APPENDIX 2
An Analysis of the Residential JUA

I. Introduction

The Florida Residential Property and Casualty Joint Underwriting Association (Residential JUA) was formed during a special session of legislature as part of the Hurricane Andrew "package" in 1992. The Residential JUA was created to provide residential insurance for applicants who were unable to gain insurance through the voluntary private market. In other words, the Residential JUA was designed to be the insurer of last resort.

The board of the Residential JUA consists of the Insurance Consumer Advocate, five members designated by the insurance industry, five consumer representatives appointed by the Insurance Commissioner, and two insurance industry representatives appointed by the Insurance Commissioner. Members are appointed to three year terms. Prima facie, the board appears to strike a meaningful balance between the private and public sectors. This balance becomes tenuous, however, when one considers the fact that the Insurance Commissioner can remove any member for cause at any time.

II. Operation of the JUA

The Residential JUA began writing policies in March of 1993, and in some respects acts much like a regular insurance company. It operates through six approved carriers. These carriers are responsible for issuing policies, collecting premiums and adjusting claims. The JUA offers traditional coverage to homeowners, renters, condominium unit owners, and mobile home owners. With respect to these lines of policies, the JUA can write policies that include wind coverage (complete multi-peril policies) or can write policies that exclude wind coverage. In the case of the latter, the Florida Windstorm Underwriting Association (Windstorm JUA) often writes complimentary policies to cover potential wind and hail damages.

The Residential JUA is not limited to any one geographic area, and as such has been writing policies throughout the state. While the Residential JUA was designed to be an insurer of last resort, the Residential JUA accepts almost all applications for coverage, refusing those only found by its risk underwriting committee to be totally uninsurable. In the rare event that an applicant is deemed uninsurable by the JUA, the only alternative available to the applicant would be to go to surplus lines coverage.

All licensed or admitted property and casualty insurers are *required* to be members of the JUA. Because the JUA has no paid in capital, any deficit incurred by the JUA is paid for by assessments on member insurers. The amount assessed is a direct function of that company's market share in Florida in the year just prior to the occurrence of the deficit. The incentive effects of such an assessment policy will be discussed in some detail below.

III. JUA Facts and Figures

The JUA has grown rather dramatically since it began writing policies in 1993. As Figure 1 illustrates, in just one year's time, the JUA had written about 400,000 policies throughout Florida, by May of 1995 this figure reached 750,862. This figure placed the JUA as the *third largest* property and casualty insurer in the state capturing 13% of the market. The total exposure associated with these policies is approximately $50.7 billion, and the total direct written premium is roughly $302 million. Of these total policies, 43.3 % are concentrated in Broward, Dade, and Palm beach Counties (down from 44.5% in November of 1994). These policies in southern Florida capture 53.79% of the total JUA exposure and 55.92% of the total written premium. Furthermore, the majority of JUA policies (84.41%) include wind coverage. By policy type, about 50% of the JUA policies are multi-peril homeowners' (HO-3) policies (see Figure 2), while an additional 20% are homeowners' dwelling policies. Roughly 12% of the policies are mobile home policies (multi-peril and dwelling) mainly concentrated in the gulf coast area, 13% of the policies are on condominium units, and renters' policies represent 5% of the total JUA policies. (For a more complete examination of JUA data on premiums, exposure and numbers of policies by region and by policy type, please see the graphs presented at the end of the appendix.)

Through the brief examination of the data above, the tremendous amount of growth in the number of JUA policies is the most impressive statistic. Considering that the JUA was designed to only provide coverage for otherwise uninsurable risks, this growth is surprisingly high. This tremendous growth is due to the reduction in the availability of property insurance throughout the entire state as a consequence of the Hurricane Andrew losses. After attempting and failing to secure coverage in the voluntary market, individuals turned to the JUA and secured coverage. A second contributing factor is that policyholders who may have been able to secure "private" coverage instead turn to the JUA. This latter scenario may typically occur since (a) JUA rates happen to be well below those offered in the voluntary market, and (b) the JUA cannot ensure that voluntary market coverage was not readily available for potential policyholders. The extent to which JUA rates fall short of voluntary market rates is discussed below.

IV. JUA Rates

To examine whether JUA rates were below competitive market values, a comparison will be made to similar rates in the voluntary market. Before examining what these differences *are*, it will be useful to examine what these differences *should be*. There should be one major difference between policies held in the voluntary market as opposed to those held in the involuntary market. That difference is the degree of risk. *By definition,* JUA policies should be considered uninsurable risks in the voluntary market. This should be reflected in higher JUA premiums when compared to policy premiums in the voluntary market.

