☒ **ACTION ITEM**	☐ **CONSENT ITEM**
☐ **New Contract**	☐ **Contract Amendment**
☐ **Contract Amendment**	☐ **Existing Contract Extension**
☒ **Other Committee Minutes**	☐ **Existing Contract Additional Spend**
	☐ **Previous Board Approval**______________
	☐ **Other**_______________________________

Action Items: Items requiring detailed explanation to the Board. When a requested action item is a day-to-day operational item or unanimously passed through committee it may be moved forward to the board on the Consent Index.

☐ **Move forward as Consent**: This Action item is a day-to-day operational item, unanimously passed through committee or qualifies to be moved forward on the Consent Index.

Consent Items: Items not requiring detailed explanation to the Board of Governors. Consent items are contract extensions, amendments or additional spending authorities for items previously approved by the Board.

Item Description	The Finance and Investment Committee meeting Minutes December 14, 2021
Purpose/Scope	Review of the December 14, 2021 Finance and Investment Committee to provide opportunity for corrections and historical accuracy.
Contract ID	N/A
Budgeted Item	☐Yes ☒No
Procurement Method	N/A
Contract Amount	N/A
Contract Terms	N/A
Committee Recommendation	Staff recommends the review and approval of the December 14, 2021 Finance and Investment Committee minutes.
CONTACTS	Jennifer Montero, CFO

CITIZENS PROPERTY INSURANCE CORPORATION

MINUTES OF THE
FINANCE AND INVESTMENT COMMITTEE MEETING
Tuesday, December 14, 2021

The Finance and Investment Committee (FIC) of Citizens Property Insurance Corporation (Citizens) convened at the Renaissance Tampa International Plaza Hotel on Tuesday, December 14, 2021.

The following members of the FIC were present:

Carlos Beruff
Erin Knight
Marc Dunbar

The following Citizens staff members were present:

Jennifer Montero
Barbara Walker
Barry Gilway
Kelly Booten
Tim Cerio
Christine Ashburn
Jay Adams
Joe Martins
Violet Bloom
Jeremy Pope
Michael Peltier
Andrew Woodward

The following people were present:

Kapil Bhatia	Raymond James
Nathaniel Johnson	Bank of America
Doug Draper	Bank of America
George Smith	Bryant Miller Olive
Duane Draper	Bryant Miller Olive
Adam Schwebach	Gallagher Re
John Generalli	Wells Fargo
Mathew Sansburg	RBC Capital Markets
Nathaniel Johnson	Bank of America

Call Meeting to Order

Barbara Walker: Good afternoon, and welcome to Citizens' Finance and Investment committee meeting that is publicly noticed in the Florida Administrative Register to convene immediately following Citizens' Audit committee meeting. Those in attendance through the public link are automatically in listen only mode. Citizens' Board and committee meetings are recorded with transcribed Minutes available on our website. Thank you for identifying yourself prior to addressing the committee. I will proceed with roll call to confirm our quorum. Chairman Fields is not attending today. In his absence our Board Chairman Carlos Beruff will be chairing this meeting. Chairman Beruff.

Chairman Beruff: Present.

Barbara Walker: Governor Dunbar.

Governor Dunbar: Here.

Barbara Walker: Governor Knight.

Governor Knight: Present.

Barbara Walker: Chairman you have a quorum.

1. **Approval of Prior Meeting's Minutes**

Chairman Beruff: Perfect, thank you. The Chair will make a **motion to adopt the Minutes from the last meeting (September 21, 2021).**

Governor Knight: **So moved.**

Governor Dunbar: **Second.**

Chairman Beruff: **The Minutes are approved**, thank you. And we will get an update from our investment guru who is fast opening up his book. Mr. Bhatia, welcome.

2. **Raymond James Financial Advisor**

   a. Market Update

Kapil Bhatia: Thank you, Mr. Chairman. Good afternoon, Mr. Chairman and Governors. I will briefly go over the -- can you hear me okay?

Chairman Beruff: Get a little closer, there you go. Thanks.

Kapil Bhatia: I will start with the market update, but please stop me at any point of time for any additional questions. The unemployment rate declined by .4% to 4.2% in November, with 6.9 million people unemployed. While the nonfarm payroll employment rose by 210,000 in the month of November. These unemployment ratios are down considerably from their recent highs in April, 2020, but remain above their levels prior to the COVID 19 crisis. The unemployment rate was 3.5% and 5.7 million people were unemployed. The labor force participation rate increased marginally to 61.8%. However, this is 1.5% below the February 2020 level, and the U6 unemployment rate which reflects real unemployment, which includes people who are looking for full time job, working part time, but looking for full time job, and who are underemployed. That rate is close to 7.8%. The U.S. federal reserves fed funds target rate is still between zero to 25 basis points, and while the official forecast is two to three rate increases in 2022, we expect only one to two rate increases in 2022. However, we will get more color from fed tomorrow regarding what they plan to do in 2022. The FOMC Chair recently talked about in a recent Senate hearing that they will accelerate the tapering of a monthly bond buying purchase program currently in the amount of $120 billion of treasuries and mortgage back securities. Currently the fed balance sheet is at $8.7 trillion as compared to $4.2 trillion. So regardless of how much they taper or how quickly they taper, fed's balance sheet is almost 36% of our GDP and has almost doubled since prior to COVID-19. The real GDP decreased by 3.5% in 2020 compared to an increase of 2.2% in 2019. We expect the 2021 annual GDP to increase by around 5.5%, and then come down to 3.5% in 2023, and then going back to its normal rate of around two to two and-a-half percent starting 2024.

The robust growth in 2021 is primarily because there was a negative GDP in 2020 and we are just playing catch up with all of the fiscal and monetary stimulus. Even with all of the high inflation numbers, you have seen it and everybody is talking about it, we still believe inflation is transient, and which means it is not really permanent. However, it is sticking around for longer than what we initially expected. Partly due to the 2021 American Rescue Plan Act which provided for $1.9 trillion of additional stimulus in March of 2021. If you really compare that $1.9 trillion in additional stimulus, that is 6½% to 7% of our annual GDP. So that is really what is affecting the inflation because of the demand coming from $1.9 trillion. We expect fiscal stimulus to run out and cash saving to deplete by the middle of 2022, and stimulus to slow down, and that should lead to a peak inflation by middle of 2022, and at the time, at that time prices will start to decelerate or decrease towards starting the third quarter of 2022. As demand stabilizes people return to labor force and supply bottlenecks fades away. However, this may change if Build Back Better plan goes through as it will provide large stimulus and some subsidies again, create distortions in the marketplace and disincentives for productive labor and output. So, it depends on where the Build Back Better program goes, that is where the inflation is going to go. At this point of time, it is still unknown, however, we don't expect that bill to go away. By the third quarter of 2022 we expect the inflation rate to be closer to 2.5% as compared to 1.75% in March 2020, and that 75 basis points is really the true increase in inflation.

The equity market is at almost record high due to robust growth, fiscal and monetary stimulus, including all time low historical interest rates, and the markets are up by approximately 20% this year. Interest rate, fixed rate markets have seen interest rates recover significantly in 2021, as the economy continues to recover. However, due to structural and demographic constraints, we expect interest rates to remain range bound from here until the end of 2022, with 5-year treasuries somewhere in the range of one to one and-a-half percent and 10-year treasury from 1.25% to 1.75%. Currently the 10-year treasury is at 1.5%, and the reason for that is simply everybody expects growth to come down and that is reflected in the fixed income market. So, the interest rates don't reflect the robust growth or inflation as the equity markets reflects. Fixed income market through October of this year, corporate bond issuance is at $1.7 trillion or 18% lower than the record breaking $2.1 trillion in 2020, and that reflects that the corporations have enough liquidity and they have gone through the crisis and they have build-up the liquidity and now they're not issuing debt as they did in 2020.

