POLICY BRIEF

Road to Recovery:

Clearing the Path to Meaningful Reforms in Florida's Insurance Arena

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Despite several commonsense reforms enacted by lawmakers over the past few years, Florida's property insurance market remains on a downward spiral. Dozens of insurers have dramatically reduced policies in the state through non-renewal, withdrawn from the market, or been liquidated in just the past two years, and the companies that remain have had to substantially increase their rates to levels almost three times the national average to compensate for massive, billion-dollar annual losses. Hundreds of thousands of policies have migrated to Florida's state-run backstop insurer Citizens Property Insurance Corporation, whose policy count has more than doubled to 1.1 million policies over just the last two years.[1]

There are many inherent risk factors unique to Florida that would justify somewhat more expensive property insurance compared with the rest of the country and a relatively more complex insurance system tailored to such circumstances. The most obvious is Florida's unique geographic location as a low-lying tropical peninsula extending hundreds of miles into some of the warmest, storm-prone

waters in the world, which makes it susceptible to more frequent largescale wind and flood events.

Another factor is Florida's economic and population growth, which for decades has outpaced most other states: in 2018 Florida's GDP surpassed $1 trillion making it the 17th largest economy in the world[2] and, last year, the state was awarded an additional congressional seat following the 2020 Census that found a population growth of 14.6 percent over the last decade.[3] In 2020 alone, Florida experienced the largest change in net move-ins of any state[4] largely due to the state's aversion to onerous pandemic restrictions and lockdowns.

Although such growth is a "good problem," it is a problem nonetheless as it further clogs roadways, increases housing costs, and concentrates more people and wealth predominantly in the state's more desired coastal areas which are naturally prone to more storms and flooding, and where it is more expensive to build and repair. Indeed, these are legitimate cost drivers that would justify some gradual rate escalation, especially when combined with the increasing price of risk transfer products (i.e., reinsurance) after recent catastrophic losses globally and inflation spikes domestically.[5]

But none of the inherent cost drivers mentioned above can account for the ongoing dramatic double-digit insurance rate increases Floridians are feeling or the multiple years of net profit losses[6] leading to insurer insolvencies even in hurricane-free years. As such, it is evident that these are being propelled by other cost drivers disconnected from the state's natural risks, global reinsurance prices, and other organic factors.

In 2019, Florida accounted for 76 percent of all insurance litigation nationwide, even though the state only accounted for 8 percent of all insurance claims filed during the same period.[7] As of August 2022, those figures have only worsened to Florida accounting for almost 80 percent of nationwide litigation and 9 percent of claims filed.[8] When these figures are broken down further, the data show that just about every other state averages under 1,000 such lawsuits annually, while Florida hovers around 100,000 lawsuits. Therein lies the principal driver of massive profit losses for insurance companies despite the double-digit rate increases imposed on consumers to offset those losses.

Florida lawmakers have taken steps to address this problem in recent years. However, many of the reforms either came too late or were too modest. Had some of those very reforms been implemented just a few years earlier, it would be unlikely Florida's insurance market would be in the dire state we find it today.

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The following report revisits the steps the Florida Legislature has taken in recent years to shore up the state's property insurance market, why the timing of meaningful reforms matter, and how it must build upon past reforms during this year's upcoming special session and 2023 regular legislative session to stabilize the insurance market and hopefully promote more investment, competition, and lower rates for consumers.

Florida's Litigation Problem

For almost two decades, the Florida property insurance market has been plagued by excessive litigation and fraud stemming from insurance claims enabled by the exploitation of legal loopholes and court decisions governing attorney fees, bad faith rules, and an insurance practice known as "Assignment of Benefits" (AOB).

An AOB allows a third party – such as a roofing contractor, water-extraction company, or other vendor – to stand in the place of the insured and assume the policyholder's benefits by collecting payments directly from the insurance company for a covered loss. In doing so, the policyholder also transfers to the third party the right to negotiate and adjust the claim in question. Hence, no payments of reimbursement are made directly to the policyholder.