With respect to the issue of JUA rates, Figure 3[1] illustrates the discrepancy between JUA HO-3 rates and the average voluntary market rate for similar coverage over a range of property values for 1993. As evidenced the JUA rate falls short of the average voluntary market rate by a minimum of 2% for homes valued at $160,000, and a maximum of 27% for homes valued at $80,000. The shortfall is greatest for homes ranging from $40,000 to $120,000 in value; and the rate differential is reduced the greater the value of the property. Although not shown here, the rate differential *grew* in

[1] The data used for this graphical depiction of public/private rate comparisons were drawn from the appendix of "Florida's Property Insurance Crisis" written by Leonard Schulte. The actual data were prepared by the FRPCJUA actuarial staff. The figures represent statewide averages.

1994. While no JUA rate increases went into effect in 1994, the private sector rate jumped 31%[2] in response to Hurricane Andrew. By allowing rates to fall so far below rates in the voluntary market, policyholders develop a very strong incentive to gain coverage through the JUA, and it appears that they have done this in the post-Andrew era. The JUA, which was intended to serve as an insurer of last resort for many uninsurable risks, has instead become a low cost alternative for many insurable risks, and an unfair and unwanted competitor with the private market. At least part of the growth in JUA policies can be attributed to their relatively low rates.

In an attempt to correct this discrepancy, the most recent piece of state legislation on the matter requires that JUA rates be set at a level equal to the highest private rates offered by county. To this end, a 24% JUA rate increase went into effect in January of 1995, and a second rate hike of 15.5% was approved in April of 1995 and will go into effect this fall. The extent to which this brings JUA rates in line with voluntary rates is neutralized in part by increasing voluntary market rates. However as Figure 4 illustrates, upon enactment of the fall 1995 rate increase of 14.5%, JUA rates will become more in line with voluntary market rates.

V. JUA Deficits and Member Assessments

One result of allowing JUA rates to fall consistently below voluntary market rates for more risky policies will be perpetual shortfalls in revenue. Using the statutory accounting principles (which do not allow for the JUA to claim deferred policy acquisition costs as credits), the JUA suffered deficits of $17.4 million and $26.9 million in 1993 and 1994 respectively. Using generally accepted accounting principles, the JUA essentially broke even, running surpluses in the neighborhood of $0.5 million.

Given that the JUA essentially breaks even in non-hurricane years, in the event of a hurricane of any magnitude, all JUA losses would become part of the JUA deficit. Considering that the JUA now has exposure levels in excess of $50 billion throughout the state, even a minor storm in south Florida could leave the JUA with a deficit in excess of $1 billion. Shortfalls like these are recouped through assessments to member insurers. This implies that a firm like Allstate which holds approximately 15% of the market would be responsible for 15% of JUA shortfalls (net of Florida Catastrophe fund reimbursement), which may be in the hundreds of millions dollars. These potential assessments clearly worry voluntary market insurers and is a major deterrent to new and existing property and casualty insurers from entering or expanding their presence in the Florida market. Many have responded by demonstrating intent to substantially reduce market share in Florida to ease potential assessment costs.

Additionally, payments of these assessments in the event of a hurricane may not be made in a timely fashion. First of all, the Department of Insurance currently will only allow assessments to be written into voluntary market premia after they have been assessed. As a consequence, current voluntary market rates do not reflect potential assessment costs for member insurers. If a storm was to strike, there is some question as to how quickly funds could be assembled by the private sector. Secondly, because the first assessment must be absorbed by the voluntary market, there is also some

[2] There is some question as to the magnitude of rate increases in response to Hurricane Andrew. Florida DOI experts calculate the rate hikes to be about 19% statewide.

question over the constitutionality of these assessments.[3] The argument that the first assessment might be legally considered a regulatory taking without compensation may hold some merit. If a legal battle ensued in the aftermath of a storm, the best case scenario would be a delay in claim payments as litigation ensued. The worst case scenario for JUA policy holders would be a ruling that JUA assessments are unconstitutional.

VI. JUA Disincentive Effects

In general, several identifiable disincentive effects result from the current organizational structure and operation of the Florida Residential Property and Casualty Joint Underwriters Association:

- Organizationally, the combination of a lack of meaningful private sector involvement in JUA decision making processes and private sector responsibility for claims payments leads to sub-optimal rate setting procedures.

- JUA assessments form a wedge between rate determination and the expected payment of claims. As long as rates are determined without consideration of having direct responsibility for the payment of claims, there is no inherent mechanism in place to insure that rates will be in line with the expected costs of insurance.

- Current assessment arrangements provide an unhealthy voluntary market environment; member insurers have an incentive to reduce market shares, or restrain from entering the Florida market.

- In the event of an initial storm under these arrangements, the expediency with which JUA claims will be paid is clouded by legal questions surrounding the assessments as well as questions surrounding the source of revenues for initial assessments.