The muni-market issuance is also strong, approximately $400 billion compared to $428 billion issued year over the same time period in 2020. Overall, there has been strong demand for all fixed income products and that is reflected in our portfolio, also. Lastly, the risk transfer market in 2020 there were $97 billion of insured losses globally, which were mostly driven by smaller event as no single event occurred which has incurred more than $3 billion of losses. As of early fourth quarter of 2021, insured losses are at approximately $107 billion globally which is 13% above the 10-year average of $95 billion. The largest event so far in 2021 is Hurricane Ida, which we all know very well. Estimates are somewhere in the range of $35 billion, followed by European flooding in the amount of $12 billion and the Tropical Storm Uri which resulted in a $15 billion of insured losses. There is enough capital in the reinsurance market, approximately $660 billion. It has increased by around $100 billion over the last three years. However, the rates are going to remain at the upward trajectory level because the overall global risks have also gone up significantly. So, the capital have increased, but not in the proportionate amount of the insured risks. So that is putting the pressure on the reinsurance and the insurance rates. While the global markets are improving marginally, the Florida market is still experiencing dislocation, again, due to litigation and social inflation, nothing new here, and continued adverse loss development. For 2022 we expect reinsurance rates to increase by 10% and most carriers will pay five to 10% more in the reinsurance for the upcoming season. With that, I will stop and happy to answer any questions.

Chairman Beruff: I have a question. When you keep talking about transitory inflation, right, which is what your determination is going forward. What is the inflation rate in the last 12 months?

Kapil Bhatia: The last 12 months was 6.8% were the most recent numbers.

Chairman Beruff: So, the 6.8 is going to get -- it is fixed, you are not going to see deflation, right?

Kapil Bhatia: We are not going to see a deflation. However, the inflation growth rate will decelerate.

Chairman Beruff: Right. So, the 6.8 we are stuck with that in our pocketbooks.

Kapil Bhatia: That is correct.

Chairman Beruff: So, when you say that inflation rate will fall and decelerate, you are talking about future inflation rates at three, three and-a-half, eventually down to two, two and-a-half percent, right?

Kapil Bhatia: That is correct.

Chairman Beruff: So, the inflation rate that we have digested over the last 18 months is out of our purchasing power.

Kapil Bhatia: That is correct, but the 6.8% includes because what we did not see an inflation in 2020. So, if you look at over a two-year period, the inflation rate is closer to four percent. The base prices will shift. The inflation will shift from -- goods and services to housing, because the housing prices have gone up.

Chairman Beruff: Okay, but we are not going to see the inflation rate going to adjust downward enough to recuperate and get it back to the average inflation rate which has been for the last decade between 1.7 and 2.1.

Kapil Bhatia: That is correct. We expect over the next five years' inflation rate to average out closer to a 2.2% to 2.3%.

Chairman Beruff: So, you think the inflation rate over a five-year period, including the six plus point inflation rate in the last 12 months will average down to 2.1?

Kapil Bhatia: 2.5% approximately, 2.2% to 2.5%.

Chairman Beruff: So, it is 25% higher than the target inflation rate that the feds set 15 years ago.

Kapil Bhatia: The target inflation rate is two percent.

Chairman Beruff: Right.

Kapil Bhatia: Everybody in the world is trying to increase the inflation rate because to some extent that is good.

Chairman Beruff: Yes, deflation is terrible, we understand that. The Japanese suffered that for two decades, but I just wanted to make sure I understood your premises is not that the inflation rate is really going to drop an average, your hope is that over a five-year period the inflation rate adjust to two and-a-half percent.

Kapil Bhatia: That is correct. It is a hope, unless there is more fiscal stimulus. When you add$5.8 trillion to the economy in just over the 24 months, then any additional stimulus will lead to the higher inflation and maybe even spiraling inflation.

Chairman Beruff: Have you penciled out a projected inflation rate if the Build Back Better plan gets approved?

Kapil Bhatia: Our numbers don't include that.

Chairman Beruff: No, I know that I am aware of that. But have you played with that scenario and what it will do to the inflation rate in '22 if it passes?

Kapil Bhatia: I mean, we can do a reverse engineering with $5.8 trillion it led us to a 6.8% inflation rate. So, if you add in another 30% more, which is $1.75 trillion, probably that itself should add two to two and-a-half percent of inflation rate just from that, but all of that will not come in one year, because $1.8 trillion will not be spent.

Chairman Beruff: Right.

Kapil Bhatia: However –

Chairman Beruff: It will take two years.

Kapil Bhatia: Part of that is going to be permanent at some point of time. I know it is the balance budget and everything else. So, there will be a much bigger impact on inflation from that $1.75 trillion which will eventually increase inflation again.

Chairman Beruff: Thank you.

Kapil Bhatia: Thank you.

Chairman Beruff: Any other questions?

Kapil Bhatia: Thank you.

3. Chief Financial Officer Report

a. Update 2021 Layer Charts

Jennifer Montero: Thank you. Behind tab three are the updated layer charts. They should also be on the screen, thank you. So, the layer charts we presented in September projected from December 2020 to 09/30/21 compared to what was actually June 30th. So, where these updated charts are based on actual September 30th compared to our projected 30th. The Cat Fund estimates for coverage in the attachment are based on June 30th in force, whereas private reinsurance premium is based on the 09/30 exposure. These updated charts show how the PML has grown and how reinsurance coverage has shifted, exposing additional surplus at the top of the layers. Due to our extensive growth, the PMLs are higher than expected, and as policy count increases, PMLs will increase. This will shift. The coverage layers to lower return times and expose more surplus at the top of the tower where the most severe storm scenarios exist. As you will see on the next two slides, the coastal account surplus exposure grew from 40% to 45%, and the PLA, it shifted more dramatically from 65% to 80%. Next slide, please. So, on the coastal account, our policy count has gone from 156,000 which was our projected 09/30 numbers, our actual 09/30/21, came out to 160,000. The total insured value went from $51 to $55 billion, and the 1-in-100 year PML went from $3.7 to $3.9 billion. The Cat Fund attachment and coverage actually went down. We overestimated the Cat Fund. We estimated that the attachment at $601 million, it came in at $599 million, and the coverage at $1.2 billion and it came in at $1.19 billion. And the 1-in-100 year surplus exposed is $.868 billion versus $1.011 billion. So, the projected 09/30 PMLs compared to the actual 09/30 PMLs, we projected growth of 15% when we originally did this, and the actual PML growth was 19% from 12/31/20. The private coverage originally exhausted around the 1-in-100 year event on our first layer chart. Now it exhausts around the 1-in-94 year event, you can see on the right. The TIV also increased in this, which is the exposure, the total insured value from 12/31 to 09/30 increase is 7.32% or from what we projected to actuals. Surplus exposed in the 1-in-100 year was 40% and now it is up to 45%. More surplus is exposed and anticipated because the PML is higher than we anticipated, but this was not nearly as dramatic as the next slide, Barbara, please. Thank you.

