STATE OF FLORIDA
DIVISION OF ADMINISTRATIVE HEARINGS

HARTFORD FIRE INSURANCE COMPANY, HARTFORD INSURANCE OF THE SOUTHEAST, HARTFORD CASUALTY INSURANCE COMPANY, TWIN CITY FIRE INSURANCE COMPANY, HARTFORD UNDERWRITERS INSURANCE COMPANY, AND HARTFORD ACCIDENT AND INDEMNITY COMPANY,	)	
Petitioners,	)	
vs.	)	Case Nos. 07-5185
	)	07-5186
OFFICE OF INSURANCE REGULATION,	)	07-5187
	)	07-5188
Respondent.	)	

RECOMMENDED ORDER

On January 22-24, 2008, a hearing was held in Tallahassee, Florida, pursuant to the authority set forth in Sections 120.569 and 120.57(1), Florida Statutes. The case was considered by Lisa Shearer Nelson, Administrative Law Judge.

APPEARANCES

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STATEMENT OF THE ISSUES

Whether Petitioners' proposed rates are justified pursuant to the requirements of Section 627.062, Florida Statutes, or whether the Department of Financial Services, Office of Insurance Regulation (OIR) was correct in denying the requested rate increases.

PRELIMINARY STATEMENT

These cases arose on September 10, 2007, when the OIR sent Notices of Intent to Disapprove four filings for rate increases Petitioners (collectively referred to as Hartford) had filed for approval. On November 9, 2007, Amended Petitions for Administrative Hearing Involving Disputed Issues of Material Fact were filed in each case, and the OIR forwarded the Amended Petitions to the Division of Administrative Hearings for assignment of an administrative law judge. All four cases were assigned to the undersigned.

On November 20, 2007, the parties filed Joint Motions to Consolidate, which were granted and the cases were consolidated by an order issued the next day. By agreement of the parties, the case was noticed for hearing January 22-24, 2008.

The cases proceeded to hearing as scheduled. The first morning of the hearing, Hartford filed an Unopposed Motion for Protective Order requesting that those matters contained in the insurance rate filings (Joint Exhibits numbered 2 through 5) that are designated as trade secrets be protected from dissemination

and remain sealed. The Unopposed Motion for Protective Order was granted and those documents in Joint Exhibits numbered 2 through 5 that were sealed and marked as trade secrets have been reviewed as necessary and returned to the sealed envelopes. Those documents maintain their trade secret designation and will be returned to the OIR at the submission of this Recommended Order as sealed documents.

At hearing, Hartford presented the testimony of 6 witnesses and Hartford's Exhibits numbered 1 through 48 were admitted into evidence. Respondent presented the testimony of one witness and Respondent's Exhibits numbered 1 through 4 were also admitted. The parties stipulated to the admission of Joint Exhibits numbered 1 through 18.

The parties filed a Joint Prehearing Statement in which they stipulated to certain facts related to the filings. Those facts have been incorporated into the findings of fact below. At the conclusion of the hearing, the OIR requested additional time for the preparation of its proposed recommended order. The parties were given until February 18, 2008, to file their proposed recommended orders. The transcript was filed with the Division February 1, 2008. Due to a change in counsel, the Department requested until March 10, 2008 for the filing of the proposed recommended orders, and an extension was granted until March 3, 2008. Proposed Recommended Orders from both sides were timely

filed. Both have been carefully considered in the preparation of this Recommended Order.

FINDINGS OF FACT

1. The Hartford companies are property and casualty insurers transacting insurance in the State of Florida pursuant to valid certificates of authority and the Florida Insurance Code. Two types of personal lines insurance filings submitted by Hartford to the OIR are at issue in this proceeding: two filings for homeowners insurance (Case Nos. 07-5185 and 07-5186) and two filings for dwelling fire insurance (Case Nos. 07-5187 and 07-5188). Hartford's substantial interests are affected by the notices disapproving the filings in this case.

2. Homeowners insurance includes coverage for a variety of perils in and around a home, is usually purchased by a homeowner, and covers both the structure and the contents of a home. Dwelling/fire insurance is usually purchased by the owners of properties that are leased or rented to others, and provides coverage for the structure only. Both types of insurance cover damage caused by hurricanes.

The New Legislation and its Requirements

3. In a special session held in January 2007, the Florida Legislature enacted changes to the Florida Hurricane Catastrophe Fund (CAT Fund), as reflected in Chapter 2007-1, Laws of Florida.

4. The special session was precipitated by a perceived crisis regarding the cost and availability of homeowners

insurance after the 2004 and 2005 hurricane seasons. As a result of the substantial number of claims incurred after multiple severe hurricanes each of these years, changes in the insurance marketplace resulted in some insurance companies withdrawing from the Florida market, others non-renewing policies, one company becoming insolvent, and the cost for reinsurance available to all insurers rising dramatically.

5. One of the primary features of the legislation was an expansion of the CAT Fund. The CAT Fund was established in 1993 after Hurricane Andrew to provide reinsurance to insurers for property insurance written in Florida at a price significantly less than the private market. The CAT Fund is a non-profit entity and is tax exempt.

6. Prior to the enactment of Chapter 2007-1, the CAT Fund had an industry-wide capacity of approximately $16 million. The purpose of the changes enacted by the Legislature was to reduce the cost of reinsurance and thereby reduce the cost of property insurance in the state. As a result of Chapter 2007-1, the industry-wide capacity of the CAT Fund was increased to $28 billion, and insurers were given an opportunity to purchase an additional layer of reinsurance, referred to as the TICL layer (temporary increase in coverage limit), from the CAT Fund.

7. Section 3 of Chapter 2007-1 required insurers to submit a filing to the OIR for policies written after June 1, 2007, that took into account a "presumed factor" calculated by OIR and that

purported to reflect savings created by the law. The new law delegated to the OIR the duty to specify by Order the date such filings, referred to as "presumed factor filings" had to be made.

8. On February 19, 2007, the OIR issued Order No. 89321-07. The Order required insurers to make a filing by March 15, 2007, which either adopted presumed factors published by the OIR or used the presumed factors and reflected a rate decrease taking the presumed factors into account. The presumed factors were the amounts the OIR calculated as the average savings created by Chapter 2007-1, and insurers were required to reduce their rates by an amount equal to the impact of the presumed factors.

9. The OIR published the presumed factors on March 1, 2007. In its March 15, 2007, filings, Hartford adopted the presumed factors published by OIR. As a result, Hartford reduced its rates, effective June 1, 2007, on the products at issue in these filings by the following percentages:

Case No. 07-5185 homeowners product:	17.7%
Case No. 07-5186 homeowners product:	21.9%
Case No. 07-5187 dwelling/fire product:	8.7%
Case No. 07-5188 dwelling/fire product:	6.2%

10. The Order also required that insurers submit a "True-Up Filing" pursuant to Section 627.026(2)(a)1., Florida Statutes. The filing was to be a complete rate filing that included the company's actual reinsurance costs and programs. Hartford's filings at issue in these proceedings are its True-Up Filings.

The True-Up Filings

11. Hartford submitted its True-Up filings June 15, 2007. The rate filings were certified as required by Section 627.062(9), Florida Statutes. The filings were amended August 8, 2007.

12. Hartford's True Up Filings, as amended, request the following increases in rates over those reflected in the March 15, 2007, presumed factor filings:

Case No. 07-5185 homeowners product:	22.0%
Case No. 07-5186 homeowners product:	31.6%
Case No. 07-5187 dwelling and fire product:	69.0%
Case No. 07-5188 dwelling and fire product:	35.9%

13. The net effects of Hartford's proposed rate filings result in the following increases over the rates in place before the Presumed Factor Filings:

Case No. 07-5185 homeowners product:	.4%
Case No. 07-5186 homeowners product:	2.8%
Case No. 07-5187 dwelling/fire product:	54.3%
Case No. 07-5188 dwelling/fire product:	27.5%

14. Case Nos. 07-5185 and 07-5186 (homeowners) affect approximately 92,000 insurance policies. Case Nos. 07-5187 and 07-5188 (dwelling/fire) affect approximately 2,550 policies.