- Payment of a 10% commission to those writing JUA policies can help lead to unconstrained growth in policies.

- The payment of assessments by voluntary market insurers will eventually be passed on (in some degree) to voluntary market policy holders. This represents a cross-subsidy from voluntary market policy holders to JUA policy holders. This results in efficiency and equity losses in the Florida property and casualty insurance industry.

- Growth in JUA debt and risk represents a major constraint to private expansion in the Florida market place.

Substantial JUA depopulation will be required to bring the actual operation of the JUA more in line with the legislative intent behind its formation; that is to effectively deal with uninsurable risks.

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[3] A more complete discussion of the constitutional issues surrounding JUA assessments is provided by Schulte, "Florida's Property Insurance Crisis" 1994 p43-45.

Figure 2: Percentage of JUA Policies by Policy Type

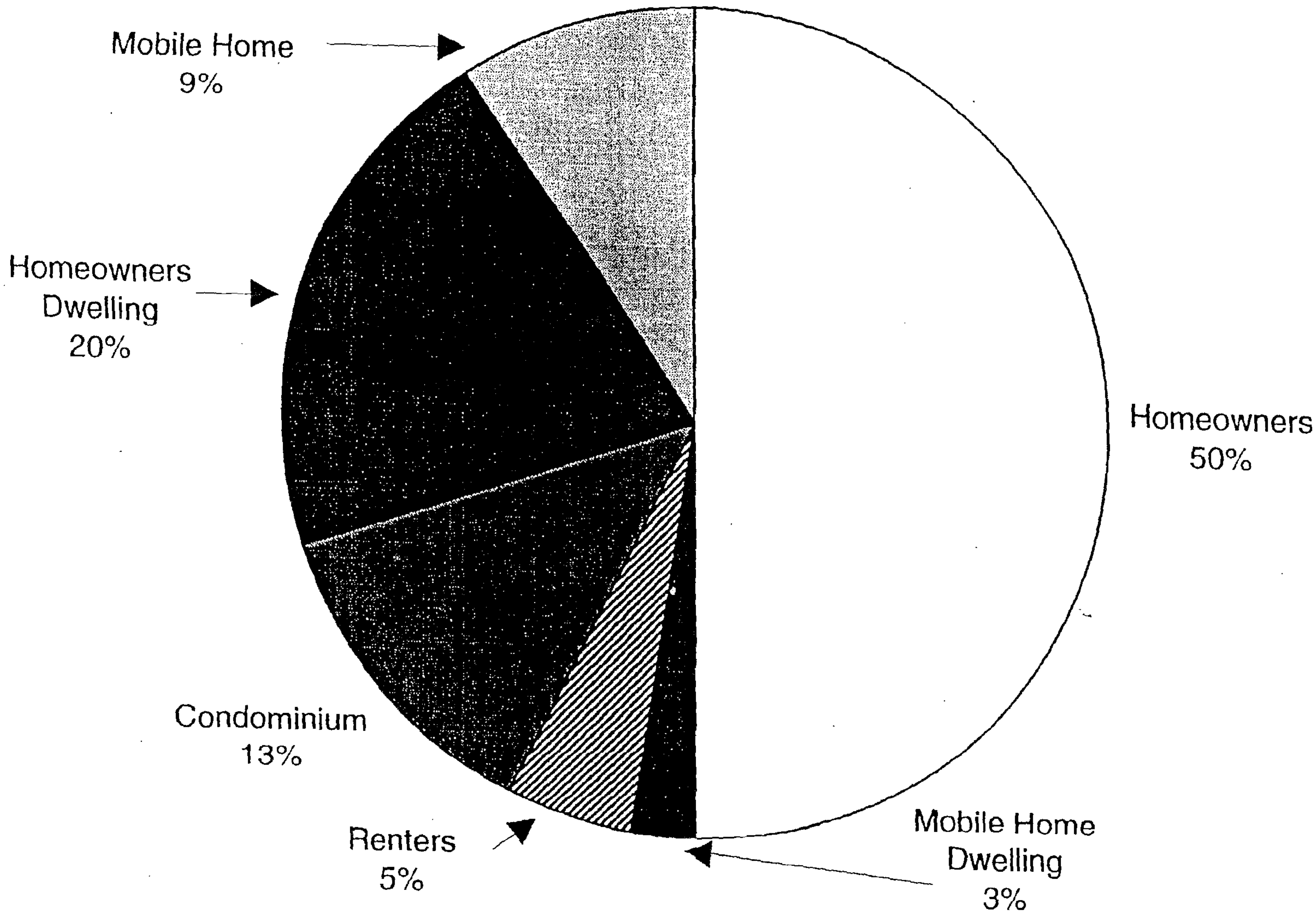


Figure 1: Number of JUA Policies

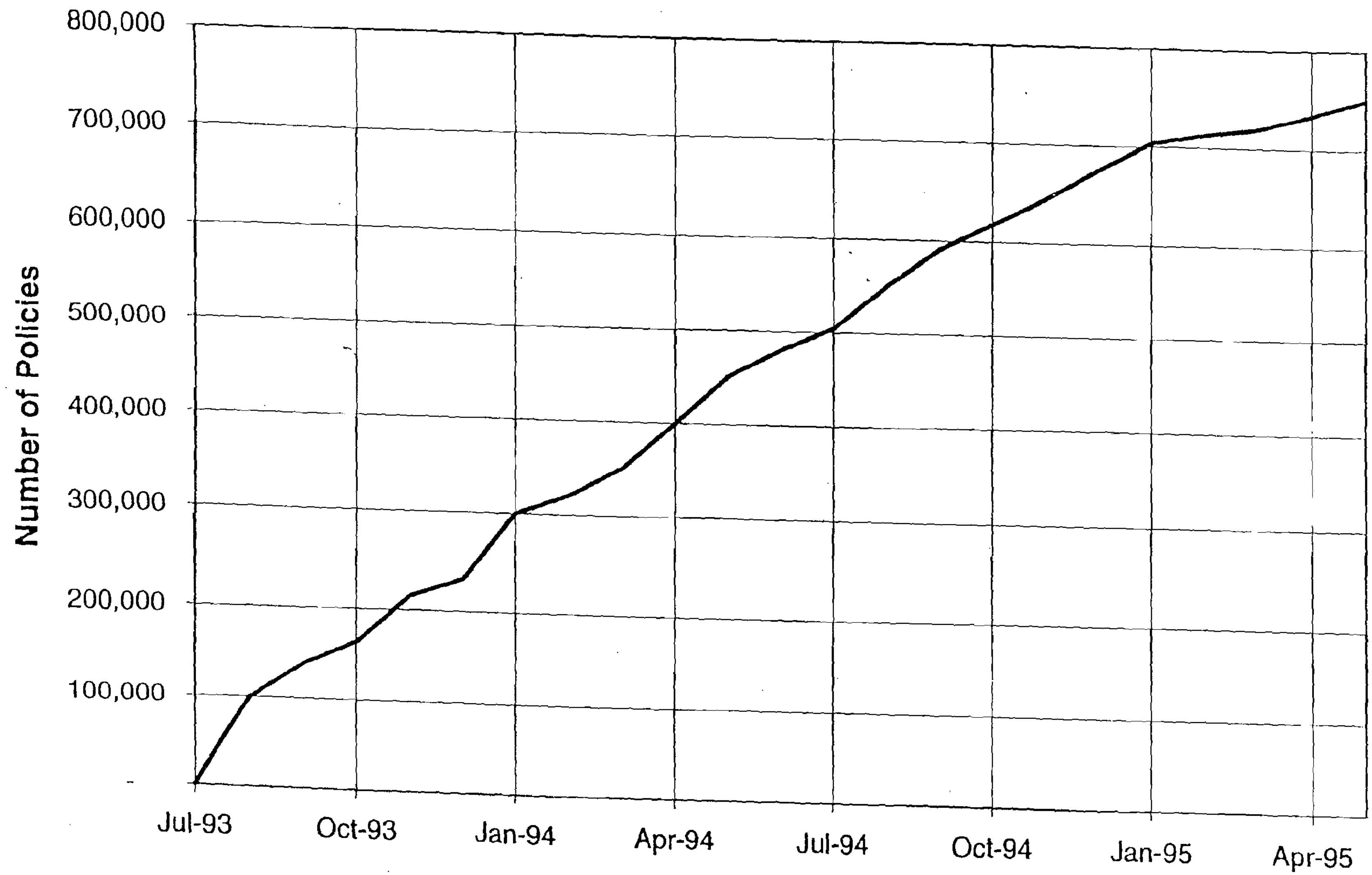


Figure 4: 1995 Rate Comparison for Major Insurers in South Florida (HO-3 Policy on a $75,000 Frame Home)

