

### SECTION 1: Legislative Direction

Pursuant to Senate Bill 408, signed into law on May 17, 2011, the Citizens Property Insurance Corporation (Citizens) Board of Governors commissioned an independent third-party consultant with property insurance company management expertise to report on and make recommendations about the costs and benefits of outsourcing policy issuance and service functions to private servicing carriers. Citizens issued a competitive solicitation for an independent third-party consultant. A contract with Perr & Knight was signed in December 2011.

Perr & Knight began working on the three-phase project in January 2012. Members of Perr & Knight performed interviews with Citizens' staff, gathered data and observed processes. Specific processes were identified and defined to align with the scope of work. Perr & Knight focused on the calendar year ending December 31, 2011, with the exception of their research into the Inspection and Outreach Program, which spanned from project inception through March 31, 2012. The report was completed and submitted to Citizens on May 31, 2012. The Citizens Board of Governors received the [final report](#) at their meeting on June 13, 2012. This report is available online here at [www.citizensfla.com/documents/SB408\\_Report.pdf](http://www.citizensfla.com/documents/SB408_Report.pdf).

This document outlines the implementation plan developed in response to Perr & Knight's final report. Pending review, modification and approval by the Financial Services Commission, Citizens will begin implementation on January 1, 2013.

Citizens requests the favorable consideration and adoption by the Financial Services Commission on this implementation plan at its meeting on December 11, 2012.

### SECTION 2: Proposed Implementation Timeline

- A. The following recommendation was addressed during 2012:
  - Conduct solicitation for additional standby vendors (CSC-2)
  - Reduce time-based compensation arrangements (CA-3)
- B. The following recommendations will be addressed during 2013:
  - Gradually increase use of external call centers (CSC-1)
  - Review endorsements to ascertain the level of effort associated with each endorsement type and renegotiate vendor pricing to better reflect each (UW-1)
  - Review renewals for potential misapplication of credits (UW-2)
  - Expand the Inspection and Outreach Program when appropriate (PI-1)
  - Consolidate inspection activities into a single site visit (PI-2)
  - Reevaluate the current fee structure for processing inspection report results (PI-3)
  - Categorize Task Assignment Model claims (CA-4)
- C. The following recommendations will be addressed in 2014 or later due to the sunseting of several legacy systems as a result of the Core program:
  - Adopt additional loss-control methods for water-damage mitigation (CA-5)
  - Review underwriting phone calls for possible automation, self-service or other means to reduce call volume and duration (UW-3)

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- Continue work on the Core Project and re-evaluate impact on the In-Scope Processes once completed (GO-1)
- Continue work on the data warehouse initiative (GO-2)
- Increase electronic delivery of policy packages (PP-1)
- Consolidate processing and distribution vendors (PP-2)
- Perform policy assembly in house (PP-3)
- Enable consistent, timely and accurate reporting (CA-1)
- Adopt uniform workflows (CA-2)
- Benchmark financial measures (CA-6)

D. The following recommendation will be addressed after the organizational assessment has been completed:

- Centralize command of data and process performance by appointing an enterprise data-steward and consolidating data retrieval and reporting functions in the office of the Chief Insurance Officer or similar position (e.g., creation of a Chief Operating Officer or Vice President of Operations post) (GO-3)

### SECTION 3: Recommendation Notes

Perr & Knight concluded that the framework in place at Citizens is well developed and effectively uses the outsourcing opportunities available in the marketplace. While there may be instances where further outsourcing is feasible, Perr & Knight recommended caution so as to not adversely affect quality within Citizens due to the additional time and attention such efforts would require from staff. Some areas of improvement were noted with the acknowledgement of management's awareness and planned action for operational enhancement.

Many of the processes identified will be addressed in the upcoming Core project. Core will be our next generation insurance operating system and will combine multiple current systems into one integrated, user-friendly platform. Core will increase our capabilities for automated handling, increase process efficiency and improve productivity while lowering operating expenses. Related projects include implementation of the Guidewire suite of insurance applications (policy, claims, billing), implementation of a new rating-engine, implementation of a new document-production application, development or modification of interfaces to supporting systems, and development or modification of business processes to support industry best practices in insurance operations.

In addition to the Core project, Citizens will also undergo an organizational review by third-party consultant beginning in the first quarter of 2013. The consultant, once selected, will conduct a complete and comprehensive review of Citizens' organization, including analysis and recommendations into the future state of operations. The future state vision is a streamlined, scalable and customer-focused organization.

The organizational review will provide analyses and recommendations that include, but are not limited to, the following:

- A. Creation of a future state organization that can scale rapidly as policies are transferred to the private market.
- B. Realization and maximization of anticipated efficiencies resulting from the implementation of the next-generation claims and underwriting systems (Core Systems Transformation).
- C. Creation of a framework to balance staffing resources (direct employees, contingent/temporary staff and outsourced contracts).
- D. Completion of a comprehensive review of management tiers and organizational structure.

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- E.** High-level evaluation of staff capabilities and talent and recommendations for maximizing operational efficiencies.
- F.** Creation of a vendor-management strategy that is consistent with the future state organization recommendation in order to meets the needs of the changing organization and ensure improved cost, performance and service regardless of policy volumes.
- G.** Use of established management-design principles to develop an outline for the optimal organizational structure.
- H.** Evaluation of the potential application of a work-from-home program.
- I.** Evaluation of Citizens’ multi-location strategy with recommendations to align with the future state organization.

### SECTION 4: PERR & KNIGHT RECOMMENDATION DETAIL

Underwriting Recommendations		
UW-1	<i>Review endorsements.</i> Conduct an assessment of the relative complexity of endorsement transactions processed by MGI. Determine which of those can be processed through either (a) automation or (b) policyholder self-service. Multiply the expected quantity to automate or enable for self-service by MGI's fee, and determine if the costs associated with automation and creating a self-service capability outweigh the expected cost savings that accrue to Citizens as a result of reducing the volume of transactions processed by MGI. (Note that this savings must also be weighed against MGI's discount for processing large volumes of transactions, and the fact that reducing transaction volumes outsourced to MGI may result in higher per-transaction costs).	Reduced pricing related to outsourced underwriting task processing for endorsements and other underwriting tasks was accomplished through a Competitive Solicitation Citizens conducted in 2012 to expand the number of contracted business process outsourcing vendors. Services under this new contract are targeted for implementation in 2013.
UW-2	<i>Review renewals.</i> Review a sample of renewal transactions and perform re-underwriting to determine the extent of changes to premiums. In the event premiums increase by an amount exceeding the cost to re-underwrite, consider expanding underwriting on renewal to a larger population of policies.	In 2013 a renewal underwriting program will be introduced with more focus on risk factors vs. credit adjustments  In Q4 2012 we have implemented a renewal underwriting process to take appropriate action on risks with three or more non-Act of God losses in prior 36 months. Initial list shows 3,500 policies for review in the first 12 months of the program. Of the first 100 files reviewed, approximately 35% are being set up for non-renewal (as the insurer of last resort, the agent will be able to rewrite these risks on DP1 policies). We will be working in 2013 to incorporate this process into Core and build an interim process for

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		automated identification and referral of these policies.
UW-3	<i>Review underwriting phone calls.</i> Seek ways to reduce the number of underwriting-related phone calls inbound from agents, which currently consume an estimated 65% of internal staff time. Our expectation is that a thorough review of such calls will confirm that a large proportion of call types are attributable to a relatively small number of possible call topics. By addressing the “vital few” topics in a manner that enables callers to retrieve frequently sought information without Citizens’ staff intervention is expected to yield a significant drop in call volume and a corresponding increase in staff availability (i.e., to perform other tasks).	<p>There are several steps being taken to reduce call volume.</p> <ul style="list-style-type: none"> <li>• Earlier in 2012 there was a ‘Hot Topic’ section of the website to address frequently asked questions</li> <li>• In October, the average processing time will be posted on the Citizens website (this will lower call volume as better expectations are set for time to handle)</li> <li>• The Underwriting Checklist Submission project is scheduled to be implemented in January 2013, which should, over time, decrease calls due to missing information requests</li> <li>• As the enhanced Wind Mitigation communications are implemented later in 2012, the number of calls we get specifically related to that initiative should decrease. A First Response team is being set up in the Wind Mit team to handle inspection calls and reduce the need to transfer those calls to Underwriters.</li> </ul> <p>Additional initiatives will require more resource commitment, and will be addressed through the Core program or post Core implementation.</p>
<b>Policy Processing Recommendations</b>		
PP-1	<i>Increase electronic delivery of policy packages.</i> The promotion of paperless options for policyholders and their acceptance of an increase in electronic	To be addressed in 2014 through Core program

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	deliveries of policy documents (including policy packages, endorsements, invoices and notices) would relieve Citizens of a significant portion of its Policy Processing expense. With more than \$5.1 million in annual postage expenditures related to policy servicing activities, this represents an area ripe for reengineering. We expect the successful completion of the Core Project to facilitate the implementation of this recommendation.	
PP-2	<i>Consolidate processing and distribution vendors.</i> We would expect the consolidation of vendors, irrespective of the deployment of the new solutions anticipated with the completion of the Core Project, to provide Citizens with a financial benefit. We are aware, however, that the terms of the current contract with CSC may prevent Citizens from pursuing such a consolidation until that contract term expires.	As a result of the implementation of the Core program, including a new document production system, Citizens plans to assess opportunities to change its print distribution methodology in an attempt to reduce related costs and consolidate the number of existing vendors involved.
PP-3	<i>Perform policy assembly in house.</i> It should be noted that this recommended solution is being contemplated in connection with the ongoing Core Project. The adoption of a document management solution that organizes policy forms and manages attachment rules in a manner that assembles complete policy packages and readies them for delivery (either electronically or via postal mail) would relieve Citizens of an annual recurring expense that exceeds \$2 million. The cost of such a solution needs to be considered (including software acquisition, infrastructure, integration, deployment and maintenance costs), however, we are aware that a solution currently contemplated as a component of the Core Project is expected to be implemented at a cost well below the current annual spend, suggesting the potential for a significant return on investment.	To be addressed in 2014 through Core program
<b>Property Inspection Recommendations</b>		
PI-1	<i>Expand the program.</i> The success of the wind mitigation and sinkhole inspection programs suggests expansion of both inspection types to a larger number of policies will yield significant additional benefits.	Citizens expanded the volume of this program during 2012 and will meet the original goal to exceed processing of 343,000 wind mitigation credit reinspections. As part of the original plan,

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		in 2013, Citizens will transition program focus to new business applications, leveraging its infrastructure, to ensure accurate inspections relating to new business. This will include consolidation of other inspection types to be serviced by Citizens reinspection vendors.
PI-2	<i>Consolidate inspection activities.</i> We would expect the consolidation of construction inspections and appraisals with wind mitigation inspections to provide cost savings to Citizens by eliminating the need for multiple site visits by inspectors, and the additional inspections to yield even greater returns.	This was always part of the original plan to first complete wind mitigation reinspection needs and then consolidate all inspection types for new business into this process, to leverage negotiated rates and complete one or more inspections all at one time.
PI-3	<i>Evaluate current fee structure with MGI.</i> Given the fee schedule currently in force with MGI for underwriting new business applications (which may include a wind mitigation inspection report processing component), we suggest evaluating the fee payable to MGI for processing inspection reports. At \$26 per report, it exceeds the average cost to underwrite a new policy.	Inspection Processing fees by outsourced vendors were reduced as part of the business process outsourcing solicitation completed in 2012 and will be implemented in 2013.
<b>Claims Adjusting Recommendations</b>		
CA-1	<i>Enable consistent, timely and accurate reporting.</i> While we found Citizens' staff very responsive to our multiple requests for information, there were multiple sources of data and further qualifications required of data and information received to resolve conflicts. This is likely a function of the multiple systems from which such data are collected and aggregated. The extensive use of outsourcing by Citizens' claims organization indicates a need for greater visibility, including more accurate and timely reporting, into the split between internally managed and outsourced activities, the complexity of each and the cost associated with each. The deployment of a state-of-the-art claims processing solution and the completion of a centralized data warehouse should help to normalize the available data and facilitate a reporting capability	In 2012 Citizens formed the Reporting and Analytics team within the Insurance Operations Business Analyst group, as another step towards consistent, timely and accurate reporting. In 2013 and 2014, as current reporting projects are completed and Core implementation of ClaimCenter is finalized, additional resources will shift to this team enhancing consistency and credibility of reporting.

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	appropriate for the management of Citizens' claims organization.	
CA-2	<i>Adopt uniform workflows.</i> Citizens manages a variety of claims types in a variety of different ways that call for many staff positions representing multiple areas of specialization within the claims organization. We believe that designing claims workflows in a manner that normalizes the intake, loss adjustment and settlement processes will contribute to operating efficiencies by reducing staff training times and facilitating cross-training of various claims management staff. We note that the pending Core Project has as one of its central objectives the deployment of a state-of-the-art claims management solution that is expected to address this very issue.	The implementation of Core program in commercial and personal lines (full delivery finalized in 2014 for Claims) provides for more uniform flow of assignments and "work." Additional movement in this direction was completed in 2012 with the initial integration of Appraisal into "front-end" Managed Claim Model workflows. However there will always be differentiating factors for various claim types that dictate varying workflows.
CA-3	<i>Reduce time-based compensation arrangements.</i> IA Firms and the adjusters they employ who are compensated based on the amount of time they work to settle a claim have less incentive to close a claim file than those who receive a fixed fee per claim. The outsourcing model that compensates based on GCA is preferable to day rate and hourly rate adjusters, and far less subject to abuse.	Citizens currently limits time and expense assignments through current workflows. Day rate assignments, however, can be beneficial from a perspective of providing the flexibility of managing a position on quality and productivity.
CA-4	<i>Categorize Task Assignment Model claims.</i> There are many scenarios where one or relatively few minor tasks are assigned on very high-value claims would call for a relatively large payment to the IA Firm if a large GCA payment is invoked for a relatively small task assignment. A provision that delineates task assignments by level of effort may help reduce outsourcing costs, provided a reasonable method could be devised to ascertain the level of effort required to complete an assigned task.	In 2011 Citizens moved from a pure desk based model engaging 85% Task Assignments to the Managed Claims Model engaging full file handling by Independent Adjusters. This transition continues in 2012 and significantly reduces Task Assignments. In 2013 we will develop an Independent Adjuster Services RFP and will incorporate revisions to how Citizens engages IAs. Additional provisions as outlined can be evaluated in the development of that RFP.
CA-5	<i>Adopt additional loss control methods.</i> The high incidence of water damage claims (representing 54.6% of all new claims in 2011) may indicate a need to	A review of actual water loss claims frequency trends, average indemnity paid and loss



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	provide better loss control through more stringent underwriting criteria and policyholder education (i.e., informing policyholders regarding remedial strategies to avoid plumbing and roofing problems and the premium credits that may be available as a result of implementing them).	adjustment expenses reveals a less critical need to address a Water Mitigation Program. We will be evaluating options in 2013, but given the resource constraints a full water mitigation program will most likely be pushed to 2014. However, in the interim we are developing additional tools to manage and review Water Mitigation bills for consistency and will be operationalizing this approach in 2013.
CA-6	<p><i>Benchmark financial measures.</i> We recommend Citizens conduct a benchmarking study to compare their average claim expenses with those of the private sector, developing metrics that compare, for example:</p> <ul style="list-style-type: none"> <li>• Claims by region</li> <li>• Claims by type of loss</li> <li>• Claims by sub-type of loss</li> <li>• Average cycle time from FNOL through resolution <ul style="list-style-type: none"> <li>○ By region</li> <li>○ By type of loss</li> <li>○ By sub-type of loss</li> </ul> </li> <li>• Number of reopened claims due to initial error</li> <li>• Number of reopened claims due to supplemental payment</li> </ul> <p>Until consistent, timely and accurate reporting is in place, Citizens management will be challenged to identify patterns in claims activity that indicates the best way to manage claims.</p>	Benchmarking data and key performance indicators are important, but will not be an effective utilization of resources until Core program implementation of ClaimCenter is completed and we have the Reporting & Analytics team “built out” to ensure consistency and credibility of reportable data.
<b>Customer Service Calls Recommendations</b>		
CSC-1	<i>Increase use of external call centers.</i> A gradual increase in the use of external (i.e., outsourced) call centers while closely monitoring rates of complaint will help ensure the readiness and availability of call center staff in the event scaling of operations is necessary, e.g., upward in response to a large-scale	This is being addressed through the 2013 implementation of the Competitive Solicitation Citizens conducted during 2012 to expand the number of contracted business process

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	catastrophe, or downward in the event Citizens' policy count declines markedly. All vendors must offer appropriately scalable and highly trained staff to ensure adequate service levels are maintained	outsourcing vendors, which includes phone answering services.
CSC-2	<i>Conduct solicitation for additional vendors.</i> The solicitation of additional vendors for price comparisons and to provide a sufficiently large, highly trained and available and call center staff in the event large-scale catastrophes or other events prompt significant call volume increases.	This was completed in 2012 through the Competitive Solicitation Citizens conducted to expand the number of contracted business process outsourcing vendors.
<b>General Operation Recommendations</b>		
GO-1	Continue work on the Core Project and re-evaluate impact on the In-Scope Processes once completed.	To be addressed in 2014 through Core program
GO-2	Continue work on the data warehouse initiative and ensure appropriate data elements are collected and readily reportable based on pre-defined key performance indicators.	To be addressed in 2014 through Core program
GO-3	Centralize "command" of data by appointing an enterprise-wide data steward and consolidating data retrieval and reporting functions in the office of the Chief Insurance Officer, or creating a similar capability by installing a new executive position, such as a Chief Operating Officer or Vice President of Operations post, for performance oversight across all areas of operations.	To be addressed after Organizational Assessment

# **Citizens Property Insurance Corporation**

Property Insurance Cost Control (SB408)

Operations Assessment Report

Monday, June 11, 2012

Prepared by Perr&Knight



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*The information, opinions and recommendations contained in this document were derived from the best available data at the time of discovery, much of which was provided by Citizens staff members. As such, there can be no assurance given by Perr & Knight that the data presented are true and correct, or that recommendations contained herein will remain valid indefinitely. Further, there can be no assurance that the discovery of additional information undisclosed and unknown to Perr & Knight at the time of preparation would not materially alter the findings.*

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## Introduction

Citizens Property Insurance Corporation (“Citizens”) has engaged Perr & Knight to perform an analysis of operations that includes (i) a review of currently outsourced functions; (ii) a cost-benefit analysis that weighs the benefits of outsourcing certain functions versus maintaining them in house; and (iii) a review of other residual market carriers and service providers to determine how they utilize outsourcing to accommodate fluctuating market conditions (the “Study”). The Study was conducted in connection with certain provisions of Senate Bill 408 (“SB408”), also known as the “Florida Property Insurance Cost Control Bill,” signed into law and made effective on May 17, 2011, which asserts:

*To ensure that the corporation [Citizens] is operating in an efficient and economic manner while providing quality service to policyholders, applicants, and agents, the board shall commission an independent third-party consultant having expertise in insurance company management or insurance company management consulting to prepare a report and make recommendations on the relative costs and benefits of outsourcing various policy issuance and service functions to private servicing carriers or entities performing similar functions in the private market for a fee, rather than performing such functions in house. In making such recommendations, the consultant shall consider how other residual markets, both in this state and around the country, outsource appropriate functions or use servicing carriers to better match expenses with revenues that fluctuate based on a widely varying policy count. The report must be completed by July 1, 2012.*

The approach to the Study was memorialized in the *Project Plan, Approach and Strategy* document prepared by Perr&Knight and delivered to Citizens on Friday, January 20, 2012 which defined the project scope, as well as the participants and project management tools and methods to be used throughout the engagement. The final project scope was also documented in a *Process Master*, annexed hereto as Appendix C.

