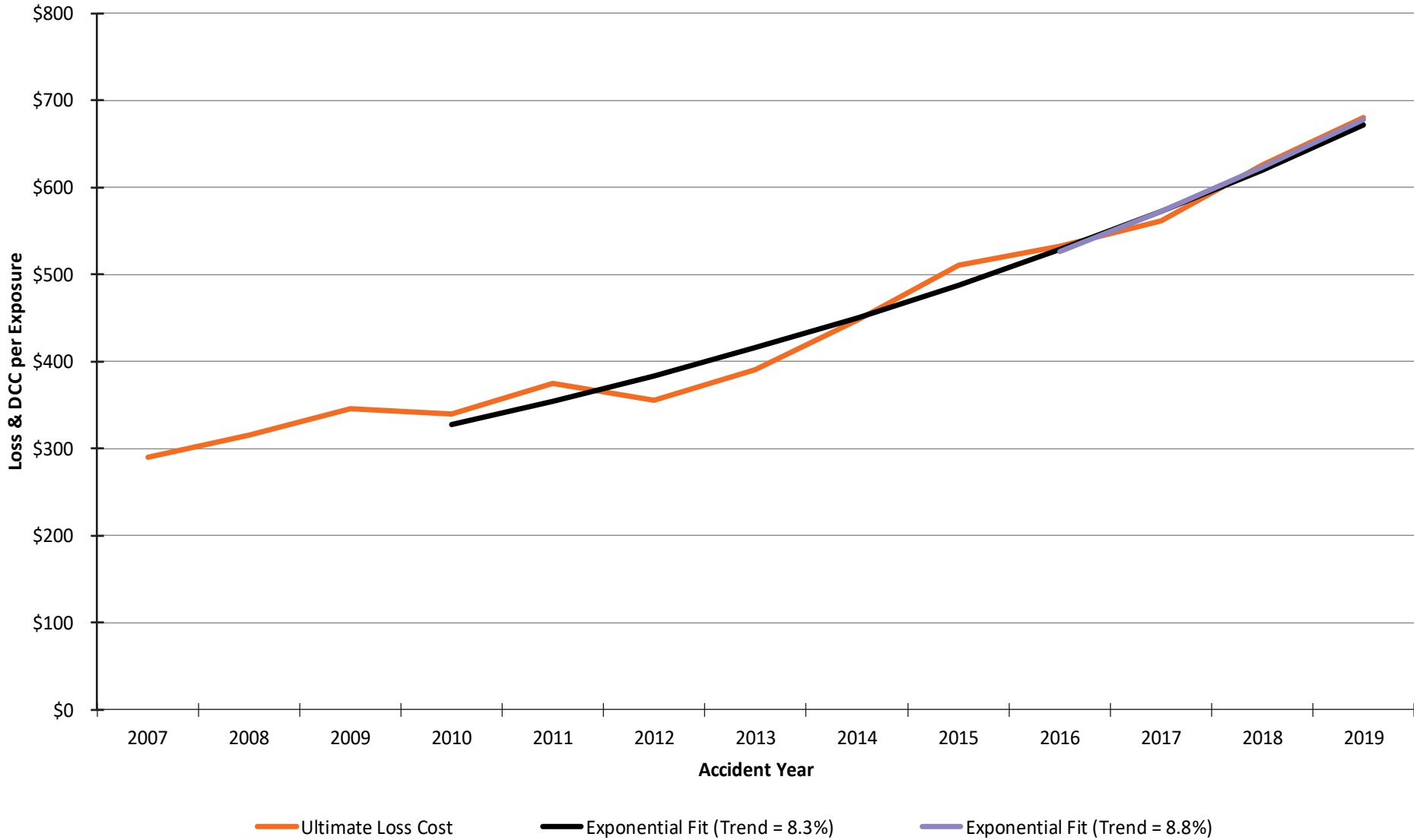




# By-Segment Comparison: Loss Cost



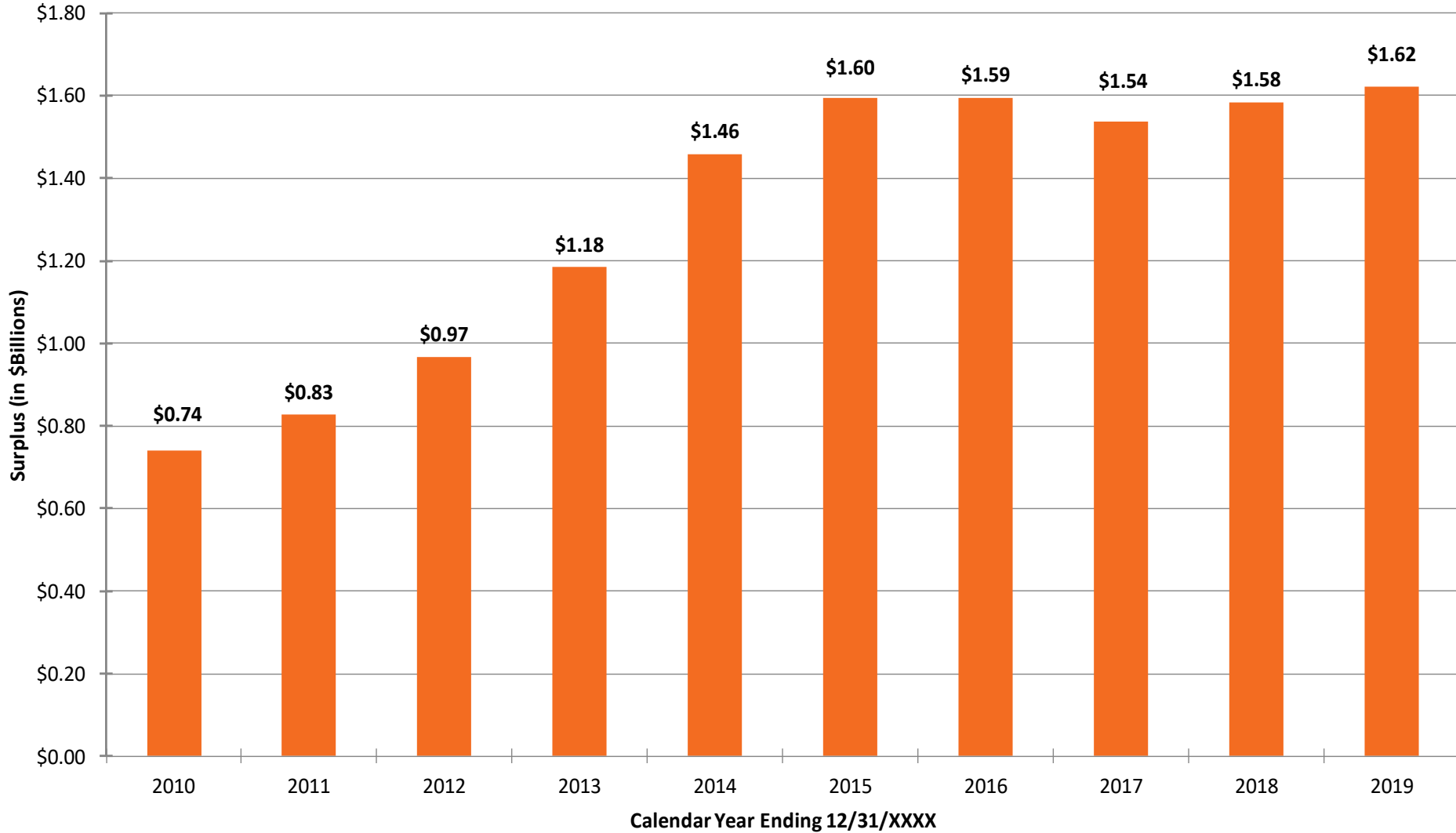
# Aggregate Non-CAT Non-Sinkhole: Loss Cost



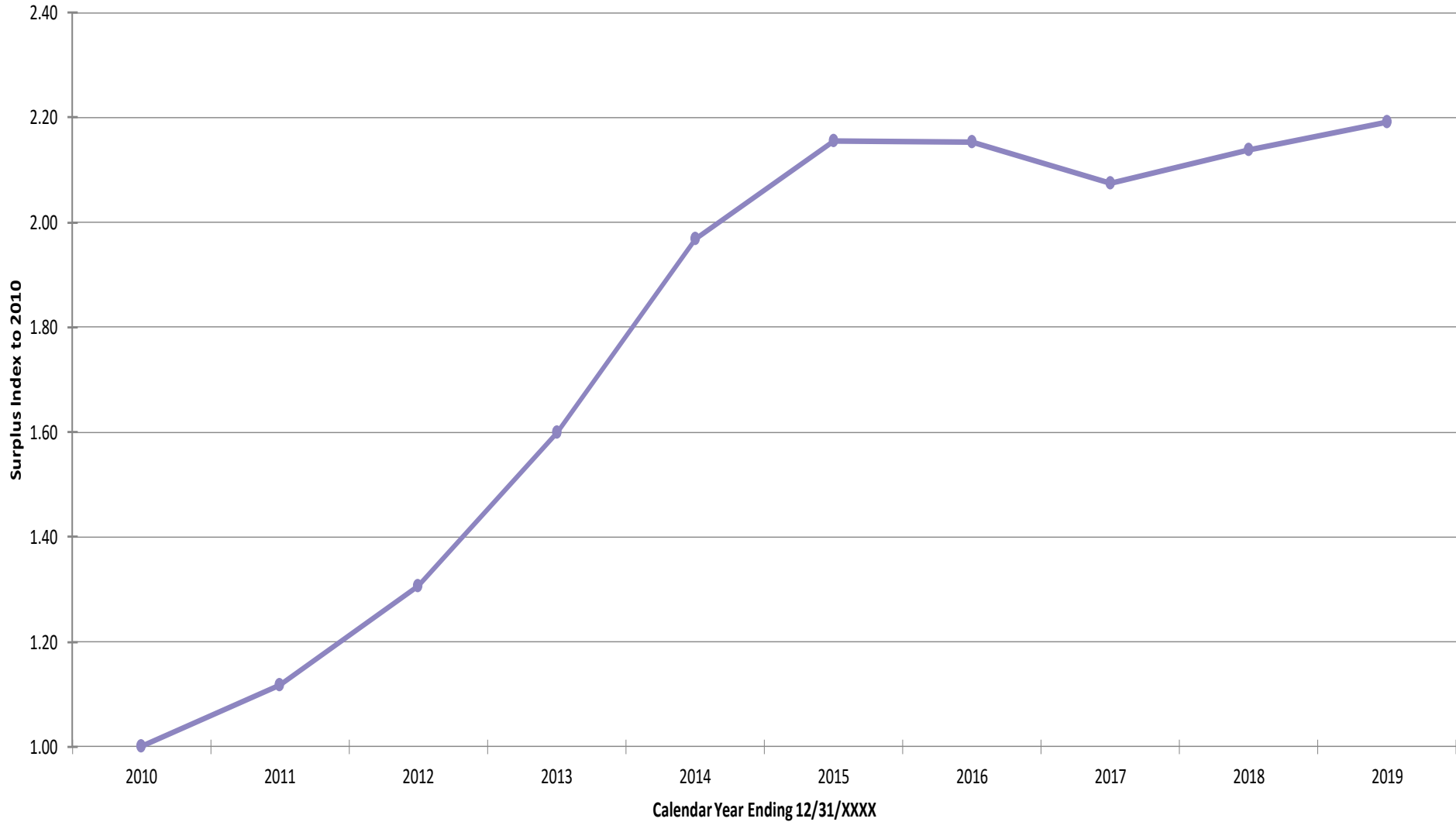
# Assignment of Benefits Era: Financial Results