Here on the PLA our estimates were much more dramatically different. It starts with the projected growth. The policy count was 514K versus 546K. The total insured value went up from $127 billion to 150, and the 1-in-100 year PML went up from $3.5 to $3.8 billion. And in this case the Cat Fund retention actually went up from $749 to $788 million which provided $40 million more in coverage, or it shifted up by $40 million, and the coverage increased from $1.497 billion to $1.575 billion or about $80 million. So, it provided about $80 million of additional coverage. And the 1-in-100 year surplus exposed went from $1.1 to $1.3 billion, and you can see again the private reinsurance originally exhausted at the 1-in-100 year, and now it exhausts at the 1-in-89. And again, there is more surplus exposed than anticipated because the PML is higher than anticipated. It is combined with the changes in the Cat Fund coverage size and placement. The TIV for this account actually increased by 14.9%, which means we triggered the growth limitation factor in the private reinsurance contract. It says that if we grow within plus or minus 10% there is an additional premium due or a premium credit due. And so, because we went over the 10% in this account for the PLA account, we will have additional premiums due to the reinsurers. And I will stop for any questions.

Chairman Beruff: What is the monetary, what is the dollars associated with our increased premium that we have to pay the reinsurers for our growth?

Jennifer Montero: It is not final yet, but it ranges between $12 and $13 million.

Chairman Beruff: In addition to what we already paid?

Jennifer Montero: Correct.

Chairman Beruff: And that will carry us to the end of the policy?

Jennifer Montero: Yes.

Chairman Beruff: Thank you. Keep going.

Jennifer Montero: Okay, great. The next section is Section four.

Chairman Beruff: I am sorry, Mr. Dunbar, are you there?

Governor Dunbar: I am, yes.

Chairman Beruff: I apologize, I should have asked if you had any questions before I moved on.

Governor Dunbar: No, sir, I am good, thank you.

Chairman Beruff: Thank you. Go ahead.

b. 2022 FIC Charter – Annual Review

Jennifer Montero: The next section is the FIC charter. So, each year we bring the charter to the committee for any reviews, comments, edits. Staff recommends no changes.

Chairman Beruff: So, do we want a motion that says we are ready with that?

Jennifer Montero: Yes, please.

Chairman Beruff: The Chair will entertain a motion.

Governor Knight: So moved.

Chairman Beruff: Do we have a second?

Governor Dunbar: Move approval, Chair.

Chairman Beruff: Thank you.

Governor Dunbar: Second.

Chairman Beruff: All right, approved. Next.

c. Investment Portfolio Update

Jennifer Montero: Thank you. Finally, behind the last tab is the Citizens' investment summary.

Chairman Beruff: Can we get this to match the screen?

Jennifer Montero: I don't know if Barbara has it.

Chairman Beruff: Don't have it, that is fine.

Jennifer Montero: We can do it tomorrow, oh wait we don’t do this tomorrow.

Chairman Beruff: No, we can do it right now, that is good. We can wing it from paper.

Jennifer Montero: Okay.

Chairman Beruff: Old fashioned, old school.

Jennifer Montero: The total portfolio is $9.56 billion with approximately $8.6 billion externally managed by 10 money managers. The remaining $900 million is internally managed and primarily consist of the operating funds, debt service funds and debt service reserve funds. The taxable portfolio is $8.9 billion or approximately 93%, and the tax-exempt portfolio is $640 million. The portfolio is very conservative and stable, with sufficient liquidity to pay any current claims or potential future claims. The total portfolio average duration is stable and is just over 4.71 years. The income return and total return for one year, approximately 1.08% and -.08% respectively. The income and total returns reflect a stable portfolio as interest rates and corporate spreads have stabilized. On slide two, the treasury rates have increased over the last 12 months, but we expect three to 10-year treasury rates to remain at current historical low levels until the end of 2022. The yield curve steepened earlier in the year, but since then have become relatively less steep. The current two to 10-year spread is 82 basis points as compared to 57 basis points a year ago. The tax-exempt rates have also increased, but at a lesser pace than the treasury rates. Slide three. Both the taxable and tax-exempt portfolios have very strong credit qualities, approximately 72 percent of the taxable portfolio is in money market funds or rated A or higher, and 100 percent of the tax exempt portfolios in money market funds are rated A or higher, and approximately 38% of the total portfolio is in treasury and agency securities or in money market funds. And then finally on slide four, the portfolio income return is stable or 1.08% over the last 12 months, and 1.25% over the last two years. And the portfolio return, total return is negative 8 basis points over the last 12 months reflecting an increase of interest rates but is strong at 2.79% over the last two years.

Chairman Beruff: Okay, I am confused. But that is easy to do. So, what is our -- what is our net yield on our $8.9 billion dollars?

Kapil Bhatia: For the last 12 months it is 1.08%.

Chairman Beruff: 1.08% net of fees.

Kapil Bhatia: Net of fees.

Jennifer Montero: Uh-huh.

Chairman Beruff: Wow, that is not good, that really isn't very good. Tell me why.

Kapil Bhatia: Our investment policies mostly, not mostly, it is all of fixed income, and over the last 10 years, 12 years you could see the interest rates have continuously declined. So, it is stable and liquid portfolio with effectively no credit risks and generating closer to 4 years of treasury return plus some spread is where the markets are.

Chairman Beruff: Should we revisit our policies, because 1.08 isn't going to keep us flush, and you have got an inflation rate even under the best case scenarios two and-a-half to three times that amount. What is our fees costing us?

Kapil Bhatia: Five basis points.

Chairman Beruff: I am sorry?

Kapil Bhatia: Five basis points.

Chairman Beruff: Five basis points. That is across all of the people that we use.

Kapil Bhatia: Correct.

Chairman Beruff: That is pretty cheap.

Jennifer Montero: We can bring the policies to the next FIC meeting –

Chairman Beruff: Well, that is next.

Jennifer Montero: In March, we can bring the investment policies to the FIC committee to review for any -- we will put some –

Chairman Beruff: What was your average yield in three years before this year?

Kapil Bhatia: The three-year income return is 1.66%.

Chairman Beruff: So, we are down 60%.

Kapil Bhatia: We are down 60% –

Chairman Beruff: 52%.

Kapil Bhatia: Yes.

Chairman Beruff: 50%.

Kapil Bhatia: And that reflects the changes in the market where the fed rate, three-year returns include everything prior to COVID. So effectively as the fed cut rates from 1.75 to zero percent, that brought down our return, income return on the yearly basis.

Chairman Beruff: Do we have other similar portfolios nationally with similar government constraints that are yielding better than one point, what did you say again, 1.18?

Jennifer Montero: 08.

Chairman Beruff: 08.

Jennifer Montero: 1.08.

Chairman Beruff: Do we have other $9 billion portfolios that we can see that have done better yield than we have?

Kapil Bhatia: We can, we can talk about the portfolio where we serve as investment consultant and there are a couple of large portfolios which produces similar returns, because most of those, most of our clients with a very large portfolio, including ours, as you know, are in fixed income with no risk because we need to pay, it is as an when event hits. So, we have a portion in liquidity fund, portion in claims paying and a long duration fund. Similarly, we have earthquake funds and a wildfire funds which are meant to be for the – to pay the claims as an event hit and their returns are very similar, because it is risk averse portfolio. There are no equities or no structured products in any of the portfolio..

Chairman Beruff: I think there was an answer somewhere in that explanation that missed me.

Kapil Bhatia: The returns are similar.

