

LOUISIANA CITIZENS PROPERTY  
INSURANCE CORPORATION -  
RATE-SETTING



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PERFORMANCE AUDIT  
ISSUED MAY 22, 2007

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May 22, 2007

The Honorable Donald E. Hines,  
President of the Senate  
The Honorable Joe R. Salter,  
Speaker of the House of Representatives

Dear Senator Hines and Representative Salter:

This report provides the results of our performance audit of the rate-setting process used by the Louisiana Citizens Property Insurance Corporation. The audit was conducted under the provisions of Louisiana Revised Statute 22:1430.15. This statute provides that the Louisiana Citizens Property Insurance Corporation shall be subject to examination by the Legislative Auditor.

The report contains our findings, conclusions, and recommendations. Appendix A contains the response from the Louisiana Citizens Property Insurance Corporation. I hope this report will benefit you in your legislative decision-making process.

Sincerely,

Steve J. Theriot, CPA  
Legislative Auditor

SJT/dl

CPICR07

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# Office of Legislative Auditor

Steve J. Theriot, CPA, Legislative Auditor

## Louisiana Citizens Property Insurance Corporation - Rate-Setting

Performance Audit (Second in a Series of Reports on Citizens)

May 2007



Audit Control # 07701186

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## HAS THE CITIZENS RATE-SETTING PROCESS RESULTED IN ACTUARIALLY-JUSTIFIED, NONCOMPETITIVE RATES?

### Audit Results

The Louisiana Citizens Property Insurance Corporation's (Citizens') rate-setting process has not consistently produced actuarially-justified, noncompetitive rates. We identified several cases where Citizens' rates for residential property were at or below the rates of private insurance companies. This report suggests ways Citizens can help ensure that it consistently produces actuarially-justified, noncompetitive rates through a more streamlined rate-setting process.

It is important that Citizens' rates do not compete with the rates of private insurance companies because competition could cause private companies to withdraw from the property insurance market in Louisiana. Such withdrawals could result in an increase in the number of Citizens policyholders. It would also contradict the legislative intent stipulated in the statutes governing the noncompetitive nature of Citizens. Furthermore, the legislation creating Citizens explicitly states that the legislature intends for Citizens to work to reduce the number of its policyholders until it is no longer needed. If Citizens were to continue increasing the number of policyholders it serves, this legislative intent would not be met.

We conducted two comparisons of Citizens' rate quotes to quotes from some of the largest private insurers of residential property in the state. We found that some of Citizens' quotes were at or below some of the private companies' quotes. Citizens' rates have been adjusted since our comparisons were made, so the discrepancies we identified may no longer exist; however, our work indicates problems with Citizens' overall rate-setting process. The process will always result in the possibility that at least some of Citizens' rates will be competitive with those of private companies.

We identified four primary factors in Citizens' rate-setting process that contribute to the competitiveness of its rates. First, Citizens' current rates do not incorporate the latest catastrophe model. Second, the market comparison process Citizens used to set its rates is prone to time lags and data errors. Third, Citizens' rate structure does not include as many discounts and surcharges for various individual risk factors, as do the rate structures of many private insurance companies. Fourth, Citizens has not reviewed and adjusted all of its rates annually, as required by law.

The recommendations contained in this report address each of these factors. If implemented, they would help Citizens ensure that its rates are actuarially-justified and noncompetitive. In addition, we have included a matter for legislative consideration. If this matter is implemented, it would streamline Citizens' rate-setting process.

## Introduction

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### Audit Initiation

We conducted this examination under the provisions of Louisiana Revised Statute (R.S.) 22:1430.15. This statute provides that the Louisiana Citizens Property Insurance Corporation (Citizens) shall be subject to examination by the Legislative Auditor. In accordance with this legislative mandate, the Legislative Auditor directed his staff to conduct an examination of the corporation in the form of a performance audit. We followed the applicable generally accepted government auditing standards as promulgated by the Comptroller General of the United States in conducting the audit.

