CITIZENS PROPERTY INSURANCE CORPORATION

MINUTES OF THE
BOARD OF GOVERNORS MEETING
Wednesday, December 9, 2015

The Board of Governors (Board) of Citizens Property Insurance Corporation (Citizens) convened in Sheraton Orlando North in Maitland, Florida on Wednesday, December 9, 2015 at 8:30 a.m. (EST).

The following members of the Board were present:

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

The following Citizens staff members were present:

Barry Gilway
Barbara Walker
Dan Sumner
Kelly Booten
Violet Bloom
Joe Martins
Steve Bitar
John Rollins
Jay Adams
Jennifer Montero
Andrew Woodward

The following people were present:

Kapil Bhatia	Raymond James
Dave Newell	FAIA

Call Meeting to Order

Barbara Walker: Good morning and welcome to Citizens December 9th, 2015 Board of Governors meeting. This meeting is publically noticed in the *Florida Administrative Register* to convene at 8:30. Citizens Board meetings are recorded and transcribed minutes are available on our website. Thank you for your patience. We are still on hold for a few moments and will convene as soon as possible. Thank you for your patience. Good morning and welcome to Citizens December 9th, 2015 Board of Governors meeting. This meeting will convene momentarily with a roll call. Thank you for your patience this morning.

1. Approval of Minutes

Chairman Gardner: Good morning, everyone, and welcome to the December 9, 2015 Board of Governors meeting. Our first order of business is the approval of the prior meeting minutes. Would you like to do a roll call first, Barbara?

Barbara Walker: Yes, sir.

Chairman Chris Gardner, Vice Chair Don Glisson, Gary Aubuchon, Bette Brown, Juan Cocuy, Jim Henderson, Jim Holton, Freddie Schinz, and John Wortman were present.

Barbara Walker: Chairman, you have a quorum.

Chairman Gardner: Thank you, Barbara. Again, the first order of business is approval of the prior meeting's minutes.

A motion was made to approve the September 30, 2015 minutes. Governor Wortman seconded the motion. All were in favor. Motion carried.

2. Chairman's Report

Chairman Gardner: I want to give a quick year-in-review and then go over a couple administrative items. As we finish off 2016, we can look back to an incredible year of accomplishments at Citizens. In fact, this Board and this staff achieved results that we previously thought as unachievable. Four years ago, our leaders tasked us to shrink Citizens as well as to reduce assessments. As you all are aware under the leadership of Barry Gilway and his staff, we have done both at a level that has outpaced our expectations and our projections. History shows us that this is not a static business. As I've said before, we must operate our business to expand and contract with very little notice. To do this effectively takes careful planning, long-term thinking, and creative ingenuity on the part of our most capable staff. What further complicates this is that we as an organization are also a public entity and must operate in a transparent, efficient way that assures our stakeholders that we are good stewards of this business. However, our policyholders expect us, above all else, to respond as a best in class claims organization in a time of crisis. Citizens has made strategic investments which has served it well. We have made investments in our Claims organization, Data Capture and Management capabilities, and our Clearinghouse initiative, all of which have shown benefit to our policyholders and the rates that they pay. These investments have also allowed us to work with the private market to encourage depopulation at an unprecedented level. Finally, all Floridians have benefited from the de-risking of Citizens and the elimination of the 1-in-100 year assessment. I'm very respectful of each member of this esteemed Board of Governors and appreciate their opinions and input in steering this organization in the right direction. As the next year unfolds, I encourage each of you to take a long view toward remaining accountable to our stakeholders while not deviating from our direction of shrinking Citizens and protecting taxpayers in the event of a storm. Thank you, Board, for a wonderful year. Two housekeeping items – there will be a Board picture at the break. I know there is a gallery full of admirers out there, so give us some privacy to take a picture, and then we can mingle. To accommodate Governor Cocuy, I'm going to move the Audit Committee Report past the CFO's Report.

