Management's Discussion and Analysis

Company Background

This discussion provides an assessment by management of the financial position, results of operations, cash flow and liquidity for Louisiana Citizens Property Insurance Corporation (LCPIC). LCPIC was established in 2003 by the Louisiana legislature as a nonprofit corporation to operate residual market insurance plans effective January 1, 2004. The objective of LCPIC is to provide essential property insurance for residential and commercial property applicants who are unable to procure insurance through the voluntary market. LCPIC is the successor to the program established by Act 424 of the 1992 Regular Legislative Session designated as the "Fair Access to Insurance Requirements Plan" or otherwise known as the Louisiana Joint Reinsurance Plan (FAIR Plan) and the Louisiana Insurance Underwriting Plan (Coastal Plan). Information presented in this discussion supplements the financial statements, schedules, and exhibits in Louisiana Citizens Property Insurance Corporation's 2016 Annual Statement.

Major events occurring in 2016 for LCPIC were:

- LCPIC renewed its reinsurance program in May 2016 for the same storm coverage of $650 million while reducing the retention from $50.0 million to $35.0 million that includes a traditional reinsurance program and cat bonds for a savings of approximately $8.0 million compared to 2015.
- LCPIC refinanced its Series 2006C and Series 2012 Assessment Revenue Bonds by issuing Series 2016A Refunding Bonds and Series 2016B Taxable Refunding Bonds, respectively. Funds from the Emergency Assessment Stabilization Fund and the Debt Service Reserve Fund were also utilized towards the refinancing. A savings of approximately $99.4 million will be realized as a result of the refinancing.
- LCPIC completed an tenth round of depopulation effective December 1, 2016 transferring 9,852 policies and approximately $2.0 billion of exposure to the private insurance market.
- There were no significant catastrophes that occurred in 2016.

Financial Position

LCPIC's financial position at December 31 was as follows:

Balance Sheet (in thousands of dollars - 000)	2016	2015
Assets		
Bonds	$984	$0
Common stocks	0	146,932
Cash, cash equivalents and short-term investments	233,881	92,101
Total cash and invested assets	234,865	239,033
Uncollected and deferred premiums	12,727	16,614
Reinsurance balances	4,108	980
Long-term emergency assessments receivable	525,318	633,202
Excess emergency assessments collected over debt service	33,671	0
Other assets	18,714	19,958
Total assets	$829,403	$909,787
Liabilities and Policyholders' Surplus		
Unpaid loss and loss adjustment expenses	$40,422	$66,263
Borrowed money	574,019	639,945
Unearned premiums	48,402	65,495
Take out premium payable	8,735	1,919
Restricted assessments	31,857	76,234
Other liabilities	19,262	20,749
Total liabilities	722,697	870,605
Total policyholders' surplus	106,706	39,182
Total liabilities and policyholders' surplus	$829,403	$909,787

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Assets

Total assets decreased by $80.4 million in 2016 compared to 2015 primarily due to:

The decrease in common stocks from $146.9 million in 2015 to zero in 2016 is due to a change in NAIC security classification guideline. The $146.9 million in money market mutual funds was moved from common stocks to short-term investments.

The increase in cash, cash equivalents and short-term investments of $141.8 million in 2016 compared to 2015 is primarily due to the security classification change in money market mutual funds described above for common stocks. Offsetting the increase of $146.9 million in short-term investments was a decrease in cash and cash equivalents of $5.1 million resulting from normal operations as described in greater detail in the cash flow section on Page 350.4.

Long-term emergency assessments receivable reflects the future assessments that will be utilized to repay outstanding bond debt from Hurricane Katrina losses incurred in 2005. The decrease of $107.9 million is due to the following three factors. (1) $45.5 million bond principal reduction from the refinancing of Series 2006C and 2012 Series Assessment Revenue Bonds, and (2) $45.6 million bond principal payment made in 2016, and (3) $16.8 million withdrawal to offset Katrina losses.