Most health insurance and personal injury protection (PIP) auto policies function under this arrangement, which allows medical providers to collect payments directly from the insurer for covered healthcare services rather than reimbursing the policyholder.

Over the last two decades, AOBs became more common in property insurance claims where a policyholder would exercise the right to assign his or her policy benefits for a specific loss,[9] including the benefit in Florida law allowing a policyholder to sue an insurance company and then have their attorney fees covered by the insurer should the policyholder prevail, also known as the "one-way attorney fee" provision.[10]

With the homeowner out of the picture and no longer in a position to negotiate and thus mitigate repair costs, crooked contractors would oftentimes inflate their bills, and/or charge for repairs that were unnecessary or unrelated to the loss in question. In more and more cases, contractors partnered with trial lawyers as a matter of practice, availing themselves of the aforementioned one-way attorney fee benefit in state law, as well as the civil remedy statute (commonly referred to as the "bad-faith" law) designed to protect ordinary consumers.

The constant threat of litigation and massive judgments far be-

yond policy coverage limits borne out of lawyers exploiting one-way attorney fee and bad faith laws served as a perverse incentive for insurers to settle for amounts greater than they otherwise would have.

These abuses amplified the number and severity of claims and caused insurance rates to skyrocket despite an unprecedented "hurricane drought" in which no storm struck Florida in the decade preceding 2016. Consumers had legitimate concerns when they complained about their rates rising so sharply, especially in the absence of hurricanes and with reinsurance rates and other risk transfer products at near-record low prices.

HB 7065 – 2019

After seven years of deliberation and several proposed reforms, the Legislature passed HB 7065 in 2019 to address unrestrained litigation incentivized by the one-way attorney fee law as it related to the unrestricted use of AOBs. The bill established common-sense rules related to executing AOBs and created an attorney fee formula based on the difference between the demand, offer, and judgement to determine which party, if any, receives attorney fees in AOB-related lawsuits.[11]

Prior to HB 7065, there were justified fears that the AOB cottage industry could easily pivot from exploiting non-catastrophe losses such as water damage from broken pipes to more lucrative hurricane-related claims should a major storm finally strike the state after its decade-long dry spell. Indeed, even reinsurers expressed concerns as early as 2016 that the issue was trickling into Florida's reinsurance pricing[12] due to fears that reinsurers would be on the hook for artificially inflated hurricane claims stemming from AOB abuse and excess litigation.

And they were right.

Although better late than never, AOB reform arrived three years too late. Florida's decade-long hurricane drought ended when Hurricane Hermine made landfall in 2016, and major Hurricanes Irma and Michael in the years that followed. The catastrophic losses from these hurricanes allowed contractors and plaintiff's attorneys to continue exploiting the laws that existed before HB 7065 was enacted in 2019, but this time for much larger hurricane claims, as reinsurers and other stakeholders feared. Just days after Hurricane Michael struck the Florida Panhandle in October 2018, for example, there were already reports of vendors pushing AOBs in storm-ravaged areas.[13]

Instead, out of 52 carriers that represented the Florida domestic insurance market in 2021, 49 companies generated net income losses in the years since 2017. This represented an annual deficit of $1 billion for the industry, including national carriers,39 and the losses are growing.

But the abuse did not simply vanish in 2019 when reforms were enacted. Florida law allowed policyholders to file a windstorm claim or supplemental claim up to three years after a storm's landfall. Although the Legislature eventually reduced the window to file claims from three to two years as a result of SB 76 in 2021,[14] the rules for any insurance claim are governed by the contractual provisions written in the policy and the laws in force at the time of the loss, not the laws in force when the claim is filed; hence, the pre-reform exploitable rules have been argued to apply.

This litigation "tail" is why the insurance market is still bleeding from those hurricanes so many years after they struck. Citizens alone was still reporting over 900 AOB-related lawsuits per month in 2021—the majority of those from losses related to Hurricane Irma in 2017 prior to the enactment of HB 7065. Even today, insurers are still paying and experiencing losses from those claims as lawsuits oftentimes take years to resolve.