3. President's Report

Barry Gilway: Good morning, Mr. Chairman and Board members. I'd like to echo some of Chairman Gardner's comments. We've had a pretty extraordinary year. In fact, as I go through some of the comments in the President's Report, you'll see that while the results have been phenomenal in terms of depopulation, that in fact, it generates a number of management issues that we have to consider and influences our overall financials, particularly in the short term. I'd like to refer you to a slide deck. I'd like to start by thanking each Board member for the extensive time you've spent with staff, Jennifer and myself, in particular, to review the budget in detail. Many of you spent considerable amount of time going into detail and asked good questions. Frankly, what you'll find going through this presentation is that many of you made suggestions that have been incorporated within the material. I'll be going over the slide deck and then I'll be turning it over to Jennifer briefly to look at the 2016 income statement that really references the budget for next year. Slide number one – the results of depopulation have been truly extraordinary. We are sitting here today at the lowest level of policies, even prior to 1996 and prior to the consolidation of the two entities that formed into Citizens in 2002. Back in 1996, we were actually at 1.4 million policies. We dropped to an all-time low to 517,000. As we sit here today before we get to the December depopulation, we're looking at 509,000 policies. In all likelihood, we'll drop below that 500,000 for the first time by the end of the year. The reason why this slide is important is the magnitude of change over a relatively short period of time. If you literally take a look at the combined numbers, we started at $3.2 billion in Direct Written Premium (DWP). If we are on target again next year, we'll be below the billion dollar level, and we'll be looking at a $900 million organization. It's a dramatic drop in DWP. Probably the most important component of this slide is in the lower right hand corner when we look at Coastal. The reality is that when we set the budget for 2015, we simply had no expectation that we'd lose close to 100,000 policies in the Coastal Account in the year. Our original projections were in the area of 25,000 Coastal Policies. The next slide is important because the earned premium following depopulation . . . the earned premium is the actual premium we're really working with as an organization. What I've done next is show what this looks like from a policy perspective. The budget in the initial 2013 is for about 1.2 billion on the combined basis. We actually came in at just a little more than 1 million policies. The interesting thing is that every single year we set aggressive objectives and every single year this staff exceeded by wide margins the expectations. That continues into 2016 and 2017. I'll be commenting on this later, but as the Chairman commented in his opening remarks, we have really changed the way we look at our business. Under the direction of Kelly Booten, who heads up our Strategic Operation and Planning, we have now taken a step back and take a much longer view over our business. We call it "scenario planning." Thanks to improvement under John Rollins' direction in the analytics area, we are getting a good picture of where we are heading. On a policy basis, as you'll see in the Coastal, we had a budget initially in 2014 of 380,000 policies. Coastal had been sitting at 460,000 policies for over a decade. Now, we're down to a little over 200,000 policies in Coastal, which is amazing. Keep in mind that we're still looking at a coastal rate deficiency in the area of 50%. And, yet, even under that set of scenarios, we're losing business in the Coastal Account. However, depopulation is slowing. We're becoming the company we're meant to be and that's the company of last resort. All of this simply shows that the interest of the private companies continues to tick up in the marketplace. In 2014, the Office of Insurance Regulation (OIR) approved 1.4 million policies and in 2015 they approved 1.35 million policies. But, as you'll see, as we become closer and closer to that residual market, we're losing fewer policies over time. We expect that to continue next year, even though we continue to see a reduction in that 70,000 to 80,000 policy in Coastal. Depopulation will become tougher and tougher. What John Rollins will spend time on later and what the next slide shows is what is happening to our overall book of business, which is changing in its nature. As we become a more residual market, you can see that Coastal is not changing as rapidly as the Personal Lines Account (PLA). The makeup of the book of business is moving toward Tri-County, Monroe County, and Sinkhole Alley – Pasco, Hernando, etc. This has an impact over time, simply because the overall book of business will become less rate-adequate. This next slide is probably the most important and displays some significant components. One, when you take a look at the overall projection for 2015, we're looking at a $70 million overall gain. On this slide, Coastal will show an operating loss. That also continues in 2016. We're anticipating an operating loss in 2016. This is driven as a result of buying reinsurance at a specified Probable Maximum Loss (PML) and having that PML drop far greater and far faster than we ever expected. During the wind season, we needed that reinsurance buy, but by the end of the year, the PML and revenue associated with that drop in PML outpaced the reinsurance buy. I'll get into that more detail in the following slide. There are two points I want to make. We will show a $67 million operating cost in Coastal in 2016. However, we're already working on some potential alternatives that might generate additional earnings in 2016. Jennifer and Kapil are working on models today to look at our mix of reinsurance to determine if there is a way to get our multi-year reinsurance placed lower in the layer chart so that would eliminate the need for $40 million placeholder that we currently have in that 2016 budget. If we can find an opportunity to pick up another $20 million to $30 million as a result of moving the current reinsurance program lower, Kapil and Jennifer will indicate some improvement in the investment earnings, then we can cut significantly into the $67 million loss in 2016. The good news and the reason why we're looking at this over a longer period of time is that if you take a look at 2017, we will have the ability to step back and redo the entire reinsurance program. We literally drop our spend from $300 million in 2015, $204 million in 2016, to $115 million. The spend in reinsurance is dropping dramatically. What you're seeing here is that in 2017 is the uptick in the earnings for the organization. The next slide is a depiction of what's happening and why it's difficult to do long term planning for reinsurance. This simply shows that when we went to market in 2015, we were looking at an $8.2 billion PML. A couple months after that, we were at $7.5 billion PML, and after the wind season, we're dropping down to about a $5.6 billion PML. The reduction in the Coastal coverage is playing havoc with our reinsurance program and will cause us to retrench. The other component is Admin Expenses. The expense ratio will be increasing. We're going from $2.9 in 2015 and we're going to be at 27 is going to be more than norm on a go forward basis. That's pretty consistent with the expense ratio that we see in the Florida private marketplace. Just to give you a feel of some elements of the expense ratio, what we show here is start personnel costs over time. While personnel costs are dropping, revenue is dropping far faster than we can drop the overall personnel costs. We consistently retain about 1,100 to 1,200 employees, and that has been the case for seven or eight years. However, the contingency employee county increases and decreases with the overall level of policies we're servicing. If you take a look at the overall number of resources, we have already dropped from 2,064 contingent resources to 1,734. The budget contains another 120 personnel budget next year, and that is a combination of contingency resources and a reduction of 50 or 60 individuals from the staff standpoint. The intent is to do that through attrition and be judicious. We do lose about 10% in turnover every year. Resource demands – this is what we're dealing with. On the left hand side, we're talking about the claims issue. I will tell you that we cannot hire people fast enough to handle the flow of litigated cases that are coming into the organization. That's the fundamental issue. In 2013, we opened 6,300 new litigated cases, and in 2014 – and this is despite the policy drop we're experiencing – we opened 7,300 litigated cases. This year, we opened 8,200 cases. We've still included in this budget the hiring of at least 25 individuals within the adjusting ranks for water damage alone. We're hiring in the claims area despite this significant drop in the policy count over time. On the right side, this is an interesting business. Typically, you'd expect that business decreases as you drop off. It doesn't. We're still averaging about 11,000 new policies coming in through that front door on a monthly basis. This year, we're contemplating 130,000 new policies this year. Anyone who is familiar with residential lines of business knows that about 80% to 90% of your resources are spent in underwriting, inspecting, etc. new business that comes through the door. By the way, we're not expecting that to really change. We did a survey that assesses the makeup of those 11,000 policies. The good news is that they are policies that fit the definition of the residual market. 3,006 agents are still submitting business and 71% are older homes. 40% are less than Coverage A; nobody in that market is really writing that business. Even in the HO6 condo area, what we're getting through the front door is Coverage A less than 50,000. You're looking at relatively low content amounts. The business is either cancelled by another carrier . . . . about 30% to 40% are new purchases of homes. That new business count is driving all of these other metrics. We're still getting about 95,000 calls a month in Steve Bitar's area. We're averaging about 6,400 PLA customer service calls a month. In the Commercial Lines Account (CLA) area, we still get consistent flow of new business. The next slide is meant to demonstrate that while the policy count drops significantly, it doesn't reflect all of the workflow. We actually service considerably more business than we have in terms of policy count. In 2015, for about every 100 policies that we have, we're servicing an additional 44 that have been assumed but not renewed by assuming companies. The workload continues. Over time this drops off. Even with the issues we're displaying here, you still see about a 27% expense ratio compared to the primary companies in Florida of about 26.5%. This is the latest information. The next few slides show how Administrative Expenses flow through the organization. We're looking at specific Citizens programs that are extensive. There's the glide path. Our expense ratio is impacted significantly as the result of the rate inadequacy. If we were to charge the rates that were actuarially sound, then that would impact our expense ratio by another 2%. We cede earned premium under the assumption of other companies. Premium loss results in another 1% to 2% impact on overall expense ratio. This shows the components of the Administrative Expense and the Variable Underwriting Expense. The pure variable expense commissions, taxes, etc. have been consistent. We're showing a 10% in Underwriting Expense. In Admin Expense we're peaking at this 16.2% level. Today we believe the 16% is reflective of the expenses over time. These include our investments into a new Vendor Management Organization and Field Management. We now look more like a standard insurance company. Probably the most compelling slide is this slide. This shows the reality of Citizens. This is historic expense and premium comparison. If you go back to 1996, we had 1.4 million policies. Then, in 2001, we dropped to 517,000 policies. In 2007 as a result of the Poe Assumption and the 2004/2005 storm season, we peaked at 1.3 policies. In 2009, we dropped down to the 800,000 level. We increased in 2012 to the peak of 1.5 million policies and now we're dropping down and we hope to be below 500,000 next year. What this shows that Citizens has done an effective job over time of managing the expenses of the organization to the ebbs and flows of the policies. While the stress tests done by the CFO on the private companies shows how strong the marketplace is today, a large part of that . . . you've got this strong marketplace. However, that doesn't mean in the event of a large catastrophe (CAT) or the variances of the reinsurance market, we'll have a movement back into Citizens and we have to be prepared for that. We have to be prepared for a flow back. I've already made my points about the cost and acquisitions slide. This shows the amount of ceding commissions that are flowing to the depopulation companies and the impact it has on our overall financials. This brings me to my final topic and that's reinsurance. It's important and we've spent time with each of you why the $67 million operating loss in Coastal and how that will turn around over time . . . I'm going to present to you on a decision that the Board does not have to make today. This will be a decision made in the April/May timeframe when we have a better picture of where the PML sits. Within that $67 million loss, we have incorporated a $40 million placeholder. This shows why. If you look at the 2015 layer chart in the lower right hand portion of the graph, it shows how much of a surplus is exposed in a 1-in-35, 1-in-50, and 1-in-100 year storm. The way we structured the program in 2015, we exposed 57% of our surplus for a 1-in-100. We would have lost that surplus. The driver here is the wrap, which is the layer of reinsurance that wraps around the Florida Hurricane CAT Fund (FHCF). In 2016, if we do not buy reinsurance we just retain the rollover in the higher layers, we would spend about $164 million. What you have in the budget is the ability for that $40 million to put us in the same position in 2015 in terms of surplus projection. We think it's prudent to look hard at an additional wrap to give us protection in the lower layers, particularly in the 1-in-35 layer. I'll draw your attention to the lower right hand side of this slide. In Coastal, if we continue the rollover coverage, we would expose about 40% of our Coastal Surplus. If we spent $40 million, then that drops to exposing about 29% to 30%. As an insurance purpose, I'm more focused on protecting our surplus. When the time comes, I think we need to look at the impact on a limited reinsurance buy. The point I want to make is that this is not a decision for the Board today. It is reflected in the budget but it depends on the PMLs in place at that time and the pricing available. The final slide I have, before I turn it over to Jennifer, is the storm assessment slide. We continue to improve the overall surplus position of the company. Obviously, as the PML drops and because of the continuing increase in surplus levels, we're better protected every year. In 2014, we eliminated any potential of assessment in a 1-in-100. That continues throughout 2015, 2016, and 2017 with an additional surplus that is not subject to loss. That presents a summary of what you're looking at within the budget itself. We've gone through what we expect to happen in 2016 and 2017. I will turn it over to Jennifer quickly to see if she can take you through the income statement.

Jennifer Montero: Within your Board books, you've received two items: 2016 Operating Budget, and Financial Schedules and Supporting Information. If I can get you turn to page 14 in that book, this is the operating budget and income statement for the 2016 budget. It's compared to the 2015 projected and the actual 2014 budget. DWP is budgeted for $909 million compared to projected 2015 of $1.2 billion. That's reduction of 30%. Our total net earned premium will go down 30% from $743 million to $516.9 million. All the underwriting expenses are all decreasing for a total of 26.04% from $703 million down to $520 million. Loss Adjustment Expense (LAE) – commissions, taxes, assessments – are all decreasing. We expect the net underwriting income to decrease as well. We have a decrease in total other income at 45.9%. That brings us of a net income of $13.39 million compared to $70.9 million. We will have a $57.6 million and $67.7 million loss in the Coastal Account in 2016. Our policies in force (PIF) reducing from 479,000 in 2015 to 417,000 at year end 2016.

Jim Holton: Would the continuing drop in PML suggest that we're looking at reinsurance buys in terms of going for multi-year or single year? I know we're getting too much into the weeds now, but for general observations . . . .

Barry Gilway: In terms of reinsurance placement, we're not ready for the substantial drop in PML. We needed that reinsurance buy in 2015. It was required to take us through wind season and give us the protection we needed. I'm not second guessing the reinsurance buy. However, it's clear to me that we need to be as flexible as we need to be. The decision in 2015 is that we were looking at all time low rates and the intent was to lock in to rates we'll ever see in the business. I would say that we'll have to take a look at that time. We'll focus on more flexibility. Instead of a two- to three-year program, we'll look at a one-year program to react quickly to any market changes. Keep in mind that we believe that at that 400,000 policy level we can't comprehend going below that lower. I don't think we'll face the same magnitude of loss. We at one point thought that 450,000 was the low. Far more analytics went into this budget and this forecast than has ever happened into the past. Confidence level in 2016 and 2017 is higher. We need to maintain the flexibility when we put these reinsurance programs together.

Jennifer Montero: I might add that our $1.5 billion CAT Bond does mature in 2017 and so does our multi-year. If in 2016 that we only buy a single-year, in 2017, we can restructure the chart to reflect our PML and to add flexibility.

John Wortman: Do you contemplate looking at any reinsurance purchase in the CLA or PLA in the spring?

Barry Gilway: No, sir. We're not considering reinsurance in the PLA/CLA. We think the surplus . . . if you go to the layer charts, I didn't spend any time but this is the projected 2016 layer chart. It shows that we have adequate surplus along with FHCF protection. In the aggregate, we're exposing 40% of our total surplus. It's the issue of the spend versus earnings. We're trying to do a good job with our reinsurance spend with our expectations. The PLA/CLA PML in 2016 is anticipated to be $2.1 billion. As you can see here, this is showing that out of that $2.1 billion that you have $800 million covered by FHCF. We're in a strong position in the PLA/CLA.