Excess emergency assessments collected over debt service reflects the excess of either unrestricted bond funds or future debt service costs. Prior to the 2016 bond refinancing, unrestricted bond funds exceeded future debt service costs. Due to the bond premium received from the 2016 bond refinancing, the $33.7 million in excess emergency assessments collected over debt service is the future debt service costs that exceed the unrestricted bond funds.

Liabilities

Total liabilities decreased $147.9 million in 2016 compared to 2015 primarily due to:

Unpaid losses and LAE decreased $25.8 million in 2016. The decrease is primarily due to settlement payments for Oubre class action suit and settlement of litigation claims related to Hurricane Katrina. IBNR reserves decreased $16.3 million due to payments made for class action suits and $8.1 million in case and IBNR reserves decreased related to Hurricane Katrina claim activity. Unpaid losses and LAE are stated at LCPIC's estimate of the ultimate cost, net of reinsurance, of settling all incurred but unpaid claims. Unpaid losses and loss adjustment expenses are not discounted and no estimate for salvage and subrogation is applied as a reduction to the unpaid losses. The estimate for unpaid losses and loss adjustment expenses is closely monitored and adjusted, if needed. LCPIC uses various development modeling techniques to assist in the evaluation of its reserves under the direction of its actuary. As an additional safeguard in the valuation of unpaid losses and LAE, LCPIC receives an opinion from an outside actuary. Management believes that its reserves are adequate, but establishing reserves is a judgmental and inherently uncertain process. It is therefore possible that as conditions and experience develops, reserve adjustments may be required in the future.

Borrowed money decreased $65.9 million in 2016 compared to 2015 primarily due to the $45.5 million bond principal reduction from the refinancing of the Series 2006C and Series 2012 Bonds, and a $45.6 million bond principal payment made in 2016. Offsetting this decrease was $24.1 million received in bond premium from the bond refinancing.

The decrease of $17.1 million in unearned premiums is primarily from LCPIC's depopulation program.

Takeout premium payable of $8.7 million represents the initial assumed premium due to the companies that are participating in the December 1, 2016 round, Round 10, of depopulation. The increase in takeout premium payable in 2016 compared to 2015 is due to the payment of the initial assumption in January 2017 for Round 10 to assuming companies was not paid as it was for the prior year. For Rounds 8 and 9, LCPIC paid assuming companies 90% of the initial assumption in December and 10% in January of the following year.

Management's Discussion and Analysis

Liabilities (continued)

Restricted assessments of $31.9 million reflects assessment revenues held by the Bond Trustee for repayment of borrowed money. Prior to the 2016 bond refinancing, restricted assessments and unrestricted bond funds exceeded future debt service costs. Due to the bond premium received from the 2016 bond refinancing, $33.7 million in excess emergency assessments collected over debt service was transferred as an asset on the Balance Sheet. Restricted assessments decreased $44.4 million in 2016 due to the following:

Description (in millions)	Increase (Decrease)
Principal and interest paid	($72.4)
Cash used towards refinance of Series 2006C and Series 2012 Assessment Revenue Bonds	($38.1)
Unrestricted funds balance at the end of 2015	($5.1)
Emergency assessments transferred from unrestricted to restricted assessments	$71.2
Net change	($44.4)

Policyholders' Surplus

The increase in total policyholders' surplus of $67.5 million in 2016 compared to 2015 is primarily due to a net income of $84.0 million. Offsetting the increase from net income was a $19.2 million decrease from the change in nonadmitted assets and $1.4 million decrease from the change in provision for reinsurance. The change in nonadmitted assets primarily resulted from the reinsurance amounts recoverable from reinsurers that is pending their review of LCPIC's reinsurance billings. The provision for reinsurance occurs when any reinsurance ceded to unauthorized reinsurers is not allowed as a credit against the company's loss reserves if uncollateralized or recoverable balances are overdue. In addition to net income, $4.1 million from tax exempt surcharge collected on LCPIC policies contributed to the increase in policyholders' surplus. Tax exempt surcharge is collected to maintain a federal exempt status and to augment the financial resources of the corporation. It is collected on each policy and represents an amount equal to the premium taxes paid which is 3% of the policy premium.