Had the Legislature enacted those reforms just three years earlier before hurricanes began to strike the state once more, Floridians would likely be looking at a far healthier property insurance market.

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If these payouts were mostly due to actual losses from an outbreak of storms or legitimate damage caused by some other covered perils, and most of that money went to make policyholders whole, that would be one thing. But that is not the case in Florida. $15 billion was paid out in claims by insurers across the state between 2013 and 2021; out of that amount, 71 percent went to pay attorney fees, 21 percent went to pay insurer defense costs, and a meager eight percent went to the policyholders for their losses.[16] In 2021 alone, Florida's domestic insurers spent over $3 billion in legal defense and containment, which is more than double what they spent for the same in 2016.[17]

SB 76 – 2021

Given the dire state of the insurance market, the industry's accruing losses, and consequent double-digit rate increases plaguing consumers, the legislature approved another insurance and tort reform package in 2021, which included provisions that built upon HB 7065.

SB 76, which passed the last day of the 2021 Legislative Session, tightens Citizens' eligibility requirements and eased—but did not eliminate—its statutory cap on rate increases; requires plaintiffs to notify an insurer before a lawsuit is filed in the form of a pre-suit demand at least 10 days before filing suit; allows an insurer to use mediation or another form of alternative dispute resolution after receiving a pre-suit notice; replaces the one-way attorney fee statute with a formula modeled after the AOB attorney fee reforms in HB 7065 to make the recovery of attorney fees and costs contingent on obtaining a judgment for indemnity that exceeds the pre-suit offer made by the insurance company; and reduces the deadline to file insurance claims from three to two years from the date of loss, except for supplemental claims, which will have an additional year.[18]

SB 76 took effect in July of 2021, but its benefits will take years to have a demonstrable effect on the property insurance market as its provisions were not applied retroactively.

The result? Florida consumers are still seeing their property insurance rates soar by double digits. The "lucky" ones will pay, on average, $4,231 for their homeowners insurance this year—almost three times the national average of $1,544 for the same coverage.[19] The unlucky ones are being canceled or non-renewed altogether.

To make matters worse, the double-digit rate increases consumers are experiencing, as well as private insurers' decisions to reduce their exposure, are forcing policies back into state-run property insurer Citizens en masse. Because Citizens premium increases are capped by law,[20] it has been unable to keep up with the necessary rate increases to remain actuarially sound, which has created a widening gap between the rates charged by Citizens and those charged by private insurers. Due to that price difference, consumers are increasingly and understandably turning to government-run Citizens for their coverage instead of admitted carriers, thus shifting more of the state's enormous risk away from the private market and onto taxpayers.

In September 2021, Citizens had almost 709,000 policies in force accounting for about nine percent of the Florida market;[21] the following month, that figure hit 10 percent, and fast-forwarding to this report's date of publication, Citizens has over 1.1 million policies. Just three years ago, Citizens had less than 420,000[22] policies and only 4.5 percent of the market.[23]

SB 2-D - 2022

After continued underwriting losses and multiple insurance company downgrades and insolvencies,[24] Governor Ron DeSantis issued a call for the Legislature to convene a special session on property insurance[25] in May of 2022 to stop the bleeding ahead of the 2022 hurricane season. The result was SB 2-D, which contained several bold provisions related to property insurance regulation and tort reform. They include:

- Eliminating the one-way attorney fee benefit in state law as it relates to AOBs; thus, the one-way attorney fee applies only to the named insured or beneficiary in the policy in suits arising under residential or commercial property insurance policies and cannot be assigned or transferred to a third party.
- The creation of a temporary Reinsurance to Assist Policyholders (RAP) program to soften insurance rate increases by providing up to $2 billion in reinsurance coverage from the state's general revenue funds via the Florida Hurricane Catastrophe Fund with the intention of passing those savings on to policyholders and buying time to stabilize the market.
- Prohibiting roofers from paying or absorbing insurance deductibles and requiring certain disclosures on roofing advertisements; allowing insurers to include a roof deductible if certain requirements are met.
- Requiring a claimant to establish that a property insurer breached the contract in order to prevail in a bad faith claim.
- Codifying the lodestar method of calculating attorney fees arising out of property insurance claims and drastically restricting the application of contingency fee multipliers to only rare and exceptional circumstances, which will significantly reduce the amounts insurers pay in attorney fees.[26]