15. A public hearing was conducted on the filings August 16, 2007. Representatives from Hartford were not notified prior to the public hearing what concerns the OIR might have with the filings. Following the hearing, on August 20, 2007, Petitioners provided by letter and supporting documentation

additional information related to the filings in an effort to address questions raised at the public hearing.

16. The OIR did not issue clarification letters to Hartford concerning any of the information provided or any deficiencies in the filings before issuing its Notices of Intent to Disapprove the True-Up Filings.

17. All four filings were reviewed on behalf of the OIR by Allan Schwartz. Mr. Schwartz reviewed only the True-Up Filings and did not review any previous filings submitted by Hartford with respect to the four product lines.

18. On September 10, 2007, the OIR issued Notices of Intent to Disapprove each of the filings at issue in this case. The reasons give for disapproving the two homeowners filings are identical and are as follows:

> Having reviewed the information submitted, the Office finds that this filing does not provide sufficient documentation or justification to demonstrate that the proposed rate(s) comply with the standards of the appropriate statute(s) and rules(s) including demonstrating that the proposed rates are not excessive, inadequate, or unfairly discriminatory. The deficiencies include but are not limited to:
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> 1. The premium trends are too low and are not reflective of the historical pattern of premium trends.
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> 2. The loss trends are too high and are not reflective of the historical pattern of loss trends.

3. The loss trends are based on an unexplained and undocumented method using "modeled" frequency and severity as opposed to actual frequency and severity.

4. The loss trends are excessive and inconsistent compared to other sources of loss trends such as Fast Track data.

5. The catastrophe hurricane losses, ALAE and ULAE amounts are excessive and not supported.

6. The catastrophe non-hurricane losses, ALAE and ULAE amounts are excessive and not supported. The particular time period from 1992 to 2006 used to calculate these values has not been justified. There has been no explanation of why the extraordinarily high reported losses for 1992 and 1993 should be expected to occur in the future.

7. The underwriting profit and contingency factors are excessive and not supported.

8. Various components underlying the calculation of the underwriting profit and contingency factors, including but not limited to the return on surplus, premium to surplus ratio, investment income and tax rate are not supported or justified.

9. The underwriting expenses and other expenses are excessive and not supported.

10. The non-FHCF reinsurance costs are excessive and not supported.

11. The FHCF reinsurance costs are excessive and not supported.

12. The fact that no new business is being written has not been taken into account.

13. No explanation has been provided as too [sic] Hartford believes it is reasonable to return such a low percentage of premium in the form of loss payments to policyholders. For example, for the building policy forms, only about 40% of the premium requested by

> Hartford is expected to be returned to policyholders in the form of loss payments. As a result of the deficiencies set forth above, the Office finds that the proposed rate(s) are not justified, and must be deemed excessive and therefore, the Office intends to disapprove the above-referenced filing.

19. The Notices of Intent to Disapprove the two dwelling/fire filings each list nine deficiencies. Seven of the nine (numbers 1-6 and 8) are the same as deficiencies listed for the homeowners filings. The remaining deficiencies named for Case No. 07-5187 are as follows:

> 7. The credibility standard and credibility value are not supported.
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> 9. No explanation has been provided as too (sic) why Hartford believes it needs such a large rate increase currently, when the cumulative rate change implemented by Hartford for this program from 2001 to 2006 was an increase of only about 10%.

20. The deficiencies listed for Case No. 07-5188 are the same as those listed for Case No. 07-5187, with the exception that with respect to deficiency number 9, the rate change implemented for the program in Case No. 07-5188 from 2001 to 2006 was a decrease of about -3%.

Documentation Required for the Filings

21. Florida's regulatory framework, consistent with most states, requires that insurance rates not be inadequate, excessive, or unfairly discriminatory. In making a determination concerning whether a proposed rate complies with this standard, the OIR is charged with considering certain enumerated factors in

accordance with generally accepted and reasonable actuarial techniques.

22. Chapter 2007-1 also amended Section 627.062, Florida Statutes, to add a certification requirement. The amendment requires the chief executive officer or chief financial officer and chief actuary of a property insurer to certify under oath that they have reviewed the rate filing; that to their knowledge, the rate filing does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which the statements were made, not misleading; that based on their knowledge, the information in the filing fairly presents the basis of the rate filing for the period presented; and that the rate filing reflects all premium savings reasonably expected to result from legislative enactments and are in accordance with generally accepted and reasonable actuarial techniques. § 627.062(9)(a), Fla. Stat. (2007).

23. Actuarial Standards of Practice 9 and 41 govern documentation by an actuary. Relevant sections of Standard of Practice 9 provide:

> 5.2 Extent of documentation - . . . Appropriate records, worksheets, and other documentation of the actuary's work should be maintained by the actuary and retained for a reasonable length of time. Documentation should be sufficient for another actuary practicing in the same field to evaluate the work. The documentation should describe clearly the sources of data, material assumptions, and methods. Any material

> changes in sources of data, assumptions, or methods from the last analysis should be documented. The actuary should explain the reason(s) for and describe the impact of the changes.
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> 5.3 Prevention of misuse - . . . The actuary should take reasonable steps to ensure that an actuarial work product is presented fairly, that the presentation as a whole is clear in its actuarial aspects, and that the actuary is identified as the source of the actuarial aspects, and that the actuary is available to answer questions.. . . .
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> * * *
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> 5.5 Availability of documentation- Documentation should be available to the actuary's client or employer, and it should be made available to other persons when the client or employer so requests, assuming appropriate compensation, and provided such availability is not otherwise improper. . . .

24. In determining the appropriate level of documentation for the proposed rate filings, Petitioner relied on its communications with OIR, as well as its understanding of what has been required in the past. This reliance is reasonable and is consistent with both the statutory and rule provisions governing the filings.

Use of the RMS Catastrophic Loss Projection Model

25. In order to estimate future losses in a rate filing, an insurer must estimate catastrophic and non-catastrophic losses. Hartford's projected catastrophic losses in the filings are based upon information provided from the Risk Management Solutions (RMS) catastrophic loss projection model, version 5.1a. Hartford's actuaries rely on this model, consistent with the

standards governing actuarial practice, and their reliance is reasonable.

26. Catastrophe loss projection models may be used in the preparation of insurance filings, if they have been considered by and accepted by the Florida Commission on Hurricane Loss Projection Methodology (the Hurricane Commission). The Hurricane Commission determined that the RMS model, version 5.1a was acceptable for projecting hurricane loss costs for personal residential rate filings on May 17, 2006.

27. In addition to approval by the Hurricane Commission, use of the model is appropriate "only if the office and the consumer advocate appointed pursuant to s. 627.0613 have access to all of the assumptions and factors that were used in developing the actuarial methods, principles, standards, models, or output ranges, and are not precluded from disclosing such information in a rate proceeding." §627.0628(3)(c), Fla. Stat.

28. Both the Consumer Advocate and a staff person from the OIR are members of the Hurricane Commission. In that context, both have the ability to make on-site visits to the modeling companies, and to ask any questions they choose regarding the models. Both OIR's representative and the Consumer Advocate participated in the meetings and had the same opportunity as other commissioners to ask any question they wished about RMS 5.1a. The Hurricane Commission members, including the Consumer

Advocate, clearly have access to the information identified in Section 627.0628(3)(c).