Gary Aubuchon: I'd like to go back to slide two, which is your budget to actual DWP. For the last three years, from what we forecasted for premium versus what we've gotten, we've missed. We've gotten less premium than we actually forecasted. There is some additional analytics in this budget, and obviously we need to because the amount of net income that we're looking at is tightening up. There is not much room for variance between what we've forecasted and what we hope to write. Help me get an additional boost of confidence in this year's predictions versus the prior year's predictions that we'll be much closer. It affects the PML and we're talking about reinsurance coming up. It has a significant impact on fixed expenses.

Barry Gilway: When I say "improved analytics," we have better improved from three years ago when the analytics were just trends. You'll see a linear trend, but we don't do that anymore. Starting a year and half ago, due to March Fisher and her analytics organization, we know from every single depopulation company the makeup of that depopulation is, what their appetite is, the kind of policies they're focusing on, so we can predict the level interest is going forward given the change in the overall makeup of our book of business. We know geographically where we are losing business at a fast or slow pace. It really is a combination of looking at every single risk characteristics and appetites and interest in our book of business; and therefore, we have a better understanding of how low we can go over time. Your observations are good. We thought we were being aggressive every single year, but we exceeded our expectations. I think we have a more refined look than we ever had. There are some anomalies that we cannot answer. When you have a rate deficiency in Coastal of 50% and you lose 90,000 policies in one year, that's an anomaly. That really has to do with the distribution of risks for these private carriers and the ability of these carriers to do business in specific areas without significantly increasing their PML and reinsurance costs. If you can add business in one territory and it doesn't increase their PML for one event, then the reinsurance costs are not significant. We even try to include that in our analysis. I can't give you a guarantee with where we we'll be. I think the numbers we're showing now for the 417,000 policies – that's an aggressive projection.

Jim Henderson: To Gary's point is that, Barry, I don't envy your job where you competition is paid to come in and open your door to take all of your best business away. "Good luck with the toughest class of business." That's our task within the state. Maybe to Gary's element, if we are in that direction of ending up with the toughest class of business and exposure, what is our rate structure there that would support our expenses and losses? Can we get those rates in place sufficient to carry our PML to operate? We are a backup to the state. We need to make sure the organization is there to catch others that fall through the cracks. The takeout companies are very reinsurance dependent. If that market changes, I suspect that we've got another task at hand. That is probably to catch business that cannot stay in those companies due to reinsurance affordability. It's a tough task. What rates we need to make sure we can cover the PML if we can get those approved.

Barry Gilway: You raise a significant issue and that is the overall book of business is clearly headed in the direction of being less rate adequate. The slide that I showed shows that while we're losing additional business in the PLA/CLA, the reality is that we are not losing Coastal business as quickly. Coastal and wind business are less rate adequate. The issue that we'll have to address is the glide path. It's done a good job in getting us where we are but it still exists with the Coastal, which is becoming the core of the business. What are the short-term issues? John will be spending a lot of time on the water damage issues, etc. What we can do is that those areas that are under our control is to focus on the loss side and claims side of the equation and really attempt to improve the overall loss picture of the business that we're retaining. Today, Miami-Dade County is out of control. When you're starting to get 800,000 new litigated policies per month, then that will exacerbate the issue that you have raised. It will reflect that the rate inadequacy in the Tri-County book of business. We're now seeing that expansion of the Tri-County into the rest of the state. We have a statutory obligation with the glide path to increase to a maximum that isn't sufficient over time. It will deteriorate with the results. What will exacerbate the results will be the litigation in the Tri-County area. Right now, we're looking at a premium for a Miami-Dade resident who is currently paying exorbitant rates - $2,800 is the average HO3 policy in Miami-Dade. It doesn't take rocket science to show that Miami-Dade residents will be paying $4,000 for an HO3 policy. It's a staggering amount of money. That is why we're focused on the language changes in the policies. The only other lever we have is rate. We're constrained from a statutory glide path and we may have to lobby for changes in the glide path percentages over time.

John Wortman: The number of assumed policies that come back to Citizens on renewal, do we know that number?

Barry Gilway: We did a study about two years ago, and frankly, it was surprisingly low. The number was around 20% to 22% that leave Citizens comes back. We're seeing a tick up. Before the latest changes in November, the depopulation companies did not have to put premiums on the assumption letter. As a result of that, you had policyholders agree with the assumptions and three months later they get a 50% rate increase. New business indicates that about 28% of policies coming back in are due to cancellations.

John Wortman: Should we consider on those policies, should we consider billing the assumed carrier for the ceded unearned premium?

Barry Gilway: It's an interesting concept. I hadn't considered that. We'll take it under advisement.

Jennifer Montero: If they do cancel in the assumption stage, we will refund the policyholder and we would get the money back at the renewal.

Barry Gilway: Your recommendation is following the assumption period if it comes back.

Jim Holton: I think you're serving a policy during the coverage period.

Barry Gilway: We are servicing the policy from the assumption date . . . .

Jim Holton: . . .on the placement date but if you reassume and require the entity to cover the service of the policy until you reassume the coverage . . . .

Barry Gilway: The way it would work is that the policy would be cancelled and then you'd start again with the earned premium on the policy.

Chairman Gardner: Excellent presentation. One of the missing components is historical surplus and where we've been over the last 15 years with surplus. I don't know of any business that contracts rapidly that adds surplus. It's just not possible. I do want to emphasize that this Board will have to consider these items going forward. Barry is a pretty talented guy but his crystal ball is pretty cloudy. I think it would be for anyone. As an "old timer" on the Board along with John Wortman and Don Glisson, we were doing high-fives for a 17.5 rate online back in 2013. It's amazing how the dynamic can change from you're winning to you're losing to you're winning. I don't want to lose sight of the progress that has been made and how fluid this environment is. It's always a 600,000 policy count with a very static 400,000 Coastal policy count. That was everyone's belief for years. The big win would have been 600,000 policies. Every six or seven months Barry would call me with a new mile marker. I do want to reassure the Board that right around the reinsurance purchase time there was a lot of spirited discussion about this buy. This is something that staff and Kapil Bhatia were very focused on. If the business contracted at a rate more rapidly than we had forecasted, then this could put us in this position. I do want to assure this Board that the deliberations and discussions about the risk transfer with this approach going forward is going to be tough. Is it our mandate to make a profit? I think it is good business and good stewardship to make a profit. When you start peeling away the onion to look at our mandate, it really is to be the insurer of last resort. To dismantle our long-term thinking and the investment we made . . . . what is lost in this conversation is how swollen our claims organization is with water claims. We think about this happening simultaneously: our business has shrunk, therefore, our staff shrinks. It's just not how it works. I think we go towards April and May, I think we need to have clarity and purpose. I do think that we have unprecedented surplus and we need to think about protecting it. Multi-year reinsurance deals don't look good right now. But, if you told us that we could pay that three years ago, we probably would have done a 10-year deal. So, we're just experiencing a lot of fluid conditions right now. Barry, hats off to you, Jennifer, and John. You've done a good job.

Barry Gilway: We're looking for Board approval on the 2016 Budget.

A motion was made and seconded to approve the 2016 Budget. Chairman Chris Gardner, Vice Chair Don Glisson, Gary Aubuchon, Bette Brown, Juan Cocuy, Jim Henderson, Jim Holton, Freddie Schinz, and John Wortman approved the motion. All were in favor. Motion carried.

Barry Gilway: Mr. Chairman, we sincerely appreciate the support of this Board. It's a very difficult budget. I appreciate the time you've spent with us on this. Thank you.

4. Chief Financial Officer Report

a. Finance and Investment Committee (FIC) Report

i. *Action Item: Sinking Fund Investment Program - Series 2009-2012*

Jennifer Montero: At the June 2015 Board of Governors meeting, we received conceptual approval by the Board to evaluate a forward deposit agreement, however the ratings requirement for providers in the Indenture restrict entry into a forward delivery agreement (there are no remaining "AA" rated counterparties in the market). So we have the outstanding Series 2009A, 2010A, 2011A, and 2012A Bonds, which require monthly sinking fund deposits for principal and interest that need to be made with the indenture trustee, Regions Bank. Currently these funds are invested in Money Market Funds. The Indenture allows for the funds to be invested in U.S. Treasury or Agency securities rated AA or higher for the Debt Service Fund Account; therefore purchasing individual securities enables Citizens to earn a higher fixed rate by moving out on the yield curve and capturing a higher fixed rate of return for the monthly deposits. Each month, Raymond James and Citizens will evaluate the economic feasibility of investing the deposited funds through a competitive bid process for U.S. Treasury or Agency securities. Upon settlement, the winning provider will deliver the securities directly to the indenture trustee. The up-front programmatic expenses will be similar to the proposed FDA expenses, not to exceed $100,000 in the aggregate. Legal expenses will be incurred to conduct the initial review of the term sheet utilized in the bid procurement of the securities. Indenture Trustee expenses will be incurred to review the process. Raymond James' fees will be paid directly by the winning provider(s) of the competitive bids, not to exceed $35,000 per bid. Due to the tax law regarding the securities, an amendment to the supplemental indenture is necessary. The amendment will clarify the tax exempt bond proceeds are required to be invested in tax exempt instruments, with the exception of investing in the debt service account. The debt service account may be invested in the US Treasury or Agency securities and constitute a debt service bond. Bond Counsel has composed a working draft amendment, and we have received consent from the Bond Insurer and the Indenture Trustee. The final documents will include a Board resolution and will require a Board approval. **Today, we're asking to move forward in finalizing the documents required for the Sinking Fund Program and to bring it back to the Board for approval during the next scheduled meeting or during a special conference call sooner.**