Chairman Beruff: So, what I would like to do between now and your March meeting, and it doesn't have to wait until March, you can give me a report next week, after the first of the year. I would like to see comparisons of other eight to $12 billion portfolios that have similar government mandated constraints as to quality and liquidity and so forth and what they have done the last 12 months, because when you are talking about splitting hairs, as you know, five basis points with this kind of numbers or 10 basis points are not insignificant money. You know, we have discussed that and going to continue to discuss with this Board and moving forward is how do we get to operational break even and we are not there, but that has other constraints which are legislative and, you know, tort reform and other boring subjects that we will have to get dealt with, but I am also concerned that we just make sure that we keep up with other returns, and if we have to change policies then I guess Ms. Montero will bring that policy forward. How much flexibility do we have in our policy changing?

Kapil Bhatia: I am happy to do it, but the returns, the answer to your question was returns are very similar within plus, minus 10 basis points, but we are happy to share that with you, not in the March meeting, even prior to that, but as you know, the returns are a function of risks.

Chairman Beruff: Right.

Kapil Bhatia: Right now it is completely riskless. So, if we add more liquid funds, for example, from private equity or long duration fund, your returns can be increased, but however, it does not provide liquidity and adds liquidity risk.

Chairman Beruff: I am sure that the staff is as confident as are you as to when you get a hit on liquidity, is the liquidity going to go out in 12 months, 24 months, 36 months, 48 months. It takes litigation, it takes time. So how much liquidity do you actually need in a 12-month period and how much do you need in a 24, how much you need in a 36, how much you need in a 48-month period. I have never asked these questions because I never realized that our returns were getting so low. 1.6 was sort of, okay, 1.6, 1.7.

Jennifer Montero: If Barbara can put the layer charts back up, we can show you some things.

Chairman Beruff: Great.

Governor Knight: How much, I think in other words, how much leeway could there be in the investment policy.

Kapil Bhatia: We certainly can go through that. It may be helpful internally, so we will have, it is just two data points we would like to share while the layer chart is coming. If you can go to the detail investment report which is the last page before the A&U tab in the book. No, just before that.

Jennifer Montero: I don't have that. That is different than I have.

Kapil Bhatia: Go to the detail one.

Chairman Beruff: Go on to portfolio material distribution sheet.

Kapil Bhatia: That is correct, yes.

Chairman Beruff: Okay, got you.

Kapil Bhatia: So –

Chairman Beruff: So, four billion is in less than five years. Is that what I am reading?

Kapil Bhatia: Our overall duration as Jennifer mentioned earlier in her report is around 4.7 years, but here you can actually see it, how the distribution of the portfolio is. So, we do manage liquidity, not everything is available on day one, but it is all fixed income. So, you can see it is a billion dollars, for example, or 11% of our portfolio is for the operating expenses, including reinsurance expenses which are large and our debt service expenses. Then we have a liquidity staggered based on where the returns are. So, the top portion which is greater than five years produces the biggest return, but then at the lowest end where we have around $2 billion, if you add up the four bottom boxes, that is really generating currently zero, because the fed funds rate is zero, but those are the funds we would need to pay the claims, which have been going through it right now and less the expenses over the next 12 months. So, our portfolio is staggered, and the policy is based on -- sorry, go ahead, Jennifer.

Jennifer Montero: Go ahead.

Kapil Bhatia: And the portfolio is based on what the layer chart is. So, everything in the layer chart is on the board.

Chairman Beruff: I guess we can't cast the company on revenues without having to manage the portfolio of investments?

Kapil Bhatia: The revenues come in to it and we invest it right away. So, the revenues don't stay. So, billion dollars basically is the revenues which are coming in, and it is going out. So, it is continuous. The money comes in and then we pay the expenses and the money, if we have anything left over, we look at the liquidity analysis and transfer to the investment managers for a longer duration. Sorry, Jennifer you were saying.

Jennifer Montero: The layer charts the way that they're built, the green that is basically our retention, up to that point, that is the liquidity of investment policies. And then the claims paying policy takes you from that green bar all the way up to the 1-in-100, and then the long duration is all the money that we have above the 1-in-100. So, we try to manage the timing.

Chairman Beruff: No, the long term problem though is that we take investment income, and we pay operational costs. That is what we have been doing for years, right? So as that becomes, as the investment income dwindles by 60% over the last 12 months, then you have less money, if any money, going into continued surplus.

Kapil Bhatia: That is correct.

Chairman Beruff: So, your margin of error gets narrower and narrower year over year. So, we have got to find a way to, there is two ways to skin the cat. One is to figure out a way to reduce our litigation rate, which is our biggest expenses, and the second way is to reduce our operational cost, and then the third way is to increase our revenue on investments. Somewhere between the three of them you have got to try to figure out this thing and make it work. So, this particular Board member being one of how many of us are in there, eight? Is there eight of us?

Jennifer Montero: Eight currently.

Chairman Beruff: Eight currently. So would like to know if there is a mechanism, you are talking about, earlier you said that the other similar portfolios are plus or minus 10 basis points. Well, 10 basis points is not an insignificant number. I want to be at the top end of that, not at the bottom end.

Kapil Bhatia: We can certainly give you a return.

Jennifer Montero: So in the audit report I mention that –

Governor Dunbar: Chair.

Chairman Beruff: Mr. Dunbar, please. You have a comment or a question?

Governor Dunbar: Yes, I do. I would say you also have a fourth item and that is to radically restructure our approach to reinsurance. Our single biggest expense item is the reinsurance cost. That is a thing that could be looked at.

Chairman Beruff: Mr. Dunbar, could you try to speak into the microphone? At this end it's a little difficult to hear you.

Governor Dunbar: Yes. What I said was, is this is little better?

Chairman Beruff: Much better, much better.

Governor Dunbar: Can you hear me?

Chairman Beruff: Yes, thank you.

Governor Dunbar: What I said was there is a fourth item, and that is reevaluating our approach to reinsurance. That is the single biggest expense item we have.

Chairman Beruff: Okay. Well, that, you know, you have got more experience on this Board than I do. So, I am perfectly comfortable to take direction on how we would go about that in a logical manner. I don't know enough about that to talk intelligently at this point.

Jennifer Montero: Chairman.

Governor Dunbar: Well, I mean, the basics of it and we certainly can explore it more, but we walk around with the back stop of the State of Florida and the assessment authority we have as our true reinsurance. If you look at the layer charts that were presented, if we get hit by two storms, we are basically wiped out and we are going to be assessing. And if you are talking about that we transfer hundreds of millions of dollars in reinsurance premium every year away, which exacerbates our losses, one of the things that we could do is we could, you know, reevaluate our approach to reinsurance to shore up our short term cash flow to try and address the situations that you have identified.

Chairman Beruff: Okay, now I understand perfectly what you said, which is basically since we have this statutory special assessment capability under the State of Florida, why buy reinsurance to save the quarter billion dollars a year that we are paying in reinsurance costs, because where is the benefit, right?

Governor Dunbar: Well, particularly when you are talking about a short term cash bleed since we are not able to offset our operational expenses with our short term interest that we are getting paid.

Chairman Beruff: Listen, the question –

Governor Dunbar: It helps –

Chairman Beruff: I am sorry, go ahead and finish your thought.

Governor Dunbar: No, actually I think you have it completely now, so.

Chairman Beruff: Yes, no, I agree with – with the idea, the question is, what do we statutorily are required to do and what do we make as a business decision as a Board. You are sitting on $9 billion earning nothing and then you are earning 1.08% which is not significant, and then you are writing a check for a quarter billion dollars a year for reinsurance which is significant. Then you have got to question the rationale. At the end of the day if we have the power to assess anyway, why don't we just take the quarter billion dollars, stick into reserves and take our chances?

