CITIZENS PROPERTY INSURANCE CORPORATION

MINUTES OF THE
AUDIT COMMITTEE MEETING
Tuesday, September 24, 2024

The Audit Committee of Citizens Property Insurance Corporation ("Citizens") was convened at 1:00 p.m. on Tuesday, September 24, 2024.

The following members of the Audit Committee were present:
Chair Jamie Shelton   Governor Scott Thomas   Board Chair Beruff

The following Board members were present:
Governor Lydecker   Governor Knight
Governor Cumber   Governor Spottswood

The following Citizens Staff were present:

Jay Adams	Eric Addison	Ravi Tadiparthi	Ken Tinkham
Tim Cerio	Carl Rockman	Sudheer Kondabrolu	Matthew Carter
Bonnie Gilliland	Mark Kagy	Joe Martins	John Schmitt
Jennifer Montero	Jon Schmidt	Andrew Woodward	
Ray Norris	Michael Peltier	Raina Harrison	
Jeremy Pope	Barbara Walker		

The following were present:
Nathaniel Johnson, B of A
James Cook, JP Morgan
Kapil Bhatia, Raymond James
Mark Weinberg, Citi

Barbara Walker: Good afternoon, and welcome to Citizens' September 24, 2024, Audit Committee Meeting, which is publicly noticed in the Florida Administrative Register to convene at 1:00 p.m. and will be recorded, with transcribed minutes available on our website.

For those attending today's session through the public link, you are automatically in listen-only mode, with presentations appearing in the webinar.

Chair Shelton, we have no speaker requests for today.

Panelists, thank you for identifying yourself prior to addressing the committee.

The roll was called, and the quorum met.

Chair Shelton: Meeting will come to order. The first order of business is the approval of the prior minutes from the July 9, 2024, Audit Committee. We'll entertain a motion to approve.

Unanimously approved.

Chair Shelton: Joe Martins, our Chief of Internal Audit, you are recognized to present.

Joe Martins: Thank you, Mr. Chair. Good afternoon, Governors. Today, I will walk you through the quick progress of the Office of Internal Audit function. Since the last meeting, we have provided updates on our audit engagements, key risks, and key control focuses.

Slide 2 shows a graph that presents progress to the plan for the period April 2024 to March 2025. Thirty-eight percent of the engagements were completed, with another 29 percent currently in progress. Two of the audit engagements, the Technology Governance audit and the Commercial Underwriting audit, are nearing completion, with draft reports currently in progress. These delays do not impact the 2024 audit plan, as we plan to complete the agreed-upon 22 engagements by year-end. Since the last meeting, we have completed three audits, and these engagements include the Finance/Purchasing Centerpoint Segregation of Duties audit, the Legislative Implementation support project, and the Reconciliation advisory engagement. In addition, we supported the Auditor General during their tri-annual operational audit, and we are currently working on the Payroll and Employee Record Management audit and supporting four major project implementations.

On this slide, we have a graph that highlights our focus areas, touching nearly every business unit within the organization, and key engagements scheduled for completion before the next meeting, including the Application Programming Interface (API) Operations and Security Audit, where we will evaluate the effectiveness of the controls around API integration, encryption, and data management, Asset Management audit assessing the efficiency, effectiveness, and protection of physical assets, the Claims Independent Adjustor (IA) Invoice Management System where we will be reviewing the newest SAAS solution for recording IA invoices, Financial Planning and Analysis engagement will be evaluating the tools used for budgeting and strategic planning, the IT General Controls audit will be assessing the processes such as access control, data backup and recovery mechanisms etc., the Office of Foreign Assets Control (OFAC) audit will be reviewing answers made to sanctions following a 2020 audit that we completed, the Remittance Processing engagement where we evaluate premium process controls, and additionally we agreed to do an advisory in Privacy Governance. The Office of Insurance Regulation (OIR) commenced with its market conduct exam, which is currently in progress.

On this slide, we focus on the Open Audit Observations. We have two medium-rated observations: the Centerpoint HRIM Segregation of Duties audit, which is being addressed and is near completion, and the seven observations from the Auditor General operational audit. These observations are being monitored, and we will report at the next committee meeting on how they have progressed.