John Wortman made the motion to approve the Sinking Fund Program as described above. The motion was seconded. All were in favor. Motion carried.

ii. September 30, 2015 Financial Statements

Jennifer Montero: My next item is the September 30, 2015 Financial Statements. I don't know how relevant they are considering we just talked about the projected year-end and budget forecast for 2016. December 1st marked our 10th consecutive year without any hurricanes. It's allowed us to accumulate our surplus, execute our risk transfer strategies, and have unprecedented levels of depopulation, all of which have eliminated our risk of an assessment in a 1-in-100 year storm. If you turn behind Tab 4, you have the September 30, 2015 financial statement and analysis. I'm going to give a broad overview of what's been going on. Our DWP decreased by approximately $652 million, or 30% compared to the previous year. Likewise, net earned premium decreased by $515 million, or 45%. The decreases are largely due to the successes of depopulation as reflected by the year over year end increase in the ceded premium. PIF of 574,000 reflect a decrease of more than 356,000, or 38% compared to a year ago. PIF decreased by more than 24,000 just for the third quarter 2015. Although net losses and LAE decreased by $89 million compared to the same period, the loss ratio increased from 27% to 45%. That's largely due to the water claims in the Tri-County area. We are receiving more than an average of 800 litigated water claims per month, with an average cycle time of 740 days from close to the first notice of loss (FNOL). Although the underwriting expenses including administrative expense more than 26%, the expense ratio has increased to 22%. That's up 4% from 18% over the year. As you recall the unearned premiums are payable to the takeout company within 20 days of the day of assumption. Citizens continues to service the policies until renewal. Citizens was servicing more than 119,000 assumed policies as of September 2015, and that's more than 20% of the PIF. Primarily as a result of the number of policies serviced driven principally by the volume of depopulation, our expense ratio has increased. Simply stated, the denominator, which is written premium, is decreasing at a faster rate than the numerator, which is the underwriting expenses. While consolidated net income at September 2015 was $55.9 million, the net loss of the Coastal Account was $14 million. Several factors contribute to the loss, including depopulation, reinsurance, and LAE loss ratio increase. We anticipate based on the forecast of depopulation that the Coastal Account will end with a loss of approximately $60 million. Finally, cash and invested assets remain constant year over year at approximately $14 billion and policyholder surplus remain constant at $7.4 billion, reflecting significant claims paying capabilities at the end of 2016.

5. **<u>Office of Internal Audit Report</u>**

   a. Audit Committee Update

Juan Cocuy: Yesterday, we had our Audit Committee meeting. We'll focus on the report of the Office of Internal Audit (OIA). We covered the OIA report and its 2016 Audit Plan and Strategy. We heard a similar report by Jennifer of the September 30, 2015 financial results. We also got a report from the external auditors and their plan. Matt Church, the managing partner, and Brian Smith, manager, provided a report and gave us a timeframe. They've already completed their interim field work, starting October 26 and finishing November 9th. Final field work will be completed for the period beginning March 28th and we're hoping to have our reports in the April 25th to May 7th date.

Joe Martins: For the record, I'm Joe Martins, Chief of Internal Audit. I like to refer to Tab 8 in the back of the book. At the committee meeting, I presented changes to the 2015 Audit Schedule as well as results from the audits completed. The chart on the first page represents the Audit Plan, which included 31 audit projects in which 80% have been completed with six audits remaining. The Citizens General Control Framework Project is moving steadily on plan, with the completion of 14 process and control reviews to date. This represents 25% of the 56 process reviews plan during the three-year implementation period. Each review involves understanding documentation and testing the identified key controls in line with 2013 and the industry 2012 frameworks. To date 42 key controls have been reviewed and formally documented. Included in your materials is a copy of the 2016 audit strategy and plan. The plan was approved by the Audit Committee and presents 26 audits and a number of engagements. Also included in the package, we presented and discussed with the committee the Audit budget, and the committee approved the budget which was presented as an element of the budget in the Citizens overall budget discussion. With the 2016 Audit Budget presentation, it has confirmed a reduced headcount of two full-time employees. On page three I provide the summary of progress for the resolution of control deficiency. Three issues are currently overdue, all of which deal with the IT security control within the organization. The Systems and Technology unit is currently refreshing Citizens IT Security Strategy and have a number of projects underway that focus on further improving Citizens security protocols. These projects are being monitored by OIA.

a. *Action Item: Audit and Control Management System*

Joe Martins: The OIA along with the Finance section will enter into contracts with a vendor Wolters Kluwer Financial Services to provide the OIA as well as Control Support Team with the software as a service administrative support tool. The proposed contract will have a five-year based term, with an optional two-year renewal terms. The OIA already uses Teammate application as an administrative tool and this contract will essentially confirm continuation of the service in a web-based environment. In addition the OIA will be adding Teammate analytics software to support its continuous audit and data analytics strategy. The audit management application system will be used to streamline support, including audit planning, fieldwork testing, report generation, and issue management. The estimated cost of the contract including renewals is not to exceed $332,000. This contract will provide the Teammate controls and management application to support internal management of internal control functions. The control management application will be used to identify, capture, analyze, manage and report evaluations and objective risk controls throughout the organization in line with the 2013 frameworks. The estimated cost of the contract, including renewals is not to exceed $143,000 over the total contracted period.

Juan Cocuy: This is a budgeted item. It's on action item letter "I."

Juan Cocuy made the motion was made to approve the recommended award and the resulting contract, including renewal periods for ITN No. 15-0017. Bette Brown seconded the motion. All were in favor. Motion carried.

Juan Cocuy: Just to note on the audit strategy in 2016, page three of that, there is an executive statement that has the mission: to provide an independent, objective assurance and consulting activity designed to add value and improve Citizens' operations. For myself and for the Audit Committee, I feel very strongly that Joe and his staff have accomplished that and will continue to accomplish that. In addition to what we talked about, we had an Ethics and Compliance Report. Debbie Kearney, who normally gives that report was not present. Dan stepped in for that. She also mentioned that she's retiring. Congratulations to her. We also got John Rollins, Chief Risk Officer, to give us an Enterprise and Risk Management (ERM) update, which was very informative.

6. Chief Systems Operations Report

Jim Holton: I want to congratulate Kelly and her team for doing an exceptional job, especially in the cyber security area. We got a Request for Proposal (RFP) and went through the process. We have some very substantive recommendations. We reached out to all the stakeholders in Citizens and agency communities. I want to congratulate them for the timeliness, promptness, and great way they handled the matter. It's a testament to your abilities, Kelly.

Kelly Booten: It was a great team effort. Thank you.

a. Information Systems and Advisory Committee (ISAC) Report

Kelly Booten: Good morning, Board. Chief Systems and Operations. The ISAC met last week and we talked about several things. The first topic was about the Third Party Security Risk Assessment in which the project has been completed and the report has been delivered along with recommendations to make change to the agent and agency appointment agreements. The reports describe the results of the independent review done by Buchanan, Ingersoll and Rooney, PC, the privacy and cyber security risk to Citizens relating to the interface and relationship to our agents and agencies. Details of the review and recommendations were presented by the ISAC. Recommendations to the agency and agent appointment agreements have been incorporated into a new proposed agreement which are under review. Changes have been distributed to the agency associations and will be distributed to the agent roundtable. The first walkthrough with the associations was conducted last week and feedback is being collected. It is anticipated that the final recommendations will be presented to the Market Accountability Advisory Committee (MAAC) and the Board in March. Other recommendations included in the report are changes to training materials that are underway. We're also incorporating some of our recommendations into the Vendor Management Program. Sarah Harrell, Enterprise Program Director, briefed the committee on the status of the ERP Solution Program. Five vendors were selected for onsite demonstrations. Four of the five demonstrations have been completed with the last vendor scheduled for next week. The business case is being developed and we'll go into negotiations later this month and into January. The business case and recommendation will be presented to the ISAC in March. Curt Overpeck, Chief Information Officer, briefed the ISAC on the ISAC Technical Advisor search. We had a final candidate that subsequently withdrew. We went to Plan B and have a couple candidates we are interviewing and hope to have an approval at the next meeting. Curt also briefed the committee on the IT Security Strategic Plan, which we intend to present to the ISAC in March. In addition, we have two approved consent agenda items that are presented each year at this time: IT Staff Augmentation and IT Infrastructure, Software and Professional Services and don't need separate approval.

Jim Holton: I want to talk about moving forward with the agency agreements. We had a lengthy discussion on Citizens requiring agencies mandate their personnel execute MDAs, which has confidential information for Citizens clients. I think that's a very important thing to do to emphasize to the agencies. I think this Board should look into that to require this with our different agents.

Kelly Booten: The recommendations do include confidentiality agreements for when there is access to confidential information. That is our current recommendation.

Jim Henderson: This is currently not in our agreement?

Chairman Gardner: I don't know the answer to that.

Kelly Booten: I would have to ask Dan or Steve to step up; I'm not as familiar with the confidentiality agreement. I believe it does but it just further amplifies the statement in the agreement with these revisions.

