Citizens Property Insurance Corporation

Minutes of the Board of Governors Meeting
Wednesday, March 29, 2017

The Board of Governors (Board) of Citizens Property Insurance Corporation (Citizens) convened in Sheraton Orlando North in Maitland, Florida on Wednesday, March 29, 2017 at 9:00 a.m. (EDT).

The following members of the Board were present:

Chris Gardner, Chairperson
Don Glisson, Vice Chair
Gary Aubuchon
Juan Cocuy
Jim Henderson
James Holton
Freddie Schinz

The following members of the Board were present telephonically:

Bette Brown

The following Citizens staff members were present:

Barry Gilway
Barbara Walker
Mark Casteel
Joe Martins
Steve Bitar
Kelly Booten
Jennifer Montero
Brian Donovan
Jay Adams
David Woodruff
Bruce Meeks
Michael Peltier
Andrew Woodward
Violet Bloom
Lori Andrade-Dillingham
Jennifer Dilmore
Carrie Thomas

The following Citizens staff members were present telephonically:

Christine Ashburn

Call Meeting to Order

Barbara Walker: Good morning and welcome to Citizens March 29, 2017 Board of Governors meeting. This meeting is publically noticed in the *Florida Administrative Register*. It will convene at 9:00 this morning. Please do not put your phone on hold. Hit *6 to mute your line and #6 to unmute your line. Citizens Board and committee meetings are recorded and transcribed minutes are available on our website. Thank you.

Roll call: Chairman Chris Gardner, Don Glisson, Gary Aubuchon, Bette Brown (silent), Juan Cocuy, Jim Holton, Jim Henderson, and Freddie Schinz are present.

Barbara Walker: You have a quorum.

1. Approval of Minutes

Chairman Gardner: Good morning, everyone. Thank you for attending today's meeting. The first order of business is the approval of prior meeting's minutes.

A motion was made and seconded to approve the December 7, 2016 and March 15, 2017 minutes. All were in favor. Motion carried.

2. Chairman's Report

Chairman Gardner: I'll be brief. I just want to say two things. I want to compliment Barry Gilway and Christine Ashburn for leadership in the messaging in the Assignment of Benefits (AOB). Barry and I have visited with five boards at the major newspapers in Florida. They are, without exception, in agreement with our message and our position. That's a result of good data, a great presentation, and a consistent message. I understand Christine is not here today but at legislative session, working very hard on our behalf. The second is piece is that our reinsurance program piece begins to gel, we continue to be very well recognized and well received in the marketplace. Barry, you and your staff, continue to strengthen the reputation of Citizens and I appreciate that. Thank you.

3. President's Report

Barry Gilway: Good morning Mr. Chairman and Board of Governors. My comments will be shorter than usual. However, we will be adding one component in Jennifer Montero's section and that is Brian Donovan, our Chief Actuary – because of the impact of reserve on our numbers – it's a brief presentation on reserving IBNR so we understand what's going on relative to reserve development. Bottom line is that the impact of AOB losses is starting to show up in our numbers. We did post the first loss since 2005: a $27.1M loss compared to about a $6M profit in the prior year. It's all coming from the loss adjustment expense (LAE). I'm sure Jennifer will get into more detail but it's generally the number of outstanding cases we have, the outstanding litigation cases we continue to see, and, the difference in severity for LAE between a litigated case and a non-litigated case is 10:1. It's $842 versus $8,500. Litigation continues despite the fact that we've doubled over the past five years the average payout on these claims. Any contention by the trial bar that we're not responding to these claims and paying the claims, the response is simple. We've already doubled the payment. Also, I don't know how you get to the claim, if the claims continue to come in 17 to 21 days after the actual date of loss. The increase litigation of claims moving from 12% to 50% is having an impact and is responsible for about $70M in adverse development in the overall last year: $60M in the personal lines account (PLA) and $11M in the coastal account. Brian will be going into much more detail there. The key issue here is that Citizen's results were reflective of what's going on in the industry. While we've had the first loss since 2005, the industry has had the highest result in terms of incurred loss ratio since 2005. It's increased from 42.4% up 10.6% from 2015. Following industry results in the 3rd quarter of 2016 that did not include Matthew or Hermine, Demotech issued a suspension relative to all of the Florida domestic companies they follow – that's 27. They identified 26 or 27 of those as being problematic. The Demotech guidance that we're going to suspend those companies really had an impact. Demotech indicated to the industry that there were Statutory Accounting Principles that can be used to put additional surplus and reserve into their numbers that might eliminate downgrades. By the end of the 2/28 filing date, 26 companies put in over $150M in surplus and added to reserves over $200M. Demotech issued a follow up report that stated it would be highly unlikely there would be any downgrades. There were only two downgrades and they did not affect Citizens directly. We were concerned because of the 1.4 million policies we sent to the private market, 257,000 of those were assumed by one of these 26 companies. The good news is that the Demotech downgrades have largely been avoided. It came with a warning, and that warning was that clearly this is short term from their perspective. Without any legislative change, you can expect that surplus to disappear, and we will be in the same position in the succeeding quarters. The industry insurers reported last week that the questions raised by Demotech are correct. These numbers are pretty staggering. The combined ratio for 2015 moved from 85.65% and a net income of $680M to a combined ratio of 100.86% with net income of $76M in 2016. But, that doesn't really tell the whole story. 21 companies posted a combined ratio over 110% and 11 of these companies were over 125%. Some of these were major companies. While the direct impact of downgrades has been avoided in the short term, the earnings calls of the major publically owned companies . . . we listened in on United, Universal, Federated, HCI, and Heritage. Those five major companies focused on the corrective action that was necessary from a distribution perspective. One of their solutions will be to reduce their exposure or limit their exposure in the Tri-County area. We can expect each one of those companies to take some actions and have in their agreement with Demotech to maintain their ratings that they would need to reduce their overall writings in those three counties. The impact on Citizens is obvious. Today, we continue to see some reductions and the reason for that is that the reinsurance rates are low. It's an opportune time to buy reinsurance without any question. The private market is buying reinsurance and arbitraging that reinsurance to make them more competitive in the wind business. So, we're still losing wind policies. We're losing Coastal policies, primarily with wind exposure. They are being replaced by PLA policies. I never thought I'd see the day where wind policies are more acceptable to the private market than multi-peril. Our numbers are also being impacted by the commercial marketplace. The E&S market is eating up the commercial business and so are the private carriers. We're down to 1,800 policies in commercial. The bad news is that it was one of the few profitable lines that we had. We are in a market condition in which we are at the lowest we've ever been in our history at 449,000 policies, but you are going to see an increase in the PLA and Coastal business as the market constricts. It won't constrict in the short term period during the 125 day notification for renewals. We're expecting some increases toward the later part of 2017, assuming there is no legislative change. Bottom line is that we're expecting some legislative action. Christine will call in and give you an overview of the key AOB bills. There are some concerning bills, for example, one by Senator Gary Farmer, in particular that would limit one of the only solutions we'll see other than legislative change and that is managed repair. It would eliminate our ability to participate in a managed repair program. That's the overview.

