

Thoughts on the Supervisors Role in the Risk Management and Insuring of Natural Disasters: Implementing ICP 13

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Insuring Natural Disasters

- A lot of Models exist for protecting the public and their property from the risk of natural disasters, taking their structure from public policy debates and discussion. Much of this occurs outside the strict scope of insurance supervision but occurs in other planning, enforcement and response functions.
- In the US we have a mix of several, depending on the disaster, we either choose not to think much about it, have a pure public “insurance” mechanism, or rely on the private sector.
- In my state of Florida, the major catastrophic risk is hurricane, which is insured primarily in the private market, though some public mechanisms exist both in Florida and in other hurricane prone areas.
- In my comments today, I will use our situation as the basis for my comments. We’ve learned a lot, maybe not because we wanted to, but nature dictated we had to.



ICP 13: Reinsurance and Other Forms of Risk Transfer

The supervisor sets standards for the use of reinsurance and other forms of risk transfer, ensuring that insurers adequately control and transparently report their risk transfer programmes. The supervisor takes into account the nature of reinsurance business when supervising reinsurers based in its jurisdiction.



Florida's Supervisory Approach

- Our approach to supervising insurers with exposure to the catastrophic risk of hurricane is based on the premise that the private market will consistently provide the most efficient outcome, allowing our economy and our residents the best approach to recovering from a storm quickly and fully.
- In addition to the wide array of financial reporting and analysis all required of all insurers in the US through our standardized reporting and model laws regarding solvency and transparency, Florida has instituted a number of other supervisory tools and analytical methods following our experience, initially resulting from hurricane Andrew in 1992, and more recently, from the 4 major land falling hurricanes we experienced within 18 months during 2004-2005.
- These tools and methodologies can be divided into two categories:
 - **Before the Storm**
 - **After the Storm**



Before the Storm

- Ongoing Exposure Reporting
- Reinsurance Data Call
- Stress Testing



Ongoing Exposure Reporting

- Following Andrew in 1992, we became acutely aware of what we did not know
- Beginning in 1996 we began implementing a reporting system known as the Quarterly Supplemental Annual Report (QUASR)
- On a quarterly basis, every insurer, public or private, writing property insurance in Florida reports their writing on a quarterly basis *by line of business and by county*



Ongoing Exposure Reporting

- Reported Information includes:
 - Number of Policies in Force
 - Direct Premium
 - Exposure (in dollars)
- This information is used to track market trends, potential hot spots and any developing specific company trends or concerns
- Following Florida's longstanding principle of government in the sunshine, and consistent with the IAIS recently embraced focus on transparency, these QUASR reports are publicly available and are used by legislators, researchers, the media and the general public



Reinsurance Data Call

- Following the storms of 2004 and going into 2005, we began a process of gathering information from our insurers regarding their reinsurance programs in advance of hurricane season
- This reinsurance data call is a two step process
 - The initial reporting from insurers provides us with their intended reinsurance activity; how much are they buying, at what attachment points, type of cover, etc.
 - This is followed by a second report after they go to market that provides us with the information on what they actually purchased.
- This tool allows us not only a better picture of their reinsurance cover, but provides for yet another opportunity for communication and transparency between the insurer and the supervisor.



Stress Testing

- After monitoring developments in best practices and supervisory tools, three years ago we began implementing an additional analytical tool, a stress test.
- Prior to the onset of hurricane season, insurers file with us the results of stressing their existing portfolios against actual storms we identify from the data catalog of Florida land falling hurricanes.
- The results provide us with information on the level of losses and stress to capital and surplus the insurers would face if a previous storm were to repeat.



Stress Testing

- This stress test provides us with broader information than just relying on the reinsurance data call.
- The test and results also provides yet another point of communication and transparency between insurer and supervisor
- Interestingly, our industry was overwhelmingly supportive when we began this initiative and remain so.



After the Storm

- Disaster Reporting System
- Additional Supervisory Analysis



Disaster Reporting System

- Immediately after the last of the 2004 storms, we realized there was a lot of information we needed to ensure that the markets were working, claims were being paid and our market could recover
- To that end, we initiated a disaster reporting framework, that in progressive stages:
 - Initially requires insurers to report claim counts and estimated losses on a by line by county basis
 - As the recovery matures, we get reporting on claims paid, claims in process claims closed, updated estimates of ultimate losses, and impact on capital and surplus.
- And lucky us, we got to use the framework again in 2005, and as we were not the only state jurisdiction with hurricane losses in 2005, we worked with the NAIC to make this tool available for all states
- It remains ready to use again when the occasion will arise



Additional Supervisory Analysis

- The tools we use on an ongoing basis provide us with an analytical background and framework to effectively supervise and regulate specific company situations following a storm
- Our analytical team and direct supervisors will engage in progressively more intense communication on a close and continuous basis, involving additional reporting and analysis if required, for company's that may be showing signs of financial distress or problems in paying or closing claims. We use all of the regulatory tools we are allowed in law to accomplish this.



Developments in “Reinsurance” Markets”

- The reinsurance market has grown increasingly sophisticated in terms of its risk and exposure measurement and analysis.
- Natural disaster models capture this sophistication and have rapidly become an integral part of the supervisory dialog. Florida has addressed model concerns in two ways: we have a Commission that “approves” models and we have developed the Florida Public Hurricane model, using our university and scientific state resources, to give us as supervisors an independent tool to check for reasonableness.



Developments in “Reinsurance” Markets”

- The financial crisis of 2008 also impacted reinsurance markets. Institutional investors, (e.g. hedge funds and pension funds), looking for reasonable yields on their investments, discovered the long known but often overlooked diversification benefits of market based risk transfer products (e.g cat bonds, ILS securities, etc.)
- The growth in this areas, supported in many cases by the expertise of the traditional reinsurers, has added billions of dollars of risk capital to catastrophe risk markets globally.
- Florida recognized the potential of this market, and in 2010 issued a memorandum to the industry to actively consider thinking about these sources as well as traditional reinsurance. This was at the time considered somewhat of a controversial action.



Developments in “Reinsurance” Markets

- As these market based products continue to expand and be used by direct insurers, additional stresses are placed on supervisors to maintain and develop the expertise and market knowledge required to ensure that transactions being reviewed are truly legitimate risk transfer products.
- As well, I would like to think our market has been aided somewhat by my conscious effort to reach out to the global reinsurance market and develop relationships so that they understand my market and our regulatory philosophy, as well as the attendant opportunities, risks and responsibilities.



Please visit us at www.FLOIR.com for more information on these tools and reports

THANK YOU

QUESTIONS??



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