Jim Holton: I don't think it requires the actual personnel of the agency to have them execute MDAs in the act of confidentiality.

Steve Bitar: That is correct. You have a confidentiality requirement but there is not a requirement for a written agreement between the agency principle, the agent, and their staff. We'll be looking to tightening that in the next version.

7. **Chief Claims Officer Report**

Gary Aubuchon: Unlike some of the other aspects we were dealing with at Citizens, even though our policy count is down, Claims is busier than ever. After Jay's report, you'll see why.

Jay Adams: I want to give a brief update on the Independent Adjuster (IA) contracts. Before I do that, I'd like to thank Gary Aubuchon as being the Board oversite representative to the process. As you recall, we did the solicitation back in December 2014. The main focus of our solicitation was to be structured around the IA firms identifying their own level of committed IA resources. They would represent their commitment to Citizens. It was our goal to obtain 5,000 resources so that we would be prepared for any level of CAT event. During the solicitation process during the question phase, we received a single complaint that we ended up resolving. At the end of the awards, we received an additional five complaints. This is what caused so much of the delay. This Board provided final approval of that contract back in June 2015. What I'd like to announce today is that as of November 30, 2015, four vendors met their obligations, meeting their committed resources numbers in providing in excess of 2,000 resources. Those firms were CIS Group, NCA Group, Bright Claims Incorporated, and Bradley Stenson and Associates. Through November 6, 2015, 14 of the awarded adjusting firms withdrew their contracts for consideration. We're still working with the nine remaining IA firms to help them provide additional time to meet more credentialing. We'll continue to research our resource needs versus the resource commitment level as we move into 2016. Since this report, we've had two other vendors come online, which has increased that number to closer to 3,000 resources. We're getting into the ballpark based on our PIF and CAT projections. Even though we estimated 5,000, under the current PIF, I think we're okay with around this amount.

a. Action Item: *Claims Flooring Valuation Services*

Jay Adams: This is a continuation of services. The contract is beginning to expire. This allows Citizens to appropriately price different types of carpet and flooring materials through an expert vendor services. We then put that information into our estimating system to provide the insured with a total package price for what those items are. The action item is to award a contract to ITEL Laboratories. This is a budgeted item. This is paid as an LAE, so it does not affect our administrative budget. The estimated spend on this contract is $710,000 for the life of the contract, including the renewal terms. This action item will seek Board approval for multi-year contract Flooring Valuation Services RFP 15-0025. Citizens solicited an RFP seeking qualified responses. There was only a single respondent who was an incumbent which was ITEL Laboratories. The contract term was anticipated to have a five-year base term and one two-year optional renewal term. On August 12, 2015, Citizens issued an RFP as stated above. **Staff recommends that Citizens' Claims Committee approve and recommend the Board to: approve the recommended award and resulting contact, including renewal periods for RFP 15-0025 [Contract #15-15-0025-00] to ITEL Laboratories Inc.; to authorize staff to take any appropriate or necessary actions consistent with this Action Item; and to approve this Action Item not to exceed $710,000.**

A motion was made and seconded to approve the Claims Flooring Valuation Services action item as stated above. All were in favor. Motion carried.

b. Action Item: *Appraisal Services*

Jay Adams: Citizens contracts with a number of independent appraisal firms that provide Citizens field appraisal services for those claims where Citizens has entered into an appraisal with a policyholder in order to attempt to resolve their claim. This also is a budgeted item and this is funded under the LAE item in the claim itself. The estimated cost of this contract, including renewals, is not to exceed $36.75 million. This Action Item seeks Board approval of Appraisal Services multi-year contract. Citizens issued a competitive solicitation seeking responses from qualified vendors. Citizens' staff evaluated the responses and recommends that the Board approve awarding contracts to the seven (7) vendors (see Attachment "A"): Team One Adjusting, LLC; Claims Question, LLC; Lozano Insurance Adjusters. In the event Citizens' resource need were to exceed the commitments from the above awarded vendors, Citizens would reserve the right to pursue contracts with the remaining responsive vendors who are Connected Point Resolution Systems; CMD Affiliates; CIS Group; and Pika and Associates. The proposed contract term will have a four (4) year base term and three (3) optional one-year renewal terms. On September 8, 2015, Citizens issued an Appraisal Services Request For Proposal (RFP) No.: 15-0022. Fourteen (14) responses met Citizens' mandatory requirements and were evaluated by an Evaluation Committee.

Vice Chair Glisson: I want to make sure I'm understanding the math. It says, "$36.75 million." It says that it anticipates 3,100 assignments. That comes to $11,800 per . . . . am I reading the math right? That seems a little high for an appraisal service.

Jay Adams: I would have to go back and verify that. Based on . . . .

Juan Cocuy: Or is that $3,100 annually time show many years?

Vice Chair Glisson: Maybe that's annual. Even that seems a little high.

Jay Adams: The actual contract-spend is correct. I believe the $3,100 assignment is the incorrect number. We are also changing our appraisal language soon, and I think that's going to create some additional uptick of the appraisal process. That is included in the $36.75 million. I will clarify that and get a response to you, Governor Glisson.

Chairman Gardner: To that end, is that something the Board is prepared to act on? Can we postpone this for an hour? Maybe Jay can make a couple phone calls.

Dan Sumner: You can certainly table any consideration. It can be recalled as an action item later in the meeting. There would be no problem procedurally doing that.

Chairman Gardner: Jay, are you okay with that?

Jay Adams: I'm absolutely fine with that.

c. Action Item: *Claims Legal Services*

Jay Adams: The next item that we have is the Claims Legal Services. This is a service that Legal and Claims partner with. Dan's group, ultimately, is responsible for these contracts. However, we stood up a Claims Vendor Program specific to litigation. The Claims group manages the day-to-day activities and Dan's group manages the overall contracts.

Dan Sumner: Good morning, Mr. Chairman and Board members. As you may recall, even though Legal Services is an exempt category under the State Purchasing Law Chapter 287, for a number of years as a best practice, Citizens has competitively procured legal services, including Claims Legal Services to provide legal defense to claims litigation. Those current contracts expire in February 2016. We issued RFP No. 15-0023 to put a new roster together for the specific categories that we use in claims litigation: first liability, second liability, subrogation, collections, and appeals. We solicited firms for all of those categories and received very good response for all of those. Again, the contracts do not guarantee work, but we prequalify a panel of lawyers, so that when legal services are needed, through the competitive process, these firms are ready to be assigned cases as needed. As Jay mentioned, I think one of the most important features of this contract period is that as part of the Claims Vendor Management process we are going to incorporate legal services and these law firms as part of a specific vendor management process with a more robust oversight process through that unit of claims. I believe that will be reflected in much better overnight, particularly with regard to the empirical measurements for performance. The specific firms are identified in Exhibit A of this action item and I will identify the specific request: **Staff recommends that Citizens' Board approve the recommended award and resulting contact(s), including renewal periods, for RFP No. 15-0023 for Claims Legal Services to the list of attached vendors (Attachment "A"); and authorize staff to take any appropriate or necessary actions consistent with this Action Item.**

A motion was made and seconded to approve the Claims Legal Services action item as stated above.

Bette Brown: I'd like to ask a question. What do we do to prequalify these law firms? What's the process?

Dan Sumner: First of all in prequalifying, the actual solicitation process will look at primarily firm's strengths – including financial – and it would also put a great deal of emphasis . . . even with a good firm, what resources within the firm are they providing to the principle attorney and what specific lawyers in the firm are being committed to do Citizens' work. It's not just the firm but the people in the firm who are committed to do the work. Those things are all identified in the solicitation. In contracting process, there are those specifics to adherence to billing guidelines. That's where the new vendor management process, the attorney scorecard, and legal dashboard will come in at that point.

Bette Brown: Thank you.

Vice Chair Don Glisson: I know we need to get our hands around the water issue, and hopefully, we'll get some legislative relief. $65 million for outside lawyers divided by 450,000 policies is $145. Are our policyholders paying $145 in their premium to pay for outside attorneys? I know you can't roll over and let these guys do what they're doing, but to me, this is a reason why we need to push that assignment of benefits. The cost is killing our policyholders – the ones who don't litigate, which is the vast majority.

Dan Sumner: In response to that question, I'm going to preview something that Governor Schinz asked me to talk about in more detail later. Governor Schinz asked me to take a look at the Right to Cure for construction defects, Chapter 558, and to see if there are any lessons to be learned from that particular legislation, which deals with a specific way to give construction firms the right to cure when construction defects occur as opposed to being subject to legal action. One of the things that the legislation said right off the bat is that the ability to have notice and the ability to cure defects and not let those go into litigation is a desirable alternative dispute resolution process. When we look at things like manager repair and the like where we have the ability to fix those things, I think the point is that we should look at those as a desirable dispute resolution process, which avoids these kinds of costs. I'll talk more about that later but I think it's a relevant point which overlay all the discussion later.

Juan Cocuy: Do we make sure that none of the firms that we had billing issues with before got on this list?

Dan Sumner: Yes, we did take that into consideration.