29. However, there are restrictions on the Hurricane Commission members' ability to share the information received regarding trade secrets disclosed by the modeling companies. For that reason, the Commission's deliberations are not, standing alone, sufficient to determine that the Office of Insurance Regulation has access.

30. In this case, credible evidence was submitted to show that RMS officials met with staff from the Office in July and October 2006 to discuss the model. RMS offered to provide any of its trade secret information to the OIR, subject to a non-disclosure agreement to protect its dissemination to competitors. RMS also opened an office in Tallahassee and invited OIR staff to examine any parts of the model they wished. In addition, both RMS and Hartford have answered extensive questionnaires prepared by OIR regarding the RMS model, and Hartford has offered to assist OIR in gathering any additional information it requires. Most of the questions posed by OIR involve the same areas reviewed by the Commission. RMS' representative also testified at hearing that RMS would not object to disclosure of the assumptions during the hearing itself if necessary.

31. Finally, OIR Exhibit 1 is the Florida Hurricane Catastrophe Fund 2007 Ratemaking Formula Report. The Executive Summary from the report explains how rates were recommended for

the Florida Hurricane Catastrophic Fund (CAT Fund) for the 2007-2008 contract year. The report stated that the RMS model, as well as three other models accepted by the Hurricane Commission, were used for determining expected aggregate losses to the CAT Fund reinsurance layer. Three models, including the RMS model, were also used for analysis of detailed allocation to type of business, territory, construction and deductible, as well as special coverage questions. The models were compared in detail and given equal weight. The report notes that these three models were also used in 1999-2006 ratemaking.

32. The report is prepared by Paragon Strategic Solutions, Inc., an independent consultant selected by the State Board of Administration, in accordance with Section 215.555(5), Florida Statutes. While OIR did not prepare the report, they show no hesitation in accepting and relying on the report and the modeled information it contains in these proceedings. Indeed, one of OIR's criticisms is Hartford's failure to use the report with respect to CAT Fund loss recovery estimates.

33. Based upon the evidence presented at hearing, it is found that the OIR and Consumer Advocate were provided access to the factors and assumptions used in the RMS model, as contemplated by Section 627.0628.

The Alleged Deficiencies in the Homeowners Filings[1/]

34. A rate is an estimate of the expected value of future costs. It provides for all costs associated with the transfer of

risk. A rate is reasonable and not excessive, inadequate or unfairly discriminatory if it is an actuarially sound estimate of the expected value of all future costs associated with an individual risk transfer.

35. In preparing a filing, an actuary identifies the time period that its proposed rates are expected to be in effect. Because ratemaking is prospective, it involves determining the financial value of future contingent events.

36. For the rate filings in question, actuaries for Hartford developed their rate indications by first considering trended premium, which reflects changes in premium revenue based on a variety of factors, including construction costs and the value of the buildings insured. Trended premium is the best estimate of the premium revenue that will be collected if the current rates remain in effect for the time period the filing is expected to be in place.

37. Expenses associated with writing and servicing the business, the reinsurance costs to support the business and an allowance for profit are subtracted from the trended premium. The remainder is what would be available to pay losses. This approach to ratemaking, which is used by Hartford, is a standard actuarial approach to present the information for a rate indication.

38. As part of the process, expected claims and the cost to service and settle those claims is also projected. These calculations show the amount of money that would be available to pay claims if no changes are made in the rates and how much increased premium is necessary to cover claims. The additional amount of premium reflects not only claims payments but also taxes, licenses and fees that are tied to the amount of premium.

39. The first deficiency identified by OIR is that "the premium trends are too low and are not reflective of the historical pattern of premium trends." In determining the premium trend in each filing, Hartford used data from the previous five years and fit an exponential trend to the historical pattern, which is a standard actuarial technique.

40. Hartford also looked at the factors affecting the more recent years, which were higher. For example, the peak in premium trend in 2006 was a result of the cost increases driven by the 2004 and 2005 hurricanes, and the peak in demand for labor and construction supplies not matched by supply. Costs were coming down going into 2007, and Hartford believed that 2006 was out of pattern from what they could anticipate seeing in the future.

41. The premium trends reflected in Hartford's filings are reasonable, reflective of historical patterns, and based on standard actuarial techniques.

42. The second identified deficiency with respect to the homeowner filings was that the loss trends are too high and are not reflective of the historical pattern of loss trends.

43. A loss trend reflects the amount an insurance company expects the cost of claims to change. It consists of a frequency trend, which is the number of claims the insurance company expects to receive, and a severity trend, which is the average cost per claim. The loss trend compares historical data used in the filing with the future time period when the new rates are expected to be in effect. Hartford's loss trends were estimated using a generalized linear model, projecting frequency and severity separately. The model was based on 20 quarters of historical information. The more credible testimony presented indicates that the loss trends were actuarially appropriate.

44. The third identified deficiency is that the loss trends are based on an unexplained and undocumented method using "modeled" frequency and severity as opposed to actual frequency and severity. As noted above, the generalized linear model uses actual, historical data. Sufficient documentation was provided in the filing, coupled with Hartford's August 20, 2007, letter. The method used to determine loss trends is reasonable and is consistent with standard actuarial practice.

45. The fourth identified deficiency is that loss trends are excessive and inconsistent compared to other sources of loss trends, such as Fast Track data. Saying that the loss trends are

excessive is a reiteration of the claim that they are too high, already addressed with respect to deficiency number two.

46. Fast Track data is data provided by the Insurance Services Office. It uses unaudited information and is prepared on a "quick turnaround" basis. Fast Track data is based on paid claims rather than incurred claims data, and upon a broad number of companies with different claims settlement practices. Because it relies on paid claims, there is a time lag in the information provided. Hartford did not rely on Fast Track data, but instead relied upon its own data for calculating loss trends. Given the volume of business involved, Hartford had enough data to rely on for projecting future losses. Moreover, Respondents point to no statutory or rule requirement to use Fast Track data. The filings are not deficient on this basis.

47. The fifth identified deficiency in the Notice of Intent to Disapprove is that catastrophe hurricane losses, ALAE and ULAE amounts are excessive and not supported. ALAE stands for "allocated loss adjustment expenses," and represents the costs the company incurs to settle a claim and that can be attributed to that particular claim, such as legal bills, court costs, experts and engineering reports. By contrast, ULAE stands for "unallocated loss adjustment expense" and represents the remainder of claims settlement costs that cannot be linked to a specific claim, such as office space, salaries and general overhead.

48. Part of the OIR's objection with respect to this deficiency relates to the use of the RMS model. As stated above at paragraphs 25-33, the use of the RMS model is reasonable.

49. With respect to ALAE, Hartford analyzed both nationwide data (4.4%) and Florida data (4.8%) and selected an ALAE load between the two (4.6%). This choice benefits Florida policyholders. It is reasonable to select between the national and Florida historical figures, given the amount of actual hurricane data available during the period used. With respect to ULAE, the factors used were based upon directions received from Ken Ritzenthaler, an actuary with OIR, in a previous filing. The prior discussions with Mr. Ritzenthaler are referenced in the exhibits to the filing. The more credible evidence demonstrates that the ALAE and ULAE expenses with respect to catastrophic hurricane losses are sufficiently documented in Hartford's filings and are based on reasonable actuarial judgment.

50. The sixth identified deficiency is that the catastrophe non-hurricane losses, ALAE and ULAE amounts are excessive and not supported. According to OIR, the particular time period from 1992 to 2006 used to calculate these values has not been justified, and there has been no explanation of why the extraordinarily high reported losses for 1992 and 1993 should be expected to occur in the future.

