

The Neal Bill and the Florida Homeowners Multiple Peril Market

The statement of the Florida Consumer Action Network in opposition to the Neal Bill notes that: “In a state accustomed to damage caused by powerful tropical storms and hurricanes, we are very concerned about the availability of affordable property and casualty insurance.” They go on to say that the changes proposed for “overseas based reinsurance companies” would “in all likelihood have adverse consequences for Florida’s consumers.” However, an examination of the effect of the Neal Bill on Homeowners Multiple Peril insurance, the line of business most relevant to consumers, shows no potential impact of the proposed legislation on reinsurance capacity or insurance rates. Direct premium for Homeowners Multiple Peril insurance was a \$6.9 billion market in Florida in 2009. The leading writer was State Farm Mutual Automobile Insurance Company followed by Citizens Property Insurance Corporation.¹ Exhibit 1 shows the top 20 writers of this line of insurance in Florida, who account for over 75% of the Florida market.

To understand the effect of the proposed legislation, it is important to distinguish between the various forms of reinsurance. A primary insurer may cede business to a reinsurer who is affiliated or unaffiliated with it. As the terms imply, an “affiliated” reinsurer is owned by the parent company while an “unaffiliated” reinsurer has no significant ownership relationship between the reinsurer and the ceding company. Reinsurers may either be domestic or offshore; offshore companies are domiciled outside the United States. The Neal Bill addresses the treatment of offshore affiliated reinsurers. That is, reinsurers headquartered outside of the United States who assume reinsurance from related companies in the United States. Affiliate reinsurance is common in the United States, and is typically used to move capital to different regulatory jurisdictions, or to align specific lines of business within a corporate structure. It does not remove risk from the group of related companies that include the primary writing company. As J. David Cummins, one of the authors of the Brattle Report,² noted, “affiliated cessions often are conducted for reasons other than risk hedging and diversification.”³ Another study cited in the Brattle Group report did an empirical analysis showing that third party reinsurance and affiliate reinsurance serve “different purposes,” and found that affiliated insurers with catastrophe exposure tend to retain risks of catastrophic losses rather than spread them through related party reinsurance to affiliates.⁴

¹ Citizens is a not-for-profit, tax-exempt government corporation whose public purpose is to provide insurance protection to Florida property owners throughout the state.

² *The Impact on the U.S. Insurance Market of a H.R 3424 on Offshore Affiliate Reinsurance: An Updated Economic Analysis, July 2010.*

³ J. David Cummins, *Reinsurance for Natural and Man-Made Catastrophes in the United States: Current State of the Market and Regulatory Reforms, Risk Management and Insurance Review*, 2007, Vol. 10, No. 2, 179, 188.

⁴ Lawrence S. Powell and David W. Sommer, “Internal versus External Capital Markets in the Insurance Industry: The Role of Reinsurance,” *Journal of Financial Service Review*, 2007, Vol. 31, pp. 180, 187 (According to the study’s empirical analysis, “the coefficient

Table 1 -- Homeowners Multiple Peril Reinsurance, 2009, All US Business (\$B)				
	Top 20 Florida Insurers		Industry	
	Amount	Percent	Amount	Percent
Direct Business	36.90		67.51	
<u>Affiliated Reinsurance</u>				
Assumed	15.19		43.39	
Ceded	15.31		46.05	
Ceded Offshore	0.12	0.3%	2.66	3.9%
<u>Unaffiliated Reinsurance</u>				
Assumed	0.27		1.91	
Ceded	4.77		9.07	
Net	4.50	12.2%	7.16	10.6%
Net Written	32.28		57.68	
Source: SNL Property and Casualty Data Base				

The approach outlined in the Brattle Report develops an analysis of nationwide premiums and reinsurance for a given line of business, and then applies that percentage to individual states, using the premium written in a particular state.⁵ By analyzing the principal writers of Homeowners Multiple Peril insurance in Florida in 2009, we can conclude that there would be no financial effect of the Neal Bill on Florida Homeowners Multiple Peril, taking into account

the use of offshore affiliate reinsurance by those companies.⁶ An analysis of the aggregate (nationwide) reinsurance utilized by those carriers shows that there is virtually no affiliate offshore reinsurance in the Florida Homeowners Multiple Peril market.⁷ As Table 1 illustrates, the principal writers of Florida Homeowners Multiple Peril insurance in aggregate cede only 0.3% of their direct business premium to offshore affiliates, although they cede net reinsurance of 12.2% of direct premiums to unaffiliated insurers, both domestic and offshore. This represents a slightly higher percentage than the industry average of unaffiliated reinsurance, but dramatically less use of offshore affiliate reinsurance. Moreover, based on the data in Exhibit 1, none of the top 20 writers have affiliate offshore reinsurance that is in excess of the 12.8% industry fraction for Homeowners Multiple Peril computed by Brattle for 2009. Thus, while it is true that unaffiliated reinsurance is a significant element in the Homeowners Multiple Peril market, offshore affiliate reinsurance appears to have no impact on the Florida market.

