



INFORMATIONAL MEMORANDUM

OIR-13-03M

ISSUED

October 28, 2013

Florida Office of Insurance Regulation

Kevin M. McCarty, Commissioner

To Property Insurers Exploring the Feasibility of Writing Primary Flood Insurance In the State of Florida

Section 239 of the federal Biggert-Waters Flood Insurance Reform and Modernization Act of 2012 (Biggert-Waters Act) specifically provides that private flood insurance sold by licensed insurers may satisfy the requirements for flood coverage established by the Federal National Mortgage Association ("Fannie Mae) or the Federal Home Loan Mortgage Corporation ("Freddie Mac"). In the wake of the Biggert-Waters Act, several insurers have expressed an interest in offering coverage in Florida that satisfies these requirements.

In response, the Florida Office of Insurance Regulation (Office) is providing the following information as suggestions for insurers considering entering this market and as a means to facilitate the filing process. It reflects the Office's initial review of federal and state legal requirements that may apply to the issuance of private flood coverage. It is **not intended to be comprehensive in scope**.

Insurers are not required to offer flood coverage. However, private insurers that choose to offer a flood insurance product may offer coverage as:

- A stand-alone allied lines insurance policy,
- An endorsement to either an existing property insurance form such as a homeowners insurance policy form or dwelling policy form, or
- Incorporated into the policy as a covered peril.

The Biggert-Waters Act allows Fannie Mae and Freddie Mac or other federal entities for lending regulation to apply their own requirements related to the financial solvency, strength, or claims-paying ability of private insurance companies from which the entity or agency will accept private flood insurance. Currently, these agencies are in the process of promulgating rules to implement the financial strength requirements and a variety of other provisions of the Biggert-Waters Act.

FINANCIAL CAPACITY

Writing primary flood insurance coverage on a statewide basis may increase the catastrophe risk assumed by admitted insurers electing to offer this coverage. As a result, insurers desiring to provide primary flood insurance coverage, whether as an endorsement to a homeowners policy or as a stand-alone allied lines policy, will need to demonstrate the financial capacity to assume this risk by providing a Plan of Operation and Financial Projections. Such a plan typically includes:

- A three year financial projection in Uniform Certificate of Authority Application (UCAA) format,
- The basis for the assumptions used in the projections,
- A statement regarding the sensitivity of the assumptions to market conditions,
- An estimate of total gross and net exposure to be written under the insurer's flood program,
- An estimate of the total gross and net exposure to be written on any one risk, and;
- A summary regarding the insurer's plans for catastrophe reinsurance for the flood exposure.

An insurer electing to offer primary flood coverage as a stand-alone allied lines policy will also need to have a certificate of authority for that line.

OPTIONS FOR DEVELOPING RATES FOR PRIMARY FLOOD COVERAGE

Develop Rates Based on National Flood Insurance Program (NFIP) Rates in Effect Prior to October 1, 2013

Because primary flood coverage is a new coverage not widely written by admitted insurers, there is little voluntary Florida loss data available to support a rate for this coverage. However, to facilitate the development of a rate for this coverage, the Office utilized actual National Flood Insurance Program experience from 1978 to 2012 to develop loss and allocated loss adjustment expense ratios for Florida. Admitted insurers may choose to use these ratios as a basis for a primary flood rate filing, supplemented with the insurer's own expense factors, while taking into account any differences in coverage. This expedited option is likely the easiest one to have filed and approved. A spreadsheet demonstrating this analysis is attached.

(See the attached file – “Florida Flood Indicated Loss and ALAE Ratio.xlsx”)

Develop Rates Based on a Competitive Analysis

Insurers may also use a comparable competitive filing as another option to justify rates for primary flood insurance coverage. Insurers may choose to conduct a competitive analysis by reviewing the rates and rating factors of insurers now writing primary flood insurance in Florida, and supplementing that filing with the insurer's own expense factors, while taking into account any differences in coverage. There may be material differences in coverage for primary flood insurance products designed for homes without a mortgage, since the requirements for federally-guaranteed mortgages may not apply.

Other Methodologies

Insurers may choose to use industry Florida flood data including surplus lines loss data, with appropriate adjustments for any change in coverage and individual company expenses.

Insurers may also use available catastrophe flood models with documentation on the model including validation to past flood events. These models currently exist for coastal areas, and a new model is reportedly being developed to include inland risks.

Excess Rate/Individual Risk Rate

Pursuant to s. 627.171, F.S., insurers may also use the Excess Rate statute (also known as "consent-to-rate") to offer rates above the filed and approved rates with the informed consent of the policyholder. The statute limits the use of this option to no more than 5% of the business written or renewed each calendar year for any line of personal insurance.

Pursuant to s. 627.062(3)(a), F.S., insurers may individually rate the risk for Allied Lines or Dwelling Fire policies only (not for homeowners), where there is an unusual or high exposure risk.