Governor Dunbar: Exactly, and the one thing that I will say is that will definitely drive the Legislature to be fully aware.

Chairman Beruff: Yes, I realize the political message. I sort of like it personally, but Ms. Montero, if you want to opine on that.

Jennifer Montero: Yes, please. The problem with that approach is that if you do wipe out everything and you do need to assess, assessment brings you back to zero. You have zero surplus.

Chairman Beruff: No, I understand.

Jennifer Montero: I mean, and then you will be assessing year after year after year if the wind blows because we won't be able to build up.

Chairman Beruff: Yes, but if the Legislature forces us to be the default 800 pound gorilla in the insurance market of Florida, which is essentially what has happened to us because we are trying to swim in an Olympics size pool with our arms tied behind our back and our ankles tied, because of all the caveats we have, then they can deal with the repercussions of the fact that they, you know, you can't bring a healthy insurance market into Florida. So, you know, the fact that you can't get that done, then the responsibility falls in their lap, right? Unless I am missing something. I don't see it. Mr. Dunbar has –

Jennifer Montero: Well, yes.

Chairman Beruff: -- brought that. And Mr. Gilway is coming up. Now this is going to get exciting.

Jennifer Montero: And this would affect our rates as well.

Chairman Beruff: All right, here we go. Who did I get mad now?

Barry Gilway: So, for the record, Barry Gilway.

Chairman Beruff: Welcome.

Barry Gilway: I do have to comment on this because this issue was raised before. The Legislature doesn't pay the tab if we run out of surplus. The consumer pays the tab if we run out of surplus, and the assessment level for the consumer is up to 45%. It is 15% per account on the current structure. So, gambling in my opinion with the gambling with the surplus of Citizens. I can't imagine how that could possibly be in the best interest of the state, and I can't –

Chairman Beruff: Well, we respect that. I mean, everybody has an opinion, but at the end of the day the consumers that get hit are the taxpayers and the insurance policyholders of Florida anyway. And the reality is that we have insurance companies in the state of Florida because of all of the legislative constraints that they have to operate in can't make any money. You have $878 billion -- how much $878 million in losses? What is the losses that is you were going to report on tomorrow?

Barry Gilway: Well, the industry.

Chairman Beruff: The industry.

Barry Gilway: Yes, the industry through three-quarters has lost $847 million.

Chairman Beruff: Million dollars operation.

Barry Gilway: $1.147 billion in underwriting loss. The point I would make is the assessment level as you know is, it doesn't just relate to Citizens' policyholders. You know, you have a fifty five, you know, a $55.4 billion base in the state. So, all policyholders ultimately –

Chairman Beruff: Right.

Barry Gilway: -- depending upon the level of assessment in the state, on your auto insurance, your, you know, all insurance with the exception of professional liability and medical are going to get hit.

Chairman Beruff: But as you will mention tomorrow in your report, 75% of the claims in the United States on property claims occur in Florida, right?

Barry Gilway: Mr. Chairman, it's staggering, and I will point on that tomorrow. Eight percent of the claims and 76% of the litigation comes from the State of Florida which is an absolutely absurd mind boggling number.

Chairman Beruff: So even a third grader can understand that we are one state out of 50, yet three-quarters of all of the problems are here. So, somebody sooner or later is going to pay attention to us if we keep pounding the hammer. Sometimes in messaging you have to tell them and tell them and tell them again, and that is what we are going to have to do, is tell them and tell them and tell them again. And it is Mr. Dunbar's comments which I happen to like, because I like to find things that get people to pay attention, and this Board has that empowerment. We respect your opinion and your recommendations, but as an independent Board we may sometimes go against those.

Barry Gilway: Oh absolutely, Mr. Chair, absolutely, Mr. Chairman.

Chairman Beruff: Okay.

Barry Gilway: But you also, you know, you also need to understand my opinion.

Chairman Beruff: Of course.

Barry Gilway: And I think the reality is gambling which is fundamentally what we are doing.

Chairman Beruff: No, we are not gambling. You are talking about $250 million that is now getting paid, and like we did this year, right. There is -- we are done. That money is gone, right. And there is no, none of that, none of the reinsurance guys are reinsuring anything, any losses we have, because there hasn't been in that 12-month period, right?

Jennifer Montero: Right.

Chairman Beruff: So, we wrote a quarter billion dollar of checks and got zero for it, except we had the insurance that if something bad happened, right, we would get, we would get claims based on the tier of coverage that you all negotiated. Again, not, I am not saying there is anything wrong with that, but the reality is a quarter billion dollars of policyholder's money, none of it went into reserve because that is a quarter billion dollars that went out. So, Mr. Dunbar's comment is, well, now that we are insuring, our returns are down to 1.08%, okay, if we instead of covering, spending $250 million on reinsurance, we spend $100 million. Let's not be a gambler, let's just be smaller gamblers and then take that $150 million and stick it into reserves, so the $8.9 billion becomes $9.50 billion, an if we have three or four years of good look like you had, not you personally, but we had in 2000 whatever, '09, '10, '11, '12, '13, when you had a million and-a-half policies, we grew up the reserve and there was no hurricanes until 2004, 2005, right.
The question is –

Barry Gilway: Yes, nine years.

Chairman Beruff: Yes. They gambled then and nobody seemed to have a problem with their gambling then. What is the difference gambling now, except we have more money?

Barry Gilway: And there is a reason they call that a 1-in-100 year storm.

Chairman Beruff: Yes.

Barry Gilway: You know, in a 1-in-150 storm. You know, et cetera. The only point I would make, we would be coming to the Board frankly tomorrow asking for a budget of –

Chairman Beruff: $400 million for reinsurance.

Barry Gilway: And $352 million in Cat Fund premium. And the whole concept is that, you know, we remain solvent as an overall, you know, insurer and we stay away from the potential.

Chairman Beruff: We understand, we understand the concept. The problem that you have is that we continue to be the only significantly well capitalized insurance company in the state of Florida which we are not supposed to be. We are supposed to be the insurer of last resort. So, either we are one thing, or we are the other. I prefer to try to get to what we are supposed to be statutorily, and we can't get there with the policy that we continue to adhere to.

Barry Gilway: I understand your position entirely, Mr. Chairman. However, you know, you hire me for my opinion. My opinion is that, you know, it's taken us many, many years to get to the point where we are reinsuring to a 1-in-100 event, and because of SB 76, you know, we get full credit in our rates, you know, for the reinsurance that we place which was not the case before. So, SB 76 and the Legislature has done a good job in terms of giving us the credibility to now charge for that reinsurance.

Chairman Beruff: Mr. Gilway. If you were running an insurance company that was a publicly traded insurance company, I would buy all the stock you are selling, because I have tremendous belief in your competency in growing a company. Unfortunately, the difference is, I don't want to grow this company, because that is not what I was told we were supposed to do. So, I am torn between your capabilities which are significant, but at the same time we don't want significant here. We do not want to be this big and instead we are this big. So it is, it is and they continue to follow the same policies, you are going to continue to make us grow because that is, if the -- and again, the fault where we are at is not your leadership or the staff. I think you guys are superstars. The fault is in the lack of the Legislature to take significant action in order to not give us that advantage that we have in the marketplace.

Barry Gilway: I completely agree with that statement. Mr. Chairman. We are just, we are just not in agreement on the solution, and the solution frankly in my opinion is to really, you know, get the Legislature to respond appropriately, and my fundamental problem is when you are running an insurance company, if I was running a private insurance company I would be required by statute to reinsure to a 1-in-130 event followed by a 1-in-170 event.