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### Scope

The audit focused on the process used by Citizens to produce its rates, which are required by law to be actuarially justified and noncompetitive. The audit examined the process in effect from 2004<sup>1</sup> through January 2007. Our audit objective was to answer the following question:

**Has the Citizens rate-setting process resulted in actuarially-justified, noncompetitive rates?**

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### Methodology

To gain an overview of Citizens' rate-setting process, we performed the following procedures:

- Researched state laws, rules, and regulations
- Listened to past legislative meetings at which Citizens' rates were discussed
- Interviewed staff at Citizens and the Department of Insurance (DOI)

To obtain information on whether the Citizens rate-setting process resulted in actuarially-justified, noncompetitive rates, we performed the following procedures:

- Interviewed staff at Citizens and the DOI, as well as the actuarial consultant used by Citizens

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<sup>1</sup> Although Citizens became effective in January 2004, the Louisiana Insurance Rating Commission adopted rates for Citizens to use in October 2003. See pages 12-14 for further information.

- Reviewed the Louisiana Insurance Rating Commission's (LIRC's) meeting minutes for calendar years 2003 through January 2007
- Reviewed Citizens' 2004 and 2006 rate-filings
- Compared Citizens' rates to the rates provided by private insurance companies included in DOI's market comparisons of the 2006 rate-filing
- Compared Citizens' rate quotes included in a Legislative Auditor's report dated October 2006 to private insurance company rate quotes from the same report

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## Overview of Louisiana Citizens Property Insurance Corporation

The Louisiana Citizens Property Insurance Corporation (Citizens) was created as a nonprofit corporation by Act 1133 of the 2003 Regular Legislative Session, which enacted, in part, R.S. 22:1430.2(A). The corporation was formed to operate two residual market insurance programs previously established by the legislature and known as the Louisiana Insurance Underwriting Plan and the Louisiana Joint Reinsurance Plan. The legislation renames the old plans as the Coastal Plan and the FAIR Plan, respectively, and designates the newly named plans as successors to the old plans. Under state law, Citizens and the two plans are subject to examination by the Legislative Auditor.

According to the enabling legislation, Citizens was created as a nonprofit corporation to provide fire, extended coverage, vandalism, malicious mischief, and homeowners insurance in the coastal and other areas of Louisiana to applicants who are entitled to, but are unable to, procure coverage through the voluntary (i.e., private) market. Citizens is to operate insurance plans functioning exclusively as residual market mechanisms. That is, Citizens was designed to be an insurer of last resort. Any person with an insurable interest in insurable property (residential or commercial) is entitled to apply to Citizens either directly or through a representative for coverage through the Coastal or FAIR Plan.

R.S. 22:1430.3(A) establishes a 15-member board of directors for Citizens. The board is responsible for adopting a plan of operation. The House and Senate Insurance Committees must approve Citizens' plan of operation, as well as all revisions to the plan. The plan must be filed with the Office of Property and Casualty of DOI.

State law includes financing provisions for Citizens to use if either plan incurs a deficit. Specifically, when the deficit meets certain criteria, the entire deficit shall be recovered through regular assessments of assessable insurers. Assessable insurers are all private insurers authorized to write the same lines of business as Citizens writes. These insurers may then recoup the costs of the regular assessment from their policyholders. When Citizens levies regular assessments, it must also charge its own policyholders a comparable fee. The law also provides that, if regular assessments are not sufficient to cover the deficit, the remaining deficit shall be recovered through emergency assessments on applicable policyholders. More information about the assessment process can be found in the Legislative Auditor's report issued in December 2006 titled *Louisiana Citizens Property Insurance Corporation - Assessments*.



State law further provides that the legislature intends for Citizens to work toward the ultimate depopulation of the Coastal and FAIR plans. The statute provides a means of dissolving the corporation when less than 1,000 policies are written in a plan year. According to Citizens' records, as of December 31, 2006, it had 125,859 policies in force, representing approximately \$18.9 billion in exposure (i.e., coverage). Exhibit 1 shows the FAIR and Coastal Plans' shares of these totals.

