



Demotech, Inc.

Advanced via email to steve.bitar@citizensfla.com

August 28, 2017

Steve M. Bitar, CPCU, Are
Chief of Underwriting and Agency Services
Citizens Property Insurance Corporation
301 West Bay Street, Suite 1300
Jacksonville, FL 32202

Dear Steve,

My thanks to you and to Citizens Property Insurance Corporation for the invitation to share my thoughts with "Demotech Introduction and Overview" at the Market accountability advisory Committee meeting scheduled for September 26, 2017. As it is my understanding that my Power Point presentation will be distributed in advance, I am attaching additional materials that I will be handing out as hard copy prior to my presentation.

The handouts will be an overview of our reinsurance review procedures and copies of our quarterly publication, *The Demotech Difference*. The overview of reinsurance review procedures are attached to this letter. Links to the online version of our publication can be found at http://www.demotech.com/demotech_difference.aspx

I look forward to the opportunity to share my thoughts.

Very truly yours,

Joseph L. Petrelli, ACAS, ASA, FCA, MAAA
President

Demotech, Inc.
2017 Florida Catastrophe (CAT) Reinsurance Summary
August 1, 2017

The information below is compiled from the data and information Demotech has requested, received, reviewed, and evaluated for Florida Financial Stability Rating[®] (FSR) client companies' respective CAT reinsurance programs for the 2017 season. Demotech has not included, or referenced, any specific company or any specific CAT reinsurance program, nor do we have knowledge of carriers that we do not review.

- The overall statutory surplus for the Florida FSR client companies has increased to \$3.9 B as of March 31, 2017, up from \$2.9 B as of December 31, 2013. This is an increase of \$1.0 B or 34.0%. The \$3.9 B compares to the collective surplus of \$1.8 B as of December 31, 2010. Demotech classified fifty-six client companies as Florida clients as of March 31, 2017, with the comparable count being fifty-one companies as of December 31, 2013, and forty-eight as of December 31, 2010.
- The average calendar year percentage of ceded premium to gross premium written has declined from 58.4% in calendar year 2012 to 49.7% in calendar year 2016. Our Florida client companies have taken advantage of the reduction in reinsurance pricing to fund greater limits relative to the 100 year event return period Probable Maximum Loss for those respective periods. Second and multiple event limits have been increased relative to prior periods as well.
- Demotech has identified and confirmed each company utilized a model currently approved by the Florida Commission on Hurricane Loss Projection Methodology (the Commission).
- All companies participate in the mandatory layer of the Florida Hurricane Catastrophe Fund (FHCF). Several companies have elected to reduce their respective participation level to 45%, while the remainder continue to participate at the 90% level. Several companies purchase private reinsurance that is redundant to the FHCF.
- In addition to each company providing model data for the 20, 50, 75, 100, and 150 year event return periods, we have collected data for each of these return periods with combinations of long-term, near-term, loss amplification, secondary uncertainty, and storm surge modifiers. The combinations provide comparison for evaluating levels of conservatism when reviewing each company's CAT reinsurance program.
- The fifty-six Florida FSR client companies included in the data represent forty-four CAT reinsurance programs, as affiliated entities within a group often share a common CAT reinsurance program supported by common Probable Maximum Loss (PML) model results.
- Insurance linked securities and CAT bonds are reviewed. Each client company utilizing CAT bonds provides copies of the reinsurance agreement, the reinsurance trust agreement, and the terms of the bond. Demotech also requires that the event trigger be indemnity based with no basis risk.
- The use of captives is supported by the review of the financial statements of the captive, as provided to us by the client company. Demotech also evaluates the funding of the captive following a first event that triggers the participation of the captive.
- Demotech has secured a listing of the participating reinsurers for each client company. A review is conducted of each reinsurer's most recent financial statement and determination of status with respect to authorization, affiliation, certification, and required collateralization.
- Demotech requires express confirmation by management that the company's CAT reinsurance program does not contain basis risk or contractual loss participation.

- Each client company has provided its formal CAT Response Plan for Demotech's review and consideration describing the procedures and practices in place in the event of a significant event.
- Each company has purchased first event cover at, or in excess of, a 100 year event return period PML using conservative modeling parameters.
- Each company has purchased second event cover at, or in excess of, a 50 year event return period PML as determined after a first event which exhausts the mandatory layer of the FHCF using conservative modeling parameters.
- Depending on the severity of the first two events, each company has addressed surplus protection for a third event or multiple event scenario.
- Total Insured Value (TIV) increased by 10.1%, comparing the 2016 season to the 2017 season, from \$1,901 B to \$2,093 B. Demotech believes this may be attributed to increased exposure through organic growth by legacy companies, exposure taken on by start-up companies, and an increase in exposure through take-out programs facilitated through Citizens Property Insurance Corporation (Citizens).
- In aggregate, the first event vertical limit provides 152.9% of the 100 year event return period PML. This compares to first event limit of 132.3% of the 100 year event return period PML for 2016. First event vertical limit purchased for 2017 increased \$3.8 B or 14.0% to \$31.1 B from \$27.3 B for 2016.
- The second event vertical limit provides 52.5% of the 100 year event return period PML. This compares to second event limit of 59.2% of the 100 year event return period PML for 2016. Second event vertical limit purchased for 2017 increased \$0.2 B or 1.2% to \$16.3 B from \$16.1 B for 2016.
- Demotech continues to collect information and data for each entity's Average Annual Loss (AAL), Occurrence Exceedance Probability (OEP), Aggregate Exceedance Probability (AEP), and Tail Value at Risk (TVAR).
- The Average Annual Loss of \$1.5 B for the rated companies, in aggregate, represents approximately 4.9% of the total first event cover in place for 2017.
- The total first event cover in place represents approximately 157.3% of the OEP of \$19.8 B, 145.3% of the AEP of \$21.4 B, and 85.4% of the TVAR of \$36.4 B.
- Each client company has provided supplemental information on its ability to cover loss adjustment expense (LAE) incurred in the settlement of catastrophe claims. As the FHCF limits the amount of recovery available for LAE, our inquiry requires that each client company has supplemental LAE cover available through their private catastrophe reinsurance program.

Comments and Disclaimers

- The information presented above is based on aggregate totals for Demotech's participating Florida FSR client companies. Although not material, in some instances the information for some entities includes CAT reinsurance for the peril of wind outside of Florida.
- Demotech has not audited or verified modeled information or data for any client company. Our review and evaluation is based solely on the information provided to Demotech within the format and according to our instructions as provided with the data call.
- Demotech does not endorse or support the use of any particular catastrophe model.
- Demotech does not warranty, guarantee, or ensure the adequacy of any model results or the related adequacy of any catastrophe reinsurance program for any company assigned a Financial Stability Rating[®].

- Demotech does not rely on any data or information provided by the Florida Office of Insurance Regulation or any other regulatory agency.
- Companies may choose to blend various model results and may rely on management's assumptions regarding the determination and measurement of CAT risk. While Demotech reviews management's assumptions and is aware of the use of blending or other model assumptions, we do not authorize or approve these assumptions or techniques.