

# 2017 Risk Transfer Program Strategy

## TRADITIONAL REINSURANCE AND CAPITAL MARKETS RISK TRANSFER

### DECEMBER 6, 2016

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#### **EXECUTIVE SUMMARY**

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Citizens' Chief Financial Officer will present an overview of Citizens' planned risk transfer to the private markets in preparation for the 2017 hurricane season. This agenda item summarizes those initiatives.

#### **BACKGROUND**

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Citizens' statute requires it to "make its best efforts to procure catastrophe reinsurance at reasonable rates, to cover its projected 100-year probable maximum loss as determined by the board of governors". Citizens considers the transfer of catastrophic risk to the global private reinsurance markets to be instrumental in reducing its catastrophic risk and reducing the amount and/or probability of assessments after a catastrophic event. Citizens has transferred risk to the private markets for the last five years. A key objective has been to consistently transfer risk in both the traditional reinsurance and capital markets to ensure adequate capacity, lower the overall cost of risk transfer, and to structure the most efficient program to minimize or eliminate any potential assessments while limiting the amount of surplus exposed.

#### *2015 and 2016 Programs*

For the 2015 season, Citizens transferred \$3.905 billion of risk for the Coastal Account: \$1.856 billion in the traditional reinsurance market and the remaining \$2.050 billion in the capital markets. For a 1-100 year event in the Coastal Account, Citizens had no probable assessments and exposed 57% of its surplus.

For the 2016 season, Citizens restructured its risk transfer program. More than \$2.4 billion of risk transfer in the Coastal Account carried over from the prior season - \$443.3 million from the traditional market and \$1.8 billion from the capital markets. Citizens' strategic plan for 2016 involved a renegotiation of the \$443.3 million of multi-year aggregate reinsurance and reallocated the related coverage alongside and above coverage provided by the FHCF (single year, per occurrence, ex-CNR losses), and the placement of \$221 million of commercial non-residential (CNR) risk transfer. For the Coastal Account in 2016, Citizens had \$2.464 billion of risk transfer, which enabled Citizens to eliminate any probable assessments while exposing 61% of its surplus.

### Proposed 2017 Program

For 2017, Citizens has \$300 million of Everglades Re II 2015-1 capital markets risk transfer carrying over from prior years while \$2.164 billion of risk transfer is expiring (\$664 million of traditional coverage and the \$1.5 billion Everglades Re 2014-1 catastrophe bond). Citizens and its financial advisor, Raymond James, propose a strategy for 2017 to replace a portion of the expiring risk transfer program with a combination of traditional reinsurance and capital markets risk transfer. This will allow Citizens to take advantage of both markets to develop a cost effective and efficient risk transfer program.

The proposed 2017 risk transfer program incorporates strategic elements from the continuation of the existing risk transfer program, which included: coverage for the mandatory layer of the FHCF, single year or multi-year traditional aggregate reinsurance, coverage for commercial non-residential (CNR) risk, and a multi-year capital markets risk transfer program.

1) **Traditional Risk Transfer:** Citizens will work with its reinsurance co-brokers in planning for a traditional reinsurance placement in order to eliminate any probable assessments while reducing the amount of surplus exposed. Staff will bring this program to the Board of Governors during the second quarter of 2017 for formal consideration of all material parameters prior to Citizens making any commitments.

2) **Capital Markets Risk Transfer:** Citizens anticipates placing a portion of its 2017 risk transfer program in the capital markets. Similar to prior years, this risk transfer mechanism will enable Citizens to diversify and expand its sources of risk transfer while minimizing its overall costs of reinsurance. Citizens intends to access capital markets investors indirectly by entering into a multi-year, fully collateralized reinsurance contract with Everglades Re II, a special purpose insurer ("SPI"). This SPI will obtain the funds and will collateralize its potential obligations to Citizens by issuing bonds directly to investors. Like the traditional reinsurance placement, staff will bring this program to the Board of Governors during the second quarter of 2017 for formal consideration of all material parameters prior to Citizens making any commitments.

## **RECOMMENDATION**

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Staff recommends that the Board approve moving forward on the development of the 2017 risk transfer program strategy for the Coastal Account by using both traditional and capital markets at a most efficient cost, with the understanding that the risk transfer program must be brought back to the Board of Governors for final approval prior to the execution of any financial transaction.