2016 REINSURANCE PROGRAM
TRADITIONAL RISK TRANSFER (COASTAL ACCOUNT)

Board of Governors Teleconference Meeting
May 24, 2016

Executive Summary

Citizens' enabling statute requires it to make its best effort to procure catastrophe reinsurance to cover up to a 100-year storm in the private market at reasonable rates. The analysis and decision to purchase catastrophe reinsurance coverage is evaluated by staff each year and a recommendation is made to the Board of Governors.

Citizens' Board of Governors and staff recognize that the event most likely to trigger assessments would be a catastrophic hurricane or series of hurricanes striking Florida. Transferring risk through the use of catastrophe reinsurance offers an effective means to reduce or eliminate the amount and likelihood of assessments after such an event. For reinsurance purposes, the PLA and CLA are evaluated together while the Coastal Account is evaluated separately. After ten years of no hurricanes, substantial surplus has been accumulated in all accounts to pay for future claims. The PLA and CLA continue to be financially stronger than the Coastal Account with respect to claims paying ability prior to assessments; as such Citizens' risk transfer programs are focused on the Coastal Account.

Citizens' goal of reducing exposure and, by extension, reducing or eliminating the amount and likelihood of its assessment burden on Florida tax payers can be achieved in part through the transfer of risk. Citizens has traditionally accomplished this risk transfer via participation in the Florida Hurricane Catastrophe Fund (FHCF) reimbursement program, traditional reinsurance markets and in the capital markets. Citizens' participation in the reinsurance markets delivers a dollar-for-dollar reduction of potential assessments that result from losses exhausting Citizens' surplus and FHCF coverage. Citizens' strategic plan considers and incorporates the transfer of hurricane risk in the Coastal Account to the global reinsurance markets. This plan has historically included both traditional risk transfer and capital markets risk transfer. The proposed 2016 risk transfer program incorporates strategic elements from the continuation of the existing risk transfer program, which included: coverage for the mandatory layer of the FHCF, a single year traditional reinsurance program, and a multi-year capital markets risk transfer program. It is noteworthy that support by the Board of Governors for consistent and aggressive pursuit of risk transfer, coupled with the significant amount of depopulation over the last four years, would eliminate any probable assessment for a 1-100 year event for the 2016 season.

Citizens has a total of $2.243 billion of multi-year risk transfer carrying over from 2015 - $1.8 billion of capital markets risk transfer and $443.3 million of traditional risk transfer as summarized below:

$1.5 billion - Year 3 of the 2014 3-year capital markets transaction – Everglades Re 2014-1

$300.0 million - Year 2 of the 2015 3-year capital markets transaction – Everglades Re II 2015-1

$202.0 million - Year 3 of the 2014 traditional aggregate 3-year reinsurance

$241.3 million – Year 2 of the 2015 traditional aggregate 3-year reinsurance

$2.243 billion total available risk transfer in place for 2016 season

Citizens' strategic plan for 2016 involves a renegotiation of the $443.3 million of multi-year aggregate reinsurance ($202 million of 2014 multi-year aggregate reinsurance and $241.3 million of 2015 multi-year aggregate reinsurance) and reallocate the related coverage alongside and above coverage provided by the FHCF (single year, per occurrence, ex-CNR losses), and transfer $221 million of commercial non-residential (CNR) risk in order to retain a portion of surplus for most catastrophic events, ultimately further reducing the amount and likelihood of assessments beyond the 1-100 year event to the citizens of Florida. This in turn also provides for additional reinsurance and claims paying resources in the event that multiple hurricanes strike Florida. Citizens' private reinsurance programs are structured to also provide liquidity to Citizens by allowing Citizens to obtain reinsurance recoveries in advance of the payment of claims after a triggering event.

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Staff has worked extensively with Citizens' co-brokers and financial advisor, Raymond James, to evaluate available options relating to the structure, terms, pricing, and other relevant matters in structuring the 2016 traditional risk transfer program. Citizens and its co-brokers, Willis Re and Guy Carpenter, convened with a number of global traditional reinsurers in the past few months to discuss reallocating the 2014 and 2015 multi-year reinsurance coverage alongside and above the FHCF coverage. This shift of multi-year reinsurance coverage to alongside and above the FHCF as single year per occurrence coverage will result in an incremental cost of approximately $15.4 million. In addition, Citizens proposes to place $221 million, or 50% of CNR losses in excess of $517 million, to the global reinsurance market. Multiple layers of traditional reinsurance coverage in the total amount of $664.3 million are summarized as follows (in millions):

	Cover	Attach	Coverage Type
Layer 1	$ 443.3	$670	Occurrence (ex-CNR)
Layer 2	$ 221.0	$517	Occurrence (CNR only)
TOTAL	**$ 664.3**		

Layer 1 of this program represents the reallocating of coverage from the 2014 and 2015 multi-year aggregate reinsurance coverage to the layers alongside and above the FHCF, and would work in tandem with the mandatory coverage provided by the FHCF to include (1) the 10% of losses not covered by the FHCF (note that the FHCF reimburses 90% of covered losses), and (2) coverage of losses in excess of the FHCF limit. Layer 2 of this program would provide coverage for CNR losses not covered by other layers of the program and for which Citizens has no FHCF coverage.

The traditional reinsurance program provides coverage for personal residential, commercial residential, and commercial non-residential covered losses. It is important to note that Citizens' co-brokers also perform reinsurer market credit analyses to evaluate the financial strength of reinsurers seeking placement on Citizens' program. The purpose of this process is to ensure Citizens' placement is with reinsurance partners that are financially stable, solvent, and properly managed in order to pay valid claims when due. This analysis includes reviews of various qualitative and quantitative factors, including, but not limited to, a review of credit ratings and reports, review of financial statements, key financial ratios, review of management, and claims settlement history.

RECOMMENDATION

Staff recommends that Citizens Board of Governors:

a) Approve the recommendation to transfer $443.3 million of 2014 and 2015 multi-year traditional reinsurance to alongside and above the FHCF coverage (Layer 1);

b) Approve the recommendation to enter into a one-year contract for risk transfer of $221 million in excess of $517 million of CNR losses through traditional markets for Layer 2; and

c) Authorize staff to take any appropriate or necessary action consistent with the Action Items for a total 2016 risk transfer program of $2.464 billion.