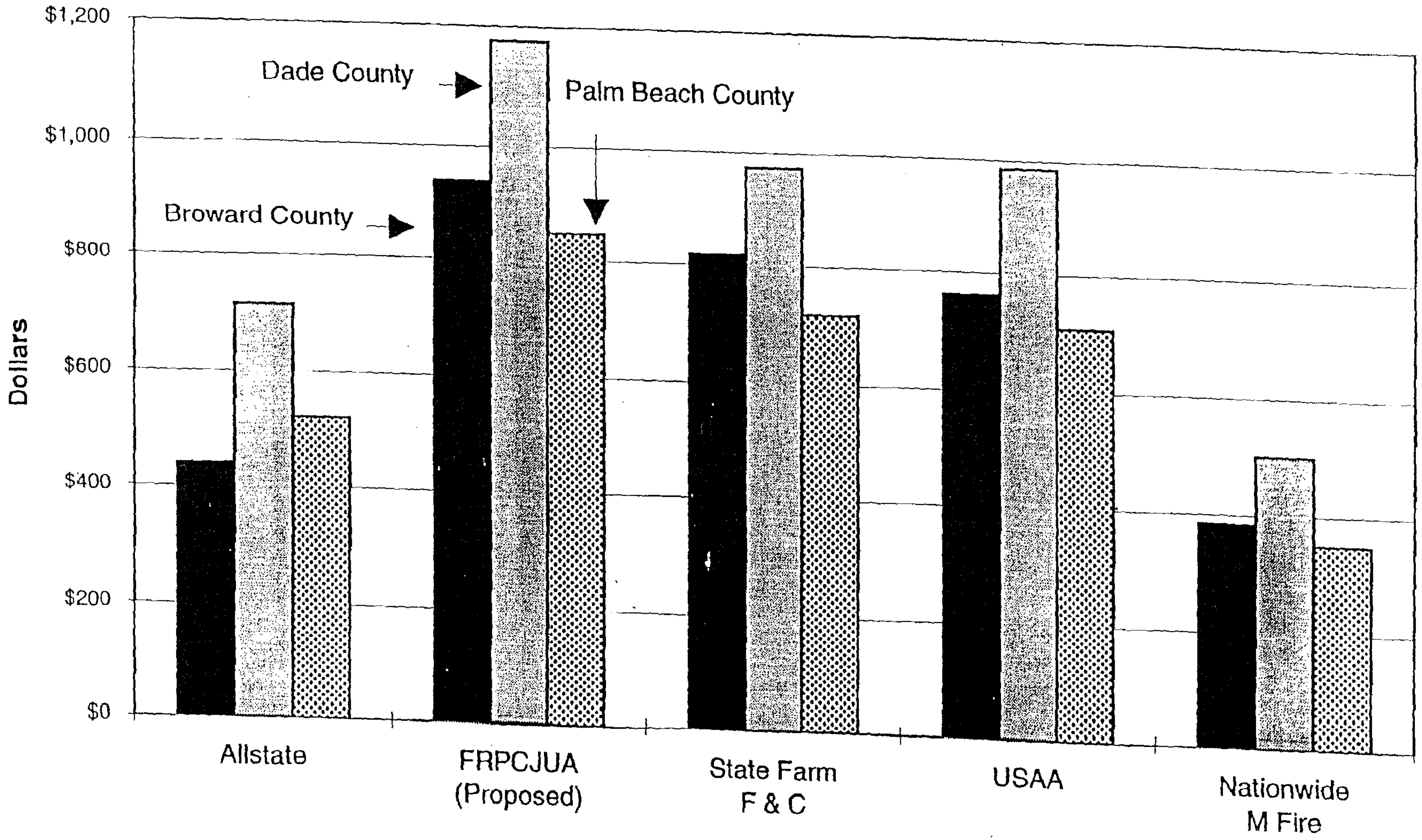
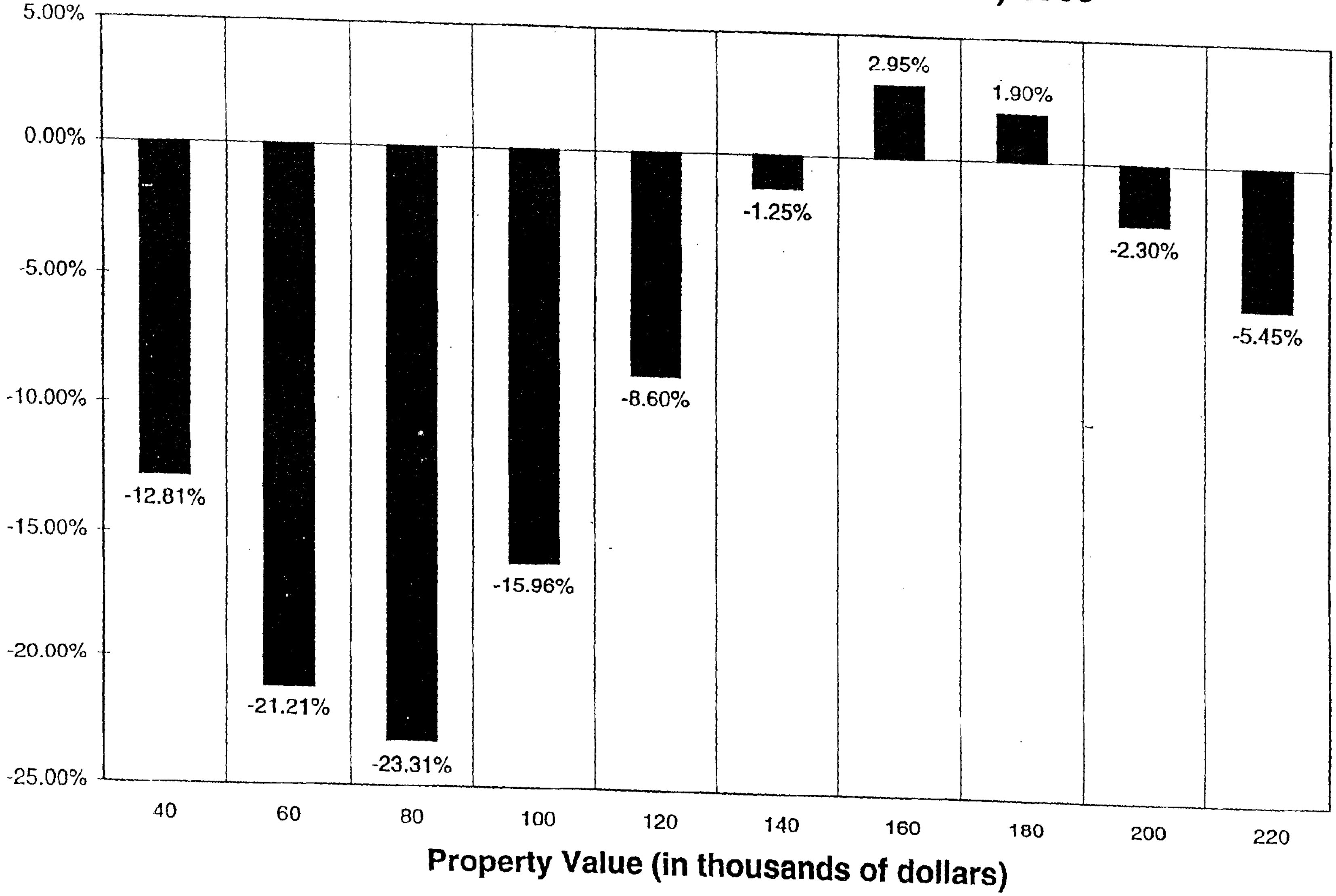