Freddie Schinz: I think I got my numbers right. In 2006, there were 406 AOB cases filed and in 2016, there were 28,000 AOB cases filed. Most come from the Tri-County area. Won't that reflect in the large insurance companies that are participating in Florida to put a moratorium – or stop writing – in the Tri-County area and reflect that Citizens will end up having to pick up those policies?

Barry Gilway: Yes, I think my reference to the five major companies each stated in part of their corrective action plan would be to reduce their exposure. The issue we're facing long term is that yes we'll pick up Tri County business and the business we will pick up is business that will be inadequate from a rate perspective. The examples we've been sharing we're charging $2,600 for a $150K home in Dade County. We're going to charge $2,900 for that home next year. That will increase to $4,700 over the next five years. We use this as an example. The number that is the most staggering is the rate adequate number for that home is $6,700. Even after five years, you'll never reach rate adequacy. Companies have already shut down new business in the Tri County area and we can expect to see more of that without legislative change. We hope to show a brief video put out by the Consumer Protection Coalition today. The numbers are more graphic than the numbers you laid out. In the video, it shows the total AOB losses in the last five years increased from $100K to over $400K in five years.

Juan Cocuy: What is the likelihood that meaningful legislation will pass this time around that will maybe resolve some of these problems?

Barry Gilway: This is a tough one. I have to be careful with what I say here. My honest assessment is that I'm cautiously optimistic that we'll get some reasonable legislation. There are two bills that Christine will get to. One is the Senate Bill (SB) 1038. This is the one that the industry and Christine, Dan, and OIR worked collectively on. That would be our best case. There is another bill on the House side. Representative Jamie Grant's Bill covers the same consumer protections and takes a slightly different approach to establishing a fee structure that would be beneficial. We're optimistic that those two bills, given the current visibility, get a lot of legs in the Senate and House. The biggest issue right now is to get the Senate to even hear the SB 1038 which is the industry solution to this. So far, it has not been on the agenda and will not be on the agenda this week. We're hoping with the most recent comments from Speaker Cochran with a favored focus on AOB and all of the work that Governor Scott has been doing that we'll get some legs on some key legislation. We have a tough fight on our hands with the trial bar. In fact, some of the bills take us in the wrong direction. They put restrictions on us that would be more damning for us than the situation for us today.

Chairman Gardner: The tragedy of this is the ultimate loser is the consumer in this. When we make our rates with the data we have and the trends we see, we are probably below 50% rate adequate in the Tri County area, and that means rate increases until it's remedied. That is regrettable. We're hoping your efforts and the rest of the industry does not fall on deaf ears.

4. **Chief Financial Officer Report**

a. Finance and Investment Committee (FIC) Report

Chairman Gardner: We had a brief FIC meeting yesterday. Kapil Bhatia gave a great update on market conditions. I'll leave it up to Jennifer to give us a reinsurance update.

Jennifer Montero: Over the last month, we've had discussions with multiple reinsurers; the feedback has been positive. There appears to be a lot of capacity and the pricing appears to be favorable. As you know, we did have a teleconference on March 15th to call the bond. On March 21st, the optional termination notice was delivered to the issuer which was Everglades Re. Their administrator Horace Shu and the reinsurer trustee Deutsche Bank were there. The reinsurance contract with the reinsurance trust agreement are to terminate on the optional termination date of May 3, 2017. Over the next month, we're going to continue with the risk transfer discussions with the capital market, and we'll come back to the Board on April 27th for approval of our entire risk transfer placement. That completes the reinsurance update.

b. Financial Statements

Jennifer Montero: If you'll turn to Tab 4, the material you have before you is the December 2016 Quarterly Financial Analysis (QFA), the 2016 Financial Statements, and the 2016 Water Loss Trends. Present unaudited year-end financial information for FY 2016 and the 2016 financial statements are the second tab behind tab four. Pages one and two are a summary of the financial results consolidated and by account. While most but not all of the year-end illustrate the continuation of trends that I've shared with the Board at prior meetings. I would like to address some of the items that have most significantly contributed to our year-end results. During 2016, approximately $1B in storm risk was removed through depopulation, marking an appreciable decline relative to 2015, which approximately $2.5B in storm risk was removed. Consolidated direct written premium decreased $294M during 2016. By account, decreases in direct written premium were by $83M, $26M, and $185M within the PLA, Commercial Lines Account (CLA), and the Coastal Accounts respectively. Relative to 2015, 2016 new business activity in the PLA decreased roughly 22% and renewal activity decreased roughly 11%. In addition to reductions in new and renewal business activity during 2016, significant number in reduction of policies assumed in 2016 was observed. During 2016, roughly $19M of premium was assumed through depopulation in contrast to the $92M that was assumed in 2015. Also contributing to the year-over decline in direct written premium was the 2015 rate filing, which was effective in February 2016 and which for the PLA generally produced overall rate decreases. Historical trends in commercial policies continued in 2016, contributing to a decline in direct written premium of $26M from $63M in 2015 to $37M in 2016. This decline was driven by three continuing trends:

a reduction in new policies, a decreasing renewal rate, and a continued depopulation. Fewer than 100 new policies were written in the CLA in 2016. Direct written premium within the Coastal Account declined by $184M, from $651M in 2015 to $466M in 2016. Both new and renewal policy counts declined by approximately 30% due to the combination of the premium that was assumed and to the declining commercial renewal rate. Commercial business continues to represent a smaller percentage for the total Coastal Account with roughly 27% in 2016, reduced from 29% in 2015 and 30% in 2014. Wind only business, which is in both commercial and personal, comprise of approximately 68% of the direct written premium, marking a slight decline from 2015. The decrease in direct written premium is partially offset by an overall rate increase as a result of the 2015 rate filing. During 2016, Citizens net loss ratio increased marginally by two percentage points from 53% to 55%, while the net LAE ratio increased considerably by 16 percentage points from 11% to 27%. Losses incurred during 2016 were $346M, representing a decrease of $57M relative to 2015. Conversely, LAE incurred during 2016 were $167M, representing a sizable increase of $80M compared to 2015. The PLA experienced a direct loss and LAE ratio of 80%, up six percentage points from 2015. While Hurricanes Matthew and Hermine contributed three percentage points to the 2016 loss and LAE ratio, the primary driver of the loss and LAE in the PLA continues to be litigated water claims. Litigated water claims from accident year 2015 account for $65M of adverse development for calendar year 2016 and as a result of the revision to the rejected number of claims that were entered into litigation. This revised project impacts both loss LAE and comprises of 15 percentage points of the overall loss and LAE ratio. For the most recent accident year, the expectation is that close to 50% of Non-sinkhole and Non-catastrophe (CAT) claims will be litigated. The expected percentage of claims entering into litigation is largely due to the volume of claims reported for AOB and claims reported with representation at the first notice of loss (FNL). However, calendar year 2016 marks the first year wherein the amount of premium earned for sinkhole coverage exceeded the number of sinkhole losses and LAE incurred. Despite substantial declines in premium volume in the CLA, commercial residential policies continue to represent a majority of the CLA books of business. In 2007, CLA reported roughly $60M of direct written premium for commercial residential business. Since 2007, direct earned premium for commercial residential business has steadily declined ending at $38M for 2016. The overall 2016 direct loss and LAE ratio is 15%, includes approximately 5% in loss and LAE related to Hurricanes Matthew and Hermine. The remaining ten percentage points are due to non-CAT events. The 2015 calendar loss and LAE ratio was -23% due to approximately $20M favorable development, stemming from the reduction of commercial residential sinkhole loss reserves from prior accident years. During 2016, no such favorable development occurred, which resulted in a large swing in year-over-year loss and LAE. The direct losses and LAE within the Coastal Account are approximately 29%, marking an increase of roughly 11 percentage points. Approximately five percentage points are due to Hurricanes Matthew and Hermine. The primary diver for the loss and LAE activity unrelated to hurricanes is due to litigated water claims and generally parallels loss and LAE in the PLA, with similar impacts to both loss and LAE impacted by water claims, Non-sinkhole non-CAT losses on multi-peril homeowners and fire and allied policies in the Coastal

Account contributed over eight percentage points loss and LAE ratio. However, the overall loss and LAE ratio, in comparison to the PLA, is lower due to the presence of wind-only policies that exhibit minimal loss activity. As with the PLA, litigated water claims impact both loss and LAE. During 2016, Citizens incurred an underwriting loss of $129M, representing an increase of $122M relative to the underwriting loss incurred in 2015 of $7M. The current underwriting loss is substantially due to the deterioration on the loss and LAE ratios with a notable increase specific within LAE PLA. Reductions in year over year costs associated with Citizens risk transfer program along with declines in underwriting expenses partially offsetting the 2016 underwriting loss. Net investment income consists of interest earned on Citizens investment assets, net realized gains on sales invested assets, and interest expense incurred on senior secured bonds outstanding. During 2016, Citizens realized a substantial year over year increase in net realized gains from the sale of invested assets largely due to the disposition of several legacy assets that resulted in gains of $10M. During 2015, net realized gains on sales were principally offset by the defeasance of Citizens 2007A post event bonds, which future interest expenses were accelerated and recognized as a loss within net realized gains in sales. The 2015 disposition of legacy assets and 2015 bond defeasance costs impact the comparability of year over year activity within net reported realized gains on sales. Increases in net investment income of $30M were primarily the result of investment policy exchanges approved in 2015 effective of the first quarter of 2016 that extended the maximum financial maturity and the maximum dollar weighted average maturity across several portfolios that improved overall portfolio returns. Despite market improvements in investment returns, the 2016 operating results were dominated by declines in written premium and increases in loss and LAE ratio, leaving to an overall consolidated net loss of $27M for 2016. We also included the 2016 management discussion and analysis (MD&A) that has been filed with the Office of Insurance Regulation (OIR). This document provides a detailed analysis of the 2016 financial results and activity. If there are no other questions, that concludes my financial report.

Vice Chair Glisson: I have a quick observation. Since we're in a loss situation last year, is there a path to profitability? Are we going to break even? Or, are we going to keep losing money for the unforeseeable future? Obviously, our surplus can absorb the losses, but I'm curious if there is a plan.

Jennifer Montero: We are doing forecasting and our actuarial group is working with the accounting group. 2018 currently doesn't look any better.

Barry Gilway: We do interim planning, and the latest interim reforecast by Paul Kutter basically shows about a $9M net operating loss for 2017. For 2018, the net operating loss will be about $85M. For the foreseeable future, there is no change. There are other, additional actions we can take. July 1st we'll roll out the managed repair program. Unlike some of the other programs in the industry, it's a very aggressive program and a very consumer-centric program. We believe that will have an impact. We are starting to see some of the impact of the policy changes that we were able to introduce nine months ago. There are other actions. Assuming there is no legislative action, there are other actions that we can take that have been taken and approved by OIR by other companies in areas like sub-limits, acceptability, language within the policies that will definitely limit our negative numbers and at least give us a chance to delay any negative financial impact until we get some legislative change. Short term the impact is minimal but in the long-term it'll be between the $80M to $100M. However, that's not going to stop us from introducing corrective actions we think will have an impact that are not included in the financials.