51. OIR's complaint with respect to non-hurricane losses is based upon the number of years of data included. While the RMS model was used for hurricane losses, there is no model for non-hurricane losses, so Hartford used its historical data. This becomes important because in both 1992 and 1993, there were unusual storms that caused significant losses.

52. Hartford's data begins with 1992 and goes through 2006, which means approximately fifteen years worth of data is used. Hartford's explanation for choosing that time period is that hurricane models were first used in 1992, and it was at that time that non-hurricane losses had to be separated from hurricane losses. Thus, it was the first year that Hartford had the data in the right form and sufficient detail to use in a rate filing. Petitioners have submitted rate filings in the past that begin non-hurricane, ALAE and ULAE losses with 1992, increasing the number of years included in the data with each filing. Prior filings using this data have been approved by OIR.

53. It is preferable to use thirty years of experience for this calculation. However, there was no testimony that such a time-frame is actuarially or statutorily required, and OIR's suggestion that these two high-loss years should be ignored is not based upon any identified actuarial standard. Hartford attempted to mitigate the effect of the severe losses in 1992 and 1993 by capping the losses for those years, as opposed to relying on the actual losses.[2/] The methodology used by Hartford was

reasonable and appropriate. No other basis was identified by the OIR to support this stated deficiency.

54. The seventh identified deficiency is that the underwriting profit and contingency factors are excessive and not supported.

55. The underwriting profit factor is the amount of income, expressed as a percentage of premium, that an insurance company needs from premium in excess of losses, settlement costs and other expenses in order to generate a fair rate of return on its capital necessary to support its Florida exposures for the applicable line of business. Hartford's proposed underwriting profit factor for its largest homeowners filing is 15.3%.

56. Section 627.062(2)(b), Florida Statutes, contemplates the allowance of a reasonable rate of return, commensurate with the risk to which the insurance company exposes its capital and surplus. Section 627.062(2)(b)4., Florida Statutes, authorizes the adoption of rules to specify the manner in which insurers shall calculate investment income attributable to classes of insurance written in Florida, and the manner in which investment income shall be used in the calculation of insurance rates. The subsection specifically indicates that the manner in which investment income shall be used in the calculation of insurance rates shall contemplate allowances for an underwriting profit factor.

57. Florida Administrative Code Rule 69O-170.003 is entitled "Calculation of Investment Income," and the stated purpose of this rule is as follows:

> (1) The purpose of this rule is to specify the manner in which insurers shall calculate investment income attributable to insurance policies in Florida and the manner in which such investment income is used in the calculation of insurance rates by the development of an underwriting profit and contingency factor compatible with a reasonable rate of return. (Emphasis supplied).

58. Mr. Schwartz relied on the contents of this rule in determining that the underwriting profit factor in Hartford's filings was too high, in that Florida Administrative Code Rule 69O-170.003(6)(a) and (7) specifies that:

> (6)(a) . . . An underwriting profit and contingency factor greater than the quantity 5% is prima facie evidence of an excessive expected rate of return and unacceptable, unless supporting evidence is presented demonstrating that an underwriting profit and contingency factor included in the filing that is greater than this quantity is necessary for the insurer to earn a reasonable rate of return. In such case, the criteria presented as determined by criteria in subsection (7) shall be used by the Office of Insurance Regulation in evaluating this supporting evidence.
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> * * *
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> (7) An underwriting profit and contingency factor calculated in accordance with this rule is considered to be compatible with a reasonable expected rate of return on net worth. If a determination must be made as to whether an expected rate of return is reasonable, the following criteria shall be used in that determination.

> (a) An expected rate of return for Florida business is to be considered reasonable if, when sustained by the insurer for its business during the period for which the rates under scrutiny are in effect, it neither threatens the insurer's solvency nor makes the insurer more attractive to policyholders or investors from a corporate financial perspective than the same insurer would be had this rule not been implemented, all other variables being equal; or
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> (b) Alternatively, the expected rate of return for Florida business is to be considered reasonable if it is commensurate with the rate of return anticipated for other industries having corresponding risk and it is sufficient to assure confidence in the financial integrity of the insurer so as to maintain its credit and, if a stock insurer, to attract capital, or if a mutual or reciprocal insurer, to accumulate surplus reasonably necessary to support growth in Florida premium volume reasonably expected during the time the rates under scrutiny are in effect.

59. Mr. Schwartz also testified that the last published underwriting profit and contingency factor published by OIR was 3.7%, well below what is identified in Hartford's filings.

60. Hartford counters that reliance on the rule is a misapplication of the rule (with no explanation why), is inconsistent with OIR's treatment of the profit factors in their previous filings, and ignores the language of Section 627.062(2)(b)11., Florida Statutes.

61. No evidence was presented to show whether the expected rate of return threatens Hartford's solvency or makes them more attractive to policyholders or investors from a corporate financial perspective than they would have been if Rule 69O-

170.003 was not implemented. Likewise, it was not demonstrated that the expected rate of return for Florida business is commensurate with the rate of return for other industries having corresponding risk and is necessary to assure confidence in the financial integrity of the insurer in order to maintain its credit and to attract capital.

62. While the position taken by OIR with respect to Hartford's filings may be inconsistent with the position taken in past filings, that cannot be determined on this record. The prior filings, and the communications Hartford had with OIR with regard to those filings, are not included in the exhibits in this case. There is no way to determine whether Petitioners chose to present evidence in the context of prior filings consistent with the criteria in Rule 69O-170.003, or whether OIR approved the underwriting profit and contingency factor despite Rule 69O-170.003.

63. Having an underwriting profit factor that is considered excessive will result in a higher rate indication. Therefore, it is found that the seventh identified deficiency in the Notices of Intent to Disapprove for the homeowners filings and the second identified deficiency in the Notices of Intent to Disapprove for the dwelling/fire filings is sustained.

64. The eighth identified deficiency is that various components underlying the calculation of the underwriting profit and contingency factors, including but not limited to the return

on surplus, premium to surplus ratio, investment income and tax rate are not supported or justified.

65. Return on surplus is the total net income that would result from the underwriting income and the investment income contributions relative to the amount of capital that is exposed. Surplus is necessary in addition to income expected from premium, to insure that claims will be paid should losses in a particular year exceed premium and income earned on premium. Hartford's expected return on surplus in these filings is 15%.

66. The return on surplus is clearly tied to the underwriting profit factor, although the percentages are not necessarily the same. It follows, however, that if the underwriting income and contingency factor is excessive, then the return on surplus may also be too high. Hartford has not demonstrated that the return on surplus can stand, independent of a finding that the underwriting profit and contingency factor is excessive.

67. Premium-to-surplus ratio is a measure of the number of dollars of premium Hartford writes relative to the amount of surplus that is supporting that exposure. Hartford's premium-to-surplus ratio in the AARP homeowners filing is 1.08, which means that if Hartford wrote $108 of premium, it would allocate $100 of surplus to support that premium.[3/] The premium-to-surplus ratio is reasonable, given the amount of risk associated with homeowners insurance in Florida.

68. The OIR's position regarding investment income and tax rates are related. The criticism is that the filing used a low-risk investment rate based on a LIBOR (London Interbank Offering Rate), which is a standard in the investment community for risk-free or low-risk yield calculations. The filing also used a full 35% income tax rate applied to the yield.

69. Evidence was presented to show that, if the actual portfolio numbers and corresponding lower tax rate were used in the filings, the rate after taxes would be the same.