Figure 3: Rate Differential (Percent by which JUA Rate Exceeded (+) or Fell Short of (-) Voluntary Market Rates) 1993



APPENDIX 3
An Analysis of the Windstorm JUA

I. GENERAL INTRODUCTION

The Florida Windstorm Underwriters Association (WINDSTORM JUA) was created by the legislature in 1970 to make available reasonable windstorm and hail insurance coverage to qualified applicants in eligible areas. With a membership of 450 licensed property insurers, Windstorm JUA is governed by a 12-member board of directors, eight of whom are elected by its member companies and the remaining four are appointed by the industry trade association. The Windstorm JUA is regulated by the Florida Department of Insurance which determines the areas of the state eligible for Windstorm JUA windstorm and hail coverage. The eligible areas have traditionally been areas of high-wind risk, many of which require a residual market even when the voluntary market is active and healthy.

II. THE ROLE OF FWUA

The purpose of the Windstorm JUA is to provide a reasonable windstorm and hail insurance coverage to qualified applicants who are unable to obtain coverage through the voluntary market. To do this, the association provides timely and efficient services to its policy holders, without making their coverage so favorable as to damage the voluntary insurance market. As a residual market, Windstorm JUA assesses member companies for any fund deficits. The potential assessment, based on a company's prior year market share, may not exceed ten percent of the company's gross coverage in any given year. To minimize the disruptive effect of assessment on the voluntary market, the association offers assessment credits to insurers for premiums written in Windstorm JUA eligible areas.

III. OPERATION OF Windstorm JUA

The Windstorm JUA has more than 90 employees at its Jacksonville headquarters, who handle all services in connection with issuing and administering Windstorm JUA policies, including new application, renewals, claims, consumer questions, and agent relations. The association specializes in providing windstorm and hail coverage for dwellings, condominium owners, mobile homes, commercial structures, and special risks. The Windstorm JUA has a number of resources available to fund its operations and pay its claims. These include premiums paid by policyholders, assessments against member insurers, reinsurance, catastrophe fund, lines of credits, and statutory authorization to issue bonds.