Perr&Knight conducted the engagement to produce the Study in three phases:

- Phase 1, *Discovery*, during which requests for information were prepared and distributed to the appropriate Citizens management team members for each process examined in connection with

the Study (each, an “In-Scope Process”). Accordingly, (i) information requests were created for Underwriting, Policy Processing (which included policy issuance, policy billing, and policy renewals), Property Inspections, Claims Adjustment and Customer Service Calls to ascertain 2011 Citizens staff headcounts, salaries and transaction volumes for both personal and commercial lines of business; (ii) the in-force contracts between Citizens and the outsourcing service providers contracted to support each In-Scope Process were requested and reviewed to ascertain the fee schedule and service level agreements between the parties; (iii) existing process workflow diagrams were requested, reviewed and validated with Citizens’ staff; and (iv) staff interviews were conducted to gain perspectives from Citizens’ management team members with respect to their use of outsourcing versus internal staff, and understand their motivations for their preferred blend of internally- and externally-managed (i.e., outsourced) processes. In addition to requests for information from Citizens’ staff members, a brief survey (the form of which is provided in Appendix D) was prepared and distributed to 17 FAIR (“Fair Access to Insurance Requirements”) Plan entities that serve residual markets, of which eight responded (47% response rate), to understand how each managed the In-Scope Processes defined for the Study with respect to their decision to internalize or outsource to servicing carriers or third-party service providers certain insurance processes.

- Phase 2, *Modeling, Simulation and Analysis*, during which spreadsheet models were created to evaluate the various costs and benefits of using internal versus external (outsourced) staff for various parts of each In-Scope Process, and workflow diagrams were reviewed with Citizens staff to validate the sequence of activities for each In-Scope Process; and
- Phase 3, *Report Preparation*, during which an initial draft report, dated May 1, 2012, was prepared and distributed to Citizens’ staff for comments, which were reviewed, validated and incorporated, which resulted in a second draft, dated May 29, 2012 being prepared and distributed for further validation. Comments and additional discovery resulting from the second draft was then incorporated and the final report (this document) was prepared and submitted to Citizens.

Reflecting the results of the Study, the balance of this document is organized in nine sections – an executive summary, one section for each of the five In-Scope Processes, an industry comparisons section and sections concerning general operations and conclusions. The process-specific sections

examine, for each In-Scope Process, the number and cost of internal staff and the number of transactions managed by them, as well as the proportion and cost of transactions outsourced to third-parties. The analysis differentiated between personal and commercial lines of business where appropriate. Sources of data and other relevant information used to perform the analysis are provided in the appendices, referenced in footnotes throughout the document and compiled in a collection of Exhibits provided with this report under separate cover, a list of which is available in Appendix F. In addition, the calculations used in performing the analysis are contained in Appendix E, "Citizens 408 Study Master Workbook," a Microsoft Excel spreadsheet also provided separately. Data from the most recent calendar year (2011) was used to perform the majority of the analysis, with the exception of Underwriting Property Inspections which used data from program inception through March 31, 2012.

**Note regarding the Core Project:** A major, ongoing initiative is currently in progress to retire Citizens' existing policy administration, claims management and billing systems and replace them with a state-of-the-art solution that consolidates insurance processing functions on a single, natively-integrated platform (the "Core Project"). We expect the completion of the Core Project, scheduled for the third quarter of 2014, to provide Citizens with the system consolidation, workflow management improvements and automation capabilities required to accommodate many of the recommendations contained in this report. Accordingly, we recommend an evaluation of anticipated improvements resulting from the Core Project and their impact on the processes that are the subject of this Study prior to initiating those suggested modifications to Citizens' processes or outsourcing strategies impacted by the Core Project. Initiating changes without first considering the impacts of the Core Project may result in the procurement and/or implementation of solutions destined to become obsolete. In the event any such solutions are implemented, only to be replaced as a result of the Core Project, the overall cost and operational risk to Citizens of deploying them in the first place may negate any anticipated interim benefit.



## Executive Summary

The scope of the Study includes a review of five areas of operations, each an “In-Scope Process,” summarized in the table below. Our objective in examining each In-Scope Process was to determine whether Citizens’ approach to outsourcing certain activities supported the SB408 dictum to “[operate] in an efficient and economic manner while providing quality service to policyholders, applicants, and agents.”

Process	Total Transactions	Outsourced Transactions	Outsourcing Cost	Internal Transactions	Internal Cost
<b>Underwriting</b> (New Business; Endorsements)	2,378,152	1,528,457 (64%)	\$ 8,920,161	849,693 (36%)	\$ 11,350,789
<b>Policy Processing</b> (Policy Issuance, Invoicing, Renewals, Endorsements)	21,525,004	21,525,004 (100.0%)	\$ 9,739,787	0	\$ 0
<b>Property Inspections</b> Wind Mitigation	94,000	94,000 (100.0%)	\$ 9,870,000	0 (0.0%)	\$ 0 <sup>1</sup>
Sinkhole	1,579	1,579 (100.0%)	284,220	0 (0.0%)	0
<b>Claims Adjustment</b> <sup>2</sup> (excluding LDCU)	125,615	89% of new claims <sup>3</sup>	\$45,252,859	11% of new claims <sup>3</sup>	\$14,149,368
<b>Customer Service Calls</b>	1,355,133	77,080 (5.7%)	\$ 427,701	1,278,053 (94.3%)	\$6,805,602

Table 1: SB408 Study In-Scope Processes<sup>4</sup>

<sup>1</sup> There is a processing component managed by Citizens’ staff that is reflected in Underwriting expenses.

<sup>2</sup> Claims transaction counts omit litigated and disputed claims in mediation, arbitration or requiring appraisal (i.e., LDCU Claims) due to the relatively high costs associated with such claims that would improperly skew our analysis. Accordingly, LDCU claims are treated separately in this report.

<sup>3</sup> Because most claims are managed through the combined efforts of internal (employee) and external (outsourced) staff, there is no clear delineation between the number of claims handled internally versus externally.

<sup>4</sup> Data sources used to prepare this table are referenced in the appropriate process-specific section of this report.

For the purposes of this Study, and in light of the fact that organizational processes necessarily overlap in the regular conduct of business operations, we have defined each In-Scope Process as more fully described below:

- *Underwriting* includes all new business and endorsement processing for both personal and commercial lines of business (from the point an application is received to the point a policy is bound for issuance), cancellations, reinstatements, rewrites, information request follow ups and agent underwriting inquiries. The vast majority of Citizens' new business underwriting and endorsement processing activities – about 90% – are outsourced to MacNeill Group, Inc. ("MGI").
- *Policy Processing* includes the assembly, printing and distribution of policy packages, invoices, endorsements and notices to policyholders. All Policy Processing activities are currently outsourced to a combination of CEDAR Document Technologies (policy assembly and electronic document delivery) and Pitney Bowes (printing and mailing) for personal lines; and Computer Sciences Corporation ("CSC") with a pass-through of expenses from their mailing subcontractor, Pinnacle Data Systems for commercial lines. The use of two separate processes is a reflection of the presence of separate policy administration applications for personal and commercial lines, and the inclusion of policy processing services with the service contract provided by CSC, the current commercial lines policy administration vendor.
- *Underwriting Property Inspections* includes wind mitigation (soon to be complemented by appraisal and construction inspection services) and sinkhole inspections performed during Citizens' initial underwriting process, upon renewal or as a re-inspection during a current policy term. Due to the ready availability of data, for the purposes of the Study we examined wind mitigation inspection results from inception through March 31, 2012. All underwriting property inspections are currently outsourced by Citizens.
- *Claims Adjustment* includes claims investigation activities that determine the extent of losses payable as a result of being covered by a Citizens policy. Citizens has contracted with twenty-seven independent adjusting firms (and an additional ten general adjusting (GA)/executive general adjusting (EGA) firms for commercial lines claims adjusting commencing in 2012) that manage claims (i) in their entirety (after receiving a first notice of loss through settlement with

the claimant); or (ii) on a task-assignment basis. Approximately 89% of Citizens' new claims received in 2011 were outsourced using either of these approaches.

- *Customer Service Calls* includes the handling of inbound calls from policyholders, agents, mortgagees, claimants and those interested or participating in the Florida Market Assistance Program ("FMAP"). Citizens maintains a large call center operation staffed by highly trained customer service representatives, and outsources approximately six percent of their inbound call volume (mostly from claimants registering first notices of loss) to one of two vendors.

The Study examines each of these processes for the calendar year ending December 31, 2011, with the exception of Underwriting Property Inspections for wind mitigation, which were examined from inception of the program through March 31, 2012.

### Summary of Findings and Recommendations

The findings and recommendations resulting from our review of the In-Scope Processes that were the subject of the Study are summarized in the table below. All findings and recommendations are further qualified in the appropriate process-specific section of this report.

Process	Findings	Recommendations
<b>Underwriting</b>	<ol style="list-style-type: none"> <li>1. The level of effort required to process different endorsement types is not captured by Citizens</li> <li>2. A high proportion of renewals are automated, yet re-inspections are yielding a large percentage of policy changes</li> <li>3. Underwriting phone calls consume about 65% of internal underwriting staff time</li> </ol>	<ol style="list-style-type: none"> <li>1. Review endorsements to ascertain the level of effort associated with each endorsement type and renegotiate vendor pricing to better reflect each</li> <li>2. Review renewals for potential misapplication of credits</li> <li>3. Review underwriting phone calls for possible automation, self-service or other means to reduce call volume and duration</li> </ol>
<b>Policy Processing</b>	<ol style="list-style-type: none"> <li>1. Processing and postage costs may be reduced with additional electronic delivery or paperless options</li> <li>2. Multiple vendors are performing similar highly commoditized functions</li> <li>3. Policy assembly requires outside support costs that may be avoided</li> </ol>	<ol style="list-style-type: none"> <li>1. Increase electronic delivery of policy packages</li> <li>2. Consolidate processing and distribution vendors</li> <li>3. Perform policy assembly in house</li> </ol>

Process	Findings	Recommendations
<b>Property Inspections</b>	<ol style="list-style-type: none"> <li>1. Program is highly effective</li> <li>2. Wind mitigation inspections are being performed independent of other inspection types that may require additional site visits and unnecessarily increase costs</li> <li>3. Outsourcing processing costs for re-underwriting may be high relative to new application processing costs</li> </ol>	<ol style="list-style-type: none"> <li>1. Expand the program when appropriate</li> <li>2. Consolidate inspection activities into a single site visit</li> <li>3. Reevalue current fee structure for processing inspection report results</li> </ol>
<b>Claims Adjusting</b>	<ol style="list-style-type: none"> <li>1. Citizens claims statistics revealed in separate reports were sometimes conflicting</li> <li>2. Multiple workflows have been adopted based on claim type, and additional normalization may be possible to reduce process variation</li> <li>3. Adjusters compensated based on time to complete a claim assignment have a disincentive to work quickly</li> <li>4. 54.6% of claims are related to water damage from plumbing, roof leaks, etc.</li> <li>5. Little basis for comparison with similarly situated insurers</li> </ol>	<ol style="list-style-type: none"> <li>1. Enable consistent, timely and accurate reporting</li> <li>2. Adopt uniform workflows</li> <li>3. Reduce time-based (hourly) compensation arrangements</li> <li>4. Categorize Task Assignment Model claims</li> <li>5. Adopt additional loss control methods for water damage mitigation</li> <li>6. Benchmark financial measures</li> </ol>
<b>Customer Service Calls</b>	<ol style="list-style-type: none"> <li>1. Well organized and staffed professional organization</li> <li>2. Apparent correlation between lower incidence of complaints and customer service quality assurance measures</li> <li>3. Lower staff attrition than industry norm</li> <li>4. Relatively little use of outsourcing</li> <li>5. Need to ensure outsourcing providers are ready, willing and able to serve in the event of large-scale call volume increases</li> </ol>	<ol style="list-style-type: none"> <li>1. Gradually increase use of external call centers</li> <li>2. Conduct solicitation for additional "standby" vendors</li> </ol>

Process	Findings	Recommendations
<b>General Operations</b>	<ol style="list-style-type: none"> <li>1. Citizens has an acute awareness of its operating challenges and is taking steps to identify and remedy them</li> <li>2. Operating data are maintained in multiple, disparate systems and are difficult to consolidate.</li> <li>3. The existence of a process improvement function affirms our belief that efficiency is an important component of Citizens' operating culture</li> <li>4. Citizens has developed an extensive vendor management capability wherein vendor relationships and performance are continually reassessed, which represents a mature organizational approach to outsourcing</li> <li>5. The planned system consolidation and replacement resulting from the completion of the Core Project is expected to yield significant operational benefits directly aligned with the mandates of SB408</li> <li>6. Compared to their industry counterparts, Citizens appears to maintain a lean internal organization while properly leveraging the advantages of outsourcing</li> </ol>	<ol style="list-style-type: none"> <li>1. Continue work on the Core Project and re-evaluate impact on the In-Scope Processes once completed</li> <li>2. Continue work on the data warehouse initiative</li> <li>3. Centralize "command" of data and process performance by appointing an enterprise data steward and consolidating data retrieval and reporting functions in the office of the Chief Insurance Officer or similar position (e.g., creation of a Chief Operating Officer or Vice President of Operations post)</li> </ol>

Table 2: Summary of Findings and Recommendations

## Underwriting

Underwriting processes at Citizens involve a combination of internal and outsourced transaction processing, with more than 90% of personal lines application processing currently being outsourced.<sup>5</sup> All commercial lines policies are currently underwritten by Citizens' staff. For the purposes of this Study, this Underwriting section includes new business underwriting, endorsement processing (which includes renewal transactions<sup>6</sup>), cancellations, reinstatements, inspection processing, missing information follow ups, accounting referrals, internal rewrites and research referrals.

### Personal Lines

Personal lines at Citizens include personal residential multiperil ("PR-M") and personal residential wind-only ("PR-W") policies. PR-M policies are in force for both regular residential (i.e., ordinary risk) and "Coastal Account" properties (i.e., properties deemed highest risk due to their proximity to coastal waters). PR-W policies are currently only in force for Coastal Account properties.

Personal lines underwriting principally comprises new policy application, endorsement and renewal processing for homeowners in the state of Florida, as well as handling hundreds of thousands of underwriting-related inquiries annually from a large agent community. Personal lines policies always originate at one of the 5,500 agencies who employ some 8,400 licensed insurance agents authorized to write Citizens business.<sup>7</sup> Agents enter applicant information directly into Citizens' ePAS policy administration system to determine eligibility and quote a policy. Once eligibility is determined, the policy application can take one of several different paths: (i) if bound and eligible for automated underwriting, the agent will print and mail a cash transmittal form to Citizens together with a check for the premium amount; (ii) if bound but not eligible for automated underwriting, the agent refers the case to underwriting via electronic transmission ("EDS"), mail or fax; and (iii) if unbound, the application is uploaded to Citizens' imaging system, ImageRight, at which point it is retrieved and reviewed by an underwriter for binding acceptability. If acceptable, the policy is underwritten and ePAS is updated to

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<sup>5</sup> Source: Exhibit 1: *Citizens Discovery Workbook – Underwriting* submitted by Deborah Murphy, Vice President, Underwriting, April 1, 2012.

<sup>6</sup> Source: Exhibit 1: *Citizens Discovery Workbook – Underwriting* submitted by Deborah Murphy, Vice President, Underwriting, April 1, 2012.

<sup>7</sup> Source: Interview with Steve Bitar, Senior Director of Consumer and Agent Services at Citizens' Tallahassee offices on April 10, 2012.

reflect the addition of a new policy.<sup>8</sup> When agents have open questions regarding the status of an application, they contact Citizens' underwriting department.