All were in favor. Motion carried.

d. Right to Repair

Jay Adams: I'd like to start by saying you'll hear more information from John Rollins. We had an Actuarial and Underwriting Committee (A&U) meeting yesterday, in which we tag-teamed on this issue. We at Claims have partnered closely with Product in trying to create a multi-pronged approach to address some of these water issues. John will provide more detail about the results. I'm going to talk more about the Right to Repair and what we in Claims can do today under our current contracts. A Board member raised an issue at the September Board meeting regarding Citizens policies under R-option. We commonly refer to that as "Right to Repair." I'd like to point out what the Right to Repair language specifies: *At the time of loss, we mail you a written notice within 30 days after we received your signed, sworn proof of loss and we have the right to invoke our option.* The key is that this policy provision begins with Citizens receiving the signed, sworn proof of loss. Under the conditions, the policyholder's responsibility is to submit a proof within 60 days after the request had been made by Citizens. The policy then proceeds to state, *We may, at our option, repair any part or the item of the damaged property of like kind and quality.* The fact is that our policy does give us the Right to Repair. However, the policy language regarding sworn proof of loss interjects at least 60 days within the process before the Right to Repair can be exercised. This is not practical for the water losses, given the need for immediate attention. Moreover, the practicality of exercising the Right to Repair provision is that with 24% of the non-weather loss claims having representation when they're submitted at their FNOL, the policy timeframe for repairing is much too late. We believe that current Right to Repair policy language is clearly not an ideal fit for addressing non-weather water loss claims. Policy language that is more custom-tailored to Right to Repair water losses is the most desirable long term solution. In the meantime, we believe an important transitional step would be to implement a contract Managed Repair Program. Citizens is currently in the final stages of a solicitation where we intend to procure an administrator for a contracted managed repair. The program will provide a statewide coverage to credentialed vendors that will be able to respond to emergency services such as water mitigation, tarping of roofs and openings, tree removal, in addition to covering the agreed upon coverage on damages to return the damage to its pre-loss condition. This program will provide the insured with the warranty and the administrator will be responsible for any warranty work that comes out of that. Citizens intends to launch the program during the first quarter of 2016 as a voluntary program that will be offered on eligible claims during the FNOL and can be offered by the adjuster when the insured requests recommendations for contractors to complete those repairs. We would like to have this program remain voluntary throughout 2016 to work out any issues with workflows or with the administrator to make sure that we have a solid program to provide the highest level of customer service. We do believe that the voluntary managed repair program will be attractive to many policyholders based on feedback we've received from our Sinkhole Managed Repair program. However, we face the likelihood of third parties discouraging participation as long as the program is voluntary. With that said, Citizens would like to explore opportunities to make this program mandatory, starting in 2017.

Dan Sumner: Mr. Chairman, I'd like to briefly follow up on the request that Governor Schinz made at the last Board meeting that I talk about the construction defect Right to Repair. Without going into the details of that law . . . I think there a couple of lessons learned. I'm going to foreshadow some things with regard to Citizens' initiative, which really has three components: communication, product changes, and the introduction of the ability to manage the repair by Citizens. Normally, if you look at this statute, what it talks about with the benefits of an alternative repair solution, they say an effective right to repair has three components: timely notice of the defect, a reasonable right to inspection, and an opportunity to cure the defect without resort to further legal process. I'm foreshadowing some things John Rollins will say. One of the product changes that we are looking at is requirements for timely notice. Again, it's very important, as this law points out, that an effective program has to have a timely notice. If you don't have a timely notice, then your ability to effectively repair is compromised. The right to inspect and the right to go in a repair – those are the things Jay talked about. All of these things are about avoiding suit. These are pre-suit procedures. I think the ability and the potential benefit with regard to Citizens claims is even more promising because these are really not a pre-suit process. This is really a claims adjusting process. The right to elect to cure – the merger of the things that we're doing – is even more promising than the right to cure. There is one other thing I would note and which is a very large issue is emergency issues. Even in Chapter 558, even though it has a very well-developed structured, even the right to cure does not limit the ability for the property owner to make emergency repairs. Emergency repairs are really a challenge in themselves. They don't even try to tackle it. One of the things I will foreshadow is that in looking in our product development we are looking into emergency services and making sure our product – as tightly and as effectively as possible – deals with the distinction between emergency repair and further repairs which need to be managed. I think the lesson here is that this isn't complicated in concept. It's reasonable notice, reasonable inspection, and right to repair as an alternative to legal proceedings. I think that's the takeaway from this. I appreciate Governor Schinz for pointing us in this direction for some very valuable items.

Jim Henderson: In managed repair and Right to Cure, the whole category here – what abilities does Underwriting have now to financially incentivize our policyholders to enter into a voluntary program? For example, to kick off this program that is comparable to what we did for sinkholes, it seems that we can approach our policyholders in the Tri-County area and give them a premium reduction or credit if they do this now to get people's feet wet.

Dan Sumner: I think John will give you a much better answer. Once you have a right to repair process, then there are empirical and actuarial analyses that you can cost that out and we would use those actuarial numbers to provide incentives and justifications for a managed repair program.

Freddie Schinz: I want to thank you so much for looking into the right to repair and staying on top of it.

e. LAE

Jay Adams: I'd like to call up Andrew Woodward. He is the Senior Director and Head Controller. He will lead our discussion on LAE.

Andrew Woodward: Good morning, Mr. Chairman and members of the Board. At the last Board meeting, you asked that staff come back with a brief discussion on some of the definitions of LAE that we commonly throw around in the meetings. I believe there are eight or nine slides. In the interest of time, we'll keep it brief and center the conversation on only two slides of the presentation. If you go to slide one, there are really only two categories of how we define LAE. The first one is what we use for internal analysis and trending, and the second one is what we use for financial reporting. In terms of financial reporting, we're obligated like any other licensed carrier to file an annual statement and quarterly statements, which require us to split LAE into two categories: Defense and Cost Containment (D&CC) and Adjusting and Other (A&O). But for the most part when we refer to LAE, we use the old definitions: Allocated Loss Adjustment Expenses (ALAE) and Unallocated Loss Adjustment Expenses (ULAE). Slide two shows more detail. We present here the different types of LAE that fall within one of those two categories. Perhaps the best way to remember ALAE – these are expenses paid through the claims system and they are specifically assignable to claims. Some of those expenses include damage remediation services, defense attorney fees, and mediation costs. Conversely, looking to the right side, we have ULAE. Those are expenses typically paid through Accounts Payable and are not assignable to a specific claim itself. Examples include daily rate adjusters and the allocation of administration expenses. Not to stray too far from our financial reporting obligations, we also color coded these different expenses into D&CC and A&O. On the last slide in the appendix is a slide that contains specific definitions of these broad categories. You may wish to look through that at a later date. We also have trending and timeline of different trends of our LAE over the past several years. If there are questions on that, I would ask that we address that offline or after the Board meeting. Some of the discussions on that can become pretty complex.

Chairman Gardner: I think we're going to take a break to wish Governor Cocuy, "Happy Holidays," because we won't see him afterwards. We'll get a quick picture. We're going to follow Barbara. Let's resume no later than 10:55. We still have a pretty thick agenda to get through. Thank you.

Barbara Walker took roll: Chairman Chris Gardner, Vice Chair Don Glisson, Gary Aubuchon, Bette Brown, Jim Henderson, Jim Holton, Freddie Schinz, and John Wortman were present. Juan Cocuy is absent.

Chairman Gardner: We're going to continue with Jay Adams who has some clarity on the Appraisal Services Action Item.

Jay Adams: Thank you, members, for the additional time. The action item has a mis-word [sic]. The contract amount should state, "This estimate is based on projection of 3,100 annual assignments." We roughly get 2,500 task or appraisal assignments. 326 come out of our litigation area and 250 come out of the late FNOL group. That gives a total annual, yearly projection of $5.2 million. That's how we rolled that up over the term to get to the $36.75 million spend.

Vice Chair Glisson: So about, $1,675 per assignment.

Jay Adams: They range based on the types of assignments. The lowest priced assignments are $900. The most expensive assignments are $1,500. They range between those two numbers. It's based on the amount of work based on the unit it comes from. For example, payment from a FNOL – they would have to do the complete investigation between no one has touched it, yet. That drives what those numbers are.

Chairman Gardner: Do you want to re-read the recommendation?

Jay Adams: **Staff recommends that Citizens' Claims Committee approve and recommend the Board of Governors to: a) Approve the recommended awards and resulting contracts, including renewal periods for Appraisal Services [Contract No. TBD] to the vendors identified**

in Attachment A of this Action Item b) Authorize staff to take any appropriate or necessary actions consistent with this Action Item; and c) Approve this Action Item not to exceed $36,750,000.

A motion was made and seconded. All were in favor. Motion carried.