Vice Chair Glisson: A point to be made is that we don't have an expense problem. We have a revenue problem because of our 10% cap on our premiums, so we can't raise revenue quick enough to offset the loss. I think that's something the legislature needs to know.

Barry Gilway: I agree. When you look at the financials, we're already out performing the private market by almost 400 basis points from an expense standpoint. We are running about 27 in an industry that averages around 31 to 32. It's a little higher for year-end 2016. We do what we can from an expense standpoint; that's not the solution. The solution is to take some actions to reduce loss flow.

Vice Chair Glisson: There is no way to cut our loss flow to profitability. You guys have done a great job with what you have and $27M in a company this size isn't a significant amount of money but it is a loss and there is no foreseeable path to profitability.

Juan Cocuy: Jennifer, on page 7 of that MD&A, in 2015, we had $19M in assessment income and nothing in 2016. Do you know what that was?

Jennifer Montero: That was the collection at the tail-end of the emergency assessment that we levied in 2007; that is the last part of that coming in.
Juan Cocuy: So we don't have any in 2016 because . . . .

Jennifer Montero: We are no longer collecting. We have some residual balance right now, but most of what's going out are refunds.

Juan Cocuy: We never really talk about the cash flow statement. Page 10 of that has the cash flow statement. I know we're talking about trends going sideways on us. If you look at the cash flow from operations in 2015 we had a -$409M. In 2016, we reduced that to -$110M, so that's kind of a positive trend in light of everything else that's going on. Cash flow from operations is doing well.

Chairman Gardner: The actions in the PLA . . . when we look at this business, no private enterprise would grow in a money losing segment. That's the position we're in right now. We're taking on more business that we know is underpriced and we can't break even on. It is important to note that in the PLA we buy no reinsurance. To take the position that we have plenty of surplus and take our eye off the ball for a CAT event, I think, would be unwise. We really need to pay attention to this and we have to understand that this business is going to grow in the short term in the absence of any meaningful reform and there is no market to take this business. The short term horizon is bleak, so we're going to buckle up.

c. Loss Reserving

Jennifer Montero: I'd like to invite Brian Donovan, who is our Chief Actuary. He has a presentation on Citizens' loss reserves practices.

Brian Donovan: Good morning, Chairman and Board members. I would like to talk about loss reserving. There are three topics I'd like to touch upon here. First is in general, high level, what is the purpose of loss reserves and why do we do it? Second, specifically to Citizens, what are some of the current trends we are seeing that are affecting the loss reserving? Thirdly, how does that roll up into the financials? So, why do we need loss reserving? At any given point in time, insurance companies are required to make a reasonably accurate evaluation of its financial position. This requires setting aside assets for future payments have already occurred. Since the ultimate liability of pending and unreported claims is not known, estimates of these future payments are needed. These estimates of the future payments on current liabilities are the loss reserves. In short, loss events happen. Some we know about and some we don't. It will take multiple years to settle. These liabilities need to be accounted for now and not later when they are paid for. There are two types of loss reserving. There is Case Reserves and then the bulk Incurred but Not Reported (IBNR) Reserves. Both are very important. For case reserves, they are set on an individual level. As a claim is reported, a claim adjuster will set a specific case reserve for that specific claim based on that cause of loss and paid based on the severity of that claim. The worse the claim then the claims adjuster will adjust the claim reserve as payments are made. Eventually, that claim will be closed and the reserve will be reset to $0. However, as important as Case Reserve is, it is not sufficient to account for all future liabilities. The Case Reserves must be supplemented with a bulk reserve. This is what we call the IBNR Reserves. These bulk reserves are set by the actuary and they are not set at a claim level. They are set at an aggregate level calculated at an Account/Line of Business level. They are there to account for all liabilities that the Case Reserves just don't cover. There are four components to the bulk reserves. First, we have to set aside reserves for claims that are currently closed that will reopen. We have to set aside payment for pending claims. Then, there are claims we don't even know about, yet. Then the last one is claims in transit. It's a lag in a claim that's reported but hasn't hit the financials, yet. It's the first three components that drive the need for bulk reserves. For the next three slides, I'd like to go through and show an example of each of these and show how impactful they are to the financials. For reopen claims, we are looking at all claims that are closed as of 12/31/2015. We are looking at HO3 water claims that were closed at the end of 2015. At that point in time, there was $1.145B losses incurred. Looking at that exact same closed claims a year later, we see that there was a $38M development. Incurred losses increased by $38M on claims that were closed. That is the impact of reopened claims in one year. That $38M of development in 2016 on prior accident year in 2015 is what needs to be accounted for in the IBNR. The next example is the development on pending claims. These are pending claims. We are looking at a set of pending claims at the end of 2015. We see there is $127M incurred on those claims. That same set of claims one year later has $156M. There was $29M development in 2016.

Chairman Gardner: When you look at 2015 and the rough math is 60% or 55% of raw loss and then it shrinks from 4% to 5%, is that because of the long term nature of the claim, the shorter nature of the claim, or is that because of a deteriorating loss trend? In 2015, you go from $50M to $74M, so that's $22M of actual development. In 2014, you go from $35M to $38M. Is that due to the shorter term tail of the claim, or is that due to a deteriorating trend?

Brian Donovan: That is due to the maturity of the accident year. If you look at 2015 going from $50M to $73M, you've got the $23M. Comparing that to 2014, where you have only $3M in development, that 2014 had an extra 12 months to develop. If we were to go back to the end of 2015 and look at accident year 2014, we'd see development closer and more in line with that $23M.

Chairman Gardner: What do you see as the life of the claim in a time period? Is it two years?

