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Evacuation Disaster: Insurers Fleeing Florida

By Eli Lehrer

A year has passed since Gov. Charlie Crist and a nearly unanimous Legislature hailed the arrival of a new era for Florida's property insurance system. They promised lower rates, greater availability of insurance, and a more vibrant insurance market.

Today, however, the outcome appears increasingly clear: The "reforms" have failed to achieve lasting rate reductions, and they have led many private insurers to reduce or eliminate their exposure to Florida's daunting risks.

Worse, in the event of a major disaster on a scale of Hurricane Katrina, these reforms also could lead to massive hikes in taxes and insurance premiums for almost everyone in the state.

Although the legislation contained dozens of new provisions, its crux lies in two related sets of regulations. One lets the Florida Citizens Property Insurance Corporation (a state agency) compete with private insurers.

The other key provision vastly expands the Florida Hurricane Catastrophe Fund's role in providing backup reinsurance coverage for Citizens and the private companies operating in the state. This backup coverage functions as insurance for insurance companies. It pays off only when claims exceed a certain "catastrophic" level.

In theory, the plan's first element – expanding Citizens -- provides affordable insurance from the state when the private market can't. The second element – expanding the "Cat Fund" – offers private insurers cheaper reinsurance, thereby allowing them to cut their rates.

But it hasn't worked out that way. While Citizens uses only Cat Fund coverage, all major private insurers writing homeowners' policies not only met their legal mandate to purchase Cat Fund coverage, but they also turned around and purchased private reinsurance anyway.

Although Governor Crist, Insurance Commissioner Kevin McCarty, and other critics have suggested that insurers did this out of greed, there's a better explanation: The insurance companies realized that Florida's Cat Fund likely couldn't survive a Katrina-class storm.

Insurers know it's not prudent to depend too much on a single state, and they lack confidence in Florida's plan to issue \$30 billion in bonds to back the Cat Fund if a catastrophe occurred.

That's a lot larger than the nation's largest-ever sale of municipal bonds: an \$11 billion California issue. Nobody—not even the Cat Fund's guardians at the State Board of Administration—can

promise that those bonds will actually find buyers. If the Cat Fund can't sell enough bonds, it will collapse and leave nearly limitless liabilities for insurers and the state.

Citizens itself isn't really any more stable. Although many Floridians currently save money thanks to its lower-than-market rates, these rates cannot last. In fact, everyone in Florida could end up paying for them after the next big storm.

That's because existing law lets Citizens and the Cat Fund impose enormous new taxes (called "special assessments") without any additional approval from the Legislature or the voters. If Florida had to issue all \$30 billion authorized in potential Cat Fund bonds, those assessments —attached to every Floridian's homeowners' *and automobile* insurance policies -- could easily double the \$1,100 average annual premium for automobile insurance.

Simply abolishing the Cat Fund won't help. Without it – and the private insurers' mandatory participation in it -- Citizens' own liabilities would increase even further. That's a problem because Citizens is already the largest insurer in the state, and it will probably write half of all the property-insurance policies in Florida by the end of 2008.

Worse, at a time when the property insurers have been fleeing the state, Insurance Commissioner McCarty has now given Floridians another reason to worry. His decision to escalate a property-insurance disagreement by barring Allstate from writing automobile insurance in Florida may herald a similar retreat of private auto insurers.

Several options loom – all unattractive. Simply deregulating the market and letting insurers set rates freely—something that worked pretty well

in Illinois—would send premiums soaring in the short run and thus seems politically impossible. Other proposals would make Citizens' policyholders pay their own way and would put the Cat Fund on firmer footing.

Meanwhile, elected officials' efforts to demonize insurers could prove counterproductive. Most already consider Florida's insurance market the nation's worst. If they're continually abused, they could well withdraw from the state, leaving Floridians with no homeowners' insurance options at all except for Citizens.

In short, retaining the 2007 "reforms" without making serious changes carries the grave long-term risk of requiring vastly higher taxes and insurance premiums for all Floridians. Given its modest, transient benefits, there's no reason do this.

Therefore, when Florida lawmakers begin mulling insurance legislation for the 2008 session that begins on March 4, they ought to consider proposals to abolish Citizens, privatize the Cat Fund, and in short, undo nearly all of last January's mischief.

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