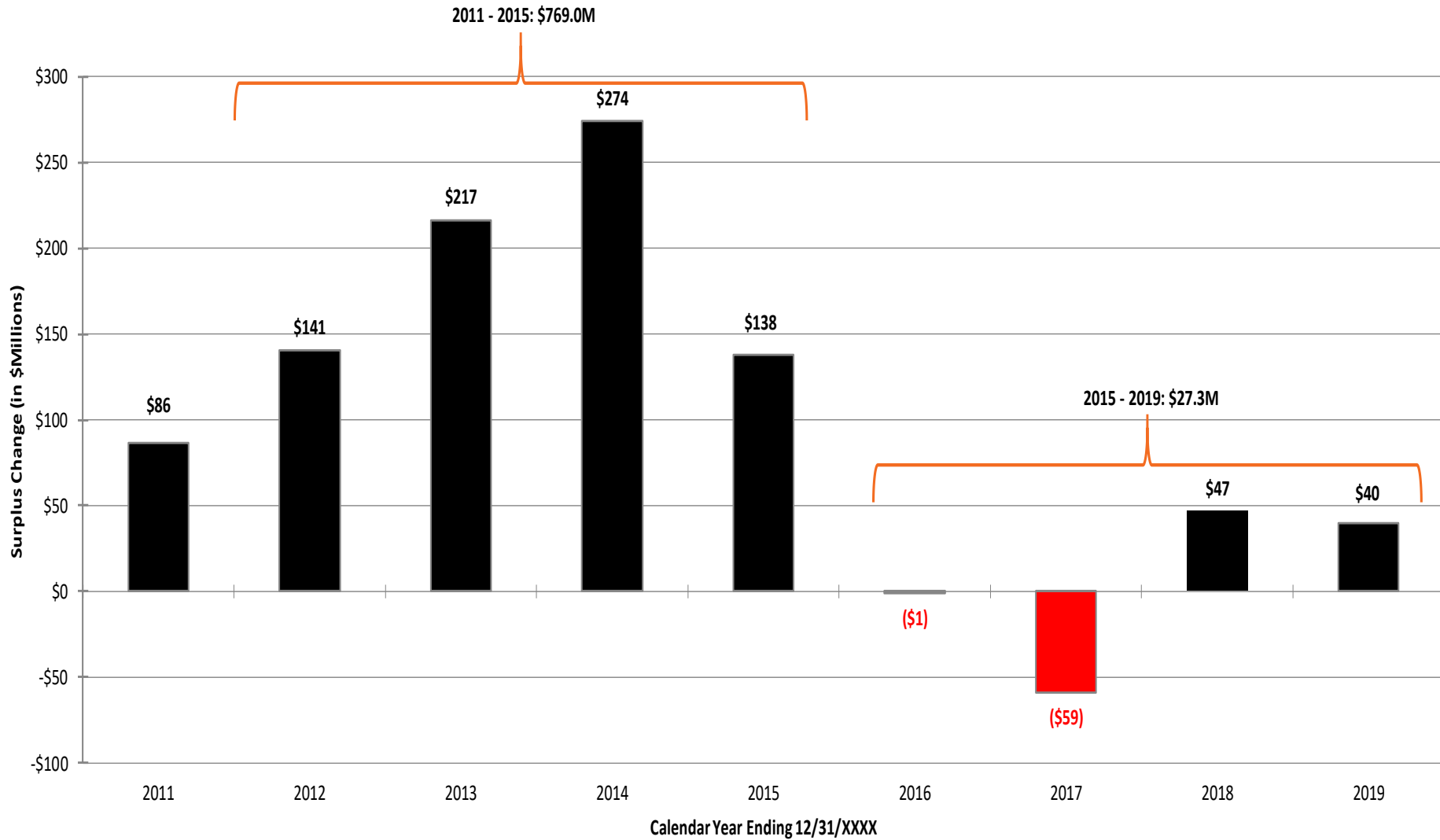
# Surplus



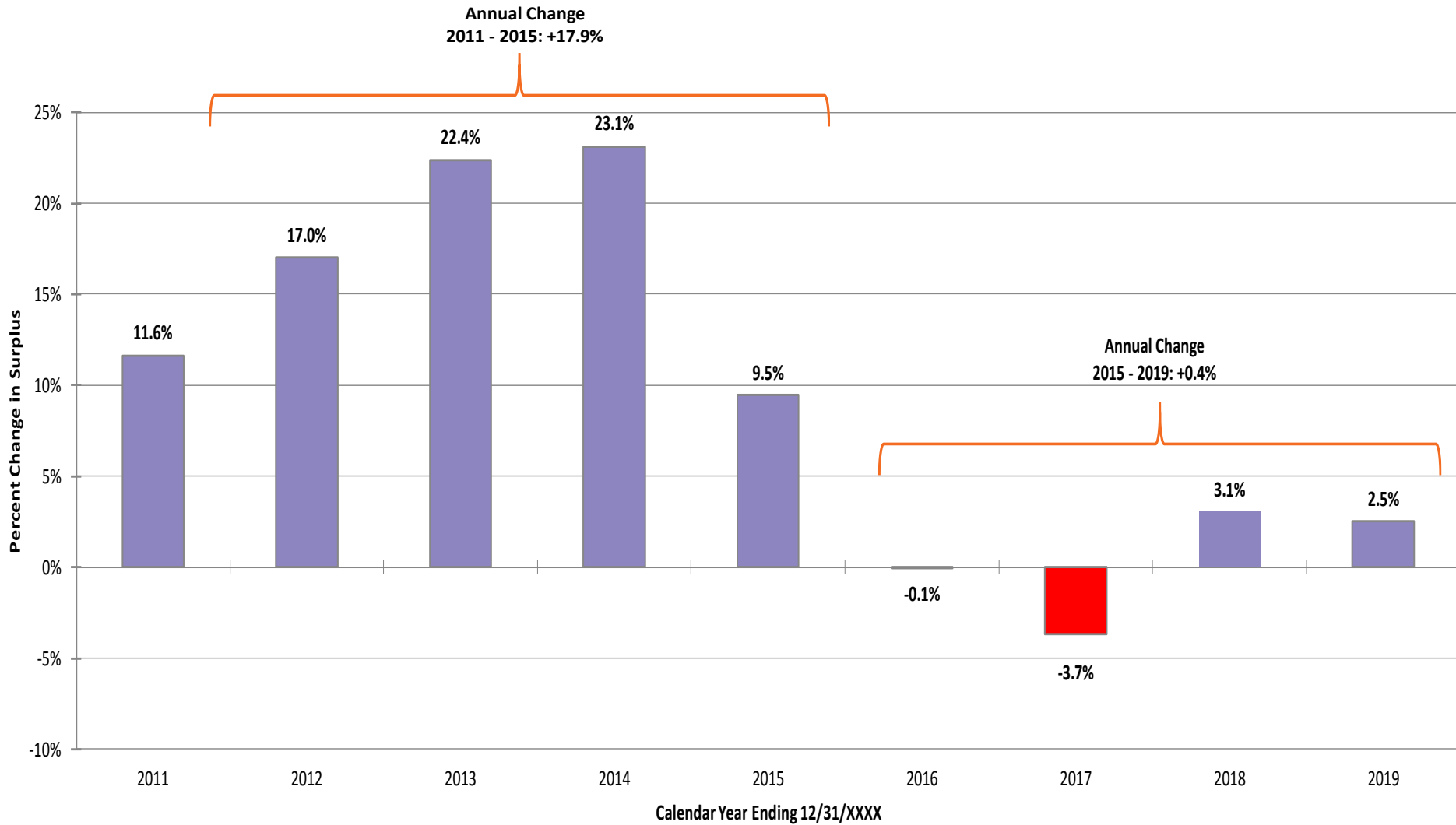
# Surplus: Relative to 2010



# Change in Surplus



# Percent Change in Surplus



# Traditional Insurance Risks

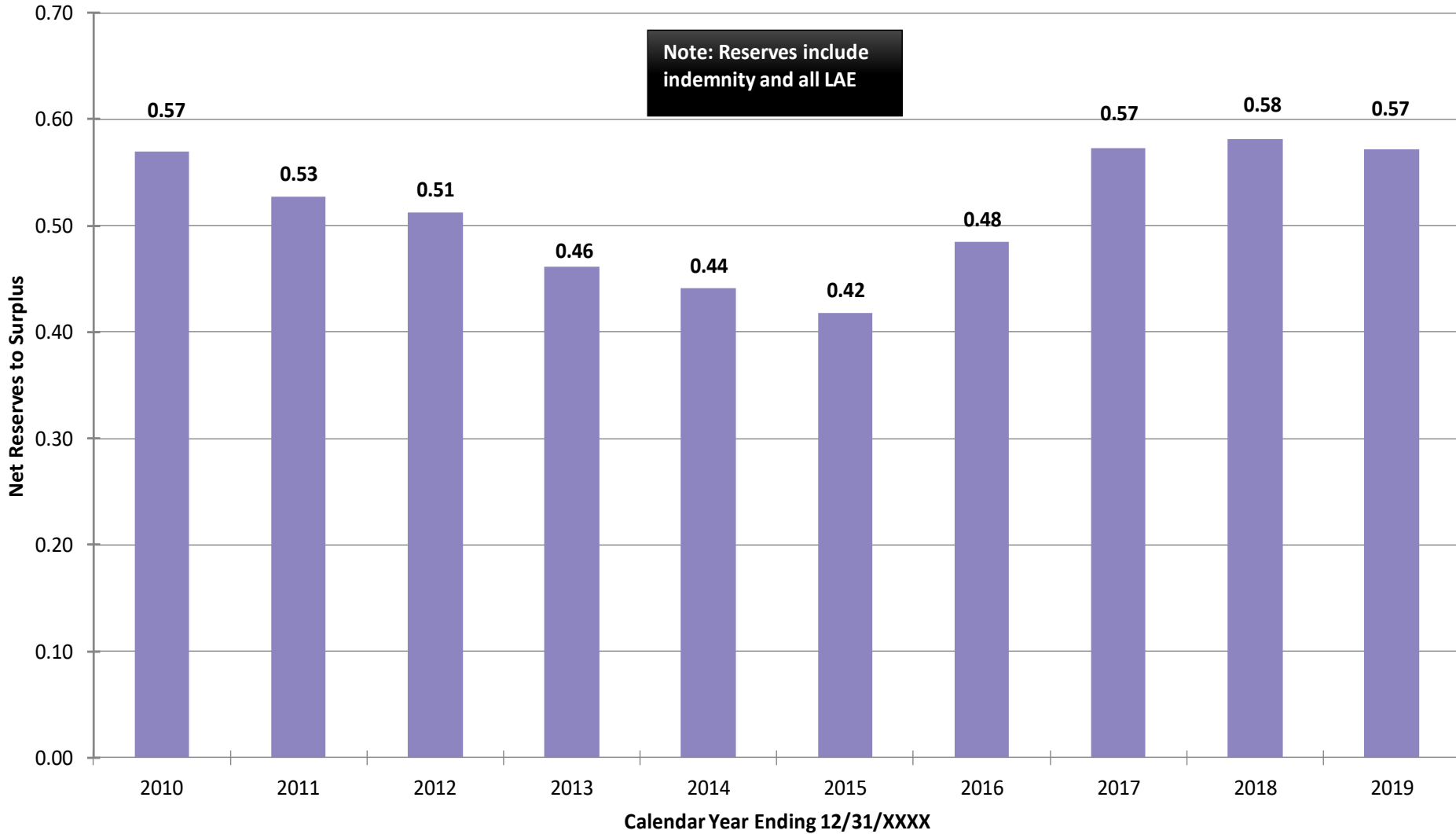
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- Reserve Risk
- Pricing Risk
- Reinsurance Risk