On this slide, we focus on the eleven strategic risks, and we indicate the audit focus on each of these risks. Although we have not done any work on reinsurance during this period, we plan to audit reinsurance claims servicing next year. Just to indicate that we are focusing on strategic risk and the strategic imperatives of the organization.

This slide shows the Global Internal Audit Standards. For many years, we have been following the International Professional Practices Framework (IPPF) of the Institute of Internal Auditors, and this has now been changed, mainly to align with current practice. The new standards will become effective on January 9th, 2025. These standards focus on five specific domains. Within the domains, we have fifteen principles and 52 standards. The effect of these standards is that it has a broader scope of internal auditing and focus on advanced governance practices, it brings a risk-based approach and integration of technology stakeholder engagements, quality assurance and improvement. These standards are now applicable throughout the world, global to every function. Many of the standards that they have identified were already in practice with us as a group. For example, we follow a risk-based approach, and we have for a long time. We have a strategic risk plan that we present to the Board and Audit Committee annually. We already have integrated technology, using data analytics tools for our audits; we utilize large language programs in the work that we do, we have robotic process automation in place, and we also apply generative AI during our work in Audit, Enterprise Risk, and Internal Control. We will also update the Internal Audit procedures to align with the new standards. At the next Audit Committee meeting, we will bring refreshers of the Audit Committee Charters to align with new standards, and we also need to update our Quality Improvement Program, which we execute every year.

As of August, we had 438 enterprise risks, including eleven strategic risks. Nine of these risks are ranked high and are being closely monitored, with eight of these being strategic risks tied to our ability to meet our strategic imperatives. The one high operational risk is tied to the implementation of the Litigation Management Solution, which we are closely monitoring.

On this slide, we focus on Internal Control, and we highlight through the internal control framework, we have identified 96 primary controls, and the businesses are currently executing the control self-assessments, of which roughly 25% have been completed, and we do monitor and review these self-assessments, and we do envision that by the end of the year all 96 will be reviewed throughout the business. With these that have been reviewed, we identified that for most, the controls are effectively designed and operating as intended. Two control enhancements have been identified, and two have been redesigned as the processes change. No material issues have been identified.

This completes my presentation.

Chair Shelton: Governors, any questions for Chief Martins before he steps aside?

Next up is Jennifer Montero, our Chief Financial Officer. Ms. Montero, you're recognized.

Jennifer Montero: Good afternoon. Behind Tab 3, you'll find the document titled "Q2 2024 Results of Operations and Financial Position." This provides an overview of Citizens' unaudited financial statement, including the cash flows, invested assets, and surplus, as well as operational results for the quarter ending June 30, 2024. In addition to that, there's a second document that provides the commentary, which is the discussion and analysis of those operating results and financial position, and that is the document that I will go over in summary.

At June 30, 2024, consolidated cash and invested assets totaled $10.8 billion, which is approximately 920 million more than at December 31st, 2023. This was driven by net cash flows from operations of approximately 924 million. Surplus at June 30th was $5.9 billion, reflecting an increase of approximately 918 million in comparison to December 31st, 2023, driven by the net income from the first half of 2024 of approximately the same amount. Direct premium written in the first half of 2024 was $2.6 billion, or 59.4 million or 2% less premium than written in the same period in 2023. The number of new policies written the first half of 2024 of 214,000 was lower than the number of new policies written the year prior by approximately 73,000 policies. In addition to renewal rates of 82% reflects a decrease of 4 percentage points relative to the renewal rate during the first half of 2023.

Premiums ceded through depopulation through June 30th, 2024, were 306.9 million, marking a significant increase in comparison to 2023, where 42.1 million of premiums were ceded through depopulation. Premiums ceded for private reinsurance and for coverage through the CAT fund totaled 980.4 million, a decrease of 145.9 million or 13%. A decrease in reinsured exposure was the primary driver for the period-over-period decrease in the premium ceded.

At June 30th, no adjustments were made to ultimate losses and LAE associated with CAT events from December 31st, 2023. Gross and net ultimate losses and LAE associated with the CAT events were as follows: Hurricane Ian $3.6 billion gross and $2.5 billion net, Hurricane Irma was $2.6 billion gross and $1.4 billion net, Hurricane Nicole was $101 million gross and $86 million net, Tropical Storms Sally and Ada were $434 million with no reinsurance recoveries, and Hurricane Adalia was $84 million with no reinsurance recoveries.