<b>Exhibit 1</b> <b>Citizens' Policies and Exposure</b> <b>December 31, 2006</b>		
	<b>Number of Policies</b>	<b>Exposure (in billions)</b>
FAIR Plan	119,478	\$18.2
Coastal Plan	6,381	\$ 0.7
<b>Total</b>	<b>125,859</b>	<b>\$18.9</b>
<b>Source:</b> Developed by legislative auditor's staff from unaudited data provided by Citizens' staff.		

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## Overview of Citizens' Rate-Setting Process

The statute governing Citizens' rate-setting process (R.S. 22:1430.12) states that Citizens' rates must be actuarially justified and adjusted annually. The statute also stipulates that Citizens' rates are not intended to compete with private insurance company rates. Since Citizens sells both commercial and residential policies, these statutory provisions apply to both types of coverage. The following paragraphs describe the four components of Citizens' rate-setting process for residential property:

1. Actuarial analysis
2. Market comparison
3. Rate determination
4. Rate filing and implementation

For commercial property, Citizens' rate-setting process involves only the first and fourth components.

**Actuarial Analysis.** Citizens uses an actuarial consulting firm to conduct an actuarial analysis. Citizens provides the consultant with historical data on its premiums and losses. To reflect the potential for catastrophes, the actuary removes from the historical data actual costs due to catastrophic events. The consultant then adds to the data, as a catastrophe loading factor, modeled losses. This calculation simulates expected catastrophic losses. The consultant uses modeled losses instead of actual losses because catastrophes do not occur often enough to be used in the same way that noncatastrophe historical data are used in actuarial analyses. Using the adjusted premium and loss data with the catastrophe loading factor, the consultant develops actuarially-indicated rates for Citizens to use to determine its residential and commercial rates.

**Market Comparison.** In addition to the stated intent for Citizens not to compete with private insurance companies, the law also requires that Citizens' rates be at least 10% higher than those of the largest private insurers within each parish (i.e., the insurance companies with the greatest total direct written premium in each parish for that line of business in the preceding year). Specific provisions of the law are as follows:

- For mobile home insurance, the average Citizens rates must be at least 10% above the rates among the five largest private mobile home insurers in each parish.
- Rates charged by Citizens for other lines of business (except wind and hail coverage) must be at least 10% higher than the rates charged among the 10 largest insurers in each parish for each individual line of business.
- The rates Citizens charges in a particular parish must be at least 10% above the rates of any insurer that has a minimum of 3% of the total premium for the parish.
- The statute excludes Citizens' wind and hail coverage rates from these comparisons until after January 1, 2009.

The statute also gives the Citizens Board of Directors responsibility for developing a methodology to determine the rates charged among the largest insurers in each parish.

For residential rates, Citizens conducts market comparisons to ensure that the statutory requirements are met. Citizens and DOI begin by developing a typical Citizens' customer and policy. DOI then surveys private insurance companies to identify the largest insurers by line of business in each parish and obtains rate quotes from those insurers for the typical customer and policy. For each line of business in each parish, Citizens identifies the highest rate quote for the typical Citizens customer. Citizens adds 10% to each of these quotes to identify the rates indicated by the market comparison to use to determine its rates.

**Rate Determination.** Citizens then determines its residential rates. To do so, it compares the rates derived from the actuarial analysis to those from the market comparison. Citizens then selects the higher rate for each line of business in each parish.

**Rate Filing and Implementation.** For residential and commercial rates, Citizens packages the information into a rate filing and submits it to the LIRC for approval. After the LIRC approves Citizens' rate filing, Citizens updates the rate tables in its Operations Manual and computer system. It then begins using the new rates on the appropriate effective dates. Citizens generally sets different effective dates for new policies versus renewal policies.

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## **Importance of Noncompetitive Rates**

It is important that Citizens' rates do not compete with the rates of voluntary market companies for various reasons. If consumers buy insurance policies based on price, Citizens' rates become competitive with private companies' rates when its rates are below those of the private companies. Consequences of Citizens using competitive rates include the following:

1. The number of Citizens policyholders would likely increase.
2. Private companies may choose to withdraw from the property insurance market.
3. The stated legislative intent of the revised statute regarding competition would not be met.
4. The stated legislative intent that Citizens work toward depopulation of the residual market insurance plans would not be met.