Chairman Beruff: So, there you give me a partial answer. Why are we being so conservative to go to 1-in-100. Why don't we go to the 1-in-130 if you were running a private insurance company? Why do we have to be superstars? Can't we just sort of be like, like you would if you were a private guy.

Barry Gilway: Mr. Chairman.

Chairman Beruff: It would save a ton of money, right.

Barry Gilway: Yes, Mr. Chairman, we are already reinsuring to a 1-in-100 event, we are not reinsuring to a 1-in-130 event. You know, as the private –

Chairman Beruff: But we can buy less insurance.

Barry Gilway: I am sorry.

Chairman Beruff: We can buy less insurance.

Barry Gilway: Oh, we could absolutely buy more insurance.

Chairman Beruff: Instead of spending $400 million, we could spend $200 million and buy the 1-in-100 like you said.

Barry Gilway: It actually is the other way around.

Jennifer Montero: Opposite.

Chairman Beruff: The one in 100 –

Barry Gilway: (Cross talking).

Chairman Beruff: The 1-in-100 is less costly than the 1-in-130, I get it.

Barry Gilway: Yes.

Chairman Beruff: The 1-in-100 is less costly than 1-in-130, I get that. But we still don't have to buy as much. Right?

Governor Dunbar: Well, and Chairman, just keep in mind that we also have reinsurance, it is called our assessment ability. It is the difference between us and the private market.

Chairman Beruff: That is where it started.

Governor Dunbar: And we walk around every day with reinsurance.

Chairman Beruff: But this Board decides we are buying less insurance, we are buying one for 1-in-100-year instead of 1-in 130, I get it, but we can buy less insurance period. Correct?

Barry Gilway: That absolutely is the decision of the Board.

Chairman Beruff: Okay.

Barry Gilway: In terms of the level of reinsurance that we elect to buy.

Jennifer Montero: Chairman.

Chairman Beruff: Yes, ma'am.

Jennifer Montero: Just to be clear, the assessment is the tax, it is not a reinsurance mechanism.

Barry Gilway: Right.

Jennifer Montero: It is not there to protect us from storms. It is there –

Chairman Beruff: No, no, no, I know the assessment is a tax.

Governor Dunbar: No, no.

Chairman Beruff: Mr. Dunbar.

Governor Dunbar: Yes, it is there to make sure that the re-- it is there to make sure that we always have an insurer of last resort, and it is not reinsurance, but it is the fact of reinsurance, because it allows us to get back on our feet if we, if we do it. But yes, it is a tax, and it impacts the state's bond rating. That is exactly.

Jennifer Montero: But it doesn't make you whole. It just brings you back to ground zero.

Chairman Beruff: Understood, I understand.

Barry Gilway: Assessments are a way to pay either debt that have occurred.

Chairman Beruff: Right.

Barry Gilway: Because we didn't have sufficient reinsurance, or to recapitalize, you know, the organization. So, it is not reinsurance in any fashion. It is basically to pay bills that we have to pay because we didn't place enough reinsurance in the marketplace.

Chairman Beruff: I understand, but we are the only company in the state of Florida that is significantly solvent, and on top of that we have the statute that backs us up that gives us the right to assess.

Jennifer Montero: But we are only solvent because we have had all these years to build our surplus. And as Brian can tell you when he talks about the rates. Every time we do the rates there is a piece of that is for future Cats. And so, every time you are building up for future, you are supposed to build a bank as you do your rates in there is basically build a catastrophe fund for yourself.

Chairman Beruff: Ms. Montero, we are supposed to be this big and we are this big.

Jennifer Montero: Well, we will just be less of that, but right now we are bigger. I need more reinsurance, not less.

Chairman Beruff: Yes, but we are not going --we are not going to get there at the rate that we are going.

Kapil Bhatia: Governor Beruff if I may and Governor Dunbar. So yes, we can assess after an event if we have a deficit. That is the only time we can assess. What exactly, what Governor Dunbar and what you are proposing is if we don't buy reinsurance, effectively you are taking a risk with additional surplus. So, on one hand I thought I heard if you have too much money because we have more money than the rest of the market combined. On the other hand, you are saying that we should build on it.

Chairman Beruff: No, what I am saying is we are operationally deficient, and the only way we make money is because we take income which is now down to 1.08 and subsidize ourselves operationally. Otherwise, we would lose money.

Kapil Bhatia: That is primarily every insurance company relies on investment income.

Chairman Beruff: I am sorry.

Kapil Bhatia: Every insurance company relies on investment income for their operations.

Chairman Beruff: Mr. Gilway has taught me the insurance business a few months ago and he said that when he was out buying insurance companies for the gentleman who he used to be associated with, the insurance companies that they looked at were making five percent operationally, and then on top of that they had the silver lining or the investment income, and then they merged back rooms and that is how you got better returns. So, it is different from the insurance lesson Mr. Gilway taught me, which I, once I get something in my head it is hard to get it out. But that is still the truth, correct?

Barry Gilway: That is absolutely true.

Chairman Beruff: I just want to make sure that we have a distinctly different opinion.

Barry Gilway: Well, I really don't think, Mr. Chairman, I don't think it is. So, if you take a look at the Florida marketplace, I can probably get the numbers for 2013, '14 and '15. For those three years the industry made over $400 million per year in profit, in positive net income for those three years. It changed in '16, you know, and then all of a sudden for the last what, five years now it has been negative, started in 2016. But that was -- and that is exactly why Citizens went from 1.5 million policies down to 414,000, because the market competed effectively. What is happening now in the private marketplace, it is horrendous. $847 million, will be over a billion dollars in negative debt income. That is 25% of the entire market surplus of $13.8 billion, $3.8 billion in surplus supports the entire marketplace. These companies are losing 25% of their surplus every year.

Chairman Beruff: And it brings the circle completely back to where it started, which is the reason that is occurring is because litigation in the state of Florida is completely increased how many percentages in five, six years, 300%?

Barry Gilway: 27,000 litigated cases in 2013. We will have 100,000 property litigated cases by the end of the year, 100,000. It was 81,000, you know, through three-quarters. We will be at 100,000 litigated cases. That is a 400% increase since 2013.

Chairman Beruff: Okay, so then it falls right back into the foot of the Legislature for not taking action to reduce the amount of litigation that occurs in the state of Florida.

Governor Knight: So, I think if I may.

Governor Dunbar: And I would add to that. It also, when there is one other, there is one other component, and that is the fact that we have got a glide path put in place by a prior Governor that we operate under. So, we don't really have a free market. If we weren't so, if our rates weren't at such a discount, the private market would be able to get in, charge a fair rate and get some of these policies that we have, and then you exacerbate that problem by placing us in the reinsurance market where we are essentially taking Florida wind out of the marketplace that some of these other private insurers could, could get. I mean, our presence in the reinsurance marketplace does increase the cost on the private insurers, because there is only so much Florida wind that people want in the global risk marketplace. So, it is twofold. I mean, the glide path combined with the litigation problems are really what is hurting the state.

Chairman Beruff: Before the staff answers that comment, Governor Knight has a comment I thought you wanted to make.

Governor Knight: Well, what I was going to say is the legislation and constraints that we have, tell me, in other words, you believe our -- could cause us to behave irresponsibly, right, by choosing to forego an amount of reinsurance and hopefully a message like that would be received with different constraints upon the company to be able to deliver its mission in a responsible way.