8. **Vice President of Human Resources Report**

Chairman Gardner: I want to give a special warm welcome to Violet Bloom, who is our new Vice President of Human Resources. I understand that you have a couple action items for us. Welcome.

a. Action Item: *Contingent Staffing Services*

Violet Bloom: Thank you, Chairman and Board of Governors. For the record, I'm Violet Bloom. I have three items. The first action item is the Contingent Staffing Services item. The Board previously approved Contingent Staffing Services Contracts in March 2011. Citizens will continue to use contingent staffing services to support a scalable staffing model. Contingent Staffing Services is a budgeted item. The contract term is five years, with five optional one-year renewals. The contract is expected to go into effect in early January 2016. The Contingent Staffing Contract is intended to support regular business operations as well as the ability to scale the workforce to respond to CAT events. Note that the contract does not include contingent IA or IT staffing. Citizens released a competitive solicitation in June 2015 and carefully evaluated approximately 50 responses from interested vendors. The top 24 would be awarded the contract. Those firms are listed in Exhibit A. **Staff recommends that Citizens' Board approve the recommended 24 vendors for Contingent Staffing Services contracts as set forth in this Item and referenced in Exhibit A and authorize staff to take any appropriate or necessary action consistent with this Action Item.**

A motion was made and seconded to approve the Contingent Staffing Contract Action Item as mentioned above. All were in favor. Motion carried.

b. Action Item: *Retirement Plan Administrator Services*

Violet Bloom: The other two items are related to the retirement plan. The first item is an action item – Retirement Plan Administrator Services. Citizens currently contracts for services with Lincoln Financial Group. That contract expires June 1, 2016. Citizens chose to re-procure the services, rather than renew the current contract. This action item is a recommendation to award Mass Mutual Financial Group Retirement Plan Administrator Services Reliance Trust Company, the contract for Custodial Trustee Services. The fees are paid from planned assets and are not an operating expense of Citizens. Mass Mutual's fees represent a 50% savings for planned participants compared to the current contract pricing. The contract term is five years with one optional two-year renewal. The Retirement Plan Administrator will work with the Retirement Plan Committee and our third party Retirement Advisor, currently Fiduciary First, to administer the Citizens employee retirement plans. Those services include, but are not limited to, Custodial Trustee services; plan record-keeping; and participant communication. Citizens entered into the competitive solicitation process in September 2015 and evaluated response from eight interested vendors. The negotiation team recommended Mass Mutual Financial Group under ITN 15-0008. **Staff recommends that Citizens' Board approve the recommended Retirement Plan Administrator Contract to Mass Mutual Financial Group for administrator services and Reliant Trust Company for custodial trustee services as set forth in this Action Item and authorize staff to take any appropriate or necessary action consistent with this Action Item.**

A motion was made and seconded to approve the Retirement Plan Administrator Services Action Item as stated above. All were in favor. Motion carried.

c. Resolution of the Board of Governors Retirement Plan Committee

Violet Bloom: The final item is a resolution. In January 2008, the Board delegated authority to administer and oversee the employee retirement plan to the Citizens President and authorize the President to delegate authority to separate committees: the Administrative and the Investment Committees. Those committees have been meeting on a quarterly basis and the plans are in good operating condition. This resolution contains recommendations regarding the ongoing management of plans that are consistent with advice from Fiduciary First, Citizens third party retirement plan advisor, as well as outside council. The specific recommendations include streamline and simplify the administration of the Citizens Employment Retirement Plan by consolidating the two retirement plan committees into one committee. That retirement committee would be comprised of five standing members and two at-large members appointed by the President. The five standing members would include the CFO, VPHR, Controller, Management and Benefits at Payroll, and Manager of Treasury and Investments. The Retirement Committee would also be authorized to amend the retirement plan as long as those amendments do not materially alter the procedural or financial provisions of the Employee Retirement Plan. In addition, the Retirement Committee would comply with the applicable provisions of the Florida Sunshine Laws and employs any other interested parties would have an opportunity to attend the committee meetings.

Bette Brown made the motion to approve the Resolution of the Board of Governors Retirement Plan Committee. John Wortman seconded the motion. All were in favor. Motion carried.

9. Chief Consumer and Agent Services Report

a. MAAC Update

Steve Bitar: The first update is from the MAAC. Our Chairman is here to provide that report.

Dave Newell: Thank you, Steve. For the record, Dave Newell, Chair of the MAAC. We had an in-person meeting yesterday. Some of the key points were stats and policy count. We heard a lot about that today. One stat that rung the bell for most of us is the Agent Management Team had about 1,400 contacts with agents. That certainly is a feather in their cap to have some boots on the ground. We heard a report about the Clearinghouse, $2.9 billion in Coverage A was averted in 2015 by use of Clearinghouse. HO6 policies will go online this month. That leads up to 59% of policies will go through the Clearinghouse for both new and renewal . . . another avenue to divert policies into the private market. 2015 amounted to about 255,000 policies through depopulation. There are another 200,000 policies that are slated for the first couple of months in 2016. The next depopulation meeting working group is scheduled for some time in January. The last bit of business was about expanding the self-service payment option that will be made available to the PLA policyholders who can pay on the telephone through an automated system. More options for people to make payments are always good. Just one final comment – Governor Holton, you mentioned the contract and the agreements, specifically FAIA. We are reviewing that and we'll give you feedback.

b. Clearinghouse Update

Steve Bitar: I was just going to hit the highlights in the interest of time. Most of them were mentioned by Mr. Newell. One additional fact that's contained here is that we'll have three additional insurers that will be joining us in the first quarter 2016, taking us to 16 active participating carriers in the Clearinghouse platform. We're on pace to avert about $3 billion in Coverage A through the new business and renewal process in the Clearinghouse. Great work is happening there.

c. Legislative Affairs and Consumer Services Committee

Chairman Gardner: Governor Schinz, do you have any comments for Legislative Affairs or Consumer Services Committee?

Freddie Schinz: Not at this time, sir.

Steve Bitar: I'm more than happy to provide the updates on Christine Ashburn's and Governor Schinz's behalf. During the Consumer Services Committee (CSC), which met on December 3rd, we had an update from Christine regarding various communication efforts that are underway at Citizens. We are launching a Call Citizens First public education campaign to try to get ahead of any claims that are being filed with any representation, making sure both consumers and agents understand that they have the opportunity to call Citizens first. Starting in February, we'll be mailing ID cards that will go out with new business issuance and renewals that will not only contain the agent's information but also the 24/7 line that can be used by the consumer that can contact Citizens first so we can get the FNOL ahead of the claims process. We also had an update on the new fraud program that's called "Fraud: Identify It, Report It, Help Stop It." We have campaign as well that has internal and external facets. We're also exploring how we can partner with the National Insurance Crime Bureau, the Insurance Information Institute, and the Florida Insurance P&C Fraud Task Force. We had an update with regard to the phone payment service that we'll launch and there will be a soft launch later this month. We had an update on Depopulation and Clearinghouse activities.

10. <u>Chief Risk Officer's Report</u>

a. Actuarial and Underwriting Committee (A&U) Report

John Wortman: The Actuarial and Underwriting Committee met yesterday. We covered the three items we included in your book. The first item is relative to so some wording changes relative to water damage. The committee voted unanimously to recommend approval of all three items to the Board. The first item is the most complex, and it relates to clarifying and updating language relative to water damage. John has background material he shared with us yesterday that will help make this clear to the Board.

John Rollins: Thank you, Mr. Wortman. We had a successful meeting yesterday. Mr. Chairman, I know we have a thick agenda. I'm going to ask us to consider the two routine items which are action items. Then, I'd like to proceed with a little more discussion about the water loss changes we'd like to make to the product.

i. Action Items: Product Changes – FHCF Reporting Enhancements

John Rollins: This action item deals with the small change we need to make to enhance our reporting and accuracy to the Florida Hurricane CAT Fund (FHCF). In Commercial Residential properties, it is essential to differentiate between residential and non-residential occupancy in order to determine whether they receive coverage from the FHCF. It is also essential for us to collect information in Underwriting to determine whether those risks belong on our Commercial Residential program. We did receive almost $3 billion of coverage from the FHCF. Over time, statutory changes and some other underwriting changes made by Citizens has caused us to drift a little bit away from the official CAT Fund definition of Commercial Residential property. We need to file a new supplementary table in our application to enable us to collect all the data that the CAT Fund says they need in order to make a proper distinction between residential and non-residential risks which do or do not receive coverage. We need your authorization to make that filing. **Citizens' staff recommends that Citizens' Board approve the above proposal to implement enhanced data collection for commercial risks as it pertains to reporting requirements of FHCF, and authorize staff to take to take any appropriate or necessary action consistent with this Action Item to include filing with the Office of Insurance Regulation and system change implementations.**

John Wortman made the motion to approve the Product Changes – FHCF Reporting Enhancements Action Item as described above. The motion was seconded. All were in favor. Motion carried.

ii. Action Item: Actuarial Consulting Services

John Rollins: The second action item is the result of the solicitation for Actuarial Consulting Services. Citizens maintains a robust and very talented in-house staff of actuaries, which I have the privilege of leading. They almost do everything we need to do in-house. There are certain cases in which Citizens requires access to an external consulting firm, notably, our external audit firm on the accounting side requires and independent peer review from us of our loss reserves and our financial values contributed by the actuaries of the financial statements. That's in accordance with auditing standards. For the past five years we have kept an independent actuary on retainer with the Insurance Services Offices. That contract expires during the first quarter of 2015, so we conducted a competitive solicitation ITN #15-0024 for Actuarial Services on August 12, 2015. Seven firms responded to this ITN. Six qualified and the evaluation selected three teams to move through the negotiation phase. It has ultimately recommended that Insurance Services Office be reappointed as the provider of actuarial consulting services with a three year contract with an optional two-year renewal at Citizens' discretion and not to exceed spend over a five-year period of $550,000. **Citizens' staff recommends that Citizens' Board approve the awarding of the Actuarial Consulting Services contract to Insurance Services Office, and authorize staff to take any appropriate or necessary action consistent with this Action Item.**

John Wortman made the motion to approve the Actuarial Consulting Services Action Item as described above. Bette Brown seconded the motion. All were in favor. Motion carried.