The 2024 non-catastrophe loss and LAE ratio continues to show improvement relative to prior years. The dominant driver behind the improvement in the loss and LAE over the past several years has been the improvement in the litigation rates, which continues to be the single most important factor in non-catastrophe losses and LAE, and which have remained stable for non-catastrophe losses in recent years.

Administrative expenses incurred in the first half of the year were 94.5 million, or 9.6 million more than in the same period in 2023, and 14.6 million less than budgeted. Citizens' expense ratio for the period ending June 30th was 14.5%, marking a .7% increase from the same period in 2023 and a .9% increase compared to budget.

Through June 30th, 2024, total investment income was 172.9 million, which is approximately 39.9 million more than in 2023, while average invested assets increased 821.7 million or 9%. The increase in the overall interest rates, specifically within short-duration instruments, has had the largest impact on investment income.

At June 30th, total unrealized losses across all portfolios were 663 million, or 44 million more than at December 31, 2023, reflecting an increase in interest rates during the first half of 2024. However, as of yesterday, September 23rd, the total unrealized losses were down by approximately 145 million, to 419 million.

I'm happy to answer any questions you may have, but if there are no questions, my report is concluded.

Board Chair Beruff: You said $663 million, and then you said we dropped by how much?

Jennifer Montero: So, it was $663 million at June, and as of yesterday, it was $418 million, so that is a drop of $145 million, reduced.

Board Chair Beruff: That's a drop of more than that, it's $245 million.

Jennifer Montero: Sorry about that.

Governor Thomas: One thing in your report, and if you said it or highlighted it in your review of administrative expenses, I apologize, I don't mean to repeat it. But one of the things when you're looking at where our expenses are year to date, they are up from where we were last year from 94 to 84, but they're under budget is the legal column which is down YTD 53% over last year and the amount of dollars we have spent on legal expenses, we can see that and we know some of the things that are working, I know some things are still rolling through the system but to see that number coming back down that significantly is very good to see.

Board Chair Beruff: I have a couple of questions which are unrelated to the report.

Chair Shelton: Mr. Chairman?

Board Chair Beruff: So, what was our max policy count when we maxed out, how many policies were we carrying?

Jennifer Montero: About 1.5 million.

Board Chair Beruff: And what is our count now?

Jennifer Montero: 1.257, I believe.

Board Chair Beruff: Let's just call it 1.25, close enough. What is our maximum FTE including outside contractors.

Jennifer Montero: Including outside contractors?

Board Chair Beruff: We have direct contractors that basically work for us as 1099 employees. Do we not?

Jennifer Montero: I know the FTEs are just over 1,400. It was 1,402 the last time I looked.

Board Chair Beruff: We talked about it on the phone. What was the other number? I thought it was about 400.

Tim Cerio: I thought the contractor's Jay, and contingent staff.

Jennifer Montero: Andrew? Jeremy? Do either of you have that? You are not referring to the independent adjustors?

Board Chair Beruff: No. I am talking about people that are basically for all practical purposes like FTEs, but they're not.

Jeremy Pope: Our peak was in 2012 with 2,511 FTE equivalents, including staff and the contingent workforce.

Board Chair Beruff: And how many was it?

Jeremy Pope: 2,511 in 2012.

Jennifer Montero: That was right after we peaked at 1.5 because that was right near the end of 2011.

Board Chair Beruff: But we have peaked at 1.5 recently.

Jennifer Montero: Again, yes, we have been there twice.

Board Chair Beruff: And where did we peak the same statistics that he shared with me? What was that, that was twelve years ago.

Jennifer Montero: But we also peaked in 2023 or 2024?

Jeremy Pope: That was the highest number, Chairman, in 2012, but in recent years, the growth pattern has been different. The highest we had was in 2022, with 3,217, and then we went down to 3,099 in 2023 and, in 2024, 3,007, equivalent. So, the peak, to answer your initial question, has been 3,217 total in the year 2022.