Brian Donovan: It can take five, six, or seven years for some of these claims. As we track the length of the settlement time, and it's very easy how it's taking much longer these days to settle these claims, it's easily trackable to the percent of claims that are being litigated. If you go back six to seven years and look at Non-sinkhole and non-hurricane claims, sure, within two or three years, the vast majority of them are done and settled. Now we look at more recent years, you can see the tail is extending.

Chairman Gardner: Do you anticipate a 12-month development factor to be higher this year?

Brian Donovan: Absolutely. There is a clear trend over the last three years. The third component is the true impact of the IBNR (late reported claims). In calendar year 2016, 553 water claims were reported for accident years 2015 and prior. That resulted in $4.3M in incurred loss. But, because of the last two slides we looked at, we'd expect that $4.3M to grow over time. Those are the reasons why we have bulk reserves. How exactly do we do that? We do that at aggregate level. We look at hurricanes separate from sinkholes at a category for "everything else." That everything else is 80% water claims at this point. We do it on an annual account level line. For every one of those segments listed there, we do a separate reserve analysis. We look up to five different methods. It's important to look at accident year versus calendar year. We just saw three examples of calendar year development affected by accident years. Accident year data is any loss activity that is mapped back to the date of the loss. So, if a loss has a 2014 loss and payments are being made in 2016 from a loss that happened in 2014. You can have actions thorough multiple calendar years pertaining to that particular accident year. Calendar year does not care about the accident date. It's what happens within a given 12-month period. There will be multiple transactions with multiple accident years in a given calendar year and there is never any development in a calendar year. How do we use that information? We need to track the historical trends of the loss in accident year and calendar year. The way we do that is with the loss development triangle. What you see here on slide 11 is a generic triangle. Down the rows, you have accident years. Across the rows, you have calendar years. For example, that yellow cell would be accident year 2013 at the end of calendar year 2014. That yellow cell shows all the transactions that took place with accident year 2013 through calendar year 2014. The next three slides are the crux of what's happening to Citizens. This is Citizens incurred loss triangles for the PLA HO Non-sinkhole and non-CAT loss. If we look at accident year 2007, there was $251M of development. We look at that same accident year at the end of 2008, $251M has grown to $298M. That is $48M of development in 12 months. As you follow that out, you'll see little development in 36 months. This is how we get our arms around the data and look at the patterns. You'll see these patterns develop in a very significant and alarming way. Let's look at accident year 2015. It's at $109M, which is a much lower level because our exposure levels are lower. Then, it jumps to $162M. There is $53M of development in 2015. This is key. If we go to slide 13, this represents percent change for each of those periods. In 2007, there was an 18.08% increase in incurred loss. Now look at 2015 and you'll see a 49% increase in loss. That's not happenstance. You see a very deliberate trend. If you go to slide 14, what we can see is another way of looking at the same thing. You'll see a percentage of reported claims entered into litigation. If we look at 2010 at 12 months, we're saying that out of all reported claims, 2% were litigated. If you follow 2010 out, it ends at 10%. It takes time to develop. You go to the end of 2013, 7% of all reported claims were already litigated. At the end of accident year 2014, 14% went to litigated claims. They nearly doubled. At the end of 2015, it went up 17%. We see that number jump to 20% in 2016. Looking at accident year 2015, from 12 months to 24 months, it jumps from 17% to 37% claims litigated. These exhibits are related. You see an increased in incurred losses. It goes from 12 to 24 months. We can flip over and look at this exhibit and see exactly where it's coming from: increased litigated claims, as we increase claims in litigation, we're going increase the development of incurred loss. So now, how does that roll up into our financials? What does that really amount to? When you look at the PLA HO Non-sinkhole, non-CAT, which is 80% water . . . if you look at the third column and say that this is our projected loss and LAE was at the end of 2015, the total at the bottom is $2.9B. The column next to it is our revised projections of those losses for each of those accident years. We can see that accident year 2015, looking at the next column with adverse favorable development, you'll see $55M of adverse development in calendar year 2016. That is directly related to the number of claims entering into litigation. We can see how that impacts the financials at the bottom. We see that for this segment of business for the loss and LAE, we're coming into the calendar year of 80.5%. It's worth noting that 17.5 of those points are from accidents from prior years. If we go to the next slide and take that a step further, that's just one segment of the business. If we go to the next slide and look at the total non-hurricane loss LAE . . . this is going to be all accounts combined. We see the exact same thing. When we roll it all out for accident year 2015, we see $80M adverse development. There is favorable development in other years, so it really amounted to $70M of adverse development in 2016. If we look at that loss LAE ratio, in the last column there, there is a lot of information buried in that column. It starts at 19, 24, 27, and then jumps up to 37 and 47 before it comes down and starts heading back up again. I think it's worthwhile to decompose that and see what's driving that. Looking at the next slide and look at that last column, we break it out into components into water, sinkhole, and other all components. We can see some pretty clear patterns. We can see accident years 2007 through 2010, there is a push up of loss ratios. The increase is due to the rate freeze and the double mitigation credits. In 2009, 2010, 2011, and 2012, you see sinkhole taking off and dominating that loss ratio. On 2011, it makes up 20 points of the loss ratio. In calendar 2011, we had an underwriting loss in the PLA driven by sinkhole loss. SB48 came along and policies for 2012, you see that 20 points drop to where it's negligible now. It seems to have done its job. Now you look at the water loss ratio and it's headed in a similar direction. That concludes my presentation. Any questions?

Jim Henderson: It seems like we're underpricing our product.   You've got $70M in cumulative adverse development over the period. This is "Monday morning quarterbacking," but certainly the worse thing we can do is underprice our product. We need to be very mindful of making sure we're looking at a very objective view of our pricing and not compounding the issue.

Brian Donovan: Absolutely. We do know we're underpriced. We're subject to the 10% glide path. I think last year our indications were very high double-digits. The loss trend is quickly and easily outpacing the amount of rate we can take because of the policy cap. Our hands are tied on that. What we can do and what we can do now is that we're working on the indication now. We will submit it in June. You'll see a very high number for an indication and we would not be able to raise our rate to that amount. That's why we're attacking it in other ways and that's what we're doing with the policy language, managed repair, and legislation. I don't think we'll be able to legally price ourselves out of this losing proposition.

