



Florida Commission On Hurricane Loss Projection Methodology

# Report on Florida Windstorm Mitigation Discounts

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Randy E. Dumm, Ph.D.  
Chair, Florida Commission on Hurricane Loss Projection Methodology  
Associate Professor of Risk Management/Insurance, Florida State University



# Legislative Charge To The Commission

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- Hold public meetings for the purpose of receiving testimony and data regarding the implementation of windstorm mitigation discounts
- Submit report that provides recommendations for improving the process of assessing, determining, and applying windstorm mitigation discounts pursuant to s. 627.0629, F.S.

# The Importance of Windstorm Mitigation



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**“It is imperative that any program focus strongly on ensuring that homes in Florida are wind resistant through mitigation, .... Strong, enforced building codes are the foundation for a sustainable market for Floridians.”**

(2006 Task Force on Long-Term Solutions for Florida's Hurricane Insurance Market)



# Windstorm Mitigation

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- Promise of Mitigation
  - Harden housing stock
  - Reduce uncertainty in insurance market
    - Effect on availability, premium volatility and premium level
  - Being Safe and Avoiding Inconvenience
- Proven Benefits
  - 2004 & 2005 hurricane seasons
    - Mitigated homes (new building code) performed better



# A Twist On The Road To The Promised Land

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- Adverse impact of mitigation credits
  - Insurer performance and financial viability
    - 2006 to 2009= No hurricanes
  - Reports of inspection fraud and abuse
- Problem Areas
  - Manner in which mitigation credits are included in the ratemaking process
  - Flawed residential structure inspection process
  - Incomplete and poor data quality
  - Hurricane computer modeling limitations

# Indications of Problems- Ratemaking



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- Windstorm mitigation credits were among a list of factors that insurers believe are adversely impacting their performance in Florida
- Reduced premiums related to windstorm mitigation credits was one of the reasons provided by State Farm Florida when it gave its notice of intent to withdraw from the state.
- A.M. Best downgraded nine insurers in 2009 that sell homeowners insurance in Florida. Demotech, who rates some of the smaller Florida insurers, withdrew its rating from six insurers. Two such insurers were ordered into receivership.



# Indications of Problems- Ratemaking (Continued)

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- Security First Insurance Company reported that its surplus position declined by \$2 million in September 2009 as compared to surplus in September 2008. Windstorm mitigation credits during this time period exceeded \$22 million.
- A majority of the homes qualifying for significant windstorm mitigation credits under the My Safe Florida Home program did so without having to undertake any additional windstorm mitigation activities.
- Citizens Property Insurance Corporation: \$741 million in mitigation credits for \$1.7 billion of wind premium (Fischer, 2009)
- Two insurers not accepting homes built after 2002

# Source of Problem Related to Ratemaking



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- The translation from windstorm mitigation relativity to windstorm mitigation credit is a probable cause of the current problems.
  - Decision to use weakest structure as the base for credits.
    - No charge for the weakest structure and larger credits (decrease) for the stronger structure
      - 80% credit (Terrain B) for strongest structure
      - If average structure is base
        - Weakest= 137% surcharge (increase)
        - Strongest= 58% credit (decrease)

# Indication of Problems: Home Inspections



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- Marketing Practices
  - Advertising their services free of charge to policyholders if the inspector cannot obtain a windstorm mitigation discount.
  - “Package” deals for various non-related services as an enticement to attract business.
- Inspection Practices
  - Incomplete inspections
    - “drive by” inspections
    - “phone” inspections
    - Failure to inspect important parts of structure
  - Other parties
- Inspection Errors



# Complexity and Solutions

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- The problems related to windstorm mitigation credits are complex and will not yield to a single solution.
  - Use of modeling to determine the impact of various mitigation features on expected loss cost,
  - Translation of mitigation relativities to mitigation credits
  - Ratemaking process (average versus specific)
  - Incomplete information at the structure level
  - Potential inspection fraud and errors in determining windstorm mitigation credits.

# Recommendations Related to Ratemaking



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- Windstorm mitigation relativities and discounts should be incorporated into the hurricane computer modeling review process.
- The **current** application of windstorm mitigation credits should be modified to allow an insurance company to use debits as well as credits if more appropriate given its base rates and offsets should be applied in an actuarially appropriate manner.
- Windstorm mitigation discounts should only apply to that portion of the premium affected by the mitigation features.
- Larger deductibles should be applied to wind losses if windstorm mitigation features such as shutters are not used at the time of a loss.



# Recommendations Related to Homeowner Inspections

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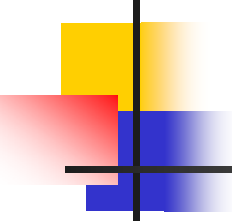
- Replace the current residential structure inspection process be replaced with an independent inspection organization
  - provide oversight and administer all aspects of the inspection process.
  - purpose would be to ensure complete, unbiased, and high quality data on residential structures.
  - board of this independent inspection organization would consist of experts that understand windstorm mitigation of residential structures, data collection, hurricane modeling, insurance and reinsurance underwriting, and the inspection of residential structures.
  - The My Safe Florida Home Program is a possible model

# Recommendations Related to Data Quality



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- Policies and procedures be put in place to ensure complete and high quality data. The data should be consistent with hurricane computer modeling needs and sufficient for the level of “granularity” required for modeling.
  - All residential structures in the state should ultimately be inspected and the results entered into a centralized database.
  - On-line data collection systems need to be utilized that have built-in data and edit checks.
  - Re-inspections of residential structures should be conducted on a random sample of the residential structures to establish an error rate as a base line for quality improvement measurement purposes.
  - The uniform home grading system should be repealed since it is not feasible and presumes a level of accuracy that does not currently exist.



# Recommendations Related to Computer Modeling

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- The current statute regarding the Commission, s. 627.0628, F.S., should be modified to:
  - task the Commission with developing the appropriate mitigation standards,
  - add a structural engineer to the Commission, and
  - revert the Commission's process of developing standards back to an annual basis rather than "every odd year." This would expedite the development of the appropriate mitigation standards and the implementation of the windstorm mitigation discounts based on the revamped system.
- Insurers should use the same hurricane loss model to justify windstorm mitigation discounts as they do for justifying loss costs.



# Closing Observations\*

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- Public Policy Issues
  - Windstorm mitigation efforts important for long-term health of insurance market
  - Key question relates to financing windstorm mitigation-
    - Who pays/who benefits and incentives
    - Insurance credits as sole financing source not viable
  - Mitigation discounts and rates
    - adequate, not excessive, and not unfairly discriminatory

\*-May not necessarily reflect the findings of the Florida Commission on Hurricane Loss Methodology