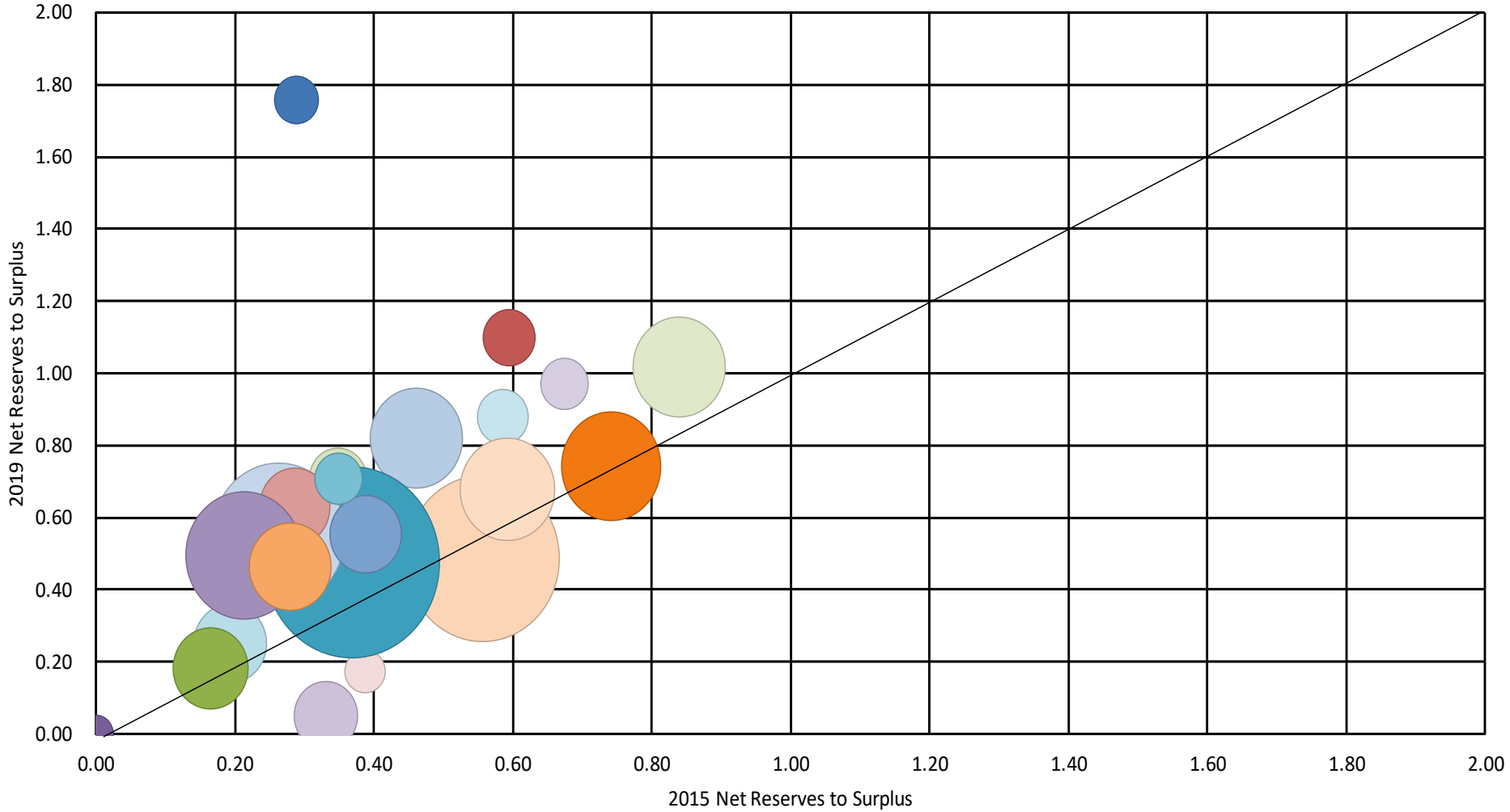




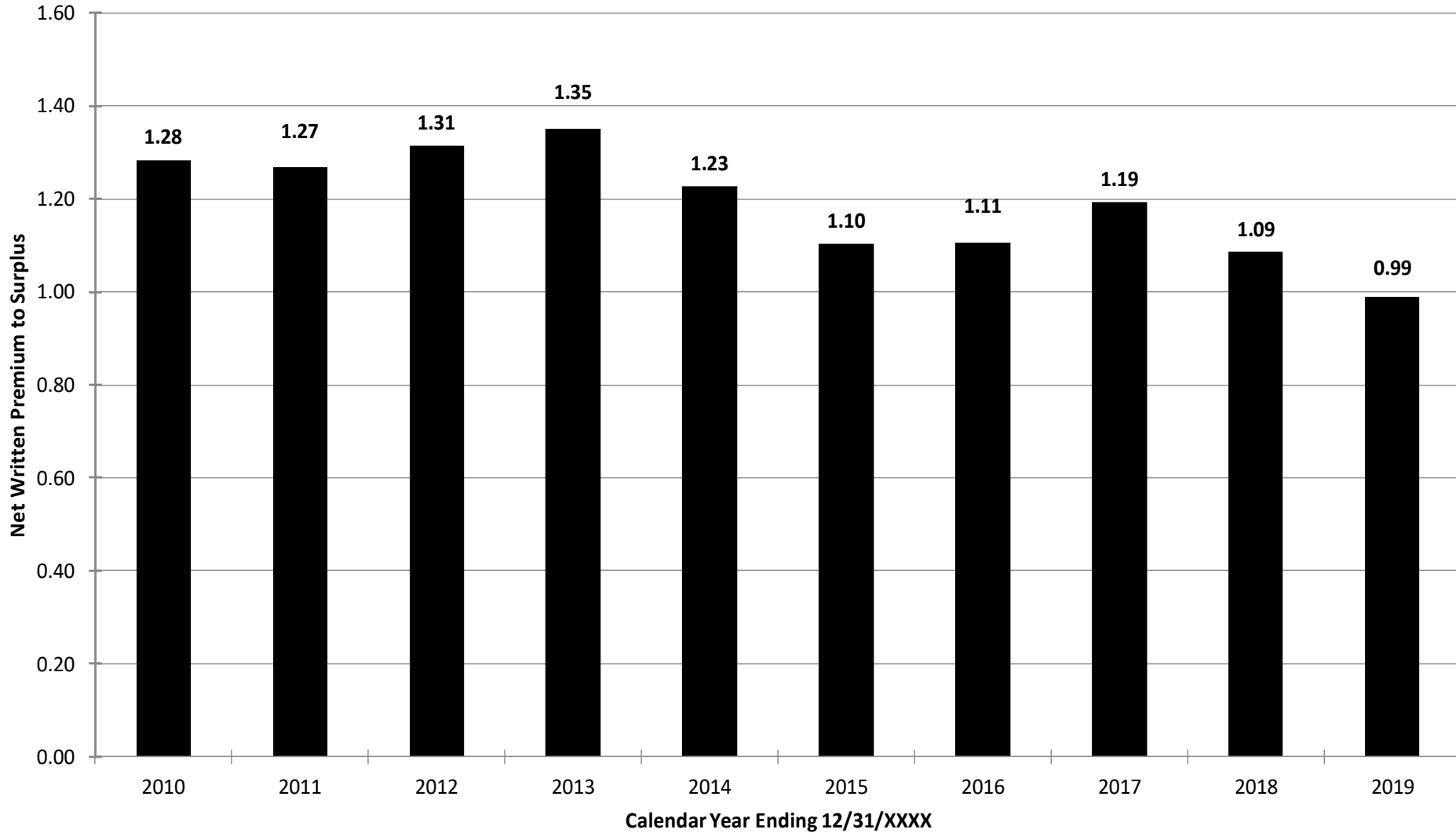
# Net Reserves to Surplus



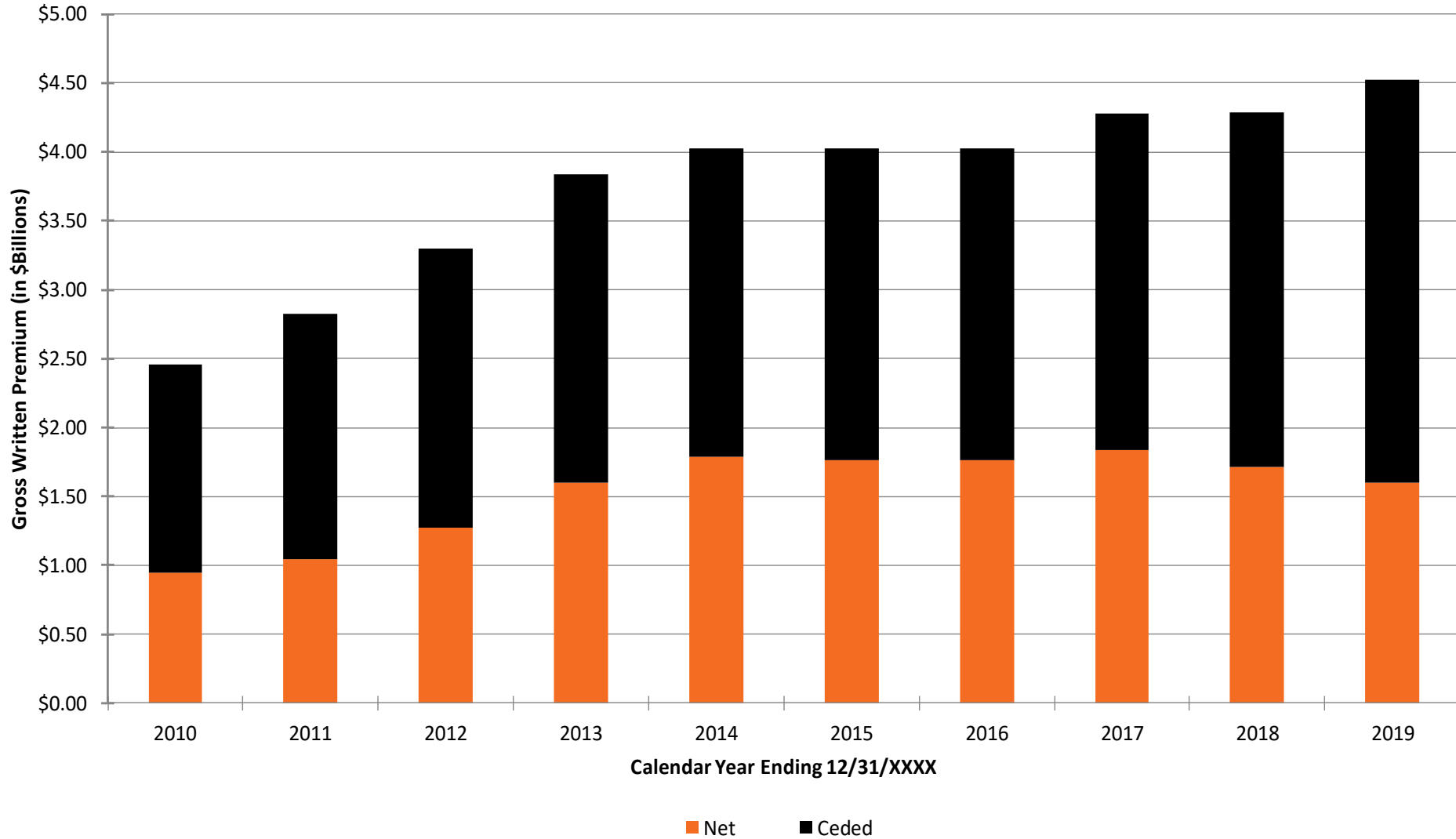