Jim Henderson: I realize that we're preaching to the choir. This is a great reminder of the challenge that we all have. Thank you for your insight.

Chairman Gardner: I want to say thanks to Brian. This is essentially how we make rates. We're looking in the rearview mirror and paying attention to trends. That's the unfortunate reality for the policyholder.

5. **Chief Systems and Operations Officer Report**

a. Information Systems Advisory Committee (ISAC) Report

Jim Holton: I'd like to thank Kelly Booten and staff for doing a great job in keeping CenterPoint in all of our initiatives online. I'd like to thank Governor Cocuy for his very salient comments and suggestions to a tweak on our charter review.

Juan Cocuy: Thank you.

Kelly Booten: Good morning. On March 14th, the ISAC met via teleconference. We had a few agenda items. One of them was a report on some changes we made in the IT organization. Effective 3/1, Robert Sellers and Aditya Gavvala will report directly to me. Curt Overpeck will be leaving Citizens in August, and he's going to be working on some transition work. We're not going to replace the CIO position. With Robert, Aditya, and myself, we will fulfill those responsibilities with me performing the highest CIO responsibilities: Board reporting, budget responsibility. Robert will be responsible for IT strategy, disaster recovery, and business continuity at the enterprise level, CAT response, IT security, the business relationship management, and enterprise architecture. Aditya will focus on IT services and delivery, keeping the lights running and operations running smoothly. I also reported on our IT audit findings. We closed all of our findings on the network audit. We have two open items, one is a low and one is a medium. Both are expected to be closed by the end of April. We also reviewed the ISAC Charter, which is behind tab 5. We do have one recommendation for change. It's in section three under Primary Responsibilities. The recommendation was to add "Review and assess IT Risk practices, including IT Security & Disaster Recovery."

A motion was made and seconded for the Board to approve the changes to Citizens' Information Systems Advisory Committee Charter as described in the action item. All were in favor. Motion carried.

Kelly Booten: In addition, Sarah Harrell, Enterprise Program Director, briefed the committee on the status of the CenterPoint (ERP) implementation. We are going live this weekend with Phase I, which includes the financials and procurement. Everything has gone very well. The production conversion is happening this week. We cut over this weekend and as of Monday we'll be up and running on the new system, which obviously we'll be able to do more automated expense reporting. Sarah, Katherine Moore, and Adam Chapman are a few important key roles there. Our business partners – Andrew Woodward and all of his staff have been tremendous in Finance and Accounting. It's the same thing with Procurement – Spencer Kraemer and Stephen Guth. Hank McNeely in HR will be starting up the next phase with HR. Once we're up and running next week, we'll be working on the next four phases that will overlap. We'll start on the HR phase, the budget phase, and advanced procurement. That concludes my ISAC report.

b. Action Item: Multi-Function Copiers

Kelly Booten: The action item is facilities related. It is for copiers. This is approximately $192,918 for a three year lease term this includes annual lease cost and projected click count charges and $4,000 for month to month continuation of one machine through 7/31/17. This is with Konica-Minolta for 15 copiers.

A motion was made and seconded for the Board to approve a three year lease term with Konica-Minolta under State Term Contract 600-000-11-1 from 11/14/17 to 11/13/20 for Jacksonville as described in this Action Item; to approve a three year lease term with Konica-Minolta under State term Contract 600-000-11-1 from 8/1/17 through 7/31/20 for Tallahassee as described in this Action Item; to approve expenditure of $4,000 for month to month lease of one machine through 7/31/17; and to authorize staff to take any appropriate or necessary action consistent with this Action Item. All were in favor. Motion carried.

6. Chief Consumer and Agent Services Report

a. Market Accountability Advisory Committee (MAAC) Update

Steve Bitar: The MAAC met yesterday and was facilitated by Chairman Dave Newell. Our Director of Agency Services Carl Rockman provided an update on our current agent and agency counts, which continue to decline. We're just at 7,500 agents and we've broken the 5,000 limit. We now have 4,977 agencies represented in our base. We also reviewed our agent and outreach initiatives, including our training and webinars that we specifically targeted toward the depopulation program. We discussed key agent management initiatives regarding claims reporting and new business cycle times and how to approve those in the agency setting. We also shared agent participation results from the training we've conducted thus far. Barry Gilway provided comments about the AOB. Our Director of Market Services Adam Marmelstein provided an update on our depopulation activity. We had 88,000 policies assumed in 2016, and up through 2017, we've had 11,399 policies assumed. Adam also provided a Clearinghouse update, which I'll be happy to provide next as part of the agenda today.

b. Clearinghouse Update

Steve Bitar: Behind the Clearinghouse tab, you'll see a report that I provide to you every quarter. The first few slides go into some detailed information by policy form. Slide six is a good summary. Our 2016 results for the Clearinghouse show that we have roughly 25,000 policies that were deemed ineligible for coverage at Citizens throughout the year, representing about $5.8B Coverage A averted and not placed within Citizens. Thus far, January and February activity, we are just at over 3,500 policies that have found homes in the private market, representing $812M in Coverage A averted. Slide seven is a graphical representation year over year. We've been in operation for over three years with the Clearinghouse, and our trends are moving in a positive direction as we find coverage for A that's redirected to the private market as well as policy counts growing year over year. Slide eight gives you an update on some upcoming activity. I am happy to report that we will be adding the wind only policy forms to the Clearinghouse platforms, specifically the HW2 and the HW6. We are going to extend that to Southern Oak that already participates as well as Westin, which is a new carrier that's being added to the platform, taking us to 17 companies. We have current participants – Monarch International and Safe Harbor – adding additional policy forms in the second and third quarters respectively.

Chairman Gardner: What does your crystal ball tell you?