During 2011, 379,738 personal lines new business applications were processed, 33,546 (8.8%) of which were processed by Citizens' internal staff, and 346,192 (91.2%) of which were outsourced and processed by MacNeill Group, Inc. ("MGI"). In addition, Citizens' underwriting staff handled 375,809 (93.0%) inbound calls from agents, while MGI handled 30,448 (7.0%). Further, for the same period, 667,398 endorsements were processed on new and renewal policies, 37,812 (5.7%) of which were processed by Citizens, and 629,586 (94.3%) of which were processed by MGI.<sup>9</sup>

*Policy renewals.* Citizens processed 1,039,102 personal lines policy renewals in 2011,<sup>10</sup> of which 252,400 (24.3%) involved underwriting intervention upon renewal.<sup>11</sup> The majority of renewals were automated, with renewal notices and invoices being sent to the policyholder ninety days prior to the end of each policy term (the costs of which are detailed in the Policy Processing section, *infra.*). Exceptions to automated renewals that require manual intervention include:

- Mobile home policies, where actual cash value (ACV) is recalculated at renewal;
- Policies covering structures with asphalt shingle roofs greater than 25 years;
- Policies on known sinkhole properties;
- Policies with referrals from the claims department to underwriting; and
- Policies re-underwritten as part of the wind mitigation inspection program.<sup>12</sup>

*Internal costs.* To perform internal personal lines underwriting and related activities, Citizens employed 107 individuals including a director, five managers, nine supervisors, four senior underwriters, ten lead

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<sup>8</sup> Source: Exhibit 2: *PL UW Master Process 12-14-11 v2*.

<sup>9</sup> Source: Exhibit 3: *UW Items Proc 2011* provided by Jonathan Owen, Enterprise Performance Metrics Manager on April 10, 2012 (forwarded by Deborah Murphy, Vice President, Underwriting on April 11, 2012).

<sup>10</sup> Source: Exhibit 4: *April 25, 2012 email from Jonathan Owen*, Enterprise Performance Metrics Manager (forwarded by Deborah Murphy, Vice President, Underwriting, April 25, 2012).

<sup>11</sup> Source: Exhibit 31: *May 11, 2012 email from Deborah Murphy*, Vice President, Underwriting.

<sup>12</sup> Source: interview with Deborah Murphy, Vice President, Underwriting, at Citizens' Jacksonville offices on April 11, 2012.

underwriters, 39 underwriters, 37 underwriting technicians, one personal lines specialist and one administrative assistant, as depicted in the table below.<sup>13</sup>

Position	Number
Director	1
Manager	5
Supervisor	9
Underwriter, Senior	4
Underwriter, Lead	10
Underwriter	39
Technician	37
Specialist – Personal Lines PM	1
Administrative Assistant	1

Table 3: Personal Lines Underwriting Staff

Generally speaking, to perform the work of the underwriting department, Citizens' staff members allocate approximately 15% of their time to new business underwriting; 65% of their time to answering underwriting-related phone calls (typically from agents); 10% of their time to endorsement processing (including renewals); and 10% of their time to miscellaneous transactions (including cancellations, reinstatements, inspection processing, missing information follow ups, accounting referrals, internal rewrites and research referrals).<sup>14</sup> Using the salary totals provided by Citizens,<sup>15</sup> and after applying reasonable allocations for payroll taxes (10%) and overhead expenses (25%), we arrive at an aggregate internal staff cost of \$6,257,924 and an average cost per transaction of \$7.36.

Internal Costs	Transactions	Staff Cost	Avg. Cost/Transaction
New Business Underwriting	33,546	<b>\$6,257,924</b>	<b>\$ 7.36</b>
Endorsements	37,812		
Inspection/Outreach	84,808		
Underwriting Phone Calls	375,809		
Miscellaneous	317,718		
<b>Total, Internal (2011)</b>	<b>849,693</b>		

Table 4: Personal Lines Internal Transaction Statistics

<sup>13</sup> Source: Exhibit 1: *Citizens Discovery Workbook – Underwriting* provided by Deborah Murphy, Vice President, Underwriting, April 1, 2012.

<sup>14</sup> Source: Exhibit 5: *April 24, 2012 email from Douglas Hageman*, Personal Lines Underwriting Operations Manager.

<sup>15</sup> Exhibit 1: *Citizens Discovery Workbook – Underwriting* provided by Deborah Murphy, Vice President, Underwriting, April 1, 2012.



*Outsourcing costs.* Following MGI's contract payment schedule,<sup>16</sup> the cost to Citizens for new personal lines policy applications underwritten, endorsements (including renewals) processed, phone calls related to underwriting issues (typically from agents), and miscellaneous items (including cancellations, reinstatements, inspection processing, missing information follow ups, accounting referrals, internal rewrites and research referrals) was \$8,920,161,<sup>17,18</sup> or an average cost per transaction of \$5.84.

Outsourcing Costs	Transactions	Total Cost	Avg. Cost/Transaction
New Business Underwriting	346,192	\$ 8,920,161	\$ 5.84
Endorsements	629,586		
Inspection/Outreach	295		
Underwriting Phone Calls	30,448		
Miscellaneous	521,934		
<b>Total, Outsourcing (2011)</b>	<b>1,528,455</b>		

Table 5: Personal Lines Outsourced Transaction Statistics

Generally speaking, personal lines policies with more complex needs are managed internally, while the simpler cases are outsourced. As a result of the more complex applications being handled internally, we noted higher internal processing costs (\$7.36 per transaction) when compared to outsourcing (\$5.84 per transaction). However, the increased complexity, skill sets and time required to complete more challenging underwriting cases, as well as the fact that internal staff focus on different activities than outsourced staff (e.g., internal staff handle more phone calls; outsourced staff handle more endorsements) make direct cost comparisons between outsourcing and internal underwriting management inappropriate.

### Commercial Lines

Commercial lines at Citizens include commercial residential, wind only ("CR-W"), commercial residential multiperil ("CR-M"), commercial-non-residential wind only ("CNR-W") and commercial non-residential multiperil ("CNR-M") policies. Wind-only commercial lines policies are only in force for Citizens "Coastal Account" (formerly "High Risk Account", or "HRA") properties, those properties deemed highest risk due to their proximity to coastal waters.

<sup>16</sup> Source: Exhibit 6: *Contract Between Citizens and MacNeill Group, Inc.* dated October 1, 2010.

<sup>17</sup> Source: Exhibit 30 - *2011 Vendor Spend - Preliminary*.

<sup>18</sup> MGI's fee schedule includes breakpoints that reduce the fee per transaction based on monthly volume. The fee schedule is provided in Exhibit 24: *Amendment #3 to 2008 Independent Adjuster Services Agreement*.

Commercial lines underwriting is handled entirely by Citizens' internal staff. While MGI has offered to provide commercial lines underwriting services to Citizens, Citizens' management determined that they were not properly equipped to process Citizens' commercial lines business. As of this writing, Citizens is preparing to release a purchasing solicitation during June, 2012 to identify an appropriate vendor for outsourcing commercial lines underwriting.

During 2011, Citizens underwrote a total of 8,802 commercial lines policies in all categories, and processed 32,178 commercial lines endorsements.<sup>19</sup>

Position	Number
Director	1
Assistant Director	2
Manager	7
Underwriter, Senior	12
Underwriter, Lead	2
Underwriter	24
Technician	5
Specialist – Commercial Field Underwriting	10
Administrative Assistant II	1

Table 6: Commercial Lines Underwriting Staff

To perform commercial underwriting and related activities, Citizens employed 42 individuals, including a director and assistant director, three managers, eight senior underwriters, two lead underwriters, 19 underwriters, five underwriting technicians, two commercial field underwriters and one administrative assistant. Citizens' commercial lines underwriting staff have an aggregate annual payroll (2011) of \$2,959,774, or \$3,995,695 after applying reasonable allocations for overhead (25%), and payroll taxes and benefits (10%).<sup>20</sup>

### Findings

Through our review of Citizens' underwriting operations, three specific areas were identified that we suspect could lead to a reduction in fees paid to MGI.

<sup>19</sup> Source: Exhibit 3: *UW Items Proc 2012* provided by Jonathan Owen, Enterprise Performance Metrics Manager on April 10, 2012 (forwarded by Deborah Murphy, Vice President, Underwriting on April 11, 2012).

<sup>20</sup> Source: Exhibit 1: *Citizens Discovery Workbook – Underwriting* provided by Deborah Murphy, Vice President, Underwriting, April 1, 2012.

- First is the uniform treatment of endorsements processed by MGI, many of which may be automated or managed entirely through self-service facilities by policyholders directly. The sheer volume of endorsements processed on behalf of Citizens' policyholders suggests that even relatively small savings per transaction could equate to large aggregate cost reductions. Admittedly, identifying endorsement types will incur additional processing overhead, however, we believe the added review to properly classify endorsements by relative complexity and automate the processing of potentially hundreds of thousands of simple policy changes would more than offset any increases to overhead.
- The second item is the automatic nature of policy renewals, which has apparently denied Citizens of favorable premium adjustments, evidenced by the success of Citizens' wind mitigation re-inspection program (see the "Underwriting Property Inspections" section, *infra*). We note that the initiation of home inspections for all new business is a significant positive step which we expect will (i) yield additional premiums from policies that erroneously earned wind mitigation or other credits; and (ii) accelerate policyholder attrition for those who return to the private market due to their unwillingness to pay the increased premiums associated with a loss of certain credits. We would expect both outcomes to contribute to a reduction in the loss ratio.
- The third area is the high incidence of agent-initiated phone calls handled by Citizens' internal (i.e., employee) underwriting staff that consume as much as 65% of their time and unduly impact the average cost per internal transaction. By publishing responses to frequently asked questions, or otherwise enabling self-service to resolve certain agent inquiries, we would expect a reduction in call volume and a corresponding increase in staff availability.

### Cost-Benefit Analysis

A direct comparison of costs per transaction between internal operations and outsourcing new business underwriting, endorsement processing and phone calls regarding underwriting issues appears to favor outsourcing if we were to assess Citizens' operations from a purely quantitative perspective. However, we note that the relative complexity of the transactions Citizens retains internally largely accounts for the higher costs per transaction associated with internal operations. Further, to properly consider the cost to outsource, one must consider purchasing activity, including costs associated with preparing and distributing a solicitation to prospective vendors, evaluating vendor responses, negotiating with vendors and contracting with prevailing vendors; contract administration, including service level agreement

reviews and adjustments, as appropriate, invoice processing and general notices as called for in the vendor contract; and vendor indoctrination, including vendor staff training and introduction to the various systems and processes associated with underwriting activities. Accordingly, there is an overhead cost associated with outsourcing that must be considered to properly evaluate the relative costs and benefits of an outsourcing decision. Finally, the process controls and quality management that are critical to efficient underwriting operations necessitate the retention of underwriting oversight and management activities internally.

### Recommendations

Consistent with our findings and subject to verification by Citizens' management and staff, we would expect financial benefits to accrue to Citizens as a result of pursuing the following recommendations:

- *Review endorsements.* Conduct an assessment of the relative complexity of endorsement transactions processed by MGI. Determine which of those can be processed through either (a) automation or (b) policyholder self-service. Multiply the expected quantity to automate or enable for self-service by MGI's fee, and determine if the costs associated with automation and creating a self-service capability outweigh the expected cost savings that accrue to Citizens as a result of reducing the volume of transactions processed by MGI. (Note that this savings must also be weighed against MGI's discount for processing large volumes of transactions, and the fact that reducing transaction volumes outsourced to MGI may result in higher per-transaction costs).
- *Review renewals.* Review a sample of renewal transactions and perform re-underwriting to determine the extent of changes to premiums. In the event premiums increase by an amount exceeding the cost to re-underwrite, consider expanding underwriting on renewal to a larger population of policies.
- *Review underwriting phone calls.* Seek ways to reduce the number of underwriting-related phone calls inbound from agents, which currently consume an estimated 65% of internal staff time. Our expectation is that a thorough review of such calls will confirm that a large proportion of call types are attributable to a relatively small number of possible call topics. By addressing the "vital few" topics in a manner that enables callers to retrieve frequently sought information

without Citizens' staff intervention is expected to yield a significant drop in call volume and a corresponding increase in staff availability (i.e., to perform other tasks).

## Policy Processing

For the purposes of our analysis, and motivated by the way in which Citizens invoices policyholders (i.e., initially combined with the issued policy package), policy issuance (including new business, renewal, endorsement and notice assembly, printing and distribution) and billing processes are combined in this Policy Processing section. Policy processing functions at Citizens are managed through different means for personal and commercial lines, and for each line the assembly, printing and delivery of all policies, endorsements, invoices and notices is outsourced.

### Personal Lines

*Policy issuance (new business).* Personal lines policies are currently issued through a three-party process. Once Citizens or its agency representative (the first party) agrees to issue a policy, the policy information is transmitted to CEDAR Document Technologies (“CEDAR”)(the second party) for policy assembly. During policy assembly, all policy components, including the declarations page, mandatory and optional forms and an invoice are brought together in a single electronic file package. While some prepared electronic file packages are subsequently distributed electronically by CEDAR, others are then transmitted to Pitney-Bowes (the third party) for printing, posting and mailing to each policyholder. For the purpose of establishing a transaction count for 2011, we combined 346,192 new business transactions with 1,081,942 policy renewals to arrive at a total of 1,428,134 personal lines policies issued.<sup>21</sup>

*Policy billing.* The initial invoice for a Citizens personal lines policy is included with the policy package assembled by CEDAR and printed and mailed by Pitney Bowes. Additional invoices are mailed to policyholders if they chose a payment plan other than full pay. According to current pay plan statistics (as of February 29, 2012), 78.33% of all policyholders chose to pay in full; 17.81% chose to pay quarterly (“4-Pay”); and 3.86% chose to pay in two installments (“2-Pay”).<sup>22</sup> Subsequent invoices are mailed in the event a policyholder requests a policy change that results in a premium-bearing endorsement. To estimate a transaction count for invoices other than those contained in the initial policy package sent to personal residential policyholders in 2011, we subtracted the total number of initial invoices

<sup>21</sup> Source: Exhibit 1: *Citizens Discovery Workbook – Underwriting* submitted by Deborah Murphy, Vice President, Underwriting, April 1, 2012.

<sup>22</sup> Source: Exhibit 7: *April 13, 2012 email from Jennifer Montero*, Senior Director of Accounting/Controller.

(represented by the number of newly issued plus renewal policies) from the total number of invoices issued, as detailed in the table below.

	Policy Count	Total Invoices (Policies X Frequency)	Add'l Invoices (Total – Initial)
1-Pay Policies (78.33%)	1,118,657	1,118,657	0
2-Pay Policies (3.86%)	55,126	110,252	55,126
4-Pay Policies (17.81%)	254,351	1,017,404	763,053
<b>Total Invoice Count Estimate</b>	<b>1,428,134</b>	<b>2,246,313</b>	<b>818,179</b>

Table 7: Estimated Personal Lines Invoice Count

The resulting number, 818,179, represents the additional number of invoicing transactions performed during 2011 over those sent with the initial policy package, exclusive of invoices sent with premium bearing endorsements (which are included in the endorsement transaction count).

*Endorsements.* Citizens processed 667,398 personal lines endorsements in 2011<sup>23</sup> (including those processed by MGI on Citizens' behalf) that required printing and distribution either electronically or via postal mail.

### Commercial Lines

*Policy issuance.* Commercial lines policies are currently issued through a two-party process. Once Citizens (or its agency representative) agrees to issue a policy, the policy information is transmitted to CSC, which subcontracts to Pinnacle Data Systems for policy assembly, printing and delivery. During policy assembly, all policy components, including the declarations page, mandatory and optional forms and an invoice are brought together in a single electronic file package, which is then printed and mailed for delivery. CSC passes through their Pinnacle expenses directly (i.e., no additional markup) to Citizens. For the purpose of establishing a transaction count for 2011, we combined all new business transactions (8,802) with policy renewals (46,988) to arrive at a total of 55,790 commercial lines policies issued.<sup>24, 25</sup>

<sup>23</sup> Exhibit 3: *UW Items Proc 2012* provided by Jonathan Owen, Enterprise Performance Metrics Manager on April 10, 2012 (forwarded by Deborah Murphy, Vice President, Underwriting on April 11, 2012).

<sup>24</sup> Exhibit 3: *UW Items Proc 2012* provided by Jonathan Owen, Enterprise Performance Metrics Manager on April 10, 2012 (forwarded by Deborah Murphy, Vice President, Underwriting on April 11, 2012).

<sup>25</sup> Source: Exhibit 1: *Citizens Discovery Workbook – Underwriting* provided by Deborah Murphy, Vice President, Underwriting, April 1, 2012.

*Policy Billing.* All commercial lines policies are paid in full (though commercial policyholders often opt to utilize a premium finance company to make the payment), and as such, an invoice is distributed along with the policy package assembled and mailed by Pinnacle Data Systems. Subsequent invoices are mailed in the event a policyholder requests a policy change that results in a premium-bearing endorsement.

	Policy Count	Total Invoices (Policies X Frequency)	Add'l Invoices (Total – Initial)
1-Pay Policies (100%)	55,790	55,790	55,790
<b>Total Invoice Count Estimate</b>	<b>55,790</b>	<b>55,790</b>	<b>0</b>

Table 8: Estimated Commercial Lines Invoice Count

*Endorsements.* Citizens processed 32,178 commercial endorsements in 2011<sup>26</sup> that required printing and distribution either electronically or via mail. An unknown number of these impacted premium and required the delivery of an invoice, all of which are included in the endorsement count.

## Findings

The assembly, printing and mailing processes used to produce and distribute Citizens' policies, endorsements, invoices and notices are enabled by the infrastructures and support capabilities of very large vendor facilities at Pitney-Bowes and Pinnacle Data Systems. Replicating their facilities at Citizens would substantially add to the capital equipment acquisition and maintenance costs necessary to accommodate Citizens' transaction volumes. Further, the likelihood of dramatic fluctuations in the policy-in-force count (not the least of which is a projected 46% reduction to 794,308 policies as a result of proposed coverage changes<sup>27</sup>) requires the ability to scale operations quickly while maintaining a reasonable capital equipment and operating cost structure. Further, the increase in capital equipment expenditures associated with developing facilities to accommodate policy printing and mailing would impart future financial burdens on Citizens as fully depreciated or obsolete equipment is retired and replaced. Finally, the use of multiple policy processing environments for personal and commercial lines and the existing contractual requirement to utilize CSC as the prime vendor<sup>28</sup> for commercial lines policy

<sup>26</sup> Source: Exhibit 3: *UW Items Proc 2012* provided by Jonathan Owen, Enterprise Performance Metrics Manager on April 10, 2012 (forwarded by Deborah Murphy, Vice President, Underwriting on April 11, 2012).