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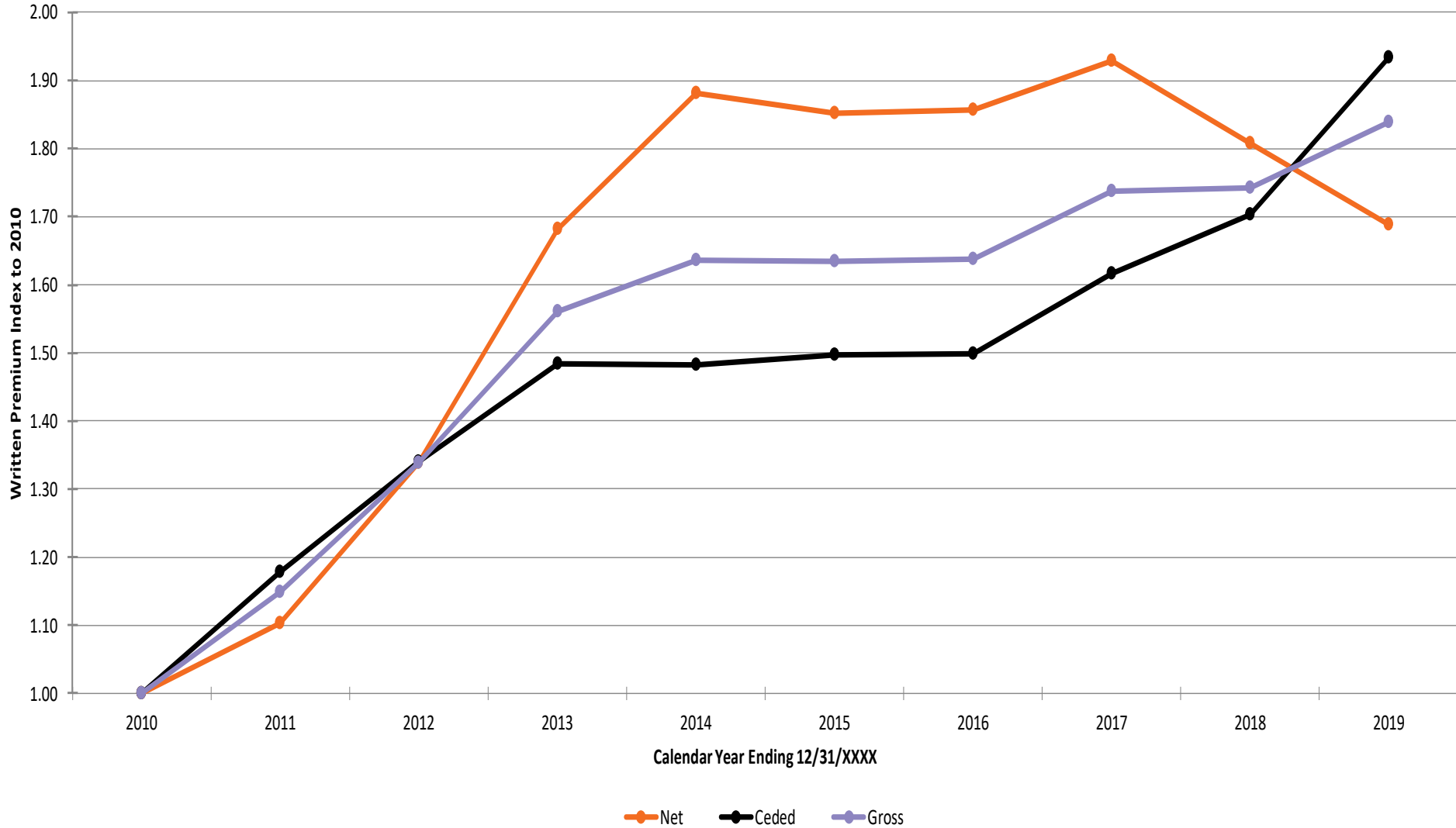
# Net Written Premium to Surplus