Chairman Beruff: Yes, thank you for verbalizing that. Before -- I would just like to finish her comment. At the end of the day from our perspective, we continue to grow in a company that is supposed to be shrinking and that is because we have huge advantages in the marketplace that other companies don't have, not the least of which is our ability to assess. Now, I would like either Ms. Montero or Mr. Gilway. You obviously had some comments to follow up on Mr. Dunbar's comments to clarify a statement he made. So, whoever would like to take that opportunity.

Barry Gilway: If you don't mind, Mr. Chairman, I will take it.

Chairman Beruff: By all means.

Barry Gilway: I will make two comments and then I will turn it over to Ms. Montero. First, it is incorrect that we are taking wind insurance away from the private market. The reality is the movement that Ms. Montero and Kapil have made relative to moving us into the insurance link security marketplace where only seven other carriers even participate at significantly lower rates online have been responsible for the placement of our business. Our plan is to significantly increase, not the traditional reinsurance, but to significantly increase the insurance link security capability where capital is plentiful. So, I have to make that point. There is no question in my mind that we are not taking wind insurance coverage away from the private marketplace. And Ms. Montero, I will turn it over to you.

Jennifer Montero: I would add to that, that the majority of our new business is transferred business from those companies to us. Therefore, they're not writing that wind reinsurance because they don't have that exposure anymore. It is not new exposure in the state of Florida that we are getting, it is everybody else dropping theirs. So, it is just being transferred from them to us, so they don't need that reinsurance anymore because they don't have that exposure. So, us buying that reinsurance does not change the capacity amount.

Chairman Beruff: Mr. Dunbar, you have a comment.

Governor Dunbar: Yes. I mean, that is not what the private market is saying. I mean, our existence in the marketplace, I mean, the global reinsurers only buy so much Florida wind and that is it. The models may say this year we buy eight billion dollars in Florida wind, and we package it with, you know, Asian Tsunami and California fire and that is the model we want. And the more we buy the less that is available for the private market, because it is just that simple. The models say buy this must risk, and the people that I am hearing from are saying, our presence in the marketplace, particularly with the fact that we are a tax exempt organization, and they are post tax, does impact the pricing of Florida wind in the reinsurance marketplace. And so, I understand the transfer and all that other kind of stuff, but the simple reality is, and this goes to the timing discussions that we have had before on whether we go out in January or whether we wait and how much we take down. It does impact the private insurers and how much is available for them and what they are going to be charged rate online.

Chairman Beruff: Mr. Gilway.
Barry Gilway: I do have a statutory reference, Mr. Chairman. 627.351(6)(c)(9). The Citizens' plan of operations must provide that the corporation make its best efforts to procure catastrophe reinsurance at reasonable rates to cover its projected 1-in-100 year probable maximum losses determined by the Board of Governors.

Chairman Beruff: I agree, Mr. Gilway, we are swimming with our arms tied behind, our arms behind our back and our ankles tied. So, we are going to be Navy seals in order to survive this thing.

Barry Gilway: I will agree with Mr. Dunbar on one very, very key point, and we made some progress under SB 76, and that is our rates are insanely low. 99% of the time according to the November competitive information report, 99% we are the lowest in the market. 97% of the time we are not even within the 15% of the private market. So, I agree with Mr. Dunbar, but I believe right now the fundamental issue in the Florida property market is you have got four solid years of incredible losses as a result, to your point, Mr. Chairman, of litigation. We had $810 million loss all of 2020, and through three-quarters, the industry has an $847 million negative debt income, and we will be over a billion dollars. So, until the private market has the ability basically to really react, either get some positive news on litigation, they are not going to provide the capacity that we need to take policies out of Citizens. So yes, it is rates, but the problem in the private marketplace is the capacity issue. Companies do not have the capital to even support their current writings, let alone the premium increases that frankly require even more capital. You know, it is principally a three to one ratio and you get a 30% rate increase you need 10% more surplus, you know, on the incremental premium. All I would say, our best recommendation to the Board, you know, will be to buy, do everything possible to buy 1-in-100 at reasonable rates. I think that in my opinion is actually the most realistic approach today to protect ourselves.

Chairman Beruff: Well, I mean, the statute, we are going to follow the law. If the statute says we have got to do something, we are going to do that. We are definitely not a bunch of cowboys up here. So, I like that statute. If somebody can print it to me and send it to me or e-mail it to me.

Governor Dunbar: Can I ask a quick question?

Chairman Beruff: Yes, Mr. Dunbar, please proceed.

Governor Dunbar: The layer chart shows us purchasing reinsurance coverage for the 1-in-100, and then additionally I think it says a 1-in-29 or a 1-in-41. Can you go back to that layer charts real quick? And that is the point that I wanted to just, and then I will just close and just making sure that I am understanding our layer charts.

Chairman Beruff: Is that the one that is up, folks?

Governor Dunbar: Jennifer, do you understand what I am saying?

Jennifer Montero: Yes.

Chairman Beruff: I do, so you are asking about the different categories and the different, the 1-in-100 obviously is less expensive than the 1-in-30 and so forth.

Jennifer Montero: The appendix is not on the screen. I told Barbara we didn't need to it, but if you look at the layer charts and you go slide six on the bottom. Approximately 45% of the coastal account surplus is exposed in a 1-in-100 year event. Surplus remaining after 1-in-100 year storm is projected to fund a 1-in-29 year event. Additional LAE multiple storms are subsequent. That is for the coastal account. And the PLA after it is –

Chairman Beruff: Is this the correct chart now that we are looking at?

Jennifer Montero: Yes. In your appendix, yes, in your layer chart.

Chairman Beruff: Right, but on the screen.

Jennifer Montero: Oh yes, that is.

Chairman Beruff: So, Mr. Dunbar, do you have this chart?

Governor Dunbar: Yes, I just wanted to make sure that I understand it, right, as it relates to our reinsurance coverage, because I think our reinsurance coverage is beyond just the 1-in-100 event, but I want to make sure I am reading the layer chart correctly.

Chairman Beruff: So -- because the statute that was just read by Mr. Gilway, I think related to 1-in-100, correct?

Jennifer Montero: It says that we have enough surplus and reinsurance to cover the 1-in-100, and then a second storm of 1-in-29, but then we have nothing. So that is not just reinsurance, that is reinsurance plus our surplus.

Chairman Beruff: I understand.

Governor Dunbar: No, I understand that. I just want to make sure that when we combine surplus plus reinsurance, we are covered beyond the 1-in-100 event. So, I just want to make, it is a simple yes or no. I want to make sure that I am reading everything correctly.

Jennifer Montero: The surplus alone would cover the 1-in-100 event, but then it is gone.

Chairman Beruff: Hold it, hold it.

Governor Dunbar: I understand.

Chairman Beruff: Again, I come to these meetings to learn. Statutorily we are required to do what, buy insurance.

Governor Dunbar: Backstop of 1-in-100.

Chairman Beruff: Between, between the surplus and the reinsurance we have got to cover 1-in-100 year event, is that correct? Did I hear that correct?

Barry Gilway: The statute basically is we will make our best efforts to –

Chairman Beruff: Best efforts to secure between our surplus and our reinsurance to cover 1-in-100 year event, yes or no?

Barry Gilway: No, I don't believe that is in the statute. As I read the statute, I don't believe that is stated in statute. I think the statute, the statute basically references, could I read –

Chairman Beruff: Yes, please.

Barry Gilway: Let me read the full phraseology. "Must provide that the corporation make its best efforts to procure catastrophe reinsurance at reasonable rates to cover as projected 1-in-100 probable maximum loss as determined by the Board of Governors. If catastrophe reinsurance is not available at reasonable rates", the corporation need not purchase as we did not two years ago.