Some of these are significant reforms that experts, stakeholders, and the insurance industry have been requesting for years. However, because of the time it takes for insurance reforms to fully kick in, these again may have come too late given the dire state of Florida's property insurance market.

Barely two months after these reforms were passed, Florida's primary insurance rating agency Demotech warned that 17 Florida insurers were facing downgrades,[27] which would be catastrophic not only for the market and companies in question, but also the hundreds of thousands of policyholders whose federally-backed mortgage lenders would not recognize coverage from downgraded insurers and would be force-placed with collateral protection

insurance carriers at devastatingly higher rates. In August alone, Demotech downgraded three major Florida insurers,[28] and one went insolvent, becoming the fifth Florida property insurer to be dissolved in 2022.[29]

During this summer's reinsurance renewal period, Florida's reinsurance rates increased by 50 percent on average, which is considered near "distress" levels for many primary insurance companies purchasing said coverage. One reinsurer noted that "the challenging and opaque regulatory situation in the admitted homeowners' market was the single largest factor [for the reinsurance rate increase] as opposed to actual weather events themselves."[30]

It is incumbent on Florida lawmakers to take further steps to tighten the tourniquet to not just reduce losses immediately in hopes of salvaging what is left of the market, but also to restore predictability, eliminate the uncertainty that repels investment, and make it to where potential losses can finally be properly modeled and priced accordingly.

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Solutions

I. Lawsuit Reform

The root cause of Florida's property insurance crisis is litigation run amok. All the other insurance-related issues facing the state—hurricane losses, reinsurance rate increases, the growth of Citizens, rating downgrades, and insolvencies—are either exacerbated or caused by the state's litigation problem.

REPEAL ONE-WAY ATTORNEY FEE LAW

In order to restore sanity and predictability to the state's insurance system, one-way attorney fee laws must be repealed and insurance litigants should have to follow the common-law American rule—that parties bear their own litigation costs, the rule applicable in most states and for most types of litigation. The absence of a one-way attorney fee benefit will not preclude aggrieved consumers from suing an insurance company they believe has low-balled or mistreated them, and they will still enjoy legal protections against insurers who legitimately act in bad faith. Most other states operate under these, or similar, arrangements and consumers are well served.

CLARIFY WHAT CONSTITUTES "BAD FAITH"

A second and equally important way to reduce frivolous and costly litigation is to clarify the state's civil remedy law to ensure that it protects consumers by appropriately penalizing bad actors in the insurance industry and not existing to reward unscrupulous lawyers with cash windfalls.

Florida's civil remedy statute outlines an insurer's responsibilities to act in good faith to settle a claim and establishes a process for claimants who believe insurers may have acted wrongfully (or in bad faith).[31] It requires a claimant to file a civil remedy notice, which starts a 60-day window for the insurer to pay or dispute the amount a policyholder believes was underpaid by the insurer and is now demanding. Oftentimes, these disputes go to an appraisal process that takes longer than 60 days. As such, if the appraiser ultimately determines that the insurer indeed owes any money due to an underpayment for a past claim—even if it is a significantly lower amount than the claimant was demanding—it likely triggers the payment of legal fees sometimes far above policy limits simply because the appraisal payment was issued after the 60-day window. Less scrupulous attorneys will even file a civil remedy notice to start the 60-day "clock" and instruct their clients to not communicate with the insurance company until Day 61 or later so that if the insurer offers or makes any payment whatsoever it will trigger the payment of exorbitant fees. This is neither fair nor the intention of the state's civil remedy law, which exists to punish insurers that legitimately and willfully engage in bad behavior.