# Gross Written Premium by Component



# Gross Written Premium: Relative to 2010



# Profitability

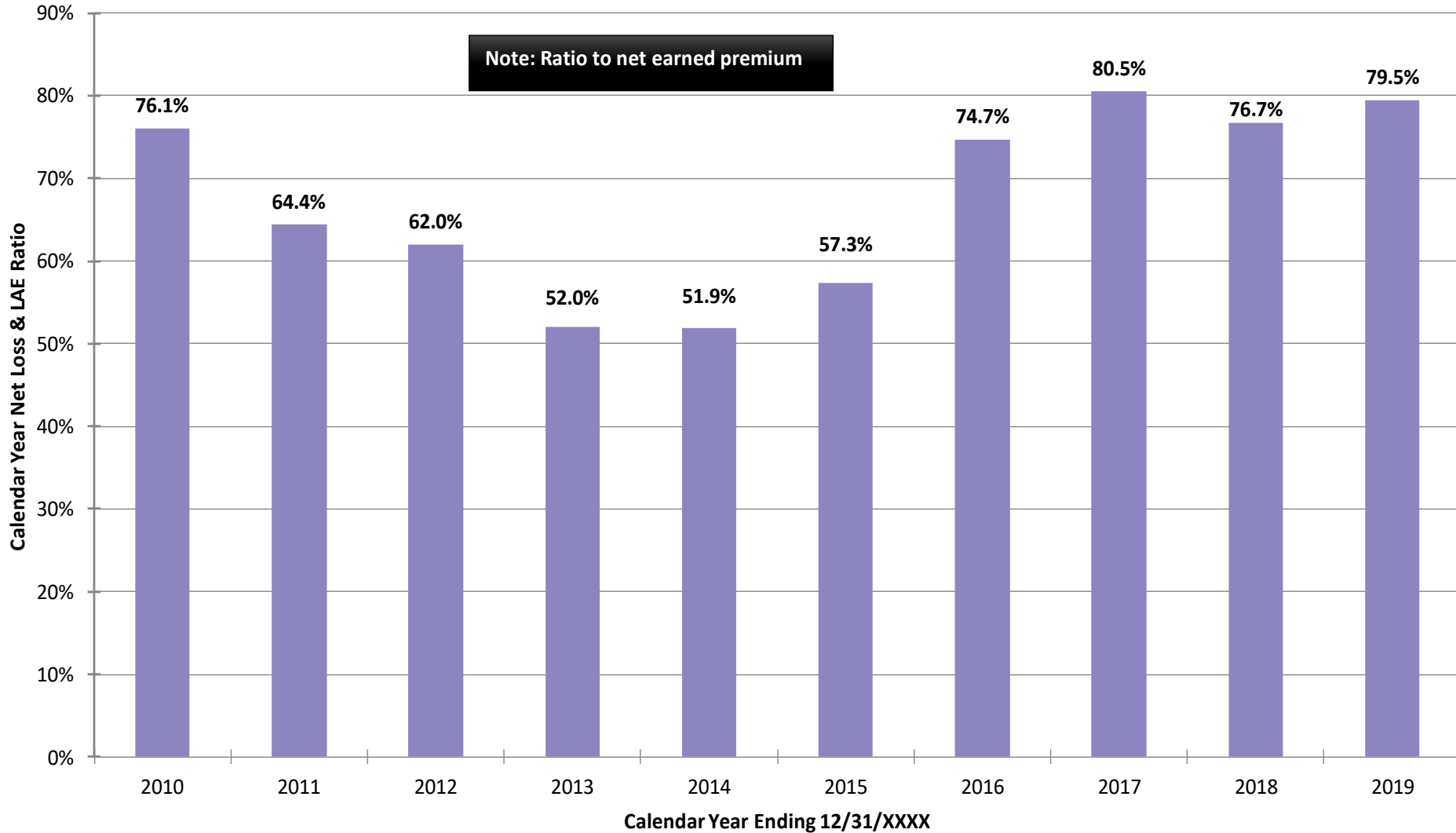
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- On a calendar year basis, measured by two key ratios:

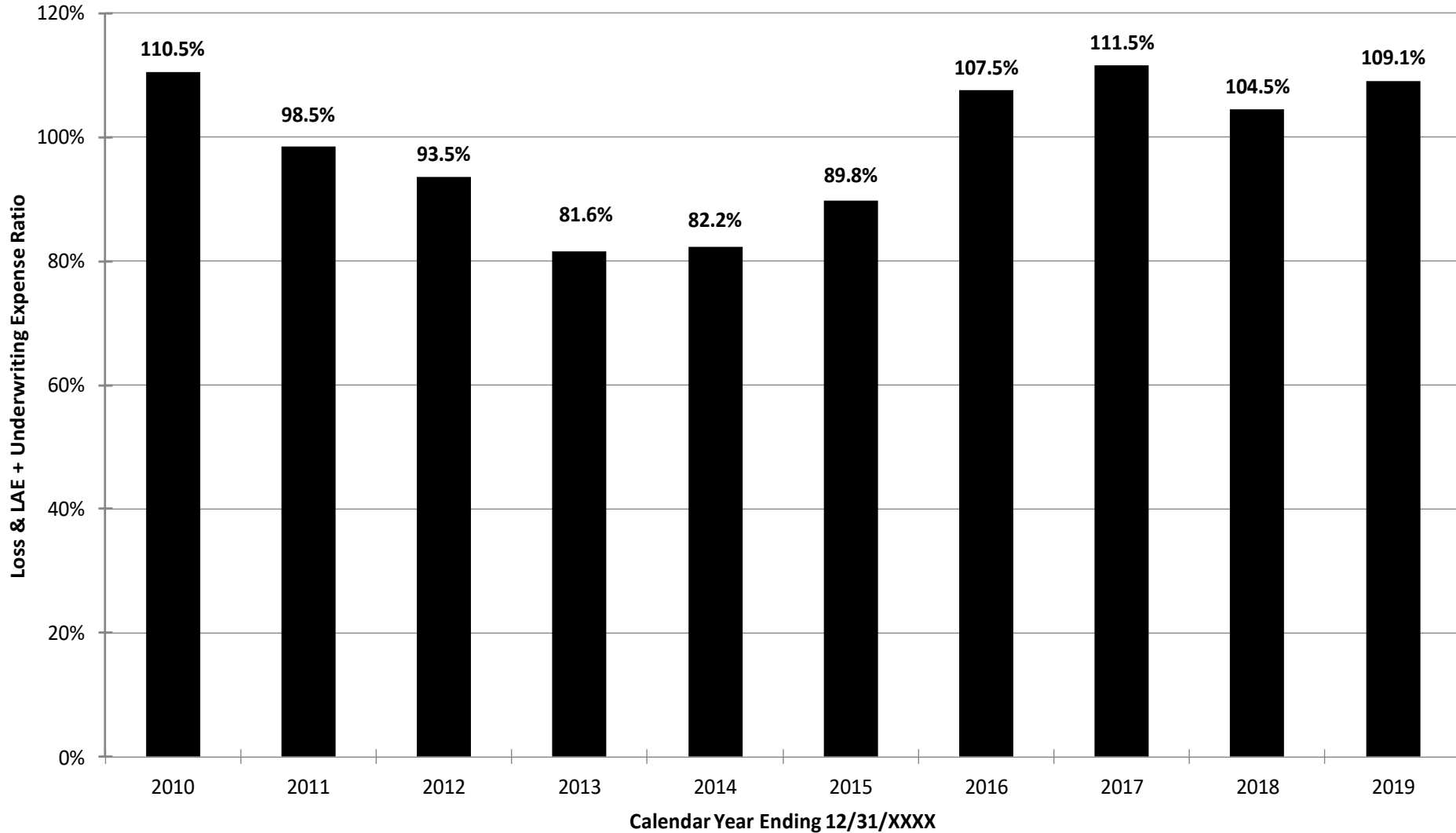
$$\text{Combined Ratio} = \frac{\text{Losses} + \text{U/W Expenses} + \text{PH Dividends}}{\text{Premium}}$$

$$\text{Operating Ratio} = \frac{\text{Losses} + \text{U/W Expenses} + \text{PH Dividends} - \text{Investment Gain}}{\text{Premium}}$$