Each of the potential consequences listed above is discussed in further detail in the following paragraphs.

**Increase in Number of Citizens Policyholders.** If Citizens' rates are competitive, it will likely increase the number of customers who buy policies from Citizens rather than from private insurance companies. As Citizens increases its number of policyholders, it also increases its exposure to risk. Increasing its exposure to risk, in turn, increases the size and likelihood of future charges on Louisiana's policyholders because of regular and emergency assessments. This effect would be especially strong if the new risk exposure were concentrated in hurricane-prone areas.

**Private Companies' Withdrawal From Market.** In the face of price competition from Citizens (a nonprofit corporation with the ability to levy assessments to pay for unexpected losses), some private insurers may decide that it is not profitable to sell property insurance in some or all areas of Louisiana. Thus, some companies may elect to withdraw from or not enter the market. When the volume of property insurance written by private companies decreases, Citizens' volume increases, which, as previously discussed, increases the risk of further assessments.

**Noncompliance With Legislative Intent Regarding Competition.** State law specifically provides that Citizens is not intended to offer rates that are competitive with the voluntary market. If Citizens' rates are below those of private insurance companies, it is, in effect, competing with the private market. If Citizens becomes competitive, it is not in compliance with the intent of the law.

**Failure to Depopulate Plans.** State law provides the following: "The legislature further intends that the corporation work toward the ultimate depopulation of these residual market insurance plans." As previously stated, if Citizens' rates compete with those of the private market, Citizens' market share would likely increase. Increasing Citizens' market share would, as a result, contradict legislative intent.

## Findings, Conclusions, and Recommendations

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### Comparison of Rate Quotes

As previously stated, by law, Citizens' rates are not to compete with private insurance companies' rates. To assess the competitiveness of Citizens' rates, we compared Citizens' rates for a hypothetical property to the rates for the same hypothetical property of each of the largest private companies in Louisiana. We used readily available information on residential rates and conducted two comparisons, one using August 2005 data and the other using August 2006 data.<sup>2</sup> Both comparisons showed that some of Citizens' rate quotes were at or below those of the largest private companies. Thus, in many cases, Citizens' rates appeared to be competitive. Using its current rate-setting process, Citizens has had difficulty keeping all of its rates noncompetitive.

For both comparisons, we compared the rate quotes by line of business and parish. The Citizens' rates in effect when we made our comparisons have since been adjusted. The adjusted rates are to become effective June 1, 2007, for new policies and August 1, 2007, for renewed policies. Even though the rates have been adjusted, however, our comparisons indicate problems with the overall rate-setting process used by Citizens.

As stated earlier, if Citizens' rates compete with private insurance companies' rates, several consequences may occur. Competition will likely result in an increase in the number of Citizens policyholders. It could also result in private companies choosing to withdraw from the market. Finally, it violates the legislature's stated intent regarding noncompetitive rate-setting and policy depopulation.

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### Factors Affecting Rate Competition

As illustrated in the previous section, Citizens' rate-setting process allows for the possibility that at least some of its rates may become competitive with private company rates. Competitive rates have emerged despite the fact that state law specifically says that Citizens is not to compete with the private market. The following factors contributed to Citizens' rates becoming competitive:

- The catastrophe loading factor Citizens used in its rate calculations
- The market comparison process Citizens used in its rate calculations
- The sophistication of Citizens' rate structure
- The frequency and timing of Citizens' and private companies' rate adjustments

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<sup>2</sup> We only compared residential rate quotes because similar data were not available for commercial rates.

## **Catastrophe Loading Factor**

As previously stated, Citizens used an actuarial consulting firm to perform the actuarial analysis for its most recent rate filing. According to the consultant, he followed a standard actuarial methodology as he would for any other company when he conducted the analysis for Citizens. DOI's actuarial staff reviewed the consultant's analysis prior to the LIRC granting approval.