<sup>27</sup> Source: Exhibit 8: *Citizens Presentation to the Financial Services Commission, December 6, 2011*.

<sup>28</sup> Though requested, we were not provided with a copy of the contract between Citizens and CSC (possibly due to confidentiality provisions).



issuance eliminates the ability to achieve the economies of scale we would expect by consolidating vendors until the CSC contract term expires and the Core Project is completed.

As such, policy processing at Citizens appears to operate as efficiently as practicable given the costs associated with equipping and staffing an internal capability, and the various constraints Citizens must endure until existing policy administration systems are consolidated (which is expected as a result of the Core Project) and the CSC contract expires.

### Cost-Benefit Analysis

Because all policy assembly, printing and mailing processes used to produce and distribute Citizens' policies, endorsements, invoices and notices is completely outsourced, and the study request calls for "[making] recommendations on the relative costs and benefits of outsourcing various policy issuance and service functions," there is no additional benefit to be derived from outsourcing what we have consolidated into the "Policy Processing" category.

*Personal lines.* To illustrate current costs and opine on their reasonableness, we note that personal residential policies were processed at a cost to Citizens of \$9.6 million during 2011, or approximately \$6.72 per policy, including all newly issued policies, policy renewals, endorsements, invoices and notices.

A review of CEDAR costs for 2011 reveal the processing of 10,734,750 documents at an average cost of \$0.11 per document, and the electronic delivery of 7,269,546 documents at an average cost of \$0.20 per document. For the purposes of this analysis, we can infer that 3,465,204 documents were transmitted by CEDAR to Pitney-Bowes (the difference between the 10,734,750 documents processed and the 7,269,546 documents delivered by CEDAR) for processing and mailing.<sup>29</sup>

Payments to CEDAR totaled approximately \$2,636,708 in 2011 for processing and electronic delivery services<sup>30</sup>, while payments to Pitney-Bowes totaled \$6,961,050 in 2011, representing \$2,015,395 in

<sup>29</sup> Source: Exhibit 9: CEDAR Annual Invoice Tracking (2011).

<sup>30</sup> Source: Exhibit 9: CEDAR Annual Invoice Tracking (2011).

processing costs (including returned mail), \$5,026,627 in passed-through postage and (\$80,972) in miscellaneous credits.<sup>31</sup>

Dividing the sum of \$2,636,708 paid to CEDAR and \$6,961,050 paid to Pitney-Bowes in 2011 by the total personal lines policy count of 1,428,134 yields an average outsourcing cost to service (i.e., assemble, print, deliver all policy documents, endorsements, invoices and notices) each personal lines policy for 2011 of \$6.72, less than four-tenths of one percent of the average policy premium of \$1,772.<sup>32</sup> Exclusive of postage, policy servicing costs totaled \$1,934,423, or an average of \$3.20 per policy, or less than two-tenths of one percent of the average policy premium.

*Commercial lines.* Payments to CSC on behalf of Pinnacle Data Systems for printing, postage and stock charges associated with commercial lines policy issuance, endorsements, invoices and notices totaled \$142,029 in 2011<sup>33</sup> (approximately 55% of which is postage) to service 55,504 policies, or an average cost per policy of \$2.55 for which the average premium is \$10,472.<sup>34</sup> This figure is more appropriately compared to the Pitney-Bowes cost associated with personal lines processing, which is \$2.01 per policy, since we understand that CSC performs other processing activities for which Citizens is charged that are not immediately separable from the aggregate payment to CSC.

## Recommendations

In reviewing Policy Processing activities at Citizens, there are several areas of opportunity that we believe could enhance the efficiency of existing operations, including:

- *Increase electronic delivery of policy packages.* The promotion of paperless options for policyholders and their acceptance of an increase in electronic deliveries of policy documents (including policy packages, endorsements, invoices and notices) would relieve Citizens of a significant portion of its Policy Processing expense. With more than \$5.1 million in annual postage expenditures related to policy servicing activities, this represents an area ripe for

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<sup>31</sup> Source: Exhibit 10: *PB Annual Invoice Tracking (2011)*

<sup>32</sup> To see how average personal lines policy premium was derived, see the “Policy Processing” tab of Appendix E, *Citizens SB408 Study Master Workbook*.

<sup>33</sup> Source: Exhibit 11: *April 17, 2011 email from David Ochoa*.

<sup>34</sup> To see how average commercial lines policy premium was derived, see the “Policy Processing” tab of Appendix E, *Citizens SB408 Study Master Workbook*.

reengineering. We expect the successful completion of the Core Project to facilitate the implementation of this recommendation.

- *Consolidate processing and distribution vendors.* We would expect the consolidation of vendors, irrespective of the deployment of the new solutions anticipated with the completion of the Core Project, to provide Citizens with a financial benefit. We are aware, however, that the terms of the current contract with CSC may prevent Citizens from pursuing such a consolidation until that contract term expires.
- *Perform policy assembly in house.* It should be noted that this recommended solution is being contemplated in connection with the ongoing Core Project. The adoption of a document management solution that organizes policy forms and manages attachment rules in a manner that assembles complete policy packages and readies them for delivery (either electronically or via postal mail) would relieve Citizens of an annual recurring expense that exceeds \$2 million. The cost of such a solution needs to be considered (including software acquisition, infrastructure, integration, deployment and maintenance costs), however, we are aware that a solution currently contemplated as a component of the Core Project is expected to be implemented at a cost well below the current annual spend, suggesting the potential for a significant return on investment.

## Underwriting Property Inspections

Citizens began conducting underwriting property inspections in 2010 in an effort to correct underwriting oversights that yielded lower premiums than Citizens' rating plans permit by providing policyholders with erroneous or unearned credits. In addition, Citizens has been compelled to perform sinkhole inspections in response to SB408 and the disproportionate indemnity and loss adjustment expenses associated with a growing number of sinkhole claims initiated by Citizens' policyholders. Accordingly, underwriting inspections fall generally into two major categories: wind mitigation inspections (with appraisals and general construction inspections to be performed in the future), and sinkhole inspections. All Citizens' inspections are currently outsourced.

### Personal Lines

*Wind mitigation inspections.* Wind mitigation inspections are currently performed by three outsourcing vendors (Mueller, Quality Built and Inspection Depot) at a cost to Citizens of \$105 per personal lines inspection. As of March 31, 2012, Citizens had completed wind mitigation inspections on 155,473 personal residential properties that are expected to yield an estimated gross premium increase of \$93.4 million and an estimated net return of \$71 million on renewal (exclusive of policyholder attrition) (see Table 9, *Personal Residential Property Wind Mitigation Inspection Results, Program-to-Date*, in the "Cost-Benefit Analysis" section below).

Through March 31, 2012, wind mitigation inspections were performed to re-inspect properties in a process that took about 63 days on average from initiation to completion.<sup>35</sup> Inspection reports that contain changes to the initial underwriting profile are submitted to MGI for policy premium adjustments at a cost to Citizens of \$26 per policy.<sup>36</sup> Additionally, Citizens has instituted an Inspection Outreach program to inform policyholders of pending changes to their premium (i.e., on renewal) when inspection report results differ from the original policy risk profile, and communicate ways to reduce their premiums in the future.

<sup>35</sup> Source: Exhibit 12: *February 23, 2012 Citizens Board of Governors Meeting Minutes Transcript*, p. 21, retrieved from [www.citizensfla.com](http://www.citizensfla.com) on April 23, 2012.

<sup>36</sup> Source: Exhibit 13: *March 23, 2012 email from Keri Dennis*, Program Manager, Insurance Operations. These amounts are also reflected in the MGI payments detailed in the Underwriting section of this report.

*Sinkhole inspections.* Citizens utilizes nine engineering firms to perform underwriting sinkhole inspections on new business applications, and employs temporary staff to process the inspection results. The contract cost is \$180 per personal lines sinkhole survey,<sup>37</sup> which is borne by Citizens and each policyholder in equal proportion (i.e., each bears 50% of the \$180 inspection expense). A total of 1,579 personal lines sinkhole inspections were completed during 2011, commencing in August, at a cost to Citizens of \$142,110.<sup>38</sup>

### Commercial Lines

*Wind mitigation inspections.* As of March 31, 2012, Citizens had completed wind mitigation inspections on 2,645 commercial properties that yielded an estimated gross premium increase of \$1.8 million and an estimated net return of \$926,000 (see Table 10, *Commercial Property Wind Mitigation Inspection Results, Program-to-Date*, in the “Cost-Benefit Analysis” section below).

*Sinkhole inspections.* No sinkhole inspections were performed for commercial lines policies during 2011. Commercial sinkhole inspections are scheduled to commence in April or May, 2012<sup>39,40</sup> at a cost to Citizens of \$240 per building (3 stories or less), \$300 (4 – 6 stories) or \$60 per hour (for buildings 7 stories or higher).

### Findings

*Wind mitigation inspections.* As of March 31, 2012, Citizens had completed 158,135 personal and commercial lines wind mitigation inspections which resulted in an estimated gross premium increase of \$95.2 million, and an estimated net return of \$71.9 million (i.e., net of inspection fees) at the time the inspections were completed. To date, 68% of inspections have resulted in a change to premium, of which 62% involved increase (removal of credits), and 6% involved decrease (\$3.8 million in additional credits). The estimated net return on inspections completed to date will not be realized until the future renewal dates of the policies associated with them. In addition, actual premium changes at renewal may vary due to other non-related changes such as rating, location data, assessments, cancellations or other

<sup>37</sup> Source: Exhibit 15: *Sinkhole Pricing Schedule* (Exhibit 1 to Citizens Sinkhole Survey Contract dated July 17, 2011).

<sup>38</sup> Source: Exhibit 16: *UW Sinkhole Tracking -3-31-2012* provided by Eric Ordway, Senior Director, Insurance Operations on April 26, 2012.

<sup>39</sup> Source: Exhibit 12: *February 23, 2012 Citizens Board of Governors Meeting Minutes Transcript*, p. 21, retrieved from [www.citizensfla.com](http://www.citizensfla.com) on April 23, 2012.

<sup>40</sup> Source: Exhibit 17: *April 26, 2012 email from Eric Ordway*, Senior Director, Insurance Operations.

factor, and the estimate does not take into consideration policies inspected that later cancel or are non-renewed.<sup>41</sup> Accordingly, it is appropriate to apply a discount to the anticipated increase in premium consistent with Citizens' annual policyholder attrition rate.<sup>42</sup>

*Sinkhole inspections.* The impact to Citizens' book of business as a result of the surveys is a dramatic reduction in sinkhole exposure; while approximately 100% of sinkhole coverage applications were approved prior to the program being initiated, the current approval rate is just 30%.<sup>43</sup>

### Cost-Benefit Analysis

*Wind mitigation inspections.* Program results from inception to date have been exceptional, with an estimated return on investment of 317% for personal lines and 107% for commercial lines. A breakdown of the expenses and expected returns on renewal from Citizens' wind mitigation inspection program for personal lines policies is provided in the table below:

	Total	Per Inspection
<b>Number completed</b>	155,473	
<b>Expenses</b>		
Inspections Expense	\$ 16,324,665.00	\$ 105.00
Project Staffing	\$ 3,919,474.00	\$ 25.21
Other Expenses	\$ 660,760.00	\$ 4.25
Systems	\$ 1,511,198.00	\$ 9.72
<b>Total Expenses</b>	<b>\$ 22,416,097.00</b>	<b>\$ 144.18</b>
<b>Return</b>		
Number Completed	155,473	
<b>Gross Estimated Premium Impact (\$)</b> (includes all policies regardless of renewal date)	<b>\$ 93,435,368.00</b>	<b>\$ 600.97</b>
<b>Net Results</b>	<b>\$ 71,019,271.00</b>	<b>\$ 456.79</b>
Return on Investment (ROI)	317%	317%

Table 9: Personal Residential Property Wind Mitigation Inspection Results, Program-to-Date<sup>44</sup>

<sup>41</sup> Source: Exhibit 14: *BOG Monthly Inspection Report – March 2012* provided by Eric Ordway, Senior Director, Insurance Operations.

<sup>42</sup> It is also important to note that Citizens is charged a fee of \$26 for each inspection report processed by MGI that is not associated with new business. These costs are also reflected in the outsourcing costs presented in the "Underwriting" section of this report.

<sup>43</sup> Source: Exhibit 18: *April 26, 2012 email from Keri Denis*, Program Manager, Insurance Operations.

<sup>44</sup> Source: Exhibit 14: *BOG Monthly Inspection Report – March 2012* provided by Eric Ordway, Senior Director, Insurance Operations.

The breakdown of expenses and expected returns on renewal from commercial lines wind mitigation inspections is provided in the table below:

	Total	Per Inspection
<b>Number completed</b>	2,645	
<b>Expenses</b>		
Inspections Expense	\$ 740,600.00	\$ 280.00
Project Staffing	\$ 87,497.00	\$ 33.08
Other Expenses	\$ 11,188.00	\$ 4.23
Systems	\$ 28,566.00	\$ 10.80
<b>Total Expenses</b>	<b>\$ 867,851.00</b>	<b>\$ 328.11</b>
<b>Return</b>		
Number Completed	2,645	
<b>Gross Estimated Premium Impact (\$ (includes all policies regardless of renewal date)</b>	<b>\$ 1,795,157.00</b>	<b>\$ 678.70</b>
<b>Net Results</b>	<b>\$ 926,306.00</b>	<b>\$ 350.59</b>
Return on Investment (ROI)	107%	107%

Table 10: Commercial Property Wind Mitigation Inspection Results, Program-to-Date<sup>45</sup>

*Sinkhole inspections.* Given the reduction in policy applications accepted with a sinkhole coverage component from 100% to 30%, we would expect at least a corresponding reduction in paid losses from sinkhole claims (perhaps in greater proportion to the reduction in exposure since the worst risks are being declined), which totaled \$143.4 million in indemnity payments, and \$49.7 million in loss adjustment expenses in 2011.<sup>46</sup>

## Recommendations

With regard to an independent assessment, the inspection program is undeniably beneficial to Citizens. Our recommendations include the following:

<sup>45</sup> Source: Exhibit 14: *BOG Monthly Inspection Report – March 2012* provided by Eric Ordway, Senior Director – Insurance Operations.

<sup>46</sup> Source: Exhibit 33: *Citizens response to info request (5.22.2012)*. Represents paid losses in 2011 on sinkhole claims initiated from 2003 through 2011.

- *Expand the program.* The success of the wind mitigation and sinkhole inspection programs suggests expansion of both inspection types to a larger number of policies will yield significant additional benefits.
- *Consolidate inspection activities.* We would expect the consolidation of construction inspections and appraisals with wind mitigation inspections to provide cost savings to Citizens by eliminating the need for multiple site visits by inspectors, and the additional inspections to yield even greater returns.
- *Evaluate current fee structure with MGI.* Given the fee schedule currently in force with MGI for underwriting new business applications (which may include a wind mitigation inspection report processing component), we suggest evaluating the fee payable to MGI for processing inspection reports. At \$26 per report, it exceeds the average cost to underwrite a new policy.



## Claims Adjustment

Citizens' claims organization manages the claims lifecycle, typically after a first notice of loss ("FNOL") is received by Citizens' Consumer and Agent Services unit. The focus of this report is the claims loss adjustment process post-FNOL, inclusive of all investigative activities employed to determine the validity and appropriate amounts to be paid in the event a policyholder suffers a loss and initiates a claim. To manage these activities, the claims organization is staffed by a combination of internal and external (field) employee staff and internal and external (field) contract staff mostly employed by independent adjusting firms contracted by Citizens.

### Counting Claims

Citizens classifies claims using various methods, including severity, peril,<sup>47</sup> the portion of the claims lifecycle being managed or other criteria. For consistency in preparing this report, we have adopted the five categories used by Citizens that map most readily to the departments that comprise the claims organization, described below:

- *Non-catastrophe claims* are regular personal lines claims from Citizens' policyholders or their proxies;
- *Catastrophe claims* are claims associated with a catastrophic event;
- *Commercial claims* are claims from Citizens' commercial policyholders or their proxies;
- *Shared Services claims* are claims on which Citizens' Shared Services unit assists in notifying the appropriate parties when a claim rejected or for which no policy is in force, and includes claims for which recoveries from subrogation or salvage are being pursued; and
- *LDCU claims* are claims received by Citizens' Litigation and Disputed Claims Unit ("LDCU") or reopened claims in mediation, subject to appraisal, resulting from a late FNOL or being litigated.

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<sup>47</sup> Examples of the categories used to differentiate claims at Citizens include burglary, lightning and theft ("BLT") claims, dropped object claims, liability claims, etc. A comprehensive list of perils is included on the "Type of Claim" tab in Exhibit 19: 2011 Claim Stats.

Due to the extensive use of external professional resources (including experts and outside counsel) and their relatively long resolution times, LDCU claims are treated separately in this report so as not to unduly weight the costs associated with undisputed claims.

To determine a 2011 claim count for the Study, Citizens provided for each category of claim listed above the number of claims still pending at year-end, 2010, new claims received during 2011 via FNOL or new assignment to LDCU, and reopened claims. Accordingly, the resulting claim count of 132,510 represents claims that were in process for at least a portion of the claims management lifecycle in 2011. Claim counts are summarized in the table below.