Chairman Beruff: Right.

Barry Gilway: But the corporation shall include the cost of reinsurance to cover its projected 1-in-100 probable maximum loss in this rate calculation.

Chairman Beruff: Got it.

Barry Gilway: So, it is best efforts.

Chairman Beruff: Got it.

Barry Gilway: At reasonable rates.

Chairman Beruff: Back to Mr. Dunbar. I just want to be clear on what your thinking is.

Governor Dunbar: Yes.

Chairman Beruff: I think what your thinking is that then I heard Ms. Montero say that we have enough cash to cover a 1-in-100 year event. Yes?

Jennifer Montero: We're broke.

Chairman Beruff: I understand, I understand we go broke, but I would extrapolate without reading the full every word of that statute that basically we don't have to buy reinsurance because we have got enough, we have got enough. Why do I have to buy reinsurance? Just being the devil's advocate here. Because if Ms. Montero says we have got enough cash to cover the 1-in-100 year event then why buy reinsurance? Mr. Dunbar, please speak up. Mr. Gilway is jumping out of this seat, but Mr. Dunbar goes next. Hold on, I would like to hear Mr. Dunbar. I am sorry, Mr. Dunbar, could you repeat your comment?

Governor Dunbar: My recollection of that language on why it was included, and Tim can probably pull this together for us, is the legislative intent was to make sure that we had a 1-in-100 back stop because they didn't have the surplus. They wanted to make sure that in the event of an assessment situation that we are not constantly resetting, you know, with no cash in there. But once you got to a surplus of 1-in-100, I don't believe that it is required to have reinsurance in that instance, and I am pretty sure that, you know, if you look at back when it was put in there was not surplus to cover the 1-in-100.

Chairman Beruff: Being the lay dumb home builder that I am, I read it the way you do, Mr. Dunbar, which is if you got the cash to cover the 1-in-100 event you don't need to go buy reinsurance. But Mr. Cerio is now here to join the party.

Tim Cerio: Mr. Chair. I would –

Chairman Beruff: At least I am keeping everybody awake in the audience, right? You are not falling asleep anymore.

Tim Cerio: Certainly not, Mr. Chair, not now. I will say, I think Governor Dunbar, he is right, I would like a chance to pull a lot of this together, but the relevant portion that Mr. Gilway read says that the statute requires our plan of operation to provide that we must provide the corporate, that the corporation make its best efforts to procure catastrophic catastrophe reinsurance at reasonable rates to cover projected 100-year probable maximum loss as determined by the Board. If it is reasonable, we have to do it, if the rates are reasonable. If they're not reasonable, the statute says we do not.

Mr. Gilway: But there is no reference in that statute, you know, there is no reference in that statute to combining surplus with catastrophe reinsurance. The statute specifically states that we make our best efforts to buy catastrophe reinsurance.

Chairman Beruff: But a couple, last year or the year before I got on this Board, you, that Board and the staff chose not to buy reinsurance because the rates didn't make any sense.

Barry Gilway: Absolutely.

Chairman Beruff: So technically that year you were gambling like we are talking about. It's just the gambling game.

Barry Gilway: You are correct. We chose under those circumstances to say, it is not in the best interest of the state or Citizens to acquire reinsurance at exorbitant rates, which at the time we believed to be the fact.

Chairman Beruff: Okay. A robust discussion and we have another member, yes, please. Sit, first sit down, be comfortable.

A VOICE: I just wonder if you would give me that subsection so I can look at the statute myself, that is all.

Jennifer Montero: 27.351(6)(c)(9).

A VOICE: (6)(c)(9), thanks. All right, thanks. It is hard to find on the phone.

Chairman Beruff: We have got some smart people that can figure this out but thank you very much. I think we have beat this horse to death for now unless there is some more discussion, let's move on to something more fun. I think this was a lot of fun personally.

Jennifer Montero: Yes, we need to go back to –

Chairman Beruff: And I like conflict and mischief and chaos.

Kapil Bhatia: Governor Beruff, can I go back to the very original question on the investment income?

Chairman Beruff: Yes, sure.

Kapil Bhatia: While we were all talking, going through different things, the reason we have a lower return as I was saying earlier, the whole conservative nature of our investment policy and its return is 1.08%. So effectively we are taking less risk, but there is a less return and we can increase the risk by the returns. So, a couple of examples. In the two entities you asked for, we have looked at it. The California Earthquake Authority and the California wildfire funds which are 8 to $10 million of both, each effectively. Have a return of 1.68%, so it is more than plus minus 10 basis points, but they have a longer duration and the timing of change of the investment policy to maximize the investment income. So, there is an additional risk attached to the duration part, not the credit risk or anything which is similar, that gives 60 basis points. The Florida Hurricane Catastrophe Fund, which is a similar portfolio, their return is closer to one percent, the risk profile is similar. So, most of the entities have somewhere between one to 1.70%. So certainly, we can take a risk as Governor Dunbar is saying and just levy assessments, if there is an event or buy less reinsurance or you can take a more risk on the investment side. So, it is effectively you are taking a risk one way or the other. How you try to take the risk is basically the Board's decision. We can come back with you with the advice of investment policy and tell you what the additional risks will be. Again, not the credit.

Chairman Beruff: Right, right. It's not a credit risk but the timing risk.

Kapil Bhatia: The timing of the liquidity.

Chairman Beruff: I understand.

Kapil Bhatia: And how much more income it can generate. So, if we add up, so if we have another 50 basis points on our portfolio, that will give us another $50 to $60 million, depends on the Portfolio's maturity distribution.

Chairman Beruff: Real money.

Kapil Bhatia: So, it is all risk management and we have been very conservative from both sides making sure we have resources to pay timely when the time comes, no tax burden, so we don't have any assessments as the last risk transfer market. Risk transfer market as I said in my market update are deep enough. There is more capital available, so it is not an issue. If the private companies can't buy it because they don't have the money, that is a different story. It is not the availability, it is the cash.

Chairman Beruff: Right, so, I understand. Thank you. Ms. Montero, do you have a comment?

Jennifer Montero: I would just add, in the audit report I did talk about in the investment section the $19.5 million in realized gains which we were mostly taken in July. So, we do monetize those gains when we see them in the market. So, it is not just the 1.08 sitting there by itself.

Chairman Beruff: No, I understand. It is just part of –

Jennifer Montero: I know.

Chairman Beruff: It is just a sliver, the $19 million is a sliver of $8 billion.

Jennifer Montero: Yes.

Chairman Beruff: I get it.

Jennifer Montero: What was this number right here?

Kapil Bhatia: $172.

Jennifer Montero: So, we looked at 2017. We paid $172 million for coverage, and after Hurricane Irma we have total recoveries of $935 million. We have billed $811million and we have received $805 million, so far. So it is like any insurance, you need it when the wind blows.

Chairman Beruff: Or one.

Jennifer Montero: You would not, not insure your home?

Chairman Beruff: Actually, I don't have a mortgage, so I don't worry about that stuff.

Jennifer Montero: The last thing I would say is the purpose of reinsurance is to protect surplus. That is the whole purpose of reinsurance to protect our surplus. So that it is there when we need it.

Chairman Beruff: I understand.

Governor Dunbar: Jennifer, we understand that.

Chairman Beruff: And our purpose is to shrink this company. That is the yin and the yang here. So how do we get there and how do we get people to pay attention. Thank you. What is our next? A&U.

(Whereupon the meeting was concluded.)