Windstorm JUA has maintained the same rates that were in place before Andrews. The average rate per thousand dollars of coverage (excluding a 15 percent reinsurance surcharge) as of June 30, 1995 are given below:

Florida Windstorm Underwriting Association
Average Rates per thousand dollars of coverage as of June 30,1995

County	Dwellings	Condo	Mobile Homes	Commercial
Broward	$1.10	0.90	7.75	3.79
Dade	1.09	0.94	7.60	4.08
Escambia	1.09	0.86	5.21	2.92
[illegible]nroe	2.91	2.86	11.41	5.39
[illegible]lusia	1.09	0.97	3.35	[illegible]47

Source: Windstorm JUA.

The association has a minimum premium of $35 for Dwellings, $50 for Mobile Homes, and Condo, and $ 100 for Commercial. All policies with premiums over the minimum are subject to a 15 percent surcharge. For example, a $ 100,000 residential dwelling coverage in Dade County would cost $1.25 per thousand dollars of coverage (- 1.09 base rate and 0.16 reinsurance surcharge).

III. GROWTH OF THE WINDSTORM JUA.

Windstorm JUA has grown dramatically since hurricane Andrew, both in terms of loss exposure (liability in force) and number of policies in force. By December 1994, the gross exposure of Windstorm JUA has reached $27 billion compared to $15.3 billion in December 1993 and $7.5 billion in December 1992. From December 1992 to December 1994 , Windstorm JUA's policies in force has increased from 62,000 to 184,000, an increase of about 184 percent. As of June 30, 1995, Windstorm JUA has a loss exposure of $31 billion on about 205,000 policies. Much of the growth in the Windstorm JUA may be attributed to growth in coverage for dwellings, which makes up over 60 percent of the association's loss exposure and policies in force. The dramatic growth in the Windstorm JUA reflects the Florida insurance crisis after Hurricane Andrews. After Andrew, the Windstorm JUA has expanded coverage to Broward and Dade Counties and now offers coverage in 27 of 35 coastal counties of Florida. However, over half of Windstorm JUA's exposure and policies are concentrated in Broward, Dade and Monroe counties. To accommodate this growth, the association has secured additional sources of fund by purchasing additional reinsurance and seeking lines of credit of one billion dollars.

IV. CONCLUSION

As a residual market, the growth in the Windstorm JUA reflects the crisis in the voluntary market. Despite its efficient management and additional sources of funds, the growth in the Windstorm JUA is not a long-term solution to the lack of adequate capacity for windstorm and hail insurance coverage in Florida. The solution lies in providing incentives that encourage voluntary writing of windstorm and hail policies in the private insurance market.

APPENDIX 4
Industry Response on Claims Paying Capacity

PRIVATE INSURANCE INDUSTRY MAXIMUM CAPACITY
(INDIVIDUALLY AND COLLECTIVELY)
FLORIDA INSURANCE COUNCIL MEMBERS' RECOMMENDATIONS

MOBILE USA INSURANCE COMPANY INC. - Frank J. Lake, President

Mr. Lake's opinion is that $20 - $30 billion is the maximum capacity of the Insurance industry including the CAT fund to pay claims associated with a Florida hurricane without impairment. The total capital and surplus that Mobile USA can dedicate to pay claims associated with a Florida hurricane without experiencing bankruptcy is estimated to be $2 million (not including reinsurance).

UNITED SERVICES AUTOMOBILE ASSOCIATION - Robert Henderson, Legislative Counsel

USAA does not have an estimate as to the maximum capacity of the Insurance Industry to pay claims associated with a Florida hurricane. However, it was stated that they would support a cap on the insurers' obligations. As far as the amount of capital and surplus that USAA could dedicate to pay claims, $400 million was the total amount of claims USAA paid to homeowners for Hurricane Andrew. However, $45 million was the total profits from writing Florida homeowner's coverage for USAA since 1966.

AUTO-OWNERS INSURANCE - Stuart R. Birn, Senior Vice President

The total capacity for the private insurance industry including the CAT fund to pay claims for a Florida hurricane catastrophe is $15 billion (approximately 10% of the capital and surplus of all companies who write insurance coverage in Florida). The total capital and surplus that Auto-Owners could risk to pay claims from a hurricane in Florida is $200 million. These numbers are subject change due to catastrophes in other states and changes in the stocks and bonds markets.

AMSTAR INSURANCE COMPANY - Pedro A. Freyre, Executive Vice Pres.

$20 billion is the maximum capacity for the private insurance industry to pay claims without impairment for a Florida hurricane catastrophe. Amstar Insurance Company could dedicate $1 million of capital and surplus for a Florida hurricane catastrophe.

STATE FARM INSURANCE - Vincent J. Rio III, Counsel

State Farm does not have a definitive number for the maximum capacity of the private insurance industry and the CAT fund to pay claims for a Florida hurricane catastrophe. However, they do state that a "hard" line should be established to limit insurers' obligations. The "hard" line should not be coupled with an increase in the CAT fund trigger. State Farm can dedicate approximately $1 billion in retention plus their co-pay in excess of the retention for claims associated with a Florida hurricane catastrophe.