	Pending, year-end 2010	New claims or assignments	Reopened during 2011	Total
<b>Non-Catastrophe</b>	7,471	64,757	23,259	95,487
<b>Catastrophe</b>	39	101	880	1,020
<b>Commercial</b>	77	1,186	264	1,527
<b>Shared Services</b>	2,819	4,076	0	6,895
<b>LDCU</b>	7,464	20,117	0	27,581
<b>Total</b>	17,870	90,237	24,403	<b>132,510</b>

Table 11: 2011 Claim Counts<sup>48</sup>

Among the total number of claims in process during 2011, 82,537 non-catastrophe, 976 catastrophe, 1,437 commercial lines, 4,476 Shared Services (mostly recoveries from salvage or subrogation) and 18,241 LDCU claims were closed during 2011, with 10,517 non-catastrophe, 44 catastrophe, 98 commercial, 2,498 Shared Services and 10,487 LDCU claims still pending at year end, 2011.<sup>49</sup>

### Claims Organization Staffing

Citizens utilizes a mix of employee and contract personnel to staff its claims organization,<sup>50</sup> including a variety of professional services from outside counsel, engineers and loss mitigation experts among others, on an *ad hoc* basis. Citizens' internal staff comprises approximately 208 employee staff (200 in personal lines and 8 in commercial lines) and an additional 148 contract or temporary staff (140 in

<sup>48</sup> Source: Exhibit 33: *Citizens Response to Information Request (5.22.2012)* provided by Gregory Golson, Claims Consultant on May 22, 2012.

<sup>49</sup> Source: Exhibit 33: *Citizens Response to Information Request (5.22.2012)* provided by Gregory Golson, Claims Consultant on May 22, 2012.

<sup>50</sup> Claims received by Citizens are classified in one of five degrees of severity, with Severity 1 claims being the least severe and Severity 5 claims being the most severe. The more complex Severity 4 and 5 claims are generally handled by internal staff, while the less complex Severity 1, 2 and 3 claims are outsourced.

personal lines and 8 in commercial lines) who manage both personal and commercial lines claims.<sup>51</sup> In addition, due to their impact, Citizens has added specialist staff to ensure they're properly addressing sinkhole claims, which represented approximately 6% of claims in 2011, but nearly 67% of loss reserves.<sup>52</sup> Citizens also outsources claims adjustment activities to 27 Independent Adjusting Firms ("IA Firms") who currently make available some 539 desktop and field adjusters for claims processing activities and ten General Adjuster/Executive General Adjuster ("GA/EGA") firms that provide outsourced commercial claims desk and field adjustment services for normal operations.<sup>53</sup> Notably, Citizens' vendor database includes records of more than 9,700 individual adjusters available to be deployed in the event of large claim events, such as a hurricane or other catastrophe.<sup>54</sup> To ensure all claims staff are properly indoctrinated into the best known way to evaluate claims, Citizens' claims organization has created the *Citizens Property Best Claim Practices* and *Claims Estimating Guidelines* manuals, both of which are updated annually to reflect lessons learned during the course of the prior year, while an in-house quality assurance team provides regular claims file reviews and feedback on claims handling performance to "calibrate" the activities of adjusters.

The vast majority of Citizens' claims management employees are dedicated to managing personal lines claims. Similarly, most IA Firm personnel are assigned personal lines claims adjustment activities, a function of Citizens' claims distribution (commercial lines policyholders initiated just 1.9% of Citizens' 2011 first notices of loss<sup>55</sup>). Commercial lines claims are handled by a combination of internal staff and IA Firm staff (with GA/EGA firms being added in 2012). In addition to adjusting personal lines claims, several IA Firms provide services to adjust commercial claims.

### Internal Operations

*Personal Lines.* Citizens policyholders initiated a combined 64,757 non-catastrophe personal lines claims during 2011, exclusive of rejected and NPIF claims and claims managed by Citizens' LDCU.<sup>56</sup> In addition,

<sup>51</sup> Source: Exhibit 21: *Citizens Discovery Workbook – Claims Adjustment* provided by Deborah Rambo, Administrative Assistant to the Vice President, Claims, April 26, 2012.

<sup>52</sup> Source: Conversation with Gregory Golson, Claims Consultant on May 31, 2012.

<sup>53</sup> Note that GA/EGA firms contracted specifically to adjust commercial lines claims were not engaged until 2012. During 2011, commercial lines claims adjustment outsourcing services were provided by several of the 27 IA Firms then under contract.

<sup>54</sup> Source: Staff interview with Lance Malcolm, Vice President, Claims Operations on February 15, 2012.

<sup>55</sup> Source: Exhibit 19: *2011 Claim Stats* provided by Gregory Golson, Claims Consultant on April 18, 2011 (forwarded by Eric Ordway on April 19, 2011).

<sup>56</sup> Source: Exhibit 22: *FNOL Analysis 2011 YEAR* provided by Gregory Golson, Claims Consultant on April 23, 2011.

some 7,471 personal lines claims remained open from prior years and 23,259 were reopened during 2011. Of new claims received, approximately 89% were outsourced where one or more claims adjustment activities were assigned to an IA Firm.<sup>57</sup> Citizens internal staff, however, retains an oversight role and manages IA Firm relationships, provides technical assistance when IA Firm authority levels are surpassed and internal approvals are needed, and participates in discussions regarding claim denials or other challenging situations. Citizens' maintenance of an active role, even with outsourced claims, is integral to quality and satisfactory claims resolution. Consequently, individual claims have varying amounts of participation between Citizens' internal staff and IA Firm (i.e., outsourced) staff.<sup>58</sup>

Citizens maintains a staff of claims management employees at its Jacksonville, Florida location. Personal lines claims are managed by a complement of claims staff who handle "standard" claims; sinkhole claims; litigated and disputed claims; special investigations-related claims; and claims recoveries, including claims in salvage or subrogation. Citizens' personal lines claims management employee positions are listed in the table below.

Position	Number
Asst. Directors	3
Consultant	1
Sr. Director	1
Directors	2
Administrative Support	4
Desk Adjusters	10
Field Adjusters	24
Sinkhole Adjuster	19
Subrogation Recovery	3
Manager	6
Catastrophe Managers	3
CTC (Claims Technical Coordinator)	12
Sr. CTC	6
LAE Coordinator (Hourly)	1
MCM Supervisor	7
Field Supervisor	3
Desk Supervisor	5
Large Loss Specialists	5

Table 12: Personal Lines Claims Management Employees

<sup>57</sup> Source: Exhibit 23: *Citizens Claims Distribution Jun 11 to Mar 12* provided by Gregory Golson, Claims Consultant on April 19, 2012.

<sup>58</sup> Resource allocation on a per-claim basis was unavailable at the time this report was prepared, making infeasible a precise quantitative comparison between internally-managed and outsourced claims.

*Commercial Lines.* Citizens received a combined 1,330 commercial lines claims during 2011,<sup>59</sup> 1,186 of which were handled by Citizens' commercial claims business unit.<sup>60</sup> In addition, 77 commercial claims remained open from prior years and 264 were reopened. Of new claims received, 323 (24.3%) were included a task assignment to an IA Firm.<sup>61</sup> The balance were handled entirely by Citizens' in-house staff.

Exclusive of staff utilized for commercial LDCU claims (described below), Citizens employs a staff of five commercial lines claims personnel, as well as five additional contract staff who perform services in Citizens' offices, as depicted in the table below.

Position	Number
Commercial Specialist	5

Table 13: Commercial Lines Claims Management Employees

*Shared Services.* In addition to those staff members directly involved in the claims adjustment process for personal or commercial lines claims, a Shared Services unit handles certain aspects of the claims lifecycle, including adjuster dispatch, check processing, commercial lines FNOL set up, LDCU case set up, subrogation, salvage, special investigations and quality assurance. Shared Services staff positions are listed in the table below.

Position	Number
SIU Manager	1
SIU Supervisors	1
SIU Investigators	12
Recovery Manager	1
Recovery Specialists	3
QA Manager	1
QA Supervisors	2
QA Specialists	10
Support Managers	1
Support Supervisors	4
Support Front line	20

Table 14: Shared Services Employees

<sup>59</sup> Source: Exhibit 19: *2011 Claim Stats* provided by Gregory Golson, Claims Consultant on April 18, 2011 (forwarded by Eric Ordway on April 19, 2011).

<sup>60</sup> Source: Exhibit 22: *FNOL Analysis 2011 YEAR* provided by Gregory Golson, Claims Consultant on April 23, 2011..

<sup>61</sup> Source: Exhibit 19: *2011 Claim Stats* provided by Gregory Golson, Claims Consultant on April 18, 2011 (forwarded by Eric Ordway on April 19, 2011).

Citizens' internal claims adjustment employee costs, exclusive of employees in the litigated and disputed claims unit (LDCU) are summarized in the table below.

Department	Total Cost <sup>62</sup>
Personal Lines	\$ 9,661,569
Commercial Lines	\$ 574,830
Shared Services	\$ 3,912,970
<b>Total</b>	<b>\$ 14,149,368</b>

Table 15: Claims Internal Staff Payroll, ex-LDCU

### Outsourced Operations

*Personal Lines.* Citizens has entered into agreements with 27 IA Firms for the provision of personal lines claims adjustment services. Relationships with IA Firms are managed by Citizens' Insurance Operations staff and supervised by Citizens' claims organization staff (i.e., they do not act with complete autonomy). All IA Firms enter into a standard agreement (first dated September 17, 2008). The standard agreement has been modified by amendment four times since the initial contract date, including (i) the imposition of a facilities/technology charge of \$15.00 per day per IA Firm resource performing services at a Citizens' office location for facilities, computer and telephone usage; (ii) the addition of litigation and disputed claims unit ("LDCU") adjusters; (iii) the addition of rate tables for Managed Claims Model and Task Assignment Model claims as more fully described below; and (iv) a provision permitting Citizens to make modifications to the IA Firm fee schedule based on market conditions and national demand. IA Firms provide Citizens with both internal and field staff. Internal staff are charged to Citizens by IA Firms at a day rate (see table below), while field adjusters provide services to Citizens for which Citizens is charged a fee based on the gross claim amount ("GCA") of the claim to which they're assigned upon closure.

Position	Number	Rate/Day
Day-Rate Desk Adjusters - Non-LDCU	12	\$ 450
IA Sinkhole	27	\$ 450
IA MCM Team Lead	31	\$ 600
IA Subrogation	5	\$ 550
IA Quality Assurance	6	\$ 600

Table 16: Personal Lines Claims "Day Rate" Contractors

<sup>62</sup> Figures include a salary load of 10% for payroll taxes and benefits and 25% for overhead allocation.

Personal lines claims adjustment activities outsourced to IA Firms are divided into two broad categories that represent the extent of their claims handling responsibility. Each category is associated with its own fee schedule that calls for payment to the IA Firm based on either (i) the day rate in the table above if the resource is located at a Citizens office, or (ii) the gross claim amount (“GCA”)<sup>63</sup> of the claim being handled (higher GCA claims earn the IA Firm a higher fee) in the event the claim is managed in the field or at a location outside of a Citizens office (i.e., at an IA Firm office location). The two categories include:

- The *Managed Claims Model* (“MCM”), which is defined as “the assignment of a property damage claim to a Vendor which it must adjust, oversee, manage and handle to conclusion”<sup>64</sup> and as such, represents a claim for which the IA firm bears complete responsibility (other than the intake of first notices of loss, which are managed through Citizens’ call center). However, even MCM claims require Citizens’ staff intervention when defined levels of authority are exceeded (e.g., indemnity payments exceeding \$20,000); and
- The *Task Assignment Model* (“TAM”), which is defined as the assignment of a property [damage] claim to a Vendor which requires that Vendor to complete specific claim tasks such as complete or partial evaluation of damages to include scoping, estimating and pricing covered repairs at the direction of the assigned Citizens inside adjuster responsible for the adjustment of the claim.”<sup>65</sup>

IA Firm resources review first notices of loss that have been received by one of two call center vendors contracted by Citizens (descriptions of which may be found in the Customer Service Calls section, *infra.*) and entered into Citizens’ Claims Tracking System (“CTS”). New claims are assigned to adjusters by dispatchers in Citizens’ Shared Services based on a variety of selection criteria, including last time utilized, geographic location, skills, availability and performance. Critical performance metrics are maintained for each IA Firm under contract, with top performers given preference for new claim assignments. IA Firm pricing is uniform across all vendors.

<sup>63</sup> Gross Claim Amount (“GCA”) is “the lesser of the policy limits or the agreed cost to repair or replace before application of depreciation, deductible or other applicable limit” unless a greater amount is approved by Citizens. (source: Exhibit 24: *Amendment #3 to 2008 Independent Adjuster Services Agreement for Non-Catastrophic and Catastrophic Claims* dated May 18, 2009, pp. 15, 16.

<sup>64</sup> Source: Exhibit 24: *Amendment #3 to 2008 Independent Adjuster Services Agreement for Non-Catastrophic and Catastrophic Claims* dated May 18, 2009, page 2.

<sup>65</sup> Source: Exhibit 24: *Amendment #3 to 2008 Independent Adjuster Services Agreement for Non-Catastrophic and Catastrophic Claims* dated May 18, 2009, page 3.

*Commercial Lines.* In addition to multiple IA Firms contracted to provide commercial lines claims adjustment services, Citizens has entered into agreements with ten GA/EGA firms that specialize in commercial property claims adjusting services commencing in 2012. GA/EGA firms utilized by Citizens employ some 450 credentialed adjusters, with a commitment to make available a total of 850 credentialed adjusters by the end of 2012.<sup>66</sup> Commercial lines claims IA Firm adjusters are priced at a higher rate than personal lines adjusters, as depicted in the table below.

Position	Number	Rate/Day
CA Desk Adjuster	4	\$ 600
GA Desk Adjuster	1	\$ 1,000

Table 17: Commercial Lines Claims Contractors

To facilitate our review of claims operations, 2011 payments to IA Firms for commercial lines claims were combined with payments made for personal lines claims (i.e., payments made to IA Firms for personal lines claims are not differentiated from payments made for commercial lines claims in the accounting reports provided by Citizens), which totaled \$44.6 million in 2011, exclusive of LDCU claims adjustment activities.<sup>67</sup> An additional \$613,000 was paid for temporary Shared Services support staff charged to Citizens at a rate of \$160 per day.<sup>68</sup> Outsourced and temporary contract staff positions are summarized in the table below.<sup>69</sup>

Position	Staff Count	Cost/Day	Cost (2011)
<b>Personal Lines</b>			\$ 44,639,849.00
Day Rate Adjusters, non-LDCU	12	\$ 450.00	
IA Sinkhole	27	\$ 450.00	
IA MCM Team Lead	31	\$ 600.00	
IA MCM Adjusters	469	See Exhibit 24	
IA Subrogation (Shared Services)	5	\$ 550.00	
IA Quality Assurance (Shared Services)	6	\$ 600.00	
<b>Commercial Lines</b>			
CA Desk Adjusters	4	\$ 600.00	
GA Desk Adjusters	1	\$ 1,000.00	
<b>Other Shared Services</b>			

<sup>66</sup> Source: Exhibit 25: *Insurance Operations Vendor Management Matrix (9.26.2011)* provided by Eric Ordway, Senior Director, Insurance Operations.

<sup>67</sup> Source: Exhibit 30 - *2011 Vendor Spend - Preliminary*

<sup>68</sup> Source: Exhibit 32 - *Request for Information - Answers (5.22.2012)*

<sup>69</sup> Staff counts represent available staff at year end, 2011 and do not necessarily represent the total number of staff engaged during 2011.



Support Temps	23	\$ 160.00	\$ 613,010.00
<b>Total, IA Firm/Contract Staff</b>			<b>\$ 45,252,859.00</b>

Table 18: Claims Adjusting Outsourcing Costs

### Litigated and Disputed Claims

Among claims unable to be resolved through the normal claims adjusting process and consequently assigned to Citizens' LDCU, 7,464 were prior-year claims that remained open at year-end 2010, and 20,117 were either 2011 first notices of loss or were assignments to LDCU resulting from reopening previously closed claims.<sup>70</sup> Accordingly, for the purposes of this report, a total of 27,581 LDCU claims were managed through some portion of the claims management lifecycle during 2011.

To manage LDCU claims, a variety of specialists are engaged, including external subject matter experts and outside counsel. In addition, disputed claims tend to take significantly longer to resolve. These factors contribute to a substantially higher average cost per claim than non-disputed claims. LDCU staff positions are listed in the table below.

Position	Number
<b>Personal Lines</b>	
Appraisal Adjusters	6
Mediation Adjusters	1
Liability Adjusters	3
Litigation Adjusters	10
LDCU Managers -Personal	5
LDCU Supervisor	4
<b>Commercial Lines</b>	
Litigation Specialist	2
Litigation Manager	1

Table 19: LDCU Claims Management Employees

Total 2011 payroll for Citizens LDCU employees was approximately \$2.1 million, or \$2.9 million after applying reasonable allocations for overhead (25%), and payroll taxes and benefits (10%).<sup>71</sup> To assist in the management of LDCU claims, Citizens utilizes IA Firm staff at a rate of \$550 per day representing a 2011 spend of \$10.2 million.<sup>72</sup> Additionally, LDCU claims incurred payments of \$29.8 million to outside

<sup>70</sup> Source: Exhibit 22: *FNOL Analysis 2011 YEAR* provided by Gregory Golson, Claims Consultant on April 23, 2011.

<sup>71</sup> Source: Exhibit 21: *Citizens Discovery Workbook – Claims Adjustment* provided by Deborah Rambo, Administrative Assistant to the Vice President, Claims, April 26, 2012.

<sup>72</sup> Source: Exhibit 34: *LDCU Spend Program 2011* provided by Gregory Golson, Claims Consultant, on May 25, 2012.

counsel and \$16.4 million for subject matter experts<sup>73</sup> during 2011. LDCU costs are summarized in the table below.