# Calendar Year Net Loss & LAE Ratio

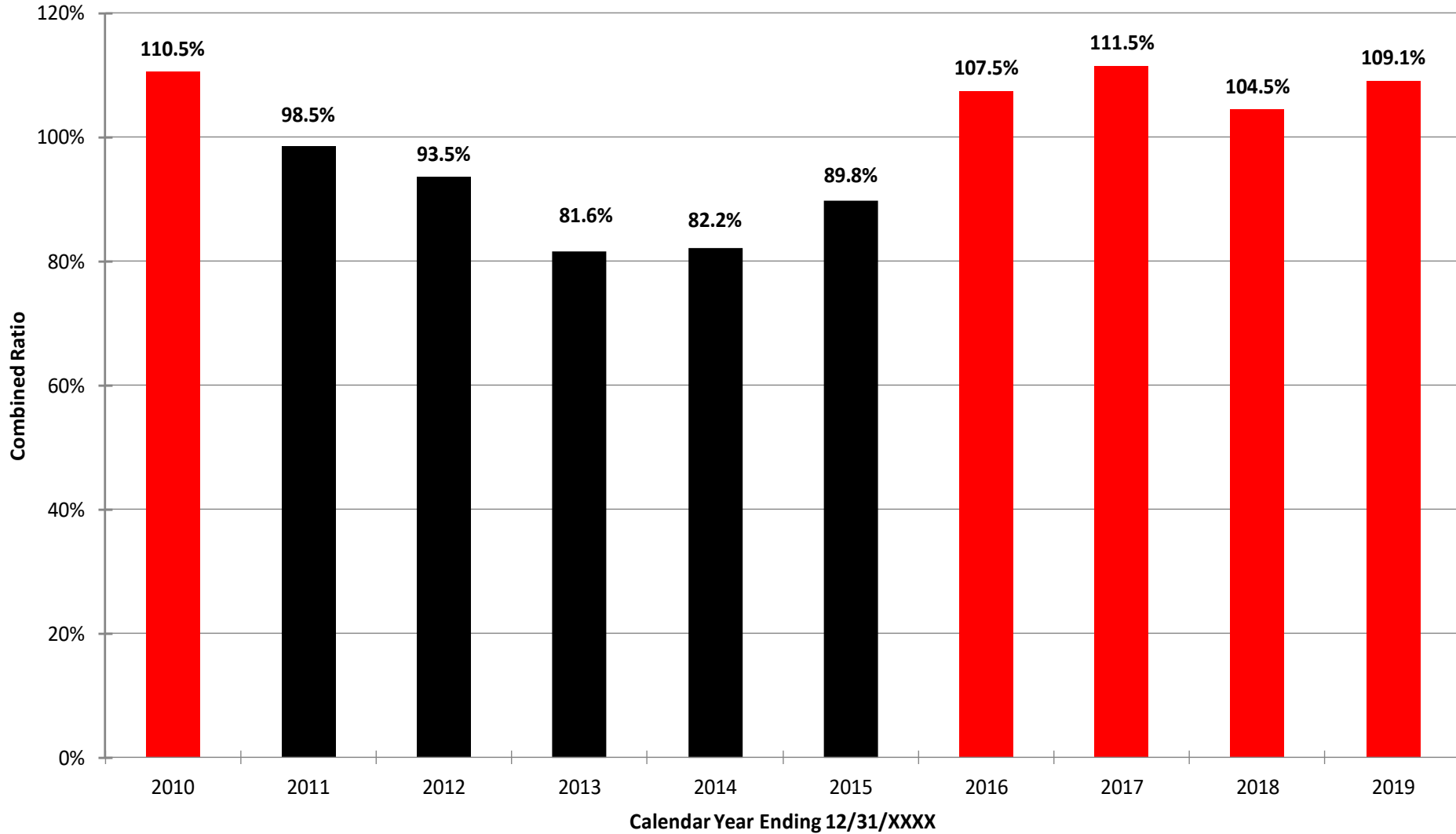


# Loss & LAE Ratio + Underwriting Expense Ratio

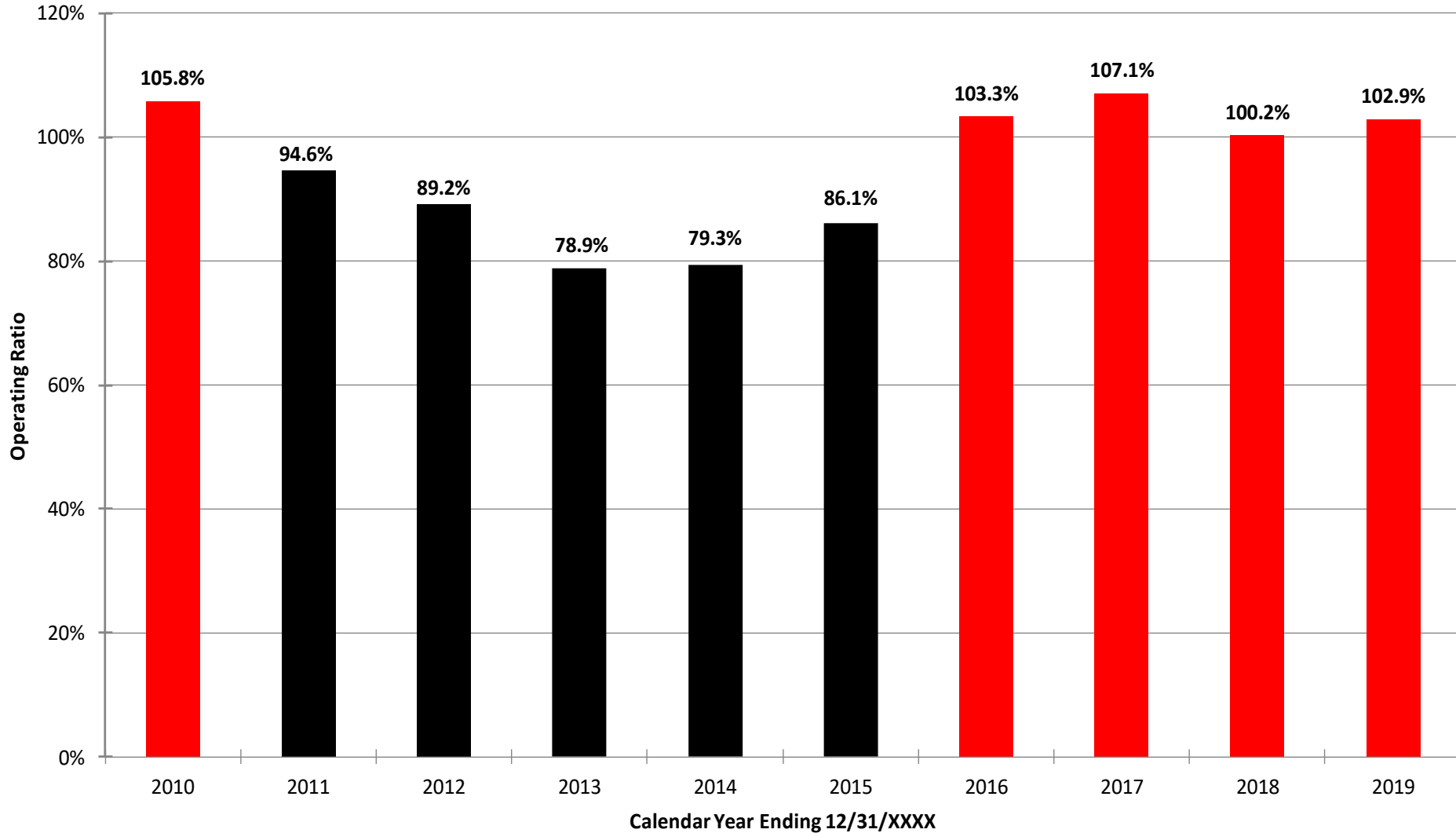




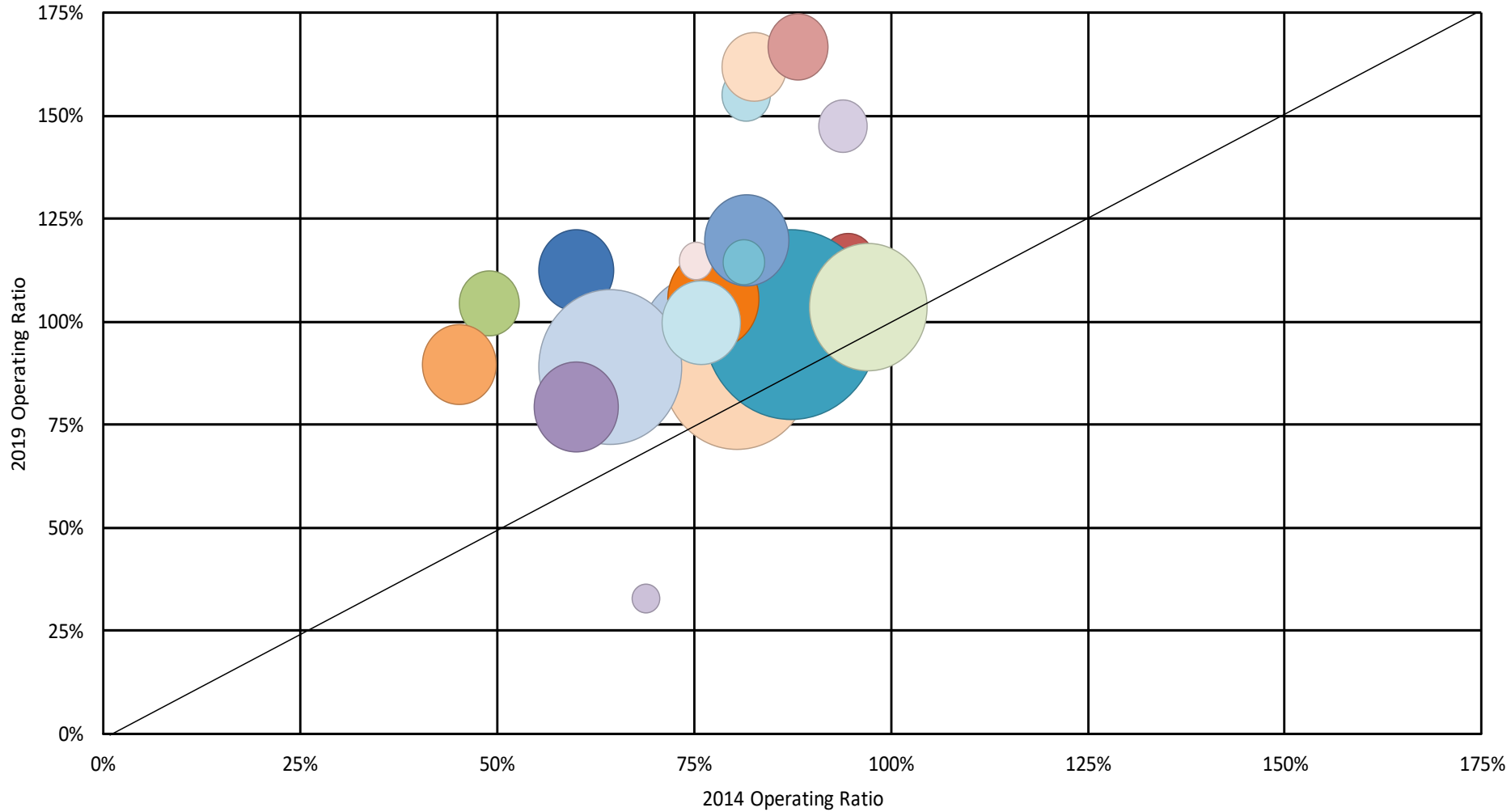
# Combined Ratio



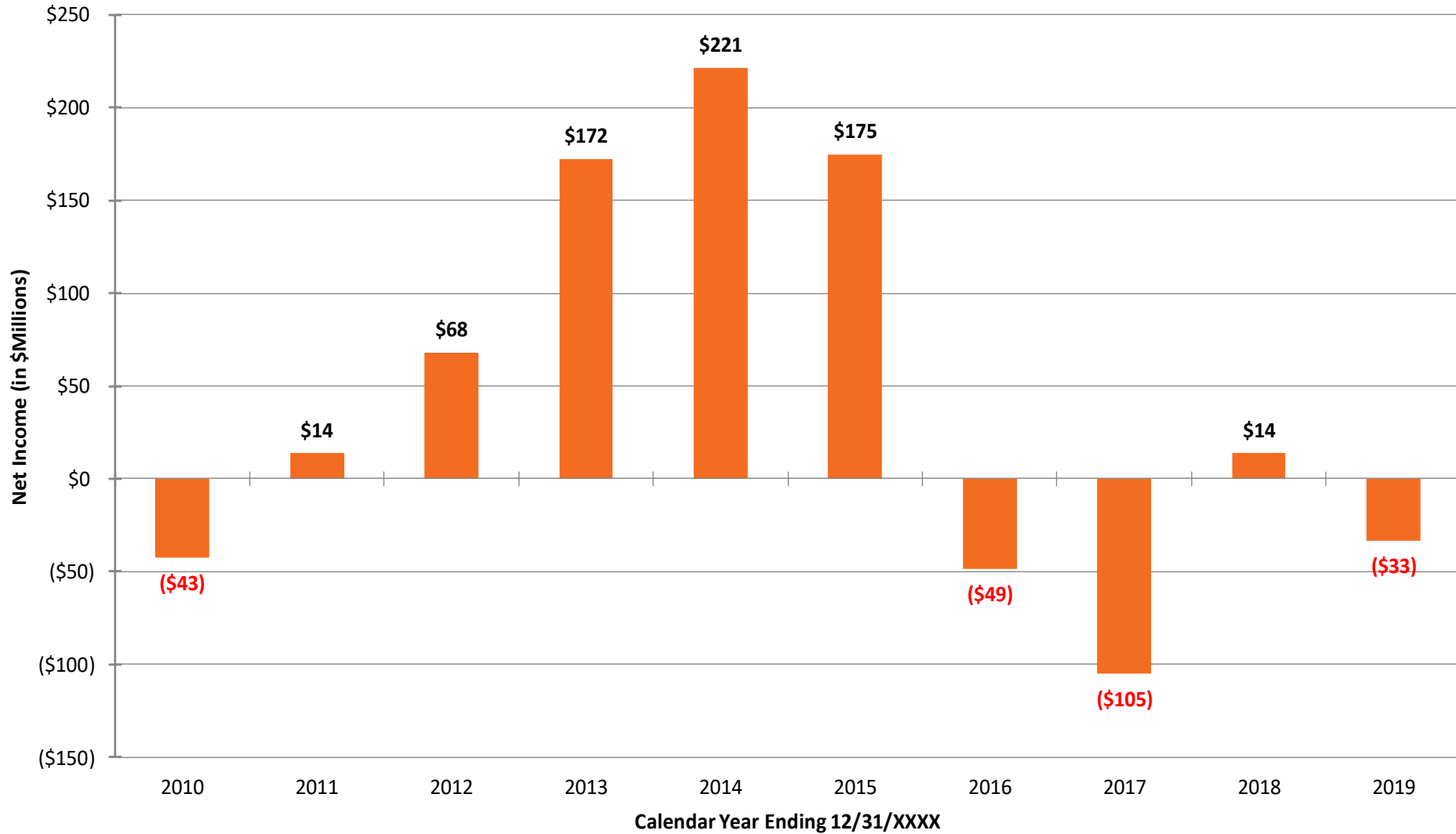
# Operating Ratio = Combined - Investment Gain



# Operating Ratio = Combined - Investment Gain