70. The problem, however, is that Section 627.062(2)(b)4., Florida Statutes, requires the OIR to consider investment income reasonably expected by the insurer, "consistent with the insurer's investment practices," which assumes actual practices. While the evidence at hearing regarding Hartford's investments using its actual portfolio yield may result in a similar bottom line, the assumptions used in the filing are not based on Petitioner's actual investment practices. As a result, the tax rate identified in the filing is also not the actual tax rate that has been paid by Hartford. The greater weight of the evidence indicates the data used is not consistent with the requirements of Section 627.062(2)(b)4., Florida Statutes. Therefore, the eighth deficiency is sustained to the extent that the filing does not adequately support the return on surplus, investment income and tax rate.

71. The ninth identified deficiency is that the underwriting expenses and other expenses are excessive and not supported. Hartford used the most recent three years of actual expense data, analyzed them and made expense selections based on actuarial judgment. The use of the three-year time frame was both reasonable and consistent with common ratemaking practices. Likewise, the commission rates reflected in the agency filings are also reasonable.

72. The tenth identified deficiency is that the non-FHCF (or private) reinsurance costs are excessive and not supported. The criticism regarding private reinsurance purchases is three-fold: 1) that Hartford paid too much for their reinsurance coverage; 2) that Hartford purchases their reinsurance coverage on a nationwide basis as opposed to purchasing coverage for Florida only; and 3) that the percentage of the reinsurance coverage allocated to Florida is too high.

73. Hartford buys private reinsurance in order to write business in areas that are exposed to catastrophes. It buys reinsurance from approximately 40 different reinsurers in a competitive, arm's-length process and does not buy reinsurance from corporate affiliates. Hartford used the "net cost" of insurance in its filings, an approach that is appropriate and consistent with standard actuarial practices. Hartford also used the RMS model to estimate the expected reinsurance recoveries, which are subtracted from the premium costs.

74. Hartford buys private catastrophic reinsurance on a nationwide basis to protect against losses from hurricanes, earthquakes and terrorism, and allocates a portion of those costs to Florida. Testimony was presented, and is accepted as credible, that attempting to purchase reinsurance from private vendors for Florida alone would not be cost-effective. The cost of reinsurance, excluding a layer of reinsurance that covers only the Northeast region of the country and is not reflected in calculating costs for Florida, is approximately $113 million.

75. Hartford retains the first $250 million in catastrophe risk for any single event, which means losses from an event must exceed that amount before the company recovers from any reinsurer. In 2006, Hartford raised its retention of losses from $175 million to $250 million in an effort to reduce the cost of reinsurance. Hartford purchases reinsurance in "layers," which cover losses based on the amount of total losses Hartford incurs in various events.

76. Hartford allocates approximately 65% of the private reinsurance costs (excluding the Northeast layer) to Florida in the AARP homeowners filing. Only 6-7% of Hartford's homeowners policies are written in Florida.

77. The amount Hartford paid for reinsurance from private vendors is reasonable, given the market climate in which the insurance was purchased. Hartford has demonstrated that the process by which the reinsurance was purchased resulted in a

price that was clearly the result of an arms-length transaction with the aim of securing the best price possible.

78. Likewise, the determination to purchase reinsurance on a nationwide basis as opposed to a state-by-state program allows Hartford to purchase reinsurance at a better rate, and is more cost-effective. Purchasing reinsurance in this manner, and then allocating an appropriate percentage to Florida, is a reasonable approach.

79. With respect to the allocation of a percentage of reinsurance cost to Florida, OIR argues that, given that Florida represents only 6-7% of Hartford's homeowner insurance business, allocation of 65% of the reinsurance costs to Florida is per se unreasonable. However, the more logical approach is to examine what percentage of the overall catastrophic loss is attributable to Florida, and allocate reinsurance costs accordingly.

80. After carefully examining both the testimony of all of the witnesses and the exhibits presented in this case, the undersigned cannot conclude that the allocation of 65% of the private reinsurance costs is reasonable, and will not result in an excessive rate.[4/]

81. The eleventh identified deficiency is that the FHCF (or CAT Fund) reinsurance costs are excessive and not supported. Hartford purchases both the traditional layer of CAT Fund coverage, which is addressed in a separate filing and not

reflected in these filings, and the TICL layer made available pursuant to Chapter 2007-1, Laws of Florida.

82. Hartford removed the costs of its previously purchased private reinsurance that overlapped with the TICL layer and those costs are not reflected in these filings and have not been passed on to Florida policyholders.

83. In estimating the amount of premium Hartford would pay for the TICL coverage, it relied on information provided by Paragon, a consulting firm that calculates the rates for the CAT Fund. As noted in finding of fact number 31, the RMS model, along with three other models accepted by the Hurricane Commission, were used by Paragon for determining expected aggregate losses to the CAT Fund reinsurance layer, clearly a crucial factor in determining the rate for the CAT fund. Hartford did not use the loss recoveries calculated by Paragon, but instead estimated the total amount of premium it would pay for the TICL coverage and subtracted the expected loss recoveries based on the RMS model alone. The expected loss recoveries under the RMS model standing alone were 60% of the loss recovery estimate calculated by Paragon when using all four models.

84. Hartford claimed that its use of the RMS model was necessary for consistency. However, it pointed to no actuarial standard that would support its position with respect to this particular issue. Moreover, given that the premium used as calculated by Paragon used all four models, it is actually

inconsistent to use one number which was determined based on all four models (the Paragon-based premium estimate) for one half of this particular calculation and then subtract another number using only one model for the other half (the loss recoveries rate) in order to determine the net premium. To do so fails to take into account the unique nature of the CAT fund, in terms of its low expenses and tax-exempt status. Accordingly, it is found that the CAT-Fund reinsurance costs for the TICL layer are excessive.

85. The twelfth identified deficiency is that Hartford did not consider in the filing that no new business is being written. OIR's explanation of this asserted deficiency is that the costs associated with writing new business are generally higher than that associated with writing renewals. Therefore, according to OIR, failure to make adjustments to their historical experience to reflect the current mix of business, means that the costs included in the filing would be excessive.

86. Hartford began restricting the writing of new business for these filings in 2002. Ultimately, no new business for the AARP program was written after November 2006 and no new business was written for the agency program after June 2006. Credible evidence was presented to demonstrate that a very low percentage of new business has been written over the period of time used for demonstrating Hartford's historical losses. As a result, the effect of no longer writing new business is already reflected in

the data used to determine expenses. No additional adjustment in the filing was necessary in this regard.

87. The thirteenth identified deficiency is that no explanation has been provided as to why Hartford believes it is reasonable to return such a low percentage of premium in the form of loss payments to policyholders. For example, for the building policy forms, OIR states that only about 40% of the premium requested by Hartford is expected to be returned to policyholders in the form of loss payments.

88. OIR pointed to no actuarial standard that would require a specific explanation regarding how much of the premium should be returned to policyholders. Nor was any statutory or rule reference supplied to support the contention that such an explanation was required. Finally, the more credible evidence presented indicates that the correct percentage is 44%. In any event, this criticism is not a basis for finding a deficiency in the filing.

Alleged Deficiencies in the Dwelling/Fire Filings

89. The seventh deficiency identified in the dwelling/fire filings, not reflected in the homeowner filings, is that the credibility standard and credibility values are not supported.

90. Credibility is the concept of identifying how much weight to put on a particular set of information relative to other potential information. Credibility value is determined by

applying the "square root rule" to the credibility value, a commonly used actuarial approach to credibility.

91. Hartford used the credibility standard of 40,000 earned house years in these filings. This credibility standard has been the standard within the industry for personal property filings for over forty years and has been used in prior filings submitted to OIR.

92. Mr. Schwartz testified that his criticism with respect to the credibility standard and credibility values is that Hartford did not explain why they used that particular standard. However, Florida Administrative Code Rule 69O-170.0135 discusses those items that must be included in the Actuarial Memorandum for a filing. With respect to credibility standards and values, Rule 69O-170.0135(2)(e)5., provides that the basis need only be explained when the standard has changed from the previous filing. Given that no change has been made in these filings with respect to the credibility standard, this criticism is not a valid basis for issuing a Notice of Intent to Disapprove.