Board Chair Beruff: And what do you project we are going to be if we get down to 800,000 policies. Which is your projections that we are going to depopulate roughly to 800,000 between now and February 1st?

Tim Cerio: So, Chairman, and I want Jeremy to correct me if I am wrong. My understanding is the smallest Citizens has been with FTEs has been about 1,000 employees. But we are running those projections now because we do believe that as the policy count drops that any reductions that we would be able to handle through natural attrition. But right now this memo has gone out from me to Citizens that we have frozen hiring with the exception of, a Chief can make an exception, a team can make the case to their Chief, and their Chief can make the case to me, but we have frozen hiring for the time being and we are waiting to see how the policy count drops. We are certainly looking at contingent as well as making sure that if we are going to backfill positions, we are anticipating shrinking and the needs of the workforce reducing, but again, we think that we can handle that through attrition.

Jennifer Montero: May I add to that, when we do reduce policies by depop, we still service those policies for what could be up to 9 months, so we try to look at policies being serviced plus once they are in force when we look at staffing needs because we are the ones still servicing those policies, for underwriting as an example. We would still be taking in all of the calls of any endorsement that would be made if they want to cancel their policy. All of that still gets done by Citizens for the takeout company until that policy is renewed onto their paper. Claims is different; they have a claim, they call us, and we send them to the takeout company's claim department.

Board Chair Beruff: So, we handle the policy administration even after depopulation for whatever period of time is left on the policy term?

Jennifer Montero: That is correct.

Board Chair Beruff: Do we get paid by the people who bought the policy?

Jennifer Montero: So, we used to hold back a ceding commission, and it ranged from 6% to 16%. Depending on if you took more policies, we would reduce the ceding commission. And we always did that until 2012 as part of an initiative to get depop motivated and get people interested again when the market started to get healthy; we got rid of the ceding commission, and we did it effective the 4th quarter of 2011. So, we have not had it since the 4th quarter of 2011.

Board Chair Beruff: Is that something this board should take up as a policy, bring it back? Because at the end of the day, I am just brainstorming up here with you guys, this is not a rehearsed speech.

Jennifer Montero: The problem I see with that.

Governor Lydecker: Rates are higher today relatively speaking, so the motivation to depop should be higher today than it would have been in 2012, which I am making that as an argument as to why you would want to put back in place some form of.

Board Chair Beruff: Administrating fee. You can prorate it per policy but at the end of the day we are not a charity. We shouldn't be working for people for free. I don't work for free. Well, I do, I work for Citizens Insurance for free. It costs me money to come up here.

Tim Cerio: I would just want to throw out there that I would not want to do anything to disincentivize takeouts.

Board Chair Beruff: Let me brainstorm with my brothers and sisters up here. I don't think we do anything that is disruptive. I think we think, we plan, we say, hey folks, starting someday in the future this is what is going to happen. So, it incentivizes the behavior to take advantage of the free ride now but come someday in the future we're going to start charging for the administration of the policies you are buying from us for the term of the amount that is left on the policy.

Jennifer Montero: They are basically getting the policies for no acquisition cost whatsoever.

Board Chair Beruff: I understand that but in addition to getting the policies for no acquisition whatsoever we are also continuing to administer the policy at our cost for the balance of the term of the policy. It doesn't make good sense to me. I think that the smarter people that know more about insurance than I do I think I have some support from some people on this board.

Governor Lydecker: I think it is a very good suggestion, Chairman. I wasn't aware of that either. It may be that the board chooses to implement that policy again. But authorizes the staff to use it as an incentive on takeout programs that maybe are of a certain size, there's some criteria that the staff could minimize that administrative cost, again, like you, spit balling up here a little bit, but I think you might consider kicking it back to staff and have them come back.