To fix this, lawmakers should clarify the existing provision in state law that requires a claimant to establish that a property insurer has breached the contract before prevailing in a bad faith claim.[32] The best way to accomplish this is to explicitly require a finding by a court that an insurer has indeed breached the contract as a precondition to file a bad faith claim. Currently, an insurer merely agreeing to pay any amount after the 60-day cure period following a claimant's filing of a civil remedy notice and subsequent suit may be considered a "confession of judgment," which opens the insurer to a costly civil remedy claim, even if the insurer took every step to settle the dispute in good faith. Requiring an actual court ruling finding that an insurer breached the contract before a bad faith lawsuit can be filed will filter out frivolous lawsuits while preserving the spirit of the bad faith law that protects consumers and holds bad actors accountable. Mere disagreements on prices when both sides have consistently acted in good faith should be resolved through appraisal processes and other conflict

resolution methods.

This elegant solution makes policyholders whole and prevents low-ball offers from insurers. In the event of a low-ball offer, the policyholder can pursue a breach of contract action. Upon prevailing, the policyholder has now established a breach of contract and bad action by the insurer. The insurer will be liable for "extra-contractual damages" under the civil remedy statute, namely the policyholder's attorney fees for having to pursue a breach of contract action. In the end, the policyholder recovers the contractual damages plus the attorney fees, which is a costly punishment for the culpable insurer. Ultimately, most disagreements on scope and price will be resolved by the appraisal process contained in the insurance contract, not contract litigation; thus, massive amounts of potential litigation will be avoided.

Ii. Insurance Regulatory Reforms

Stopping the bleeding of massive losses due to excess litigation should be the Legislature's top priority, but to stabilize the market and ensure its long-term viability, lawmakers also should take steps to attract investors and outside capital to promote competition and spread Florida's enormous risk beyond its borders. Given current realities, it is doubtful investors will want to risk their capital in the state's "dire" property insurance market, but a few tweaks to existing law may encourage some modest investment to buy some time, keep the market afloat, and hopefully attract greater investment as the market improves.

A. OPEN SURPLUS LINES TO HO3 MARKET

First, lawmakers can and should explore opening the HO3* policies market to surplus lines** insurance carriers, which would not be burdened by the "tail" of claims and litigation of past storms as new entrants into the market. As such, that "baggage" would not be reflected in their rates, and they would have the added benefit of operating fresh under new reforms designed to mitigate against those problems prospectively.

B. TIGHTEN CITIZENS' ELIGIBILITY

Another way for lawmakers to attract new capital is by reining in the growth of Citizens and creating a level of predictability and measurability as it relates to transferring Citizens' policies to the private market. SB 76 tightened Citizens' eligibility by steering potential Citizens policyholders to private carriers if a comparable policy was available within 20 percent of the premium Citizens was charging. However, incumbent Citizens policyholders are currently under no obligation to switch to a private carrier even if one or more offers them a quote within the 20 percent range; instead, a Citizens policyholder must affirmatively opt-out of Citizens at his or her discretion.[33] If Citizens is truly meant to be an "insurer of last resort," it should extend the same eligibility standards to its existing policyholders so they do not remain with Citizens in perpetuity when comparable coverage is available in the private market. This change would allow private insurers to quantify how many policies they could realistically take and thus would be far more likely to attract investors to do so and enter into depopulation agreements with Citizens to write policies at rates unburdened by the litigation "tail" from past losses.