As explained earlier, calculating a catastrophe loading factor is part of the actuarial analysis. After Hurricane Katrina, catastrophe modeling companies updated their catastrophe models to predict more hurricane activity, thereby increasing predicted losses. However, Citizens' most recent rate-filing did not include the latest version of the catastrophe model. The actuarially-indicated rates included in that filing would have been higher, in some cases, if the consultant had used the new catastrophe model.

The consultant stated that the model was updated after the Citizens analysis was completed but before the rate-filing was submitted. Thus, while an actuarial analysis was conducted, as required by law, and was independently reviewed, it did not reflect the most current catastrophe loss predictions. As a result, Citizens' rates may be at or below the rates of private companies that used catastrophe loading factors based on updated models.

**Recommendation 1:** Citizens should file a rate adjustment as soon as possible using the most recent (post-Katrina and Rita) catastrophe model. Filing a rate adjustment will help ensure that Citizens' rates do not compete with those of private insurance companies that set their rates using current catastrophe models.

**Summary of Management's Response:** Citizens agrees with this recommendation and states that as soon as the Systems/Financial plan and private company rate review project are completed, it will develop another rate review to be filed in early 2008.

## **Market Comparison**

Overall, Citizens' market comparison process is prone to time lags and data errors. For example, the data collected for the market comparison used in Citizens' 2007 rate filing were due at DOI from insurance companies on July 15, 2005. The market comparison was expected to be used for a rate filing that would go into effect in early 2006; however, the hurricanes delayed implementing the new rates until early 2007. According to Citizens, it generally has taken six months from the beginning of the market comparison process until rate filings become effective anyway.

In addition, as mentioned on page 7, DOI surveys private companies to identify the insurers that have the largest market share in each parish and then obtains rates from those companies for a typical customer and policy. According to Citizens, during the survey for its most recent rate-filing, two companies gave DOI inaccurate data to use in the market comparison. To move forward, DOI fixed the errors by manually recalculating those companies'

rates using information provided by the companies in their own rate-filings. In addition, Citizens removed a company from the analysis that had been erroneously included. These time lags and data errors could cause Citizens' rates to become competitive.

**Matter for Legislative Consideration:** In keeping with the legislative intent for Citizens' rates to be noncompetitive with the private market but to improve Citizens' rate-setting process, the legislature should amend R.S. 22:1430.12 to require Citizens to set its rates at a specified percentage above the rates determined through actuarial analysis. This provision would replace the existing requirement that Citizens' rates be at least 10% above those of the largest private companies. The new method would streamline Citizens' rate-setting process by eliminating the market comparison, which is currently hampered by time lags and data errors.

**Recommendation 2:** If the legislature does not amend the law as stated in the matter for legislative consideration, Citizens should improve its monitoring of the private insurance market. Regular, periodic monitoring would help Citizens meet the legal requirement of annual rate adjustment and help ensure that its rates remain 10% above those of the largest private companies in each parish. The following list provides options that Citizens should consider implementing in lieu of conducting the market comparison.

- Citizens could work with DOI and the industry to establish an automated reporting procedure that would allow it to monitor market rates more frequently than annually. Private companies could periodically provide Citizens with their actual average rates and information on the types of policies they write (e.g., average amount of insurance, adjustment factors for various fire protection classes, and adjustment factors for various tiers and credits offered). To protect the confidentiality of proprietary information, DOI could solicit the information from the private companies for Citizens and then compile it in a way that would protect its confidentiality. Citizens could then adjust this information to make it represent its typical policyholder and compare the adjusted information to its current rates.
- Citizens could continually monitor the largest private companies' rate filings to determine if its rates consistently remain 10% above those of the largest private companies in each parish.
- Citizens could monitor the market by investigating anomalies in its own sales trends. For instance, unusual increases in the number of policies sold in a particular parish may signal that Citizens has become competitive in that market. Citizens should follow up on identified anomalies to determine their cause.

**Summary of Management's Response:** Citizens agrees with this recommendation and points out that since Citizens has no authority to obtain rates from the competitive market, it will have to work through the Department of Insurance to obtain them.