Board Chair Beruff: And again, do it in a very organized manner so the industry isn't surprised. We aren't trying to do anything but make it known that we come back to this committee or the full board with some ideas of how we would reimplement what used to be done anyway. We just stopped doing it 12 years ago and never reimplemented it, is what I'm hearing. But in that 12-year period, this board, the legislature, the Governor's office, everybody did the most important thing, which was tort reform which was the big problem that I learned four years ago when I got on this board was the biggest impediment to the rate increases in the insurance industry and the unbalancing of the insurance industry in Florida. Unfortunately, we got caught in a bind because the state of Florida did all the right things on stopping the ridiculous litigation rates, but what we couldn't control was the Biden inflation. Which made everything costlier to repair, replace and so forth. So, even though we might have seen significant improvements in premiums, those are being offset by significant cost increases that nobody could factor in. So, we, as a state who did the right things. You're not going to be able to get the credit because of the things that the federal government did not do that created an inflation rate that increased 20 some-odd percent in 36 months. So, anyway. Now that I have made my point and Mr. Lydecker agrees with me, I expect some of the other board members, I see them nodding that they sort of think it's a possibility, I would like to move that forward and just ask that staff look at that and bring that back to Chair and we can address that in 2025 and talk about that and as you are doing that what we were doing in 2012 and just some analytics on what is if you go back or what is the day, what is the servicing fee or the servicing rights worth and how many policies are we actually pretending would be doing that because it is not an infinite revenue stream because the theory is they come off, you service them until expiration, and then they go away to whoever is picking them up so it is good to be paid for that so just if you could include that in your analysis and we can talk before the next board meeting.

Jennifer Montero: Absolutely. In fact, the former way it was calculated is very similar to what Governor Lydecker mentioned. It was based on the number of policies, and it continued, so if you had 10, it was the higher 16 percent; maybe you did 20, and you hit the next layer, so it would drop, and it was retroactive as you added on. It was an aggregate. So, it worked well, and everybody understood it. We can easily put something together like that and bring it to you.

Governor Spottswood: I was just going to add my perspective on this. With us fronting all of the acquisition cost for these policies that are moved into the private market and continuing to pay the administration costs, I think it is somewhat of a disincentive for the private market to go out and really try to book as many policies as they can, they would rather just come and buy them from us and avoid these costs. These are not small dollar amounts on our income statements, it is a huge amount of money that we are spending to do this.

Tim Cerio: Not to point out the obvious, but I think there are some great points being made and an incentive that may be appropriate when Citizens is 1.4 million policies may not be appropriate when we are 500,000 policies. But we will definitely, as a staff, come back and make a recommendation, and I suspect, based on Governor Spottswood's comments, and I think they are great ones, it is the question that has come up again, which is as CEO, and we have talked about this a lot, we want to incentivize depopulation, but yes sometimes you are giving up what a private company would call great business, but it is the cost-benefit of getting it off our books, getting the liability off our books, and there is a balance, but we will go back and come back to you with some options.

Governor Lydecker: It is actually worth looking at because, you know, it’s not an incentive at the moment. Right, because it hasn’t been around since 2012, it is the course of doing business. It used to be an incentive, so do we turn it back into an incentive? To me, at least, that is one way to look at it. The thing I would say is we got a storm, and Friday or Saturday, hopefully, everything works out; we’re all crossing our fingers. But that will have a very substantial impact on this conversation. Let’s see how that storm goes.

Governor Cumber: As part of looking at it, if we could get, because I feel like at least for me, I’m kind of guessing whether it is a disincentive or an incentive, can we, since we have comparisons when we kind of go back and see if it does really have an impact, do people really notice it. Does it have the impact of disincentivizing people and disincentivizing the depop, or did we not see it?

Jennifer Montero: It was a huge incentive. Depop went straight through the roof.

Governor Cumber: But did it? I guess the question is, did that level off? If we could just look at that for those of us who weren’t around, then to help make a decision with a kind of understanding what the impact really was. I intuitively agree that we are not a charity and shouldn’t be, but I think having all the facts would be helpful.

Board Chair Beruff: I agree 100% if it wasn’t for the fact that in that 12-year period we changed the litigation rates significantly that makes the business they are buying from us significantly more, they can model their profits better. So, I think they are buying business from us intent on making a lot of money because at least from the experts on that side have been telling me for four years that the problem is not that insurance can’t model hurricanes, they can’t model litigation rates. So anyway, thank you for taking the time and look forward to see what you recommend to do.

Chair Shelton: Next on the agenda, the Inspector General quarterly report has been included in our package for information only and has been made available to all of the governors.

Chair Shelton: Any new business?

Whereupon the meeting was adjourned.