Steve Bitar: My crystal ball tells me that we will continue to have activity coming into Citizens. Unfortunately, I don't think we're going to have many players in the Tri County area that will be making offers. We'll see some opportunities outside of the Tri County area, but that is why we're adding wind. That is where there is appetite. We have two companies coming in and a couple knocking on the door, wanting to participate. Again, it will not keep up with the activity that we're seeing on the PLA side. I do have one more request. As you know, the Clearinghouse has been up and running for three solid years. It's part of our normal business operation. Initially, I was sending to the Board a report every quarter that gives the results for the Clearinghouse. What I would like to do is move the purview of the Clearinghouse reporting to the Depopulation Committee instead of taking up time during our Board meetings every quarter. I think it makes sense with the work of the Clearinghouse aligning with what the Depopulation Committee oversees. I can provide regular Clearinghouse updates there. If there are any issues to bring before the Board, I will do so as with the other committees.

Chairman Gardner: Don, how do you feel about that?

Vice Chair Don Glisson: It makes sense.

Chairman Gardner: I don't have any objection to that and that's probably where it belongs. I think it's a good move.

7. Chief of the Office of Internal Audit Report

a. Audit Committee Update

Juan Cocuy: The Audit Committee met yesterday, and we went through the Office of Internal Auditor (OIA) dashboard, which included projects completed, projects in process, and open projects. We went through the OIA charter and determined that no changes were necessary. Jennifer Montero reviewed the financial statements that we've just looked at also. The external auditor discussed their plan to come during the first week in April with drafts available by mid-May. Finally, we discussed our Chief Internal Auditor's year-end evaluation, which resulted in "meets or exceeds expectations" with a few "outstandings" [sic], especially in strategic and consulting advisory attributes.

Joe Martins: We discussed the progress in the Audit Plan, with 31% of the plan is either in progress or completed at this point in time, which is good progress. We discussed the results of the audits and we included some summaries of audit report results in the pack we provided to you. We talked about the progress of the roll out of the Citizens Internal Control Framework (CICF), which focuses on finance and operational processes. We have 37 of the 42 processes either completed or in progress, and we foresee that we will be completed with that rollout at the end of this year.

We are commencing with the IT processes in April and we will be completed with that by the end of next year. We presented a Citizens revised risk management framework and the revised charter of the Risk Steering Committee. We also presented the annual review of the Audit Committee charter and proposed that there are no changes to the charter. We brought to the committee an action item. For the past seven years, the OIA had a panel of 19 suppliers, which we could tap into to assist us when we needed technical support. These agreements are expiring, and we are bringing before the Board an action item for approval.

.

b. Action Item: Internal Audit Consulting Services

Joe Martins: this action item seeks Board approval to enter into contracts with a panel of fourteen auditing/consulting firms to augment the OIA staff on an as-needed basis. The number of recommended firms is considered reasonable due to the variety of potential engagements and the possibility of conflicts. Assignments of work will be made pursuant to Task Orders issued by OIA primarily in certain areas. Compensation will be based on the hourly rates set forth in the contract or on a negotiated fixed fee. Execution of a contract does not guarantee any work to a firm. The contracts will have a five year base term and may be renewed for up to five additional years upon mutual consent.

A motion was made and seconded for the Board to approve the recommended awards and resulting contracts with the fourteen firms identified on Exhibit A for a five year base term and five year optional renewal term for a total cost not to exceed $2,000,000 and to authorize staff to take appropriate or necessary action consistent with this Action Item. All were in favor. Motion carried.

8. Chief Legal Counsel and General Counsel

Chairman Gardner: I understand that Dan Sumner is not here, but Mark Casteel will speak in place.

a. Action Item: Business Insurance Agent of Record

Mark Casteel: I have one action item I'd like to present on Business Insurance Agent of Record. That springs from ITN 16-0023, which was issued in October 2016. There were three responsive vendors that replied. Author J. Gallagher and Co. was selected. The contract term is for three years with a two year renewal. As you know, we've purchased ten types of coverage at Citizens: D&O, workers compensation, cyber insurance, etc. They will also be providing us with consulting services on vendor insurance issues.

A motion was made and seconded to for the Board to approve the recommended award and resulting contract, including renewal periods, for ITN No.: 16-0023 to Arthur J. Gallagher & Co. as set forth in this Action Item and to authorize staff to take any appropriate or necessary action consistent with this Action Item. All were in favor. Motion carried.

9. **Vice President Communications, Legislative & External Affairs Report**

a. Consumer Services Committee (CSC) Update

Freddie Schinz: We discussed at our meeting the new AOB brochure that each and every one of you should have in your packet to explain to every policyholder the complexities of AOB and the financial impact that has on each and every citizen in Florida. I think it does a fantastic job.

Christine Ashburn: The CSC met last week via teleconference on March 23rd. As Governor Schinz has indicated, the committee received an update on the AOB outreach and education efforts we've been undertaking over the last several months, including to policyholders, agents, and the public in general. We've completed editorial board visits with six major papers around the state. We've spoken with more than 15 of them. Last week sent out an educational email to more than 100,000 impacted policyholders in Dade, Broward, and Palm Beach Counties. We've also been tracking and are happy to report that we've seen close to 70 articles published since the beginning of 2017 on AOB related issues. Chairman Gardner, as you've indicated at the outset of the meeting, it seems clear that most of the newspapers around the state understand the issue and that this ultimately hurts consumers. We are tracking all of these efforts and look forward to sharing more detailed analytics with the Board in the coming weeks. We will be showing the video that Barry references following the CSC report before I jump into the legislative update. Additionally, the second item that the committee heard about was the overview of Citizens Self Service Strategy Plan. We are gathering information and evaluating opportunities for self-service in the 2018 budgeting process. Incremental improvements will be made where possible within budget and prioritized on best value. There were no actions taken by the committee.

b. Legislative Update

Christine Ashburn: I'll be happy to go over my legislative update while they go over the video's technical issues. As Barry indicated in the President's Report, I am in Tallahassee unable to be with you due to the fact that we are in the midst of the 2017 legislative session. We are on day 23 with 37 days remaining. We are just over one-third of the way through. The only bill that has seen any action is HB 1421. That bill takes a little bit of a different attempt at resolving AOB issues and will take us a long ways forward. I want to walk you through the AOB bills out there. Several bills, while not AOB specific would have a significant impact.