## Rate Structure

Over time, private insurance companies have added various factors to be considered when setting their rates. Citizens, however, has not done so. For example, Citizens does not consider policyholders' claims histories when setting its rates, whereas some private insurance companies do. Private companies that consider claims histories when setting their rates can charge policyholders significantly more or less based on how many claims the policyholders have had. Because Citizens does not consider this factor, it charges policyholders with favorable claims histories the same premium it charges policyholders with unfavorable claims histories.

As previously stated, Citizens uses the market comparison process in an effort to set its rates so that its average policyholder in each parish is charged at least 10% above the highest premium charged by the largest 10 insurers in the parish. Because Citizens does not use factors that private insurers use to set rates, its rates for policyholders who differ from the average policyholder may be lower than those charged by private insurers.

**Recommendation 3:** Citizens should mimic the property insurance industry's rate structure by incorporating into its rate structure common factors used in the private industry. For example, Citizens could include customers' claims histories in its rate structure. If Citizens makes its rates structure comparable to those of private insurers, the likelihood that Citizens' rates are competitive for atypical policyholders (i.e., those who differ from the average policyholder) would decrease.

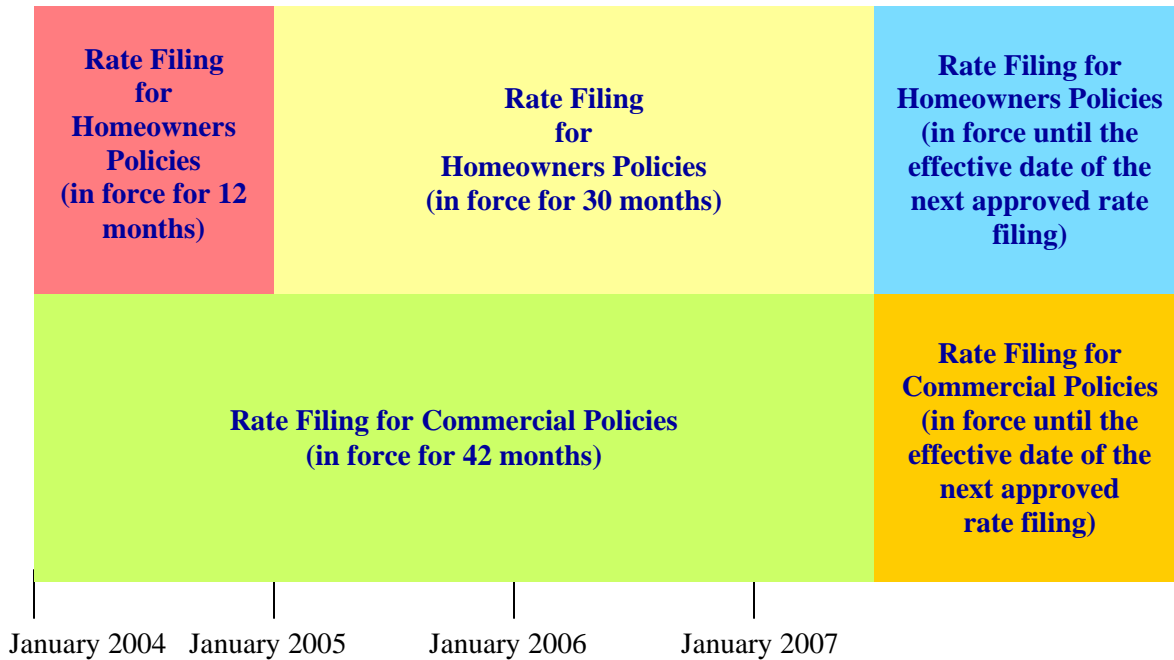
**Summary of Management's Response:** Citizens agrees with this recommendation and will include such information in its next rate filing.

## Rate Adjustments

State law requires Citizens to adjust its rates annually. Citizens, however, has not met this requirement. Exhibit 2 on the following page illustrates the implementation dates of Citizens' rate filings since its initial rate filing, which occurred in October 2003.