estimate for Catastrophe Exposure is significant and positive in the external [*i.e.*, third party] reinsurance equation. It is not significantly different from zero in the internal [*i.e.*, related party] reinsurance equation. This evidence is consistent with internal and external reinsurance serving different purposes.”

⁵ In developing individual state data, the Brattle Report applies results based on national data to individual states. This implicitly assumes that the national market share for each line of business also applies uniformly on the state level, which is not the case.

⁶ Some of these companies may be owned by U.S. domiciled companies and subject to U.S. tax.

⁷ Reinsurance utilization cannot be traced to individual risks or geographic regions, but is reported in the aggregate on NAIC Annual Statements.

Exhibit 1. -- Florida Homeowners Multiple Peril Market Share, 2009 (\$Thousands)

		Florida Homeowners Multiple Peril		All US Homeowners Multiple Peril							
Rank	Company	Direct Premium	Market Share	Direct Premium	Assumed from Unaffiliated	Ceded to Unaffiliated	Ceded % Direct plus Assumed	Assumed from Affiliates	Ceded to Affiliates	Affiliated Offshore Net Ceded	Affiliate Offshore Fraction
TOTAL		6,932,094	75.8%	36,899,850	269,784	4,772,530	12.8%	15,187,438	15,310,841	123,404	0.3%
1	State Farm Mutl Automobile Ins	888,326	12.8%	14,737,236	4,118	536,566	3.6%	-	-	-	0.0%
2	Citizens Property Ins Corp.	790,756	11.4%	790,756	-	170,469	21.6%	-	-	-	0.0%
3	Universal Insurance Hldgs Inc.	507,450	7.3%	513,341	-	406,793	79.2%	-	-	-	0.0%
4	USAA Insurance Group	347,315	5.0%	2,969,698	(767)	287,994	9.7%	226,403	226,304	(99)	0.0%
5	Tower Hill Group	293,217	4.2%	293,217	-	100,294	34.2%	288,815	323,632	34,817	11.9%
6	St. Johns Insurance Co.	269,871	3.9%	271,371	1,507	276,873	101.5%	-	-	-	0.0%
7	Florida Peninsula Holdings LLC	225,467	3.3%	225,467	17,436	129,607	53.4%	-	-	-	0.0%
8	ARX Holding Corp.	201,690	2.9%	321,405	-	115,006	35.8%	66,911	101,324	34,413	10.7%
9	Allstate Corp.	190,906	2.8%	6,837,286	14,360	588,123	8.6%	3,473,219	3,473,219	0	0.0%
10	HomeWise Holdings Inc.	185,010	2.7%	189,709	(294)	172,188	90.9%	-	-	-	0.0%
11	Liberty Mutual Holding Co.	183,668	2.6%	3,461,188	1,005	1,097,615	31.7%	4,828,452	4,820,154	(8,298)	-0.2%
12	American International Group	180,432	2.6%	716,389	268,279	125,810	12.8%	1,381,019	1,449,653	68,633	7.0%
13	Chubb Corp.	154,689	2.2%	1,772,268	2,329	169,383	9.5%	1,512,191	1,506,135	(6,056)	-0.3%
14	Royal Palm Insurance Co.	153,912	2.2%	153,912	28	72,071	46.8%	-	-	-	0.0%
15	United P&C Insurance Co.	134,906	1.9%	134,906	1,501	79,403	58.2%	-	-	-	0.0%
16	Nationwide Mutual Group	134,057	1.9%	2,909,148	(66,612)	136,554	4.8%	3,377,418	3,377,418	(0)	0.0%
17	Universal Group Inc.	112,222	1.6%	176,275	15,756	88,134	45.9%	-	-	-	0.0%
18	Northern Capital Insurance Co.	103,482	1.5%	103,482	10,707	65,406	57.3%	-	-	-	0.0%
19	Sthrn Farm Bureau Cas Ins Grp	100,281	1.4%	229,011	500	84,731	36.9%	33,010	33,005	(5)	0.0%
20	Security First Insurance Co.	93,783	1.4%	93,783	(69)	69,513	74.2%	-	-	-	0.0%