Position	Rate/Day	Cost (2011)
Citizens LDCU employees	N/A	\$ 2,901,982
Day Rate Desk LDCU Adjusters (Personal)/Litigation Specialists (Commercial)	\$ 550	\$ 10,174,657
Outside Counsel	N/A	\$ 29,795,054
Additional Experts	N/A	\$ 16,403,326
<b>Total</b>		<b>\$ 59,075,219</b>

Table 20: LDCU Claims Management Costs

## Findings

Making direct comparisons between the efficiency of Citizens' claims management staff and that of IA Firm staff is complicated by several factors, including the fact that (i) a much higher proportion of complex claims (high-value or more severe claims) that involve far more effort to resolve are managed entirely by in-house staff; (ii) TAM claims that involve IA Firms vary with respect to the specific type and number of tasks assigned to an IA Firm adjuster, depending upon the claim; (iii) MCM claims that exceed the IA Firm authority level for payment must be referred back to Citizens; (iv) most claims involve some level of Citizens' employee oversight; and (v) there is additional overhead associated with IA Firm costs not directly reflected in the contract pricing, including purchasing and contracting, contract administration, training, indoctrination, certification and workload balancing activities that are integral to the initiation, maintenance and management of multiple vendor relationships. Further, outsourced staff members are highly integrated with Citizens claims team members, and a single claim is often touched by multiple department employees within Citizens, internal contractors, employee and IA Firm field adjusters, outside counsel, appraisers, loss mitigation specialists and other professionals, depending upon the type and complexity of the claim. As such, simply comparing a cost per outsourced claim that divides aggregate fees paid by transaction volume with a cost per internally-managed claim that divides salary and overhead expenses by transaction volume will yield an inappropriate result that may lead the reviewer to erroneous conclusions.

Inasmuch as this Study aims to determine the efficiency with which Citizens utilizes outsourcing while maintaining acceptable levels of agent and customer satisfaction, we note the reduction in claims-

<sup>73</sup> Source: Exhibit 32 - Request for Information - Answers (5.22.2012).

related complaints from 1.49% of claims handled in January 2009 to 0.89% in March 2011.<sup>74</sup> Further, prior to 2011, the vast majority (approximately 85%) of claims were simply “tasked” to IA Firms, whereas after 2010, the “Managed Claims Model” was adopted and IA Firms began to manage the entire claims lifecycle. This implies a strong correlation between the current Managed Claims Model and customer satisfaction, one of Citizens’ principal corporate objectives<sup>75</sup> and a mandate of SB408. Appropriately, the number of MCM claims rose steadily to represent approximately 40.5% of newly initiated personal lines non-catastrophe claims through 2011, subsequently increasing to a current level of approximately 90%.<sup>76</sup> We also note the codification of operating procedures, and a mature quality assurance function to “calibrate” the activities of internal and outsourced claims adjusters and ensure they act according to known best practices.

In addition, the uniqueness of Citizens’ market position and risk exposure mandates an ability to rapidly scale their operations in response to large claim events. During the 2004 and 2005 hurricane seasons, for example, Citizens experienced a dramatic increase in claims volume (more than 150,000 in 2004; more than 200,000 in 2005, or *nearly ten times their regular claim volume at the time*). One can infer that similar events would call for a rapid tenfold increase in available claims adjustment staff, a feat that could only reasonably be accomplished by having a large population of properly trained resources ready and able to join forces with Citizens’ staff on a moment’s notice. Conversely, during relatively quiet periods with little or no major storm activity, such as the period from 2006 to present, it is important to manage costs by not maintaining a large staff of idle claims adjusters in the absence of major catastrophic events, given the unpredictability of hurricanes, tornados and other weather-related perils to which Citizens is exposed in the state of Florida. Notably, Citizens total in-force policy count has increased by 75% since 2005; as such, future similarly active hurricane seasons could conceivably produce a doubling of the claim volume experienced during the 2004 and 2005 claim years.

Citizens’ exposure to catastrophic events that could potentially impact the entire state of Florida also necessitates the availability of remote alternative facilities to service policyholders during disaster recovery operations. The use of multiple IA Firms with facilities throughout the nation provides an

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<sup>74</sup> Source: Interview with Lance Malcolm, Vice President, Claims at Citizens’ Jacksonville offices on April 11, 2012. Complaint ratio percentages represent a 12-month moving average.

<sup>75</sup> Source: Citizens Property Insurance Corporation. (2009). *2009 – 2012 Strategic Plan: Insuring Florida’s Future*.

<sup>76</sup> Source: Interview with Citizens’ claims leadership team (Lance Malcolm, Dawn Sexton, Gregory Golson, Anne Olson) on May 22, 2012.

appropriate platform for disaster recovery in the event Citizens' own offices or in-state IA Firm offices are damaged and deemed uninhabitable by staff.

Limitations with existing systems result in inaccurate or misleading claims statistics. For example, one such limitation mandates the reopening of a claim for even very minor activities, such as small error corrections. As a result, we see a large number of reopened claims and little reporting to define the level of effort required to complete the reopened claim.

### Cost-Benefit Analysis

With day rates between \$450 and \$1,000, a flat fee based on gross claim amount regardless of the level of effort required to resolve a claim, and a fully loaded average employee salary \$98,987 (exclusive of LDCU salaries), it is academic that, taken individually, employee staff provide a more cost effective alternative to outsourcing professionals, who at the lower end represent about \$108,000 in annual costs each (\$450 per day X 240 working days per year<sup>77</sup>). However, to properly evaluate whether the claims organization "is operating in an efficient and economic manner while providing quality service to policyholders, applicants, and agents," our analysis must assess claims operations in the context of Citizens' entire organization and its unique market position. Accordingly, our analysis must consider multiple qualitative factors, including:

- The need to use a combination of internal (i.e., employee) oversight and outsourced staff to maintain adequate quality control;
- The need to engage internal staff for outsourced claims when certain levels of authority have been exceeded;
- The need to maintain a large "bench" of available, properly trained adjusters to enable rapid scaling of claims operations in the event of a large loss event, such as a hurricane or other catastrophe;
- The need to ensure otherwise idle contract staff maintain sharpness in skills and knowledge of Citizens' systems and internal processes during non-catastrophe operations;

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<sup>77</sup> 240 working days derived by taking available work days (260) and subtracting vacation (10) and holidays (10).

- The need to promote loyalty among IA Firms such that, when demand is high during large loss events, they readily offer priority to Citizens; and
- The need to manage operating costs, by not maintaining hundreds or thousands of staff on payroll during normal (i.e., non-catastrophe) operations.

As such, we examined claims adjustment operations with these factors in mind and draw conclusions that qualify financial measures accordingly.

Taken separately, if we divide total personal lines claims expenses paid during 2011 (\$90.8 million)<sup>78</sup> by the number of claims initiated (70,245), we derive average paid allocated expenses per claim of about \$1,293.<sup>79</sup> However, to properly evaluate the claims organization's cost structure (and its operating efficiency), we must acknowledge (i) prior claims that are still in process at the beginning of the year; (ii) claims that are reopened during the course of the year; and (iii) claims in dispute that are referred to LDCU where longer cycle times and more expensive external resources (e.g., outside counsel subject matter experts) necessarily drive up the average cost per claim, improperly skewing the resulting cost per claim. Accordingly, to perform a more appropriate analysis, we reviewed aggregate costs for the management of 125,615 non-LDCU claims *at various stages of the claims lifecycle*, the management of which involved a fully-loaded internal employee component of \$14.1 million in payroll and overhead, and outsourcing (ex-LDCU) costs of \$45.2 million, yielding loss adjustment expenses of \$54.9 million, or approximately \$473 per *claim in process* during 2011,<sup>80</sup> an amount representing approximately 6.3% of the average indemnity payment of \$7,500 paid in 2011.<sup>81</sup>

Assuming 89% of new claims (FNOL) were outsourced and 11% managed internally, we calculate a total of 62,518 outsourced claims and 7,727 managed entirely in-house during 2011. We note that 24% of claims adjustment costs (\$14.1 million) were attributed to internal expenses, while 76% (\$45.2 million) were paid to IA Firms, from which we might be tempted to infer a cost advantage for outsourcing (89% of claims account for just 76% of the cost).

<sup>78</sup> Source: Exhibit 19: *2011 Claim Stats* provided by Gregory Golson, Claims Consultant on April 18, 2011 (forwarded by Eric Ordway on April 19, 2011).

<sup>79</sup> Source: Exhibit 19: *2011 Claim Stats* provided by Gregory Golson, Claims Consultant on April 18, 2011 (forwarded by Eric Ordway on April 19, 2011).

<sup>80</sup> See the "Claims Adjustment" tab in Appendix E, *Citizens SB408 Study Master Workbook*.

<sup>81</sup> Source: Exhibit 19: *2011 Claim Stats* provided by Gregory Golson, Claims Consultant on April 18, 2011 (forwarded by Eric Ordway on April 19, 2011).

That simple analysis leads to erroneous conclusions, however. In reviewing our findings (described above), we note that there are many functions required internally to properly manage vendor relationships and which mandate the retention of internal staff. Indeed, it is the combination of Citizens' training and indoctrination of adjusters at IA Firms (referred to as "calibration") and its attention to vendor management and performance monitoring that supports the positive results of Citizens' claims adjustment activities. Further, higher-cost claims managed by internal adjusters and day-rate contract staff that do not follow the GCA payment schedule for MCM claims will contribute to outsourcing costs such that the per-claim average may exceed what the GCA schedule indicates.

It is certainly useful to evaluate the various costs and benefits of outsourcing versus handling internally the claims management process from a purely financial perspective once it is acknowledged that significant internal support would be required even if Citizens' entire claims operation was outsourced to a servicing carrier or third-party administrator. To perform such an analysis requires the contemplation of a theoretical claims operation capable of handling Citizens' claim profile while maintaining the capacity to accommodate large-scale, even exponential, increases in claims volumes in the event of a catastrophe. If completely outsourced, the servicing vendor(s) would inevitably adopt a strategy similar to Citizens, wherein multiple adjusting firms would be subcontracted to accommodate rapid scaling of operations. In our view, this introduces a middle-tier between Citizens and adjusting firms that would necessarily increase the current cost structure.

### Recommendations

Generally speaking, Citizens' claims organization is a well-run and adequately staffed operation ready to scale dramatically in the event of a large catastrophic event, such as a hurricane. As a result of our assessment, we offer several recommendations to better satisfy the mandates of SB408.

- *Enable consistent, timely and accurate reporting.* While we found Citizens' staff very responsive to our multiple requests for information, there were multiple sources of data and further qualifications required of data and information received to resolve conflicts. This is likely a function of the multiple systems from which such data are collected and aggregated. The extensive use of outsourcing by Citizens' claims organization indicates a need for greater visibility, including more accurate and timely reporting, into the split between internally managed and outsourced activities, the complexity of each and the cost associated with each.

The deployment of a state-of-the-art claims processing solution and the completion of a centralized data warehouse should help to normalize the available data and facilitate a reporting capability appropriate for the management of Citizens' claims organization.

- *Adopt uniform workflows.* Citizens manages a variety of claims types in a variety of different ways that call for many staff positions representing multiple areas of specialization within the claims organization. We believe that designing claims workflows in a manner that normalizes the intake, loss adjustment and settlement processes will contribute to operating efficiencies by reducing staff training times and facilitating cross-training of various claims management staff. We note that the pending Core Project has as one of its central objectives the deployment of a state-of-the-art claims management solution that is expected to address this very issue.
- *Reduce time-based compensation arrangements.* IA Firms and the adjusters they employ who are compensated based on the amount of time they work to settle a claim have less incentive to close a claim file than those who receive a fixed fee per claim. The outsourcing model that compensates based on GCA is preferable to hourly rate adjusters, and far less subject to abuse.
- *Categorize Task Assignment Model claims.* There are many scenarios where one or relatively few minor tasks are assigned on very high-value claims would call for a relatively large payment to the IA Firm if a large GCA payment is invoked for a relatively small task assignment. A provision that delineates task assignments by level of effort may help reduce outsourcing costs, provided a reasonable method could be devised to ascertain the level of effort required to complete an assigned task.
- *Adopt additional loss control methods.* The high incidence of water damage claims (representing 54.6% of all new claims in 2011) may indicate a need to provide better loss control through more stringent underwriting criteria and policyholder education (i.e., informing policyholders regarding remedial strategies to avoid plumbing and roofing problems and the premium credits that may be available as a result of implementing them).
- *Benchmark financial measures.* We recommend Citizens conduct a benchmarking study to compare their average claim expenses with those of the private sector, developing metrics that compare, for example:

- Claims by region
- Claims by type of loss
- Claims by sub-type of loss
- Average cycle time from FNOL through resolution
  - By region
  - By type of loss
  - By sub-type of loss
- Number of reopened claims due to initial error
- Number of reopened claims due to supplemental payment

Until consistent, timely and accurate reporting is in place, Citizens management will be challenged to identify patterns in claims activity that indicate the best way to manage claims.



## Customer Service Calls

Citizens' customer service call center organization, comprising both internal and outsourced customer service representatives, serve agents, policyholders, inquiries regarding the Florida Market Assistance Program ("FMAP") and inquiries from policyholder mortgagees. In addition to a large internal customer service organization, Citizens contracts with two vendors to support inbound customer service calls, Interactive Response Technologies, Inc. ("IRT") and ACS State & Local Solutions, Inc. ("ACS").

In addition to the Senior Director of Consumer and Agent Services, Citizens' call center organization includes three management staff and nine supervisors who oversee internal call center operations and manage the two outside vendors. Citizens' call centers are staffed with approximately 150 customer service representatives ("CSRs") who are either full-time (114), part-time (15) or contract (21) workers.<sup>82</sup>

Call center managers are certified by the Society of Workforce Planning Professionals ("SWPP") and assess call volumes in fifteen-minute intervals to forecast demand for CSRs and predict expected wait times for callers. Forecasts are "usually within 3% to 5% accurate."<sup>83</sup> Call volume forecasts also provide Citizens' with the data they need for call routing to internal CSRs or one of the vendor call centers.

## Personal lines

The total number of personal lines-related calls handled by Citizens and its vendors during 2011 was 1,301,516. Agent inquiries during 2011 included 38,410 technical support calls (typically regarding access to various Citizens systems), 795,482 policy servicing calls (tier 2 calls related to underwriting are routed to Citizens' underwriting department, and are reflected in the Underwriting operations assessment, *supra*), and 6,578 depopulation-related calls. Citizens policyholder inquiries included 276,392 policy servicing calls and 77,080 claims servicing calls. In addition, 24,155 calls were made regarding FMAP, and 83,419 calls came from policyholder mortgagees.<sup>84</sup> Currently, only calls to accept first notices of loss are outsourced to IRT and ACS. Outsourced calls represent approximately 5.7% of

<sup>82</sup> Exhibit 26: *Citizens Discovery Workbook – Customer Service* provided by Lewis Kyle Brown, Project Manager on March 28, 2012.

<sup>83</sup> Source: Interview with Steve Bitar, Senior Director of Consumer and Agent Services, at Citizens' Tallahassee office on April 10, 2012.

<sup>84</sup> Source: Exhibit 26: *Citizens Discovery Workbook – Customer Service* provided by Lewis Kyle Brown, Project Manager on March 28, 2012.

Citizens' customer service call volume (including policyholder and agent inquiries), all of which are first notices of loss or other claims-related inquiries.<sup>85</sup>

### Commercial lines

The aggregate number of commercial lines-related calls handled by Citizens and its vendors during 2011 was 53,617, of which 48,873 were from agents and 4,744 were from policyholders. All commercial lines calls were related to policy servicing.<sup>86</sup>

### Staffing

Because CSRs handle calls for both personal and commercial lines inquiries, we have combined Customer Service staff into a single group.

Position	Number	Average Salary
Management (Ass't Director, Manager, Ass't Manager)	3	\$ 76,459
Supervisor	9	\$ 50,510
CSR	114	\$ 33,252
Part-Time CSR	15	\$ 16,205

Table 21: Internal Employee Call Center Staff

Using the salary totals from the table above, and after applying reasonable allocations for payroll taxes (10%) and overhead expenses (25%), we arrive at an aggregate internal staff cost of \$6,369,097. In addition, employee staff are augmented by 21 contract staff who were provided to Citizens at a cost of \$436,585 in 2011.<sup>87</sup> Internal (employee plus contractor) staff handled approximately 94.3% of inbound calls at Citizens in 2011, at a cost per call of approximately \$5.33.

The two call center vendors utilized by Citizens to handle inbound calls during 2011 were paid a total of \$427,701 in 2011<sup>88</sup> to handle approximately 77,080 calls, at an average cost per call of \$5.55.

<sup>85</sup> Source: Exhibit 27: *Data Request – Customer Service (4.30.2012)* provided by Lewis Kyle Brown, Project Manager on April 30, 2012.

<sup>86</sup> Source: Exhibit 26: *Citizens Discovery Workbook – Customer Service* provided by Lewis Kyle Brown, Project Manager on March 28, 2012.

<sup>87</sup> Source: Exhibit 28: *April 30, 2012 email from Lewis Kyle Brown.*

<sup>88</sup> Source: Exhibit 28: *April 30, 2012 email from Lewis Kyle Brown.*

## Findings

Citizens' call center operation is well-organized and well-managed and represents a model for other organizations with respect to the efficiency of its call handling, the currency of its management facilities and the morale of its workforce. The call volume forecast accuracy is exceptional; the systems and processes it has adopted represent the state of the art in call center technology. While the call center industry suffers annual attrition as high as 30% of staff, Citizens has managed to create career paths for their CSRs to higher-paying positions in the claims management and underwriting business units. Consequently, Citizens' annual staff attrition is as low as 22%, far superior to the industry as a whole.<sup>89</sup> By not enduring the same level of staff retraining as its industry counterparts, we believe Citizens enjoys relative cost advantages with respect to its operational efficiency.