**Exhibit 2**  
**Implementation Dates for Citizens' Rate Filings**



On October 15, 2003, the LIRC approved Citizens' initial rate filing. In that rate filing, Citizens adopted the rates and rules from the previous FAIR and Coastal Plans for commercial and residential (i.e., dwelling fire and homeowner) policies. Those rates and rules became effective on January 1, 2004, the date on which Citizens replaced the previous plans. On September 29, 2004, the LIRC approved an overall 26.9% rate increase for Citizens' residential policies. These rates went into effect on January 1, 2005, for new policies and on March 1, 2005, for renewal policies. Citizens did not request rate changes for commercial policies in this filing. On January 17, 2007, the LIRC approved rate increases for Citizens' residential and commercial property policies. These rates will go into effect on June 1, 2007, for new policies and August 1, 2007, for renewal policies. As can be seen, Citizens has not adjusted its rates annually.

It should be noted that all private companies do not adjust their rates at the same time each year. As a result, Citizens' rates may not always incorporate the most recent private rate filings. This situation may cause Citizens' rates to become competitive, thus a quick turnaround on rate filings is important.



**Recommendation 4:** Citizens should ensure that all of its rates are reviewed and adjusted (if needed) at least annually. During periods when private insurance companies raise rates significantly and regularly, it is essential for Citizens to keep up with those rate changes to remain noncompetitive.

**Summary of Management's Response:** Citizens agrees with this recommendation and will review rates at least once a year.

**APPENDIX A: MANAGEMENT'S RESPONSE**





**Louisiana  
Citizens**

**Property Insurance  
Corporation**

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Thursday, May 17, 2007

Mr. Steve J. Theriot  
Legislative Auditor  
State of Louisiana  
1600 North Third Street  
P.O. Box 94397  
Baton Rouge, LA 70804-9397

Re: Audit on Louisiana Citizens Property Insurance  
Corporation—Rate Setting

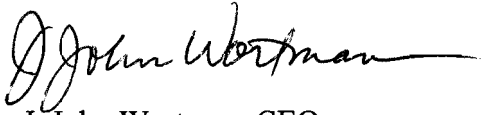
Dear Mr. Theriot:

First let me say that although I was not hired by Citizens until the captioned audit was basically completed, the people involved in the process have told me of the professionalism of Mr. Farrar, Ms. Klein, and Ms. Fitzgerald throughout the audit process. I know we both share the opinion that professionalism and co-operation on the part of both parties in this process delivers a more meaningful product for everyone involved.

While our formal response to your findings is attached, I thought I would summarize our comments for you in this cover letter. Very briefly, other than one minor issue, we accept your findings and are committed to implementing procedures to comply with your recommendations. The only minor exception is that in recommendation 2 it is difficult, under the current Statute, for Citizens to obtain pricing data directly from the private insurance sector to monitor the 10% rule. We are; however, working closely with the Actuarial Division of Insurance Department to secure data. In fact, correspondence from the Insurance Department has recently been sent to the relevant private carriers to secure the necessary pricing information.

Again, as outlined above, we are committed to implement procedures to comply with your recommendations.

Sincerely,

A handwritten signature in black ink, appearing to read "J. John Wortman". The signature is fluid and cursive, with a long horizontal stroke at the end.

J. John Wortman, CEO  
Louisiana Citizens Property Insurance Corporation

C: Bill Newton, Chairman, Louisiana Citizens Property Insurance Corporation  
Joe Deutsch, Acting CEO, Property Insurance Association of Louisiana



Louisiana Legislative Auditor  
Performance Audit Division

Checklist for Audit Recommendations

**Instructions to Audited Agency:** Please check the appropriate box below for each recommendation. A summary of your response for each recommendation will be included in the body of the report. The entire text of your response will be included as an appendix to the audit report.