93. The ninth deficiency in the Notice relating to the dwelling/fire filing in Case No. 07-5187 provides: "No explanation has been provided as too (sic) why Hartford believes it needs such a large rate increase currently, when the cumulative rate change implemented by Hartford for this program from 2001 to 2006 was an increase of only about 10%." With respect to Case No. 07-5188, the deficiency is essentially the

same, except the cumulative rate change identified for the same period of time is a decrease of about -3%.

94. Testimony established that the dwelling/fire rate increases were larger than those identified for the homeowners filings because Hartford did not seek rate increases for these lines for several years. The decision not to seek increases was not based on the adequacy of current rates. Rather, the decision was based on an internal determination that, based on the relatively small number of policies involved in these two filings, the amount of increased premium reflected in a rate increase was not sufficient to incur the costs associated with preparing the filings.

95. Mr. Schwartz pointed to no authority, either in statute, rule, or Actuarial Standard, that requires the explanation he desired. He acknowledged that he understood the basis of how Hartford reached the rate increase they are requesting. The failure to provide the explanation Mr. Schwartz was seeking is not a valid basis for a Notice of Intent to Disapprove.

CONCLUSIONS OF LAW

96. The Division of Administrative Hearings has jurisdiction over the subject matter and the parties to this action in accordance with Sections 120.569 and 120.57(1), Florida Statutes.

97. The Notices of Intent to Disapprove issued by the OIR represent preliminary agency action. This proceeding is a de novo proceeding. Boca Raton Artificial Kidney Center, Inc. v. Florida Department of Health and Rehabilitative Services, 475 So. 2d 260, 262 (Fla. 1st DCA 1985); Florida Department of Transportation v. J.W.C. Co., 396 So. 2d 778, 786-87 (Fla. 1st DCA 1981).

98. The Hartford Companies, as Petitioners in these proceedings, have the initial burden of going forward with the evidence and the ultimate burden of persuasion to show by a preponderance of the evidence that the proposed rates are not excessive, inadequate or unfairly discriminatory. § 627.062(2)(b), (g), Fla. Stat.

99. Although Hartford has the ultimate burden of persuasion, the burden of going forward with the evidence may and does shift during the course of the proceeding. J.W.C., 396 So. 2d at 787; In re Estate of Ziy, 223 So. 2d 42, 43 (Fla. 1969)("Generally speaking, the burden of proof, in the sense of producing evidence, passes from party to party as the case progresses, while the burden of proof, meaning the obligation to establish the truth of the claim by a preponderance of the evidence, rests throughout upon the party asserting the affirmative of the issue. . . .").

100. Hartford had the initial burden of going forward to establish a prima facie case that supports the four filings.

OIR had the burden of presenting evidence that Hartford's filings were deficient in accordance with the statutorily enumerated basis and thus would result in rates that were inconsistent with the statutory mandate. The ultimate burden of persuasion remains with Hartford. Department of Banking and Finance v. Osborne Stern and Company, 670 So. 2d 932, 934 (Fla. 1996).

101. The issues in this case are framed by the requirements of Section 627.062, Florida Statutes, which states in pertinent part:

> (1) The rates for all classes of insurance to which the provisions of this part are applicable shall not be excessive, inadequate, or unfairly discriminatory.
>
> (2) As to all such classes of insurance:
>
> (a) Insurers or rating organizations shall establish and use rates, rating schedules, or rating manuals to allow the insurer a reasonable rate of return on such classes of insurance written in this state. A copy of rates, rating schedules, rating manuals, premium credits or discount schedules, and surcharge schedules, and changes thereto, shall be filed with the office under one of the following procedures except as provided in subparagraph 3.:
>
> 1. If the filing is made at least 90 days before the proposed effective date and the filing is not implemented during the office's review of the filing and any proceeding and judicial review, then such filing shall be considered a "file and use" filing. In such case, the office shall finalize its review by issuance of a notice of intent to approve or a notice of intent to disapprove within 90 days after receipt of the filing. The notice of intent to approve and the notice of intent to disapprove constitute agency action for purposes of the Administrative Procedure Act.

Requests for supporting information, requests for mathematical or mechanical corrections, or notification to the insurer by the office of its preliminary findings shall not toll the 90-day period during any such proceedings and subsequent judicial review. The rate shall be deemed approved if the office does not issue a notice of intent to approve or a notice of intent to disapprove within 90 days after receipt of the filing.

* * *

3. For all filings made or submitted after January 25, 2007, but before December 31, 2008, an insurer seeking a rate that is greater than the rate most recently approved by the office shall make a "file and use" filing. This subparagraph applies to property insurance only. . . ..

(b) Upon receiving a rate filing, the office shall review the rate filing to determine if a rate is excessive, inadequate, or unfairly discriminatory. In making that determination, the office shall, in accordance with generally accepted and reasonable actuarial techniques, consider the following factors:

1. Past and prospective loss experience within and without this state.

2. Past and prospective expenses.

3. The degree of competition among insurers for the risk insured.

4. Investment income reasonably expected by the insurer, consistent with the insurer's investment practices, from investable premiums anticipated in the filing, plus any other expected income from currently invested assets representing the amount expected on unearned premium reserves and loss reserves. The commission may adopt rules utilizing reasonable techniques of actuarial science and economics to specify the manner in which insurers shall calculate investment income attributable to such classes of insurance written in this state and the manner in which such investment income shall be used in the

calculation of insurance rates. Such manner shall contemplate allowances for an underwriting profit factor and full consideration of investment income which produce a reasonable rate of return; however, investment income from invested surplus shall not be considered.

5. The reasonableness of the judgment reflected in the filing.

6. Dividends, savings, or unabsorbed premium deposits allowed or returned to Florida policyholders, members, or subscribers.

7. The adequacy of loss reserves.

8. The cost of reinsurance.

9. Trend factors, including trends in actual losses per insured unit for the insurer making the filing.

10. Conflagration and catastrophe hazards, if applicable.

11. A reasonable margin for underwriting profit and contingencies. For that portion of the rate covering the risk of hurricanes and other catastrophic losses for which the insurer has not purchased reinsurance and has exposed its capital and surplus to such risk, the office must approve a rating factor that provides the insurer a reasonable rate of return that is commensurate with such risk.

12. The cost of medical services, if applicable.

13. Other relevant factors which impact upon the frequency or severity of claims or upon expenses.

* * *

(d) If conflagration or catastrophe hazards are given consideration by an insurer in its rates or rating plan, including surcharges and discounts, the insurer shall establish a reserve for that portion of the premium allocated to such hazard and shall maintain the premium in a catastrophe reserve. Any removal of such premiums from the reserve for

> purposes other than paying claims associated with a catastrophe or purchasing reinsurance for catastrophes shall be subject to approval of the office. Any ceding commission received by an insurer purchasing reinsurance for catastrophes shall be placed in the catastrophe reserve.
>
> (e) After consideration of the rate factors provided in paragraphs (b), (c), and (d), a rate may be found by the office to be excessive, inadequate, or unfairly discriminatory based upon the following standards:
>
> 1. Rates shall be deemed excessive if they are likely to produce a profit from Florida business that is unreasonably high in relation to the risk involved in the class of business or if expenses are unreasonably high in relation to services rendered.
>
> 2. Rates shall be deemed excessive if, among other things, the rate structure established by a stock insurance company provides for replenishment of surpluses from premiums, when the replenishment is attributable to investment losses.
>
> * * *
>
> (f) In reviewing a rate filing, the office may require the insurer to provide at the insurer's expense all information necessary to evaluate the condition of the company and the reasonableness of the filing according to the criteria enumerated in this section.