C. FURTHER RESTRICT WHERE CITIZENS CAN WRITE NEW POLICIES

Citizens should also further limit where it can write policies to encourage private insurers and their investors to enter those markets. In 2013 the Florida Legislature restricted[34] Citizens from writing policies covering newly constructed structures, or buildings whose footprints have been substantially expanded after 2015 if they lie seaward of the Coastal Construction Control Line (CCCL) or in any federally-designated wetland (existing structures were grandfathered for coverage eligibility).[35]

The CCCL is a line of jurisdiction in Florida law defining the landward limit of the state's authority to regulate coastal construction. It has been established along most of Florida's sandy beachfront properties but does not extend into the Florida Keys or the mostly vegetated coastline of the state's "Big Bend" area.[36] This coverage prohibition has served a dual purpose:

- Prospectively reducing the growth of Citizens' risk exposure by prohibiting it from covering the newest, most expensive structures in the state's most storm and flood prone areas; and
- Keeping this enormous risk in the appropriately priced private market thereby encouraging any new development in these high-risk areas to be built stronger and more resiliently in order to obtain the most affordable coverage possible.

Lawmakers should consider expanding this prohibition to include more of the state's most storm and flood-prone areas by expanding the prohibition to include newly built or substantially

**HO-3 insurance policies are the most common form of single-family home insurance that protect policyholders against property damage, legal liabilities and other expenses associated with unexpected disasters.*

***Surplus Lines carriers, also known non-admitted or unlicensed insurers, are authorized to write certain property and casualty insurance policies, but are not regulated by the state. They are usually specialized insurers covering certain risks that traditional regulated carriers are unable or unwilling to cover.*

expanded structures within a *certain distance* of the CCCL (instead of merely seaward of the line). This would limit the growth of Citizens in the areas at highest risk of natural disasters and serve as a disincentive to over-develop and concentrate more wealth and people on barrier islands and other high-risk coastal zones. It would have positive environmental impacts as well as incentivize capital investments into Florida insurers that specialize in coastal properties as they would not be competitively undermined by the artificially suppressed rates offered by Citizens.

These solutions would inject much-needed predictability into the state's insurance market, which would make investors look upon it more favorably; additionally, any efforts to slow and eventually reverse the migration of policies into government-run Citizens will protect the state's taxpayers and allow for more competition between private carriers.

> All throughout, the common denominator remained: laws like the one-way attorney fee that incentivized litigation and an overall culture of "sue first and ask questions later."

Conclusion

High insurance rates are appropriate when they reflect actual risks. Costs inherent to a particular region may be impossible to remedy through laws or the insurance system. However, it is apparent Florida's entrenched culture of litigiousness has been the root cause of the state's insurance problems for decades—from the medical malpractice and workers compensation insurance crises of 20 years ago, to property insurance lawsuit abuse today.

To tackle each of those insurance market crises, lawmakers enacted modest reforms around the margins to address specific abuses and fraud in hopes that it would be more difficult or otherwise less enticing for unscrupulous actors to continue fleecing insurers and consumers. But then the bad actors would simply pivot to exploiting other loopholes and attempting to catch up with their schemes became an almost yearly game of whack-a-mole in Tallahassee. All throughout, the common denominator remained: laws like the one-way attorney fee that incentivized litigation and an overall culture of "sue first and ask questions later."

It took meaningful tort and legal reforms, including limits on attorney fees and damage caps in 2003, to finally restore sanity to the state's medical malpractice and workers compensation insurance systems.[37]

Almost 20 years later, it is clear that Florida's current property insurance malaise is likewise due almost entirely to the state's legal climate, which is ranked near the bottom at #46 among the 50 states.[38]

Lawmakers correctly identified many of the culprits behind the state's current property insurance woes and enacted meaningful legal and regulatory reforms in recent years. Unfortunately, in the time it will take for all those reforms to fully kick in, the market is still being plundered by litigation and the losses it is incurring are putting insurers out of business and ravaging policyholders. As such, the time for timid, modest intervention has passed. The Legislature must tackle the holy grail of litigation incentives: the one-way attorney fee statute. It should also get ahead of other legal issues such as clarifying the state's bad faith laws so the cottage industry of insurance fleecers does not pivot there after the one-way attorney fee statute is repealed.

Florida cannot afford to put off these tough but needed reforms any longer. If there is one lesson to be learned it is that the consequences of delaying bold action are enduring and expensive.

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