Vendor call center facilities are located in multiple locations to mitigate risks associated with large-scale catastrophic events. In addition to its Fort Lauderdale, Florida headquarters, IRT maintains facilities in Miramar, Florida; Hackensack, New Jersey; Ada, Oklahoma; and Houston, Texas. In addition to their Tallahassee, Florida location, ACS (part of Xerox Corporation since 2010) maintains disaster recovery sites that can accommodate call volume overflow in San Antonio, Texas and Sandy, Utah. In our view, Citizens is well-equipped to deal with large-scale catastrophic events that call for rapid scaling of operations to accommodate massive call volumes, without undue exposure to service interruption risks.

Notably, Citizens had previously outsourced a much larger volume of inbound consumer and agent calls, and experienced a markedly higher incidence of complaints from agents.<sup>90</sup> As highly-trained professionals knowledgeable about most aspects of Citizens' personal and commercial lines of business, Citizens' call center representatives are uniquely qualified to satisfy agent and consumer inquiries.

The scale of Citizens' call center operations affords certain economies smaller operations would not enjoy. The degree of control over operations, CSR training and performance monitoring aligns well with the SB408 mandate to "[provide] quality service to policyholders, applicants, and agents."

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<sup>89</sup> Source: Interview with Steve Bitar, Senior Director of Consumer and Agent Services, at Citizens' Tallahassee office on April 10, 2012.

<sup>90</sup> Source: Interview with Steve Bitar, Senior Director of Consumer and Agent Services, at Citizens' Tallahassee office on April 10, 2012.

### Cost-Benefit Analysis

Our analysis reveals a cost per call that favors internal call handling (\$5.33 per call) over outsourcing (\$6.24 per call). Further, there is overhead associated with outsourcing not directly reflected in the contract pricing, including purchasing and contracting, contract administration, training, indoctrination, certification and workload balancing activities that are integral to the initiation, maintenance and management of multiple vendor relationships that is absent in the internal staff model. We expect the addition of such overhead, even considering the facilities and technical infrastructure required to maintain internal call centers (which we would argue would be necessary regardless of the sourcing model adopted) to enhance the cost advantage of internally managed calls. Further, the fact that Citizens had previously outsourced a larger proportion of calls only to experience greater rates of complaint from the agent community suggests that the training and quality assurance controls facilitated by maintaining internal call center staff contribute to higher rates of agent (and consumer) satisfaction. Reverting to that sourcing model appears to run counter to the mandates of SB408. However, it is important that Citizens has available sufficient call center resources ready to scale in the event a large catastrophe or material change to policyholder terms causes a rapid increase in inbound call volume.

### Recommendations

Inasmuch as the current cost per call handled internally is lower than the average cost per call outsourced, it appears as if Citizens is making judicious use of outsourcing for customer service calls, especially in light of the reduced incidence of inbound complaints from the agent community. However, we note the large cost differential between IRT (\$7.50 per call) and ACS (\$5.19 per call)<sup>91</sup> shifts the equation decidedly in favor of outsourcing if ACS or a vendor providing similar pricing is used for all outsourced calls.

We also noted a reduction in claims-related complaints (See Claims Adjusting section, *supra*.) and the use of call center outsourcing exclusively for handling claims-related calls during 2011. Like other areas of investigation in this report, we cannot rely solely on quantitative analysis to draw conclusions and make recommendations. Realizing the specific knowledge requirements of Citizens' call center staff, we're reticent to recommend a wholesale move to outsourcing call center activities. However, given the

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<sup>91</sup> Source: Exhibit 35: May 30, 2012 email from Jeremy Pope, Assistant Director of Consumer and Agent Services.

economics of the cost-benefit equation for the lower cost call center alternative (ACS), we do recommend:

- *Increase use of external call centers.* A gradual increase in the use of external (i.e., outsourced) call centers while closely monitoring rates of complaint will help ensure the readiness and availability of call center staff in the event scaling of operations is necessary, e.g., upward in response to a large-scale catastrophe, or downward in the event Citizens' policy count declines markedly. All vendors must offer appropriately scalable and highly trained staff to ensure adequate service levels are maintained; and
- *Conduct solicitation for additional vendors.* The solicitation of additional vendors for price comparisons and to provide a sufficiently large, highly trained and available and call center staff in the event large-scale catastrophes or other events prompt significant call volume increases.

## Industry Comparisons

In addition to the evaluation of Citizens' use of internal and outsourced personnel to manage certain policy servicing and customer service operations, Perr&Knight developed a brief survey which was distributed to 17 FAIR Plan organizations that serve residual markets (the form of which is provided in Appendix D) to better understand their use of, and motivations for, outsourcing certain parts of their operations. Of the 17 contacted by Perr&Knight, eight responses (47%) were received (Illinois, Indiana, Kansas, Kentucky, Louisiana, Mississippi, Ohio and Oregon). The respondents represent a reasonable cross-section of FAIR Plans in the United States, with Louisiana Citizens Property Insurance Corporation being among the larger plans (only Florida Citizens and Massachusetts have higher policy counts, and only Florida Citizens and California have higher exposures); Illinois, Kansas, Kentucky, Mississippi and Ohio representing the middle-tier plans; and Indiana and Oregon representing the smaller plans. Plan statistics are provided in the table below.

Notably among the respondents, one (12.5%), Louisiana Citizens, outsourced underwriting functions (other than inspections) and all (100.0%) outsourced most or all of their property inspections. Five (62.5%) of the respondents outsourced claims adjustment activities, four (50.0%) of which also outsourced their claims intake (FNOL). All (100.0%) respondents indicated they handled all call center activity internally.

State	Organization	Habitational Policies	Commercial Policies	Exposure (\$000)	Direct Written Premium (\$000)
California	CA FAIR Plan Property Insurance	135,023	6,796	\$41,276,819	\$65,304
Connecticut	CT FAIR Plan	3,178	152	594,327	3,476
Delaware	Insurance Placement Facility of Delaware	2,054	92	289,691	628
Florida	Citizens Property Insurance Corporation	1,446,892	56,852	460,703,299	2,604,265
Georgia	Georgia Underwriting Association	24,592	1,748	3,393,587	20,139
Illinois	IL FAIR Plan Association	6,185	114	543,708	5,543
Indiana	IN Basic Property Insurance Underwriting Association	1,780	55	156,122	1,405
Iowa	IA FAIR Plan	811	38	57,515	539

State	Organization	Habitational Policies	Commercial Policies	Exposure (\$000)	Direct Written Premium (\$000)
Kansas	KS FAIR Plan	10,229	185	530,543	4,792
Kentucky	KY FAIR Plan Reinsurance Association	10,550	606	NA	5,738
Louisiana	Louisiana Citizens Property Insurance Corporation	154,897	6,101	23,923,775	209,946
Massachusetts	MA Property Insurance Underwriting Association	214,991	579	77,597,516	283,010
Michigan	MI Basic Property Insurance Association	32,461	598	3,795,954	34,021
Minnesota	MN FAIR Plan	6,872	5	643,595	5,216
Mississippi	MS Windstorm Underwriting Association	11,096	-4	643,264	7,156
Missouri	MO FAIR Plan	5,089	233	275,006	2,526
New Jersey	NJ Insurance Underwriting Association	22,057	758	3,016,107	11,755
New Mexico	NM Property Insurance Program	11,597	270	NA	3,511
New York	NY Property Insurance Underwriting Association	54,255	4,695	14,219,672	35,735
Ohio	OH FAIR Plan Underwriting Association	35,338	669	7,163,529	22,374
Oregon	OR FAIR Plan Association	2,674	106	196,554	1,055
Pennsylvania	Insurance Placement Facility of Pennsylvania	25,138	1,695	1,767,885	8,843
Rhode Island	RI Joint Reinsurance Association	17,530	134	4,121,242	21,206
Texas	TX FAIR Plan Association	110,593	-4	14,246,998	73,924
Virginia	VA Property Insurance Association	29,239	590	3,429,181	15,901
Washington	WA FAIR Plan	32	36	18,446	154
West Virginia	West Virginia Essential Property Insurance Assn	668	79	28,845	414
Wisconsin	Wisconsin Insurance Plan	2,915	57	NA	NA
		<b>2,378,736</b>	<b>83,235</b>	<b>662,633,180</b>	<b>3,448,576</b>

Table 22: FAIR Plan Statistics<sup>92</sup>

Given the relative incompatibility of Citizens' organization, which represents 60.8% of all FAIR Plan policies, 69.5% of all FAIR Plan risk exposure and 75.5% of gross written premium, with those of other

<sup>92</sup> Source: Insurance Information Institute (July, 2011). *Residual market property plans: From markets of last resort to markets of first choice*, page 12.

FAIR Plan residual markets participants, direct comparisons are inappropriate. However, there is nothing in our assessment or our experience that suggests any other FAIR Plan has adopted sufficiently different operating models to warrant further investigation. Indeed, we believe many aspects of Citizens' operations define best practices in the residual markets, including how to properly balance outsourcing and internal support, evaluate and manage vendor relationships and undertake technology initiatives designed to improve operations, with Citizens often looked to for leadership by its industry counterparts.

### Private Market Comparisons

While it is statutorily compelled to insure certain risks that other insurers would turn away, Citizens derives certain financial benefits from its quasi-government status. The challenge to management is to balance these advantages against the disadvantages associated with compulsory risk assumption and rate regulation often motivated by political considerations (the result of which is a prolonged period of actuarially unsound rates). Operational considerations that negate any reasonable comparison between the operating strategies of private market insurers and Citizens include:

- *Compulsory insurance.* Citizens is statutorily obligated to provide insurance to even the worst risks. Citizens has not been in a position to manage their book of business in a manner that optimizes their assumption of risk and enhances their ability to maximize profits. Pending changes to Citizens policy terms will help to reduce some of their risk exposure,<sup>93</sup> however, they are still prohibited from excluding certain problematic perils (such as sinkholes) by statute.
- *Lack of advertising and marketing expenses.* While Citizens engages in public outreach programs and public relations initiatives, it does not advertise in traditional media outlets and relies exclusively on the agency community to generate premiums. The absence of advertising and marketing expenses (representing 4% or more of gross written premium for some large private market insurers) alleviates a financial burden its private market counterparts must bear to compete in their respective markets.
- *Insurance business focus.* Citizens offers personal and commercial property insurance in the state of Florida. Similarly sized insurers typically offer policies across multiple lines of business in

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<sup>93</sup> Source: Exhibit 8: *Citizens Presentation to the Financial Services Commission, December 6, 2011.*



many or all states, districts and territories. The singular focus of Citizens on property insurance relieves it of many of the market and regulatory complexities faced by multi-line, multi-state insurers in the private sector.

- *Product simplicity.* The lack of a need (or desire) to compete in the private insurance market removes from Citizens the relatively complex product development functions found at most large insurers that serve the private market.
- *Active legislature.* Because of its role as an important insurer in a state where catastrophic events are relatively frequent and insurance costs among the highest in the nation, as well as its ability to levy surcharges on all insurers in the state, Citizens is beholden to the politics of the State of Florida, whose citizens and their elected representatives are intensely interested in Citizens' financial adequacy and operating efficiency. Consequently, Citizens had been subject to legislatively mandated caps on insurance rates, which yielded a rate structure that was inadequate given the total insured value of Citizens' risks, which exceeds \$500 billion today. In response, Citizens is currently revising the coverages available and establishing other guidelines designed to return it to being an insurer of last resort.
- *Other operational differences.* Citizens is a state-regulated association that has tax exempt status, unlike its private-industry brethren. When losses exceed claims paying ability, Citizens imposes assessments on insurers doing business in the state; such assessments are subsequently passed through to their policyholders as a surcharge. Citizens also has the ability to finance loss payments by issuing tax-exempt bonds that carry low interest rates, benefiting from the state of Florida's strong credit rating.<sup>94</sup> Private market insurers are largely dependent upon the capital markets, which demand strong balance sheets and profitable operations when offering low interest rates.

It is notable that Citizens, with approximately 1,175 employees, manages more than 1.4 million policies in force that contribute approximately \$3 billion in gross written premiums annually – more than \$2.5 million in gross written premium per employee. By contrast, we find recent data for Erie insurance, with

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<sup>94</sup> Source: Insurance Information Institute (July, 2011). *Residual market property plans: From markets of last resort to markets of first choice*, page 32.

4,480 employees managing 4.3 million policyholders who contribute just over \$4 billion in 2011 GWP,<sup>95</sup> or about \$890,000 in GWP per employee, and Hanover Insurance Group, with \$3.9 billion in 2011 GWP and 5,100 employees,<sup>96</sup> or \$765,000 in GWP per employee. In fairness, both Erie and Hanover (as well as most other similarly-sized insurers) maintain multiple lines of business across several operating companies in several countries that complicate their businesses and their corresponding operations while making less use of outsourcing than Citizens. However, the contrast is worth noting as demonstrable of the operating efficiencies Citizens has been able to achieve in just ten years since its formation. By engaging and managing outsourcing vendors to accommodate the always present potential need to rapidly scale operations, it has successfully traded fixed costs (i.e., employee staff) for variable costs (i.e., outsourced staff) and continuously seeks ways to improve its operations.

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<sup>95</sup> Source: Retrieved from [www.erieinsurance.com/about/profile.aspx](http://www.erieinsurance.com/about/profile.aspx) on May 24, 2012.

<sup>96</sup> Source: *Hanover Insurance Group 2011 Annual Report*.

## General Operations

Citizens is in an extraordinarily unique position among insurers nationwide. As an organization that is statutorily compelled to insure some of the highest risks in one of the most catastrophe-prone states in the nation, their operations should not be expected to mimic those of any other carrier. They have unique needs, including the need to rapidly scale operations upward in the event of a large catastrophic event, or downward in the event depopulation activities or legislative policy initiatives designed to return them to a bona fide insurer of last resort cause an exodus of policyholders. Appropriately, outsourcing is a major part of their operating strategy. The administrative burdens placed upon Citizens, often driven by legislative mandate, call for management to be responsive to uncertainties beyond those normally endured by an insurer, adding significantly to operational risk.

Inasmuch as the commission of this study called for “[ensuring] that the corporation [Citizens] is operating in an efficient and economic manner while providing quality service to policyholders, applicants, and agents,” we were encouraged to find many ongoing internal initiatives designed to serve precisely that goal. Notably:

- A major ongoing systems replacement initiative, known as the “Core Project,” which aims to consolidate three policy administration systems on a common platform and integrate state-of-the-art claims management and billing systems. We would expect the consolidation of systems and the deployment of modern workflow management capabilities throughout Citizens’ insurance operations to enable the automation of key functions while facilitating interaction with outsourcing vendors in the underwriting, claims management and billing areas and provide significant cost savings as a result. Further, consolidation of systems will eliminate the need to maintain multiple vendor relationships for policy printing and mailing functions.
- The anticipated installation of a policy document management solution is expected to eliminate the need to outsource any policy assembly functions, such as those currently handled by CEDAR Document Technologies and CSC or their subcontractor Pinnacle Data Systems.
- A currently contemplated information technology project to aggregate data from multiple sources into a consolidated data warehouse to streamline management reporting should provide Citizens executives with more timely, consistent and actionable information that informs an improved decision-making process.

- A mature vendor management process that continuously evaluates vendor performance and increasingly assigns work to those vendors who demonstrate superior results, overall lower costs and excellent quality demonstrates a capability necessary to ensure efficient and effective outsourcing operations.
- A business unit dedicated to process improvement and enterprise performance metrics demonstrates the enterprise-wide cultural significance of efficient and effective operations.
- Claims adjusting training programs, designed to “calibrate” the many IA Firm adjusters by indoctrinating them into Citizens’ known good practices reduces process variation, known to be a significant cause of poor quality process outputs.

In information requests to different departments we found different methods of classifying data. For example, in response to an information request for “unallocated loss adjustment expenses (ULAE) by line of business,” the data set provided by Citizens actuarial unit classified ULAE by account (Citizens’ Personal (PLA), Commercial (CLA) and High Risk (HRA) accounts).<sup>97</sup> Other areas of the company differentiate between Personal Residential Multiperil, Personal Residential Wind, Commercial Residential Multiperil, Commercial Residential Wind, Commercial Non-Residential Multiperil and Commercial Non-Residential Wind lines of business. Alternatively, claims were classified as Personal Non-Catastrophe, Personal Catastrophe, Commercial, LDCU and Shared Services. We emphasize that this is not unusual in insurance companies, especially those comprised of formerly independent merged entities such as Citizens, where one finds vestiges and cultural artifacts of pre-merger organizations long after any such mergers have been completed.

While we found Citizens’ staff to be very responsive to our multiple requests for information, its origin (i.e., as the merger of the Florida Residential Property and Casualty Joint Underwriting Association (FRPCJUA) and the Florida Windstorm Underwriting Association (FWUA)) resulted in a combination of multiple, disparate systems to create the comprehensive insurance processing platform required to manage Citizens’ business. As a result, the number of individuals with whom we had to consult to develop a complete picture of Citizens’ operations (within the scope of this engagement) created

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<sup>97</sup> See, for example, question 3 on Exhibit 32: *Request for Information – Answers (5.2.2012)*, and the corresponding data set provided in response contained on the “Q3 ULAE 2011” tab in Exhibit 33: *Citizens Response to Information Request (5.22.2012)*.

significant challenges for our team. In all, we had to interact with no fewer than 23 Citizens staff members, some of whom provided conflicting data sets that required multiple inquiries to reconcile. In other instances, individual data points did not sum up to aggregate numbers provided. Vendor spend data was located in four different systems. We would expect the general unavailability, extraction effort and conflicts evident in operational data to present similar challenges for Citizens' management and executive leadership.

### General Recommendations

- Continue work on the Core Project and re-evaluate impact on the In-Scope Processes once completed.
- Continue work on the data warehouse initiative and ensure appropriate data elements are collected and readily reportable based on pre-defined key performance indicators.
- Centralize "command" of data by appointing an enterprise-wide data steward and consolidating data retrieval and reporting functions in the office of the Chief Insurance Officer, or creating a similar capability by installing a new executive position, such as a Chief Operating Officer or Vice President of Operations post, for performance oversight across all areas of operations.