# Net Income or (Loss)



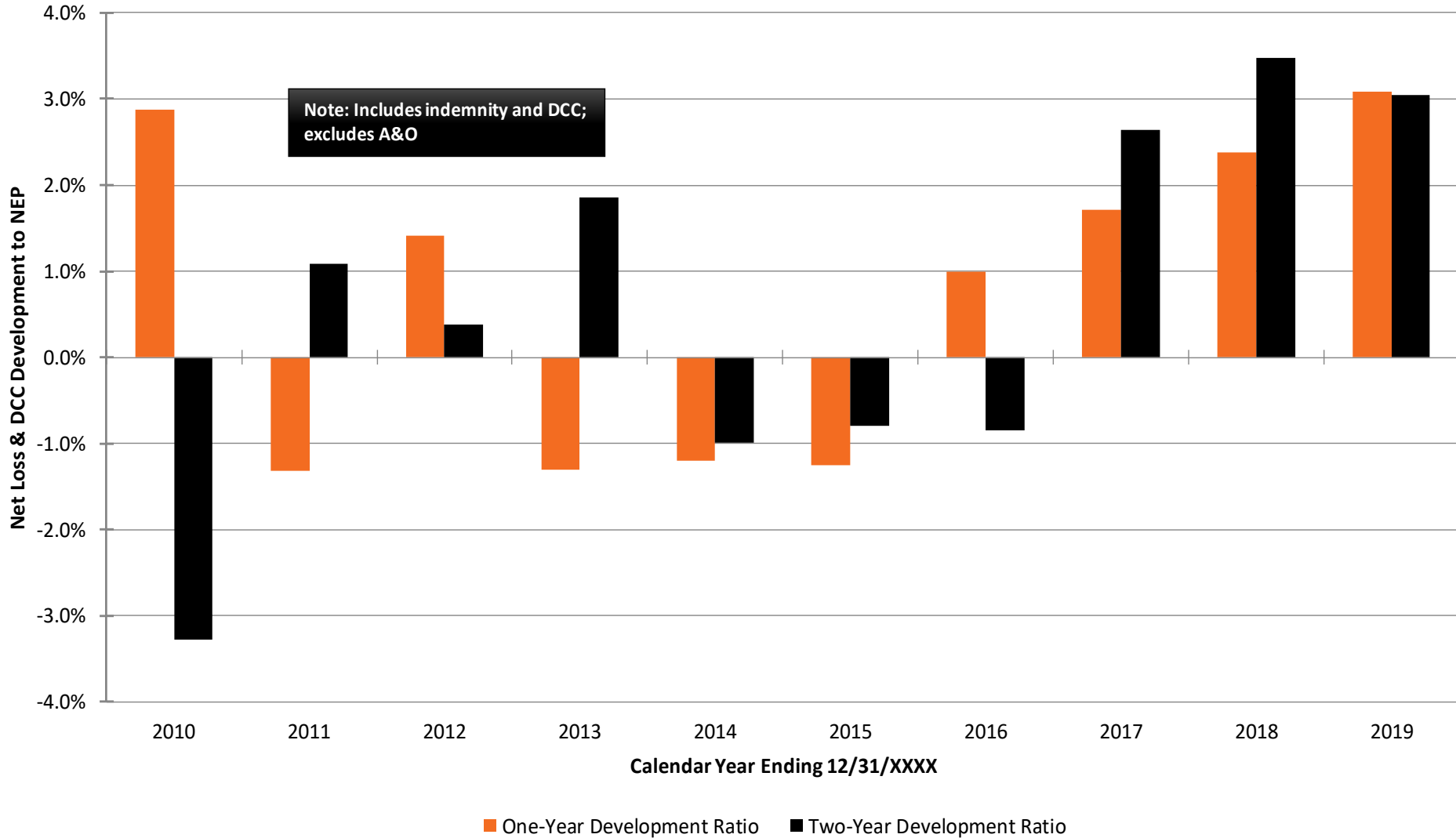
# Several Questions Determine Likelihood for Future Profitability

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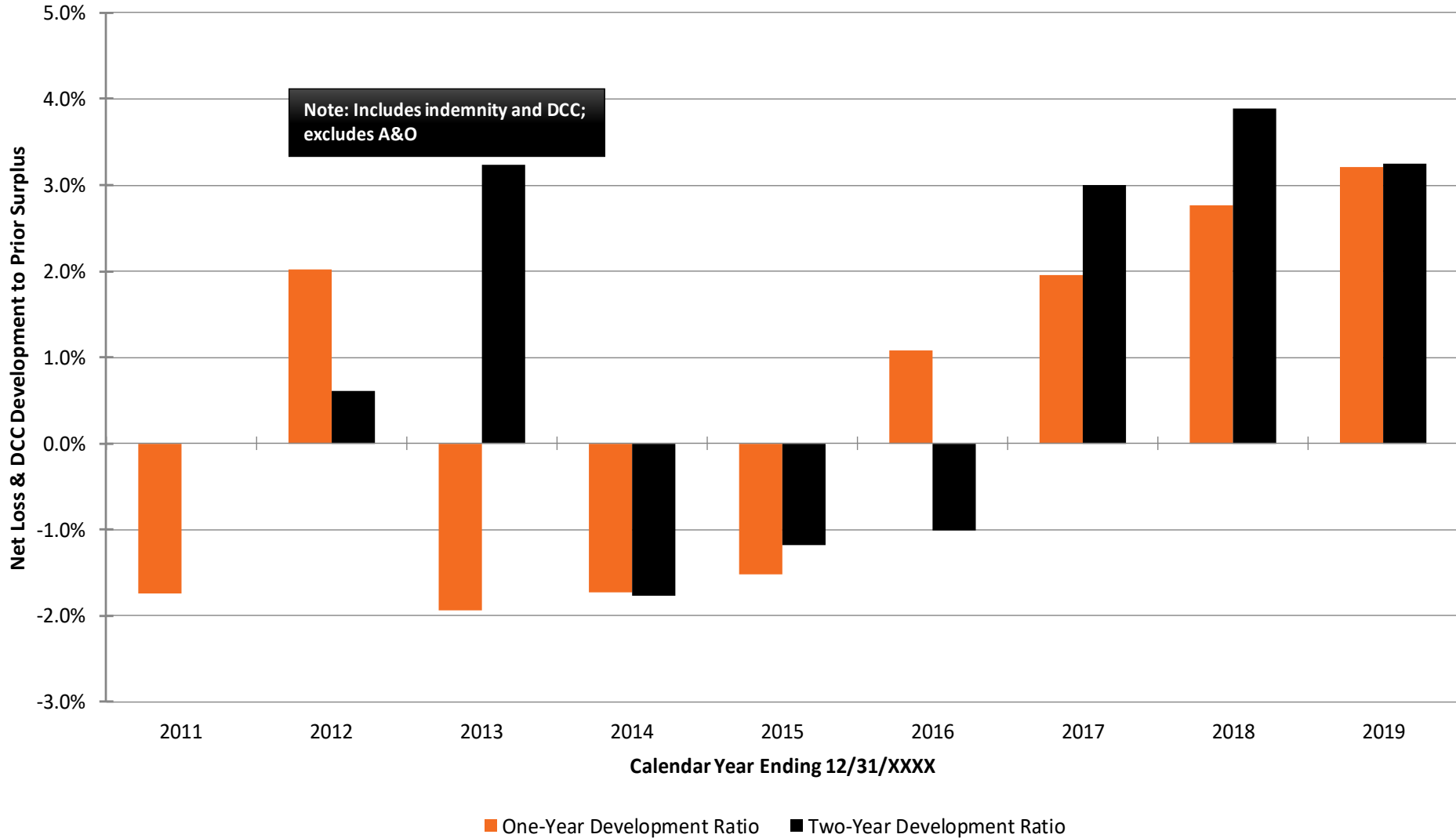
- Will adverse loss development continue to increase?
- How will future loss cost trends affect profitability?
- Will AOB reform be impactful?