102. As a preliminary manner, the parties have asserted different views regarding the issuance of clarification letters, or the lack thereof, with respect to these filings. Hartford claims that it has always been the practice of OIR to issue clarification letters to insurers making rate filings and that many issues regarding documentation may be cleared up through ongoing communication with the OIR. OIR responds that the

issuance of a clarification letter is not statutorily required. Further, OIR asserts that the amendments to Section 627.027 make it a requirement that all documentation must be included in the filing, and therefore there is no longer a place for a clarification letter in the rate review process.

103. OIR bases its position on the addition of Subsection 627.062(9), Florida Statutes, which states in pertinent part:

> (9)(a) Effective March 1, 2007, the chief executive officer or chief financial officer of a property insurer and the chief actuary of a property insurer must certify under oath and subject to the penalty of perjury, on a form approved by the commission, the following information, which must accompany a rate filing:
>
> 1. The signing officer and actuary have reviewed the rate filing;
>
> 2. Based on the signing officer's and actuary's knowledge, the rate filing does not contain any untrue statement of material fact or omit to state a material fact necessary in order to make the statements made, in light of the circumstances under which such statements were made, not misleading;
>
> 3. Based on the signing officer's and actuary's knowledge, the information and other factors described in paragraph (2)(b), including but not limited to, investment income, fairly present in all material respects the basis of the rate filing for the periods presented in the filing; and
>
> 4. Based on the signing officer's and actuary's knowledge, the rate filing reflects all premium savings that are reasonably expected to result from legislative enactments and are in accordance with generally accepted and reasonable actuarial techniques.

104. Contrary to the OIR's assertions, nothing in this amendment requires that all documentation upon which an insurer might possibly rely must be included in the filing itself. The amendment does require that the insurer closely scrutinize its filings and insure that all factors identified in Section 627.062(2)(b) "fairly present in all material respect the basis for the filing." The filing cannot, by commission or omission, make any misleading or untrue statements. Florida Administrative Code Rule 69O-170.013(5) clearly makes it the insurer's responsibility to include all information it wants considered to support the rate filing, and this requirement is not new. However, other parts of Section 627.027 which the Legislature chose not to delete still clearly allow for additional information to be provided to the OIR upon request, and the OIR's rules still contemplate such a process. See, e.g., §627.027(2)(a)1.,(f), Fla. Stat.; Fla. Admin. Rule 69O-170.013(2), (6)(a), (b). However, issuance of a clarification letter is a matter within the discretion of OIR. While it might have been better practice to issue letters of clarification to address some issues in the filing, failure to do so is not fatal to the Notices of Intent to Disapprove.

105. As stated in the findings of fact, the level of documentation provided in these filings is consistent with both the Standards of Actuarial Practice and with the level of documentation previously required by OIR. Given that actuarial

practice is not by definition an exact science and involves the exercise of judgment by reasonable professionals, Hartford's general position with respect to the level of documentation required is reasonable.

106. The parties also have divergent views regarding what is required with respect to the use of catastrophic models. The operative statute is Section 627.0628, Florida Statutes, which provides in pertinent part:

> (1)(c) It is the intent of the Legislature to create the Florida Commission on Hurricane Loss Projection Methodology as a panel of experts to provide the most actuarially sophisticated guidelines and standards for projection of hurricane losses possible, given the current state of actuarial science. It is the further intent of the Legislature that such standards and guidelines must be used by the State Board of Administration in developing reimbursement premium rates for the Florida Hurricane Catastrophe Fund, and, subject to paragraph (3)(c), may be used by insurers in rate filings under s. 627.062 unless the way in which such standards and guidelines were applied by the insurer was erroneous, as shown by a preponderance of the evidence.
>
> * * *
>
> 3) ADOPTION AND EFFECT OF STANDARDS AND GUIDELINES.--
>
> (a) The commission shall consider any actuarial methods, principles, standards, models, or output ranges that have the potential for improving the accuracy of or reliability of the hurricane loss projections used in residential property insurance rate filings. The commission shall, from time to

> time, adopt findings as to the accuracy or reliability of particular methods, principles, standards, models, or output ranges.
>
> (b) In establishing reimbursement premiums for the Florida Hurricane Catastrophe Fund, the State Board of Administration must, to the extent feasible, employ actuarial methods, principles, standards, models, or output ranges found by the commission to be accurate or reliable.
>
> (c) With respect to a rate filing under s.627.062, an insurer may employ actuarial methods, principles, standards, models, or output ranges found by the commission to be accurate or reliable to determine hurricane loss factors for use in a rate filing under s. 627.062. Such findings and factors are admissible and relevant in consideration of a rate filing by the office or in any arbitration or administrative or judicial review only if the office and the consumer advocate appointed pursuant to s. 627.0613 have access to all of the assumptions and factors that were used in developing the actuarial methods, principles, standards, models, or output ranges, and are not precluded from disclosing such information in a rate proceeding. In any rate hearing under s. 120.57 or in any arbitration proceeding under s. 627.062(6), the hearing officer, judge, or arbitration panel may determine whether the office and the consumer advocate were provided with access to all of the assumptions and factors that were used in developing the actuarial methods, principles, standards, models, or output ranges and to determine their admissibility.

107. The disagreement stems from the perceived requirements of Subsection 627.0628(3)(c). OIR contends that "access" as contemplated by this subsection means that the assumptions and factors be provided as part of the rate filing under review by the insurer. Hartford contends that both the consumer advocate

and the OIR were provided access to the factors and assumptions, both through the Hurricane Commission approval process and through meetings with RMS, and written submissions to OIR.

108. The operative language of subsection (3)(c) is that OIR and the consumer advocate must "have access to all of the assumptions and factors that were used in developing the actuarial methods, principles, standards, models, or output ranges, and are not precluded from disclosing such information in a rate proceeding." OIR's interpretation of this language is that the insurer, as opposed to the modeling entity such as RMS, must furnish the information as part of the rate filing itself. While it complaints that not enough information has been provided, OIR has never identified in this proceeding what it believes it needs in order to have sufficient information, or why it chose not to take full advantage of the access offered. Moreover, the statute does not state who must provide access, or when the access must be provided. It simply says the OIR must have the access and it must be able to disclose the information in a rate proceeding.

109. Given the limited number of approved models compared to the number of insurers required to make rate filings with the Office, it seems more reasonable that having access to the assumptions and factors would come from the entity developing the models, whose trade secrets are often at stake, and who seeks approval from the Hurricane Commission for the models to be used.

The plain language of the statute requires access. It does not require the insurer to provide the factors and assumptions.

110. As stated in the findings of fact, both the Consumer Advocate and the OIR were provided access to the factors and assumptions used by RMS in connection with its catastrophic model. RMS offered access directly, both in terms of information furnished to the OIR, and by offers to allow direct access at its Tallahassee office. Hartford offered to assist OIR in obtaining any information that it felt it needed but did not have. These actions met the requirement of access as contemplated by Section 627.0628(3)(c).[5/]

111. With respect to the homeowners filings, OIR identified thirteen items that it contended represented deficiencies in the filings, and upon which it concluded the rates requested in the filings would be excessive. While the alleged deficiencies arguably all related to the requirement that the rates not be excessive, inadequate or unfairly discriminatory, the Notices of Intent to Disapprove do not reference the standards enumerated in Section 627.062(2)(e), Florida Statutes, and do not reference any rule.

112. With respect to the deficiencies numbered 1-3, 5, 6, 9 and 12, based on the evidence presented, Hartford has demonstrated by a preponderance of the evidence that the factors at issue were sufficiently documented in accordance with

actuarial standards and based on reasonable actuarial judgment.