## Conclusions

Citizens is uniquely positioned as an important provider of financial security to residents of the State of Florida who may not otherwise be able to obtain property insurance for their homes and businesses. Its operational strategies must balance the potential for large-scale catastrophic events that demand significant increases in properly trained and available staff against initiatives designed to reduce policy coverages and limits to return it to an insurer of last resort that are expected to effectively halve the number of policies in force. Given this constant state of uncertainty and potential instability, there is no single “right way” to manage Citizens’ operations.

Given these circumstances, Citizens’ operating strategy appears to be well developed and properly avails itself of the benefits outsourcing has to offer. Management appropriately balances the need for process effectiveness (i.e., the ability to complete certain outputs, such as an issued policy or closed claim), efficiency (at least cost), agility (while being adaptable to change) and quality (ensuring customers are properly served). A purely quantitative approach to this Study might suggest greater efficiencies could be gained in the short term by outsourcing more activities, however, we believe there is sufficient evidence to suggest that quality would be compromised without proper participation by Citizens’ staff. Alternatively, adding internal staff might result in short-term cost reductions if a greater proportion of underwriting or claims adjustment activities are handled internally, however, current efforts to reduce Citizens’ size may ultimately require reductions in force that result termination costs and additional risks. The qualitative factors influencing our findings, recommendations and this concluding section are at least as important as the financial analyses that accompany them.

To be sure, there are areas of Citizens’ operations in need of improvement, however, we found many of these areas to be widely acknowledged by management and already being addressed in some form or fashion, in no small part by the Core Project and an ongoing data warehouse initiative. In reality, there is only so much that can be done given the time and business constraints of any organization, and Citizens seems to have a remarkably mature approach to managing operations given its relative youth as an organization, evidenced by the leanness of operations when compared to similarly-sized private insurers and its unique need to be responsive in one of the nation’s most catastrophe-prone states.

## Appendix A: Citizens Participants

The following Citizens employees provided information through direct interview or email correspondence, fulfilled requests for information from Perr&Knight and/or provided data sets used in the preparation of this report.

Name	Title	Data/Information Provided
Baldwin, Ed	Assistant Director, Insurance Operations	Claims data
Binnun, Sharon	Chief Financial Officer	Interview; general report criteria
Bitar, Steve	Senior Director of Consumer and Agent Services	Interview; Call center data
Brown, Lewis Kyle	Project Manager, Consumer and Agent Services	Call center data
Deeb, Fred	Assistant Director of Accounting Operations, Financial Analysis & Budget	Interview; vendor payments data
Dennis, Keri	Program Manager, Insurance Operations	Inspections data
Gilroy, Yong	Chief Insurance Officer	Interview; General report criteria
Golson, Gregory	Claims Consultant	Claims data
Hageman, Douglas	Personal Lines Underwriting Operations Manager	Underwriting activity time allocation
Malcolm, Lance	Vice President, Claims Operations	Interview; claims staff headcounts, salaries, claim counts
Montero, Jennifer	Senior Director of Accounting / Controller	Interview; personal lines payment plan percentages by plan type
Murphy, Deborah	Vice President, Underwriting	Interview
Murphy, Susanne	Chief Administration Officer	Interview; general report criteria
Ochoa, David	Commercial Lines Systems Manager (IT)	CSC/Pinnacle Data Systems data
Olson, Anne	Assistant Director, Claims Operations Litigation and Disputed Claims	LDCU expenses, claim counts
Ordway, Eric	Senior Director, Insurance Operations	Interview; vendor contracts; Property Inspection Results
Overpeck, Curt	Chief Information Officer	Interview; IT considerations
Owen, Jonathan	Enterprise Performance Metrics Manager	Underwriting items
Pope, Jeremy	Assistant Director of Consumer and Agent Services	Call center outsourcing vs internal split; split between IRT and ACS; costs
Popko, Tom	Director, Personal Lines Underwriting Operations	Underwriting data
Rambo, Deborah	Senior Administrative Assistant to the Claims Vice President	Claims staff budgeted headcount
Sellers, Robert	Vice President, IT Strategy and Architecture	Interview; IT considerations
Sexton, Dawn	Claims Director – Shared Services	Interview; Shared Services activities

Table 23: Citizens Study Participants

## Appendix B: Perr&Knight Consultants

The following Perr&Knight consultants participated in the creation of this report.

### Rob Berg, Project Lead and Principal Author

Rob Berg is a Principal and Director of Perr & Knight's Insurance Technology Group, and editor-in-chief of the firm's *Journal of Insurance Operations*. Over a career spanning more than twenty years, Rob has led or advised the management teams of dozens of companies in the financial services, consumer retail, software and telecommunications industries. His expertise includes strategic planning, feasibility and breakeven analyses, project management and process improvement methodologies, including workflow design, analysis and simulation. Prior to joining Perr&Knight, Rob was chief operating officer of SmartReply, a leading retail marketing firm that enjoyed three consecutive years of triple digit growth during his tenure. Prior to SmartReply, Rob was chief executive officer of Ecor Solutions, a New York-based IT consulting firm.

Rob has worked with many senior-level executives in the property and casualty insurance industry, including those from AIX Group (Hanover Group), Beazley USA, Capitol Insurance Companies, Citizens Property Insurance Corporation, Imperium Insurance Company, Knightbrook Insurance, Liberty Mutual (Liberty International Underwriters), Lincoln General Insurance Company, North American Risk Services, XL Capital Corporation, and others. His work has included business process improvement initiatives, technical project rescues, vendor selection, requirements management, technology feasibility, cost-benefit analyses, outsourcing strategy development and staff training.

In addition to holding a BA in Economics from Stony Brook University and completing graduate work in technology management, decision theory and organizational behavior, Rob's practical experience is supported by credentials from the American Society for Quality (Six Sigma Black Belt) and Stanford University (Advanced Project Management). He is a member of ISACA (and has extensive knowledge of their CobiT, ValIT and RiskIT frameworks), a Senior Member of the American Society for Quality and is a frequently sought speaker at industry trade events. He has conducted technical sessions at multiple industry conferences, including *Enterprise-class systems deployment: A framework for success* (ISOTech 2007); *Order from chaos: Making sense of the requirements gathering process* (ISOTech 2008); *Aerodynamic operations: Straight-through processing comes of age in the insurance industry* (IASA 2008); and *Process perfection: Using simulation models to optimize claims operations* (ISOTech 2009). He



has also been quoted or published in insurance industry trade publications including *IASA Interpreter*, *Best's Review* and *Insurance News Net*.

**James F. Cerone, Insurance Company Operations Subject Matter Expert**

Jim Cerone served as Executive Vice President of the Travelers Property Casualty Corporation and President of the technical services division of the claim organization. Prior to joining Travelers, Mr. Cerone served as Senior Consultant and Equity Principal of Milliman & Robertson, Inc. (M&R). At M&R, he founded and directed the claims management consulting practice, specializing in consulting with management on a wide range of strategic and organizational issues. He has provided expert testimony in the course of litigation. His background also includes service as Vice Presidents and Consultants with Tillinghast, Nelson & Warren, Inc.; Kramer Capital Consultants; and senior executive positions with three other U.S. insurers; Commercial Union, John Hancock, and American Reserve. In these positions, he was responsible for organizational design, development and implementation of strategic initiatives, acquisitions, operating systems, training and education, and the general management of large scale claim operations. As a consultant, he serves as a subject matter expert (SME).

Mr. Cerone has been active in a number of industry organizations including serving as a member of the claim executive committees of the American Insurance Association and the Alliance of America Insurers where he also served as a member of the legal committee. Mr. Cerone is appointed to the National Roster of Neutrals of the American Arbitration Association. He serves as an arbiter/umpire in insurance disputes, and as a Special Master appointed by the U.S. District Court.

As a guest speaker, Mr. Cerone has addressed national meetings of the American Academy of Actuaries on the use of annuity settlements for casualty claims; the Insurance Institute of America on anti-fraud techniques; the Casualty Actuarial Society (CAS), the Canadian Institute of Actuaries, and the Society of Chartered Property and Casualty Underwriters on case basis reserving; the CAS on case reserving generally and for environmental claims, the effects of managed care on medical malpractice exposures, and controlling allocated expenses; the Society of Financial Examiners (SOFE) on the analysis of case reserves; the Illinois Administrators' Academy on insurance procurement; the ISO Technology Conference on using simulation models to optimize claims operations; and, served as a lecturer and trainer to the Illinois Department of Insurance. He has been a member of the M&R faculty, at the U.K., which provides seminars to the European market. He serves as a lecturer/trainer to the claim and

commercial lines marketing staff at client insurers. He also provided testimony to the U.S. House Small Business Committee on the Liability Insurance Crisis, and to the State of Connecticut Task Force on Insurance Fraud. He has served as technical advisor to the Federal Emergency Management Agency (FEMA).

Mr. Cerone is the author of a monograph for the Massachusetts Bar Association on the use of annuity settlements for casualty claims, an article on case reserving which appeared in *Business Insurance* and *The Examiner*, a publication of the SOFE, and articles on voluntary claim payments, and the control of legal costs for *Best's Review* and the *Journal of Insurance Operations*. He has also written and recorded a video on "Reviewing Individual Claim Files" for the SOFE.

Mr. Cerone has a BS in Business Administration from Villanova University and a MBA from the University of Chicago, Graduate School of Business.

#### **Atul Poladia, Insurance Technology Subject Matter Expert**

Atul Poladia is Practice Manager of Perr & Knight's Insurance Technology Group. During a career spanning fourteen years, Atul has led major project initiatives, including a \$106 million software development program and a staff of 180 onshore and offshore technical resources. As a Director of IT at Nationwide Insurance, Atul oversaw the deployment of their Enterprise Internet Portfolio, created a proof-of-concept team to rapidly develop and test new features in reaction to competitor activity and decreased average release time for new projects by 50%, which contributed to a 300% increase in policy binding capacity over previous systems in less than nine months.

Also at Nationwide, Atul was instrumental in the realignment of software applications to reflect portfolio priorities, resulting in \$18 million in savings over a three-year period. He also developed and conducted staff training and reassignment of key technical resources, effectively transitioning technical staff from a WinDNA to a Java skill set, saving Nationwide approximately \$25 million in retraining costs in the process, while eliminating reductions in force, improving morale and increasing employee retention to 90%. He is the recipient of Nationwide's 2008 Outstanding IT Contribution Award, was a finalist in the same competition in 2007 and won First Prize in *Application Development Trends* magazine's 2001 Innovator Awards.

Atul has an extensive set of technology and supporting skills, having knowledge of project management and software development lifecycle methodologies, software development languages and database tools.

Atul holds a BS in Computer Science from the University of Mumbai.

**Kyle Bonestell, Discovery Analyst**

Kyle Bonestell is a Manager with Perr & Knight's Insurance Technology Group. Kyle is accomplished in the areas of project management, technology solutions planning and implementation, functional and technology requirement definition, vendor evaluation and selection, and business process improvement. Kyle's background includes extensive experience managing the selection, customization and deployment of client/server and web based systems. Kyle brings expertise in insurance, data processing, and managing information system departments. In addition, Kyle has deep knowledge in the administration of Worker's Compensation programs.

Kyle's career started in the accounting department of a large residential contractor where he ultimately became the company's manager of IS operations. Kyle was then named IT director of the TPA company for the North Carolina Home Builders Self-Insured Fund. Subsequent to this position, Kyle accepted the IS Director position with Builders Mutual Insurance Company. Kyle oversaw the IS operations for Builders Mutual during a time of significant expansion in their geographical presence and lines of business offered to their customers. Kyle also worked for a major insurance industry software vendor in the capacity of Account Executive managing tier one clients for that organization. Kyle then transitioned to consulting and was named a Director with ATSC.

Kyle attended North Carolina State University studying Economics and Business and Computer Science.

*Peer Reviews were performed by Brett Horoff, ACAS, ASA, MAAA, Principal and Director of Consulting Services at Perr & Knight, and Karen Daley, FCAS, MAAA, Principal and Director of Actuarial Services at Perr & Knight.*

## Appendix C: Process Master

A summary of processes considered in-scope for the purposes of this study are described in the table below. The process master was used to inform the development of the *SB408 Study Master Workbook* provided under separate cover.

Business Process	Input(s)	Key Steps	Output(s)
<b>Underwriting</b>	Completed Application	1. Agent submits application 2. Application is received by Citizens 3. Application is routed to MGI	Premium/Quote
<b>Policy Processing*</b>	Bound Policy	1. Policy forms assembled by vendor 2. Assembled policy package sent to vendor 3. Vendor mails policy package	Policy Package
<b>Underwriting Property Inspections</b>	Policy Application	1. Order inspection 2. Dispatch inspector 3. Receive report 4. Adjust premium	Inspection Report
<b>Claims Adjustment</b>	First Notice of Loss	1. Adjuster is dispatched 2. Adjuster evaluates claim 3. Adjuster settles claim 4. Payment is mailed to claimant	Settlement
<b>Customer Service Calls</b>	Agent inquiry Policyholder inquiry	1. Agent or policyholder calls 2. Call is routed via IVR 3. Call is answered 4. Call is completed	Resolved Issue

\* Policy processing includes policy issuance, billing and renewal processes.

## Appendix D: Form of FAIR Plan Survey

We have been retained by Citizens Property Insurance Corporation (CPIC) to conduct an assessment of their internal operations. The engagement includes a discussion regarding the means by which other residual markets organizations conduct their operations. Specifically, CPIC is interested in knowing how many such organizations outsource portions of their operations, and to what extent. As such, can you please assist us with the following 5 questions:

1. Do you current outsource all or any portion of your operations?

2. Which of the following process(es) are currently handled by third parties (outsourcing vendors or servicing carriers), and what percentage of each is outsourced?

- ☐ Underwriting? \_\_\_\_ (Y/N) \_\_\_\_ (%)
- ☐ Property Inspections? \_\_\_\_ (Y/N) \_\_\_\_ (%)
- ☐ Customer Service/Call Center? \_\_\_\_ (Y/N) \_\_\_\_ (%)
- ☐ Claims Intake (FNOL)/Adjustment? \_\_\_\_ (Y/N) \_\_\_\_ (%)
- ☐ Policy Issuance? \_\_\_\_ (Y/N) \_\_\_\_ (%)
- ☐ Policy Billing? \_\_\_\_ (Y/N) \_\_\_\_ (%)
- ☐ Policy Renewals? \_\_\_\_ (Y/N) \_\_\_\_ (%)
- ☐ Depopulation? \_\_\_\_ (Y/N) \_\_\_\_ (%)
- ☐ Other? Please list \_\_\_\_\_

3. For each process handled by a third party, do you pay:

- ☐ A percentage of premium?
- ☐ A flat fee per day/week/month/year?
- ☐ Some other method? Please explain \_\_\_\_\_

4. If you use servicing carriers, how do you allocate the work among them?

- ☐ By lines of business? (Y/N)
- ☐ By peril? (Y/N)
- ☐ By availability? (Y/N)
- ☐ By skill set? (Y/N)
- ☐ Another method? Please list \_\_\_\_\_

5. What motivation do you have to maintain your current operating model?

- ☐ Legislative mandate?
- ☐ Pure economics?
- ☐ Some other reason? Please explain \_\_\_\_\_

## Appendix E: Citizens SB408 Study Master Workbook

Please see Microsoft Excel spreadsheet document provided under separate cover.

## Appendix F: List of Exhibits

Original file names were preserved where feasible to facilitate comparisons with original documents provided to Perr&Knight. Exhibits provided under separate cover in their native file format.

- Exhibit 1: Citizens Discovery Workbook – Underwriting
- Exhibit 2: PL UW Master Process 12-14-11 v2
- Exhibit 3: UW Items Proc 2012
- Exhibit 4: April 25, 2012 email from Jonathan Owen
- Exhibit 5: April 24, 2012 email from Douglas Hageman
- Exhibit 6: Contract Between Citizens and MacNeill Group, Inc.
- Exhibit 7: April 13, 2012 email from Jennifer Montero
- Exhibit 8: Citizens Presentation to the Financial Services Commission – Dec 6 2011
- Exhibit 9: Cedar Annual Invoice Tracking (2011)
- Exhibit 10: PB Annual Invoice Tracking (2011)
- Exhibit 11: April 17 email from David Ochoa
- Exhibit 12: Feb 23 BOG Meeting Minutes Transcript
- Exhibit 13: March 23, 2012 email from Keri Dennis
- Exhibit 14: BOG Monthly Inspection Rpt-Mar-2012 e Ordway
- Exhibit 15: Sinkhole Pricing Schedule (Exhibit 1)
- Exhibit 16: UW Sinkhole Tracking-3-31-2012
- Exhibit 17: April 26, 2012 email from Eric Ordway
- Exhibit 18: April 26, 2012 email from Keri Dennis
- Exhibit 19: 2011 Claim Stats
- Exhibit 20: April 19, 2012 email from Lance Malcolm
- Exhibit 21: Citizens Discovery Workbook – Claims Adjustment
- Exhibit 22: FNOL Analysis 2011 YEAR
- Exhibit 23: Claims Distribution Jun 11 to Mar 12
- Exhibit 24: Amendment #3 to 2008 Independent Adjuster Services Agreement
- Exhibit 25: Insurance Operations Vendor Management Matrix (9.26.2011)
- Exhibit 26: Citizens Discovery Workbook – Customer Service
- Exhibit 27: Data Request – Customer Service (4.30.2012)
- Exhibit 28: April 30, 2012 email from Lewis Kyle Brown

Exhibit 29: LDCU Dashboard Report 2011

Exhibit 30: 2011 Vendor Spend – Preliminary

Exhibit 31: May 11, 2012 email from Deborah Murphy

Exhibit 32: Request for Information – Answers (5.22.2012)

Exhibit 33: Citizens Response to Information Request (5.22.2012)

Exhibit 34: LDCU Spend Program 2011

Exhibit 35: May 30, 2012 email from Jeremy Pope