iii. Action Item: Policy Language Changes – Water Losses

John Rollins: We need to address the policy language changes with regard to water losses. It's a growing problem and it's spreading around the state. At the Rate Hearing in August, Citizens has convincingly demonstrated that we have a growing problem with frequency and severity of water losses. It began as a problem primarily concentrated in South Florida. In those demonstrations, we showed that water losses were relatively low with stable trends elsewhere in the state and higher, and growing and accelerating trends in South Florida – Palm Beach, Broward, and Miami-Dade Counties. Since the rate hearing, we have looked at data coming from claims reports in 2015. Mr. Chairman, if you'd allow me to break a little news that literally has come hot off the press, we had our committee meeting yesterday. Also outstanding has been a mandatory data call issued by the OIR. This data call relates one to specific issue, which is Assignment of Benefits (AOB). We see AOB policy language that encourages dubious trigger and accelerated expansion of water claims as a root cause. AOB has been a situation that has been clearly indicated by the courts to be a problem for resolution by the legislature. It is not something Citizens can solve on its own. I need to be very clear about that. The water loss product changes that we will bring you here attempt to put our policy in its best decision to not be abused with regard to triggering coverage over things that were never intended to be covered in a homeowner's policy. We're taking this approach to best protect our customers and use a scalpel to address this problem without using blanket restrictions. However, the AOB problem is pervasive, it's growing, and it's also spreading statewide. In analyzing our response through the OIR data call, which was just called yesterday, we have already seen some key insights. While we've had a change to look at litigated claims and their incidences of AOB, we have never looked at a sample of our non-litigated claims and the frequency of use of AOB on those claims. Looking at a sample of 1,400 HO3 and DP3 claims that were reported in 2015, is that 43% of that sample had an assignment in place. That consisted of 46% of the sample in Tri-County but 36% in the rest of the state. What the AOB does is service a potential pipeline or a time bomb that can go off as a tsunami of future litigation if it is not addressed. AOB positions the contractor, often with the help of an attorney, to stand in the shoes of the insured without having to fulfill the duties required of the insured. So, we have a pipeline of claims standing behind a dam that could burst into a group of litigated files. When we drill down into that data, the average loss severity of non-litigated claims with an AOB ($16,000) vs. non-litigated claims without an AOB ($8,500) was about doubled. Bottom line is that this problem is liable to get worse before it gets better. It's a problem that requires Citizens to put language in place to address the problem, and it will require a legislative solution because we cannot fix the AOB issues on our own. We had some questioning during the President's Report and about the Right to Repair with regard to our budget and depopulation projections and rate adequacy. Rate adequacy takes two forms: one for wind and one for non-wind. Notwithstanding all the work we've done, all of these budgets and forecasts depend crucially on the assumption that we can have a stable loss ratio assumption for non-CAT claims. That assumption is clearly threatened by any continued spike in water loss claims and anything accelerated by AOB or points to future litigation. Finally – is the pocketbook impact. We've discussed this at the Rate Hearing but it bears repeating. This problem is hitting the pocketbook of every consumer in South Florida and it's about to hit the pocketbook of every consumer in the state. Because of the glide path, there are certain checks and balances there, whereby any policyholder cannot get more than a 10% increase in one year. However, as Barry said, you talk about 10%x10%x10% year after year and what you get is that we are behind the curve and we cannot catch up. You're looking at multi-peril increases applied to the rest of the state. Overall claims frequency has spiked from 4.9% (2014) to 9.3% (2015). If I sound like a guy who is hitting the panic button, it's because I am. This is raw data. We have to get the steps we need to take. We need to get our communications in line. We have to get our Claims and Legal strategies aligned. We have to get our Voluntary Managed Repair Program established. On my side, we have to get our product changes in place so that the policy is in position to allow all those other efforts to be a success. This is detailed in Attachment A. I'm not going to go through the changes that the A&U went through, but I would like to point out that they fall into four major categories. One is duties after loss, particularly with temporary repairs and emergency services. No one would argue that emergency services are within the purview of the policyholder immediately after the loss. What we've seen is excessive billing and excessive severity being associated and characterized as emergency services and being done without notifying Citizens. When you have a situation that allows for unlimited emergency services, we simply can't help the policyholder resolve the claim. We're proposing is introducing a special coverage amount in the amount of $2,500 to $5,000 for emergency services and temporary repairs. This is immediate emergency coverage that can be enhanced and extended by immediately calling Citizens. The $2,500 to $5,000 would be waived once prior approval has been received by Citizens. This is an incentive to have the insurer call Citizens first or call Citizens before excessive emergency repairs are in place. This is not applied toward a CAT. The second issue is timely reporting of losses. We want to introduce a requirement that losses must be reported within 72 hours of when the insured knew or should have known that the loss occurred. That language is intended to give us a broad safe harbor for the insured who are on vacation, ill, or otherwise, in a position they did not know a loss occurred. It does put us into position in which the insured is calling a plumber, attorney and a host of other third parties . . . it allows us to demonstrate that the insured should have known a loss occurred. We want to exclude coverage for any permanent repairs that are completed prior to allowing Citizens to inspect the damage. The other issue is dealing with expansions of scope, particularly in the area of matching. What is matching? It's defined in Florida Statute as making the policyholder whole – any replacement that is not covered by the policy shall be included in the loss to the extent of any applicable elements. In practice, the insured is entitled to be in a position they were in before with respect to tile, kitchen equipment, etc. The definition commonly used in the industry – line of sight, contiguousness, etc. – are definitions that have been subject to some abuse. What we're proposing to do is modify the policy to clearly state that the policy covers only direct physical damage and does not provide coverage for cosmetic or aesthetic differences. An example would be replacing all of tile in the house when one or two tiles have been damaged by a water leak. However, to ensure that the policyholder has comprehensive coverage for reasonable uniformity and appearance, we would introduce a specific coverage limit to be determined in consultation with the OIR with $5,000 to $10,000 for matching as additional coverage. You're limiting the scope of the main policy so that the abusive matching is common place. It's similar to the coverage we've used to cover for mold but it does not require a blanket supplement to the policy. The third category is expansions of scope and expansions of loss severity; therefore, replacing entire systems that are worn out. So, plumbing systems, for example, we have policy language that requires access to tear out and replace the system that caused the loss. An example would be the peril of collapse where coverage is asserted for a collapsed underground pipe. We do have exclusion to pipes in the policy but we have exceptions to the exclusion. Another one is water backup without any sign of damage at all. You can have a blockage that causes water backup. Our policy language recommendations are to limit coverage for tear out and replacement of only part of the portion of the system that caused the loss and not necessarily the entire system. We'd also exclude collapse of underground pipes due to deterioration of age and condition. There are a couple of other or more targeted contract changes that I won't go into detail. They deal with exclusions on mold and mold testing. Mold testing will be included only when offered by Citizens. A couple of limitation on the cost of water – if the water bill goes up due to a leak, then that would not be covered. In total, we feel these changes are absolutely necessary and we are in the process of explaining to our OIR that we feel these contract changes are necessary to address the root causes of the frequency and severity, particularly water related losses. Those losses are not trigged by AOB but often accelerated by the legal system to use more AOB.

John Wortman: I think staff worked well with all of the areas in the organization. I think the wording needs to be updated and clarified. This demonstrates the intent that's been there all along. I support John was presented. We did go through a series of slides that clearly demonstrated that a change over time and people are using old language to get unjust enrichment. This is intent to resolve that issue.

Vice Chair Don Glisson: While we're doing this, let's anticipate what's next. They'll try to find the hole so let's plug the hole before they drill it.

John Rollins: We know the legal system – with the one-way attorney's fee statute – so there is tremendous incentive for legal entrepreneurs to look critically at the insurance policy all the time and no matter what changes are made to find the next loophole to become the middle man. I don't want to promise the moon and stars here. We know that we've drilled down into the root causes and triggers the expansion of coverage to increase. We think these are the things will work to put the average policyholder in a fair position while discouraging the abuse.

John Wortman: There is one last thing that I think should be mentioned, too. When we did the 2016 Rate Filing, we did contemplate that this issue could be solved. We did not build into it an escalation. We bet that we would solve this problem in our rate filing.

John Rollins: We promised the OIR that hope would not be a strategy. We will do something about it. We can't bend that curve without making proper changes to our policy and without an assist from OIR and the legislature.

Chairman Gardner: I just want to make sure there are no other questions.

John Rollins: **Staff recommends that the Board approve the proposal to adopt policy product changes as it pertains to water damage as described in Attachment A and authorize staff to make any necessary and appropriate action consistent with this recommendation, including filing these changes with the OIR as well as systems implementation and supporting activities.**

Vice Chair Glisson made the motion to approve the policy product changes as it pertains to water damage as described above. The motion was seconded. All were in favor. Motion carried.

11. Consent Agenda Items

Barbara Walker: There are three items for consideration.

- **2016 Corporate Insurance Renewal. This is a budgeted item. It is recommended that Citizens' Board approve the renewal of the 2016 corporate insurance policies (Business Owners, Workers' Compensation, Business Auto, and Financial Institution Bond) above and to authorize staff to take any appropriate or necessary action consistent with this Consent Item.**
- **IT Staff Augmentation Services. This is a budgeted item. Citizens request Board approval of the IT Staff Augmentation Services (spending authority) Consent Item.**
- **IT Infrastructure, Software, and Professional Services. This is a budgeted item. Citizens requests Board approval of the IT Technology Infrastructure, Software and Professional Services (spending authority) Consent Item.**

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

New Business

Meeting adjourned.