# Percentage Increases in Net Ultimate Loss & DCC Estimates through 12/31/2019 (to NEP)



# Percentage Increases in Net Ultimate Loss & DCC Estimates through 12/31/2019 (to Prior Surplus)



# Several Questions Determine Likelihood for Future Profitability

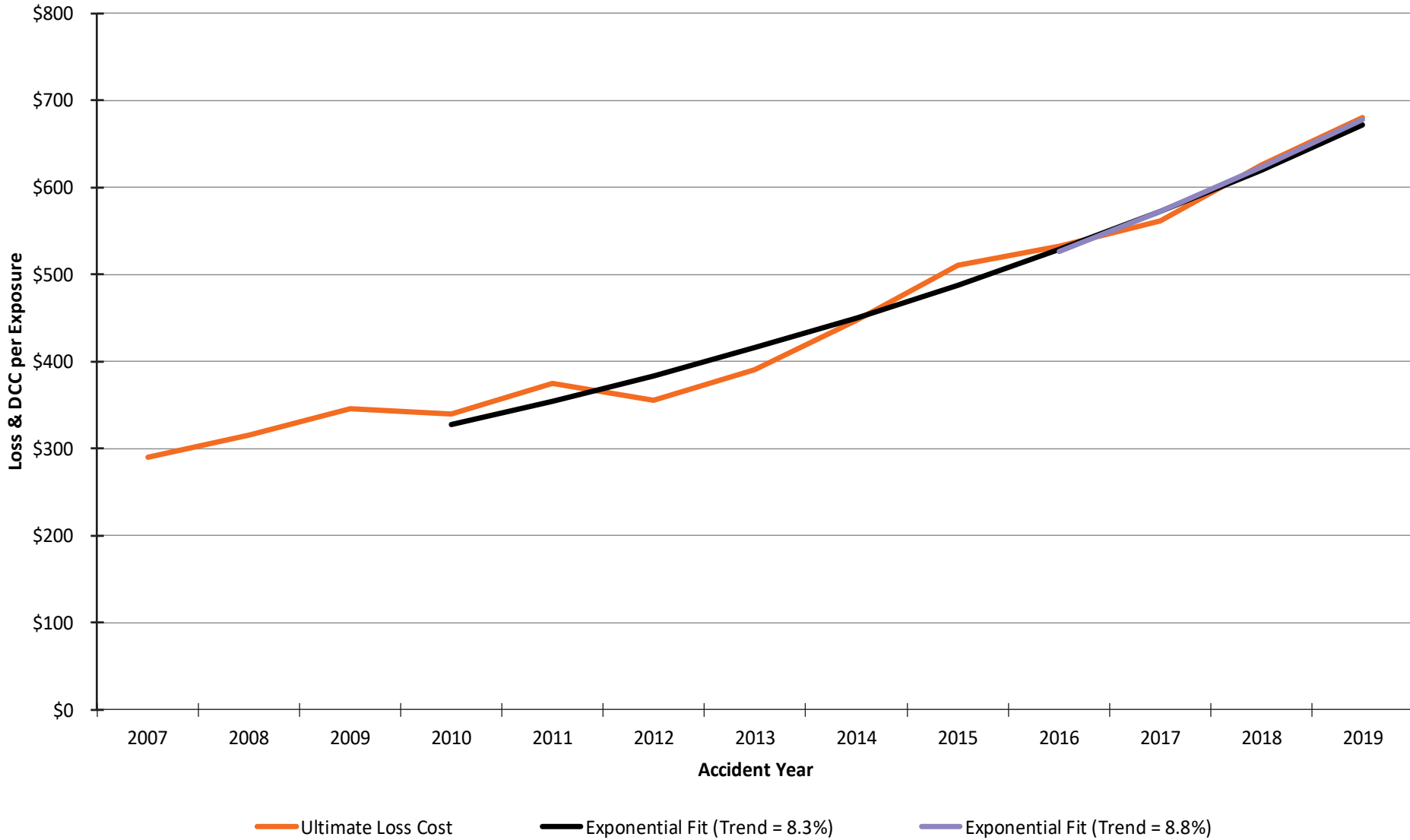
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# Aggregate Non-CAT Non-Sinkhole: Loss Cost



# Reserving Considerations

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- Believe it when you see it – don't be in denial
- Biased projection parameters – trended LDFs
- Ranges of reasonableness
- Reported and settlement lags
- Geographic concentration
- Analysis segmentation
- Impact of COVID-19

# Characteristics: Medical Professional Liability

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- 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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# The Assignment of Benefits (AOB) Problem

- An assignment of benefits (or “AOB”) allows the assignee to receive the benefits of the insurance policy.
- Once the assignment is made, Florida law has historically allowed the assignee to file a lawsuit to recover insurance benefits. *See Nationwide Mutual Insurance Company v. Pinnacle Medical Inc.*, 753 So2d. 55, 57 (Fla. 2000)(“The right of assignee to sue for breach of contract to enforce assigned rights predates the Florida Constitution”).
- Section 627.428, Florida Statutes, allows an insured to recover attorney fees if the insured prevails in an action to enforce an insurance policy. The insurer does not recover fees if it prevails.
- The Florida Supreme Court held that assignees could recover attorney fees pursuant to Florida’s “one way” attorney fee statute. *See All Ways Reliable Bldg. Maintenance, Inc. v. Moore*, 261 So.2d 131 (1972).

# The Assignment of Benefits (AOB) Problem

- Vendors such as water restoration companies increasingly used AOBs to obtain the benefits of insurance policies and file lawsuits if the insurer did not pay the often-inflated claims.
- In 2006, the DFS reported 8 lawsuits for water claims with an assignment of benefits. In 2011, the DFS reported 989 such lawsuits. By 2015, the number had increased to 5,328. In 2018, the DFS reported 16,890 such lawsuits.
- From 2013-2018, a number of bills were considered in the Florida Legislature to address the assignment of benefits issue. None of the bills passed the Legislature.
- Insurers attempted to address the issue by changing policy forms but the OIR and the courts rejected the form filings. *See e.g. Security First Ins. Co. v. Florida Office of Insurance Regulation*, 232 So.3d 1157 (Fla. 5<sup>th</sup> 2017); *Security First Ins. Co. v. Florida Office of Ins. Regulation*, 177 So.3d 627 (Fla. 1<sup>st</sup> DCA 2015).

# 2019 AOB Reforms

In 2019, the Legislature enacted section 627.7152, Florida Statutes. The statute requires:

An assignee to provide a notice of intent to initiate litigation before filing suit and to provide a presuit settlement demand. The assignee must provide a detailed written invoice or estimate of services, including itemized information on equipment, materials, and supplies; the number of labor hours; and, in the case of work performed, proof that the work has been performed in accordance with accepted industry standards.

The insurer to respond within 10 business days by making a presuit settlement offer or requiring appraisal.



# 2019 AOB Reforms

Section 627.7152, FL Statutes, provides that “one way” attorney fees do not apply in litigation between assignees and insurers.

Instead, attorney fees are calculated by determining the difference between the assignee’s presuit demand and the insurer’s presuit offer. This number is called the “disputed amount.”

Once the court reaches a decision, the judgment obtained is compared to the disputed amount. If the difference between the judgment obtained by the assignee and the insurer’s presuit settlement offer is:

- Less than 25 percent of the disputed amount, the insurer is entitled to an award of reasonable attorney fees.
- At least 25 percent but less than 50 percent of the disputed amount, no party is entitled to an award of attorney fees.
- At least 50 percent of the disputed amount, the assignee is entitled to an award of reasonable attorney fees.

# 2019 AOB Reforms

Section 627.7152, FL Statutes, imposes duties on assignees. An assignee:

- Must provide the assignor with accurate and up-to-date revised estimates of the scope of work to be performed as supplemental or additional repairs are required.
- Must perform the work in accordance with accepted industry standards.
- May not seek payment from the assignor exceeding the applicable deductible under the policy unless the assignor has chosen to have additional work performed at the assignor's own expense.
- Must submit to examinations under oath.
- Must participate in appraisal or other alternative dispute resolution methods.

# 2019 AOB Reforms

Section 627.7152, FL Statutes, requires an assignee to demonstrate that the insurer is not prejudiced by the assignee's failure to:

- Maintain records of all services provided under the assignment agreement.
- Cooperate with the insurer in the claim investigation.
- Provide the insurer with requested records and documents related to the services provided, and permit the insurer to make copies of such records and documents.
- Deliver a copy of the executed assignment agreement to the insurer within 3 business days after executing the assignment agreement or work has begun, whichever is earlier.

# Case Study: Strem's Law Firm

In June, the Florida Supreme Court granted the Florida Bar's petition for an emergency suspension of Scot Strem's from the practice of law. In its petition for suspension, the Florida Bar alleged numerous acts of wrongdoing by Strem's including:

- Obtaining retainer agreements through third parties without consulting with the clients.
- Filing of multiple lawsuits relating to the same occurrence in order to obtain additional attorney fees.
- Ignoring discovery deadlines and notices of deposition such that court intervention is required.
- Making fraudulent statements to the court or opposing counsel.
- Dismissing cases after the court imposes sanctions, resulting in a waste of judicial resources.
- The Bar's exhibits included affidavits from a sitting judge noting a pattern by Strem's of bad-faith conduct and in dilatory tactics in "virtually every case." Another sitting judge said unethical actions by Strem's are shown by "clear and convincing evidence."

# Case Study: Stremms Law Firm

The disciplinary case against Stremms is ongoing. The petition and other pleadings can be found at the Florida Supreme Court's site:

<http://onlinedocketssc.flcourts.org/DocketResults/CaseDocket?SearchType=Case+Number&CaseTypeSelected=All&CaseYear=2020&CaseNumber=806>

In addition to action by the Florida Bar, Stremms is the defendant in a class action lawsuit alleging his signature appears on retainer agreements with homeowners even though he has never met with the homeowners. The litigation is ongoing.

...if not, what's next?



# Questions

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# Contact Information

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