113. With respect to the deficiencies numbered 4 and 13, the alleged deficiencies were either not tied to the standards enumerated in Section 627.027(2)(e) or not required under OIR's rules related to ratemaking. Specifically, with respect to deficiency number 4, there is no requirement that an insurer use Fast Track data when its own data is sufficient and provides a more complete picture with respect to loss trends, as was the case here. With respect to deficiency number 13, OIR pointed to no actuarial standard or factor in Section 627.027(2)(b) addressing documentation regarding the percentage of premium to be returned in the form of loss payments. In both instances, Hartford has demonstrated by a preponderance of the evidence that the information provided in the filing was reasonable.

114. With respect to asserted deficiencies 7-8 and 10-11, however, the totality of the evidence leads to the conclusion that Hartford has not demonstrated that the proposed rate is not excessive, inadequate or unfairly discriminatory. Specifically, with respect to the underwriting profit and contingency factor at issue in deficiency number 7, Hartford has not met the criteria specified in Rule 69O-170.003(7), and an excessive underwriting profit factor will by definition result in a rate indication that is excessive.

115. Because the underwriting profit factor proposed by the rate filing is excessive, the return on surplus comes into

question. Hartford has not demonstrated that the return on surplus identified in the filing can stand independently of the proposed underwriting profit and contingency factor. Asserted deficiency number 8 also questions the use of a low-risk investment yield and 35% income tax rate when neither is indicative of Hartford's actual investment portfolio. Section 627.027(2)(b)4., Florida Statutes, contemplates use of actual practices, as opposed to what was submitted here. As a result, to the extent that alleged deficiency number 8 deals with these issues, it must be sustained.

116. With respect to private reinsurance costs (deficiency number 10), the greater weight of the evidence indicates that while the overall costs of reinsurance and its purchase on a nationwide basis is reasonable, the percentage of the private reinsurance costs allocated to Florida is excessive, which would lead to a higher rate indication. Likewise, for the reasons expressed in the findings of fact, the amount allowed for loss recoveries in determining the premium for CAT Fund reinsurance rates results in an excessive premium. This also would lead to a higher rate indication. Therefore, the bases for disapproval identified in both deficiency numbers 10 and 11 are sustained.

117. With respect to the dwelling/fire filings, OIR indicated at hearing that it was withdrawing deficiency number 1. Hartford has met its burden of showing that the factors identified in 4 and 8 were sufficiently documented, consistent

with actuarial standards and based on sound actuarial judgment. With respect to deficiency number 7, the asserted deficiency is inconsistent with the requirements of Florida Administrative Code Rule 69O-170.0135(2)(e)5. With respect to this deficiency, as well as deficiency number 9, Hartford has demonstrated that the filings were appropriately documented and based on reasonable actuarial judgment.

118. Finally, with respect to alleged deficiencies numbered 2-3 and 5-6, these deficiencies have been sustained for the same reasons expressed above for the corresponding deficiencies in the homeowner filings (homeowner deficiencies 7-8 and 10-11).

RECOMMENDATION

Upon consideration of the facts found and conclusions of law reached, it is

RECOMMENDED:

That a final order be entered that disapproves the rate filings in Case Nos. 07-5185 and 07-5186 based upon the deficiencies numbered 7,8,10 and 11 in the Notices of Intent to Disapprove, and that disapproves the rate filings in Case Nos. 07-5187 and 07-5188 based on the deficiencies numbered 2,3,5 and 6 in the Notices of Intent to Disapprove.

DONE AND ENTERED this 28th day of March 2008, in Tallahassee, Leon County, Florida.

LISA SHEARER NELSON
Administrative Law Judge
Division of Administrative Hearings
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Filed with the Clerk of the
Division of Administrative Hearings
this 28th day of March, 2008.

ENDNOTES

[1/] As previously noted, the deficiencies identified for both homeowners filings are identical, and seven of those deficiencies are repeated for the dwelling fire filings. While the figures are different for each filing, the method used and the rationale for using the method is the same. For the sake of simplicity, each deficiency will be identified by the number associated with the homeowners filings, followed by the additional asserted deficiencies identified with dwelling/fire policies. Further, counsel for OIR stated at hearing that deficiency number 1 with respect to the dwelling/fire filings was not going to be pursued.

[2/] In 1992, non-hurricane losses were listed as 66.4% of premium, while in 1993, they were 27%.

[3/] The ratios vary from 1.08 to 1.5 in the various filings.

[4/] The documents presented in the filings seem to be contradictory in this regard. Compare, for example, Exhibit VIII, sheet 7a with Exhibit VIII, sheet 7c in Joint Exhibit 2. While sheet 7a appears to support the assertion that Florida represents 65% of catastrophic loss, sheet 7c appears to indicate that Florida homeowners hurricane losses represents only 27.7% of such losses. No testimony was presented to explain the apparent

inconsistency between these statements. Absent such an explanation, the undersigned cannot conclude that the current allocation is reasonable.

The undersigned also notes that the numbers reflected in the findings of fact reference only the homeowners filing in Case No. 07-5185. At hearing, both parties used that particular filing as representing the methodology for all four filings. No testimony was presented regarding the specific percentages in the other filings, but based upon the witnesses' testimony that their responses would be the same for each filing, the determination that the allocation of reinsurance is not a reasonable allocation applies to all four filings.

[5/] At hearing, OIR, who was the Respondent in this case, attempted to present the testimony of Howard Eagelfeld, as "rebuttal" to testimony regarding the role of the OIR's representative on the Hurricane Commission. Mr. Eagelfeld was not listed as a witness for the OIR in the parties' Prehearing Statement.

The issues related to the access provided to OIR with respect to hurricane models was clearly an issue pursued by OIR in the cross-examination of the Petitioner's witnesses. The undersigned did not allow Mr. Eagelfeld to testify because OIR cited no authority for allowing a respondent to present "rebuttal." OIR claims this was error, citing Rose v. Madden & McClure Grove Service, 629 So. 2d 234, 236 (Fla. 1st DCA 1993), and quoting the following:

> Under the usual order of presentation of evidence at trial, the plaintiff will first introduce evidence to prove the facts necessary to enable recovery. Then the defense presents evidence in support of its case, including evidence not only that denies or contradicts plaintiff's claim but also that supports any pleaded affirmative defenses. The plaintiff is now entitled to present a case in rebuttal, refutation evidence that denies, explains, disproves or otherwise sheds light on evidence offered by the defense. If new points are brought out during plaintiff's rebuttal, the defendant may meet them by evidence in rejoinder, otherwise known as surrebuttal.

What OIR does not state is that in the Rose case, the employer/carrier did not name two expert witnesses on its pretrial witness list. Just before the presentation of the E/C's

case, it informed the judge that it would be presenting the two experts' testimony, claiming they were "rebuttal" witnesses. The witnesses were allowed and on appeal, the district court found that allowing their testimony was error, stating,

> The E/C endeavors to stretch the meaning of rebuttal far beyond its common definition and usage. If one were to accept the E/C's definition, then arguably those defendants who intended to present contradictory testimony -- a majority of cases --would be able to take advantage of the rule excusing them from pretrial disclosure of rebuttal witnesses.

629 So. 2d at 236. The same could be said here. In any event, the undersigned has carefully reviewed the transcript to see whether the rebuttal presented by Hartford had anything to do with the Hurricane Commission or access pursuant to Section 627.0628. It did not.

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NOTICE OF RIGHT TO SUBMIT EXCEPTIONS

All parties have the right to submit written exceptions within

15 days from the date of this recommended order. Any exceptions to this recommended order should be filed with the agency that will issue the final order in this case.