OPTIONS FOR DEVELOPING FORMS FOR PRIMARY FLOOD COVERAGE

Insurers have several options in developing a proposed flood insurance policy form.

Federal Private Flood Insurance Requirements

Section 239(a)(7) of the Biggert-Waters Act requires federal agency lenders to accept private flood insurance as satisfaction of the federal flood insurance requirement if the coverage meets certain conditions. These conditions include, but are not limited to:

- The private flood insurance coverage must be at least as broad as the coverage provided under a standard NFIP policy, including deductibles, exclusions, and conditions offered by the insurer.
- The policy must provide for 45 days written notice of cancellation or non-renewal to the insured and the lending institution or the federal agency mortgage lender.

- Information must be provided about the availability of flood insurance coverage under the NFIP.
- The policy must contain a mortgagee interest clause similar to the mortgagee interest clause contained in a standard NFIP policy.
- The policy must contain a provision requiring an insured to file suit not later than one year after the date of a written denial of all or part of a claim under the policy.
- The cancellation provisions must be as restrictive as the provisions contained in a standard NFIP policy.

Develop Forms as a Stand Alone Allied Lines Policy Based on NFIP Coverage

Insurers may choose to offer primary flood coverage based on the coverage provided by the NFIP, recognizing that these forms will need to be amended to: 1) remove references to community flood program and other NFIP/Federal Emergency Management Agency (FEMA) requirements; 2) incorporate provisions specifically required under Florida law; and 3) add new provisions to meet the federal definition of “private flood insurance.” For example:

- Provisions pertaining to the (NFIP, Federal Emergency Management Administration (FEMA), the National Flood Insurance Act of 1968, the Code of Federal Regulations (CFR), the Federal Government, the Federal Insurance Administrator, and Federal common law should generally be removed.
- The Summary of Significant Changes should be eliminated.
- A \$500 deductible must be offered and the deductible provision should be modified to comply with s. 627.701(7), F.S.
- The cancellation, nonrenewal and renewal provisions must comply with s. 627.4133(2), F.S.
- The form should be modified to comply with the Valued Policy Law (s. 627.702, F.S.)
- Amendments are necessary to satisfy the requirements of s. 627.714, F.S., regarding a unit owner’s residential property policy.
- For unit owner’s property policies, coverage for property which is the policyholder’s insurance responsibility under a condominium association agreement should be added pursuant to s. 718.111(11)(g)2., F.S., and any conflicting policy restriction should be modified accordingly.
- The refund provisions that apply after policy cancellation need amendment for consistency with Rule 69O-167.001, Florida Administrative Code.
- The loss payment provision must be modified to comply with s. 627.4265 and s. 627.70131(5), F.S.
- Language should be added to address s. 626.854(14), F.S., regarding 48 hours’ notice to meet with the claimant or inspect the insured property.
- The supplemental claim guidelines need to be removed.
- The form needs to satisfy the readability requirements of s. 627.4145, F.S., including the addition of a table of contents.

- The following provisions should be removed: Amendments, Waivers, Assignment; Reduction and Reformation of Coverage; and Continuous Lake Flooding.
- The policy execution signature should be updated.
- The Concealment or Fraud and Policy Voidance provision should be amended to comply with s.627.409, F.S.

Develop Flood Forms as an Endorsement to a Homeowners Policy

Offering flood coverage as an endorsement to a homeowners policy may be a simpler option for insurers since Florida's statutory requirements would already be included in the base policy. However, the insurer should be aware that:

- Coverage must meet the federal private flood insurance requirements described in this informational memorandum.
- Florida statutory requirements applicable to homeowners insurance coverage must be satisfied, such as:
 - o Replacement Cost coverage must be offered (s. 627.7011, F.S.).
 - o Law and Ordinance coverage must be offered (s. 627.7011, F.S.).
 - o A \$500 flood deductible must be offered (s. 627.701(7), F.S.).
 - o The cancellation, nonrenewal and renewal provisions must comply with s. 627.4133(2), F.S.

Develop Forms Based on Private Flood Insurance Policy Forms Already Approved

The Office has approved forms for several insurance companies that have been writing primary flood insurance coverage or excess flood insurance coverage in Florida long before the Biggert-Waters Act became law. This coverage typically has been for properties not subject to a mortgage, properties requiring coverage in excess of the \$250,000 limit historically available from NFIP, and properties that may not meet the requirements for properties subject to a federally-guaranteed mortgage. As a result, there may be material differences in coverage. Insurers would need to amend the forms to comply with the new federal provisions.

If you have questions regarding this memorandum, please contact Sandra Starnes, Director of Property and Casualty Product Review, Florida Office of Insurance Regulation at Sandra.Starnes@flor.com or (850) 413-5344.

Resources: The Biggert-Waters Flood Insurance Reform and Modernization Act of 2012