ALLSTATE INSURANCE COMPANY - David G. Nadig, Counsel

The total capacity for the private insurance industry and the CAT fund to pay claims for a Florida hurricane without impairment is $7.5 billion. Allstate can dedicate $1 billion of its capital and surplus to pay claims for a Florida Hurricane catastrophe.

Allstate completed initial calculations of the savings consumers could realize with the non-profit state fund as opposed to the private market. It was actuarially calculated by Allstate that overall the non-profit state fund accounts for approximately a three percent savings over the rate that would be charged in the private market. Additionally, the non-profit state fund could realize further savings with the inclusion of a 10% deductible or a 10% deductible/10% co-pay. With these attributes, a savings rate of 24% or 32%, respectively, can be achieved with respect to the private market. Allstate recommends the 10% deductible coupled with the 10% co-pay.

Examples:

		Non-Profit State Fund		
Rpl/cost	Private market	$250 deductible	10% deductible	10% deductible/co-pay
Miami 75K	$894	$867	$659	$593
Miami 150K	$1,741	$1,689	$1,284	$1,156
Tampa 75K	$210	$203	$154	$139
Tampa 150K	$432	$419	$318	$286

WESTFIELD COMPANIES - Jack Adornetto, Senior Vice President

The Westfield Companies do not have an answer as to the maximum capacity of the private insurance industry, but they do suggest that the results of hurricane Andrew be used as a gauge. Additionally, the Westfield Companies do not allocate capital and surplus by states or territories, therefore an amount as to how much they can allocate to pay claims for a Florida hurricane catastrophe can not be provided.

INDEPENDENT PROPERTY & CASUALTY INSURANCE - David Klaitz, Sr., President and CEO

Independent P & C Insurance could not provide an answer to the question of total capacity for the private insurance industry and CAT fund to pay claims associated with a Florida hurricane because of a lack of resources to do research. However, they did recommend that the number be low enough to avoid extraordinary reduction of capital and surplus to the individual carriers within Florida. As of 5/31/95, Independent Fire Insurance Company of Florida could dedicate approximately $6 million in capital and surplus to pay claims for a single Florida hurricane. Additionally, they also have a private reinsurance program with $18 million in capacity.

FLORIDA FARM BUREAU INSURANCE - Robert Jarratt, Executive Vice President & CEO

Florida Farm Bureau Insurance estimates the total capacity for the private insurance industry to pay claims associated with a Florida hurricane to be between $20 and $25 billion. Additionally, this estimate could increase with adequate rate levels and with more insurance companies coming into the Florida market. $200 million (100% of their capacity) could be allocated by Florida Farm Bureau Insurance to pay claims associated with a Florida Hurricane.

SERVICE INSURANCE COMPANY - David C. Cruikshank, President

The Service Insurance Company projects the claims paying capacity of the insurance industry to begin at $25 billion. This number is predicated by the marketplace sustaining a fair return on investment. Additionally, the company indicates that Florida should concentrate on spreading the exposure and risk to the companies who represent 95% of the companies who write insurance in Florida but who have only a combined 40% market share. Service Insurance Company also asserts that it can handle $4 million in losses. This number translates into a $400,000 effect on Service Insurance Company's capital and surplus.

Robert Polakowski

Mr. Polakowski does not have a response to the Sam Miller alert. However, he does suggest a possible solution to the Florida Catastrophic insurance problem. His solution suggests the following:

1. The majority of the risk should be placed in the private market.
2. If the majority of the 1500 property/casualty companies in the U.S. could be persuaded to use some of their surplus to write property insurance in Florida, then the Florida insurance market would experience an increase in capacity with little needed support from the reinsurance market.
3. A properly structured Exchange with a disciplined underwriting approach would act as the vehicle for the influx of funds from the national and international insurers.

FOREMOST CORPORATION OF AMERICA - Richard Lee Antonio, President and CEO

Mr. Antonio did not respond to the Sam Miller letter. Instead, he offers comments concerning the impact of Florida rating law on availability of insurance in Florida. The crux of the problem is that the current Florida rating law and environment makes it difficult for insurers to charge rates adequate enough to exercise proper fiduciary responsibilities to stockholders. Therefore, insurance companies are forced to reduce their presence in Florida. The major issues involved with the problem include the following:

1. Extreme differences in rates computed by private industry actuaries and Florida Department of Insurance (DOI)actuaries.

2. There is a threat of regurgitation of premiums with little preliminary indication of the amount.

3. The burden of proof is placed on private industry to justify increased rates as opposed to that burden being placed on the government proving that rates are excessive.

4. The regulation of rates is performed by DOI as opposed to rates being regulated by competitive market forces.