RECOMMENDATIONS	AGREE	PARTIALLY AGREE	DISAGREE
<p><b>Recommendation 1:</b> Citizens should file a rate adjustment as soon as possible using the most recent (post-Katrina and Rita) catastrophe model. Filing a rate adjustment will help ensure that Citizens' rates do not compete with those of private insurance companies that set their rates using current catastrophe models. (p. 9 of the report)</p>	X		
<p><b>Recommendation 2:</b> If the legislature does not amend the law as stated in the matter for legislative consideration, Citizens should improve its monitoring of the private insurance market. Regular, periodic monitoring would help Citizens meet the legal requirement of annual rate adjustment and help ensure that its rates remain 10% above those of the largest private companies in each parish. The following list provides options that Citizens should consider implementing in lieu of conducting the market comparison.</p> <ul style="list-style-type: none"> <li>• Citizens could work with DOI and the industry to establish an automated reporting procedure that would allow it to monitor market rates more frequently than annually. Private companies could periodically provide Citizens with their actual average rates and information on the types of policies they write (e.g., average amount of insurance, adjustment factors for various fire protection classes, and adjustment factors for various tiers and credits offered). To protect the confidentiality of proprietary information, DOI could solicit the information from the private companies for Citizens and then compile it in a way that would protect its confidentiality. Citizens could then adjust this information to make it represent its typical policyholder and compare the adjusted information to its current rates.</li> <li>• Citizens could continually monitor the largest private companies' rate filings to determine if its rates consistently remain 10% above those of the largest private companies in each parish.</li> <li>• Citizens could monitor the market by investigating anomalies in its own sales trends. For instance, unusual increases in the number of policies sold in a particular parish may signal that Citizens has become competitive in that market. Citizens should follow-up on identified anomalies to determine their cause. (p. 10 of the report)</li> </ul>		X See response attached	

<p><b>Recommendation 3:</b> Citizens should mimic the property insurance industry's rate structure by incorporating into its rate structure common factors used in the private industry. For example, Citizens could include customers' claims histories in its rate structure. If Citizens makes its rates structure comparable to those of private insurers, the likelihood that Citizens' rates are competitive for atypical policyholders (i.e., those who differ from the average policyholder) would decrease. (p. 11 of the report)</p>	<p>X</p>		
<p><b>Recommendation 4:</b> Citizens should ensure that all of its rates are reviewed and adjusted (if needed) at least annually. During periods when private insurance companies raise rates significantly and regularly, it is essential for Citizens to keep up with those rate changes in order to remain noncompetitive. (p. 12 of the report)</p>	<p>X</p>		

**Louisiana Citizens Property Insurance Corp.**  
**Response to Legislative Audit on Rate Making Procedures**

**Summary of Recommendations and response**

- 1) Recommendation 1. - Citizens should file a rate adjustment as soon as possible using the most recent (post Katrina and Rita) catastrophe model.

Response: We agree with the recommendation. A June 1, 2007 rate change was recently implemented. This rate change was based on pre Katrina and Rita data. As soon as the Systems/Financial plan and the private company rate review project are completed we will develop another rate review. We expect to be able to file this in early 2008 for a March 1, 2008 effective date, well within the one year Statutory Requirement.

- 2) Recommendation 2. - Citizens needs to improve its monitoring of the private insurance market. Regular monitoring will help Citizens meet the legal requirement of annual rate adjustment and help ensure that its rates remain 10% above those of the largest private companies in each parish.

Response: We agree with the recommendation except for one point. The recommendation states that Citizens should work with the Insurance Department and the industry to establish an automated procedure to monitor industry rates. The recommendation also states that private companies should periodically provide Citizens with their rates. Currently, Citizens has no authority to obtain rates from the competitive market. This has to be completed through the Insurance Department. Citizens is currently working with the Insurance Department to secure regular updates of private sector rates.

- 3) Recommendation 3. - Citizens should mimic the property insurance industry's rate structure by incorporating into its rate structure common factors used in the private industry.

Response: We agree with this recommendation and will this will be included in the next rate review that will be filed in early 2008.

- 4) Recommendation 4. - Citizens should ensure that all of its rates are reviewed and adjusted (if needed) at least annually.

Response: We agree with this recommendation and Citizens will review rates at least annually.