- SB 1038 is the bill that the industry, Citizens, and OIR worked on and we believe would ultimately be the silver bullet fix for the abuse we're seeing. The bill will prohibit vendors working on the AOB seeking fees under the one-way fee statute. If mitigation occurs, it requires an assignment containing a written itemized written cost estimate of the work to be performed work by the assignee. It requires that an AOB be provided to the insurer within three business days after it is executed. It requires assignee to comply with the responsibilities that are parallel to those or required of our policyholders under the policy examinations under oath, appraisal, and cooperation of the investigation. It will prohibit the use of cancellation fees and would also allow consumers an opportunity to rescind the agreement within seven days following them entering into an agreement. It will prohibit liens on property with respect to insurance proceeds. That bill – if you look back at our December meeting – tackles all of the bullets that were on our legislative list. This bill has not been heard in the Senate. It is sitting in the Banking and Insurance Committee. We do believe that if there is going to be any movement on the AOB, we expect to see it on next week's agenda. While we do not have that right now, we will later this afternoon. I can email that to the Board.

- Senator Gary Farmer has filed SB 1218. This bill would license water damage restoration and vendors that are currently not licensed, provided that assignments are not valid, and the agreement is limited to the work performed. It allows the policyholders to rescind if work has been performed. It requires an update of the work. It requires that if you do the work you must be licensed under current law. None of those provisions are troubling to Citizens; although, we don't believe standing alone that they will fix the problem. Where we have some concern is that the bill would basically require that if a carrier has a managed repair or a preferred vendor program, then anyone who meets certain requirements including being certified by a certain organization must be considered preferred vendors or managed repair vendors for anyone's program. Ultimately, we're shutting down your ability to negotiate to work with certain vendors that are willing to do business for certain pricing and meet certain standards. That is an avenue we're moving forward with later this year under current law that would allow us to tackle this problem in absence of legislative action. There is no house companion to Senator Farmer's bill and that does provide some hurdles for him but we do anticipate that the bill could be heard in the Senate next week.
- I referenced Representative Grant's Bill (HB 1421). The bill would do a lot of what Senator Hukill's bill does and would put responsibilities on the policy and require certain things like detailed estimates, rescission periods, notification to the insurer, etc. It does take a different approach tackling the one-way attorney's fees issue. By prohibiting the use of that, it limits certain parts of the statute in recovery of fees and outlining a process under which it would be a prevailing party concept with details. There is a difference if you owe someone with fees and then you owe someone else on another end without fees. There are provisions that we as the insurer could recover fees from the plaintiff. It is a step in the right direction and we have worked on some amendments to clean up his intent.

We do believe that the Grant Bill with some minor amendments could be another approach that could work. There are two bills, while not specific to the AOB issue, would absolutely affect the assignment or escalate the AOB problem. One is SB 1684 by Senator Gary Farmer. This bill is broad and wide-reaching and would prohibit the pass through the plaintiff and the defense costs into rate making for many lines of insurance and this would clearly include the pass through of costs of AOB suits. While it wouldn't have a rate impact, it would absolutely have a bottom line financial impact for Citizens and all carriers. It would be detrimental to the health of the market. Carriers could pay claims to avoid litigation at all costs, which would then go into the rate base. We could see a more accelerated closing down of the market across the state. That bill has not been heard in any committee. Senator Flores' SB 1746 outlines a number of changes in property insurance, some of which would be specific to Citizens. I do want to point out one provision similar to that which is SB 1684. That allows the prohibition of pass through of plaintiff's fees in rate making. We are happy to provide you with any copies of bills and we will keep you updated as we move through the process. From a housekeeping standpoint, regular committees will stop meeting after week seven. With this being week four and with legislation taking break during week six, time is of the essence. We do believe if there is going to be movement, we anticipate it being next week. We anticipate that Grant's bill will be heard.

Jim Holton: Can you give us some indication of the amount of support from industry and other public advocacy groups that are behind the senate bill that's stuck in the Insurance and Banking Committee right now?

Christine Ashburn: There is a broad collation of consumer groups, industry members, citizens, other agent groups, and contractors called the Consumer Protection Coalition. They are the authors of the video you are about to watch. One of the criticisms of the insurance industry has been that we cannot get on and stay on the same page on this issue. That has not been the case this year. Everyone is aligned and agrees that SB 1038 or HB 1421 is the way to go. We all agree that the components in the bill are the right components. There seems to be broad consensus except for the attorneys and water mitigators. I can't speculate the reasons why the bill has not been heard, except that Senator Flores indicated that there is concern about how to attack attorney's fees following what we've seen happen with the Supreme Court with worker's comp fees strike down. I would argue that this is different. Unlike this as a fee cap that was stricken by the court as unconstitutional, we believe it clarifies what was always the intent of the attorney's fees which is to protect consumers. Even the courts in some rulings have commented that while their hands are tied, the one-way fee statute clearly never intended for access to business to business litigation.

https://youtu.be/3eXibwquOHQ

10. Consent Agenda Items

Barbara Walker:

- **Investment Performance Compliance and Risk Analytics – Two Month Contract Extension, Contract # 12-11-0034-00: It is recommended that Citizens' Board approve a contract extension for two months and at a total payment not to exceed $120,000 for Clearwater Analytics, Inc. Contract 12-11-0034-00 as described above to allow for transition of services to a new vendor and to authorize staff to take any appropriate or necessary actions consistent with this Consent Item.**
- **Telecommunication Network and Services – Extension, Contract 0908003100: The Citizens Information Services Advisory Committee approved and recommends the**

Citizens Board of Governors approve contract extension from June 11, 2017 to December 10, 2017 or the amount of $730,000 and to authorize staff to take any appropriate or necessary action consistent with this Consent Item.

A motion was made and seconded to approve the consent agenda items. All were in favor. Motion carried.

New Business

Meeting adjourned.