Results of Operations

LCPIC's operating results and key financial ratios are presented in the following table.

Statement of Income and Ratios (000)	2016	2015
Premiums earned	$78,749	$101,222
Losses incurred	(26,514)	19,531
LAE incurred	4,641	9,891
Underwriting expenses	18,930	23,295
Underwriting gain (loss)	81,692	48,505
Net investment loss	(47,361)	(36,669)
Other Income	49,697	38,792
Net income	$84,028	$50,628
Loss Ratio	(33.7%)	19.3%
LAE Ratio	5.9%	9.8%
Underwriting expense ratio	30.7%	26.8%
Combined ratio	2.9%	55.9%

Net income in 2016 was $33.4 million greater than 2015 due to:

Premiums earned decreased $22.5 million due to LCPIC's depopulation efforts.

Management's Discussion and Analysis

Results of Operations (continued)

Losses and LAE incurred was ($21.9) million in 2016 compared to $29.4 million in 2015 for a net change of ($51.3) million that was due to the following:

Description (in millions)	Cash Provided (Cash Applied)
In 2016, based on new information, LCPIC was able to re-categorize past settlements for the Oubre class action suit to policyholders impacted by Hurricane Rita. Previously, these policyholders had been classified as being impacted by Hurricane Katrina. As a result, LCPIC ceded losses and LAE of $20.0 million attributed to Hurricane Rita that had not previously been ceded.	(20.0)
In 2016, LCPIC contracted a third party to review its claim database to identify claims that had not previously been ceded. As of 12/31/16, LCPIC has ceded $10.4 million identified from the review and attributable to three prior catastrophe recovery events.	(10.4)
In 2016, LCPIC settled the majority of remaining litigated claims pertaining to Hurricane Katrina that resulted in a $7.1 million decrease in incurred losses and LAE.	(7.1)
In 2016, LCPIC received a return settlement payment of $6.8 million related to the Press class action suit.	(6.8)
In 2016, $3.6 million of unpaid losses pertaining to the Oubre class action suit was ceded under Hurricane Rita reinsurance coverage that had not previously been ceded.	(3.6)
All other decreases in incurred losses and LAE.	(3.4)
Net decrease in losses and LAE incurred	($51.3)

Combined ratio – the combined ratio in 2016 was 2.9% compared to 55.9% in 2015 is primarily due to the decrease in premiums earned and losses incurred. The combined ratio expresses the sum of the costs for losses, LAE and underwriting expenses as a percentage of premiums (premiums earned for the loss and LAE ratios and premiums written for the underwriting expense ratio). The ratio is a recognized industry measure of underwriting performance.

Cash Flow and Liquidity

Cash Flow

Primary sources of cash include cash from premiums collected, miscellaneous income, proceeds from investments sold, matured or repaid; and primary uses of cash include debt service costs, losses and expenses paid, and the cost of investments acquired.

The cash flows of LCPIC are summarized as follows:

Cash Flow Statement (000)	2016	2015
Operations		
Premiums collected	$64,447	$99,248
Net investment income received (paid)	(47,606)	(36,669)
Miscellaneous income	49,697	38,792
Losses paid	(17,952)	(22,847)
Expenses paid	(27,219)	(33,757)
Net cash from operations	$21,367	$44,767
Investment Activities		
Proceeds from investments sold, matured or repaid	$377,066	$236,073
Cost of deficit long-term investments acquired	(231,119)	(212,634)
Net cash from investments	145,947	23,439
Financing Activities		
Other cash provided (applied)	(25,533)	(47,921)
Net cash from financing activities and miscellaneous sources	(25,533)	(47,921)
Change in Cash and Short-Term Investments		
Net change in cash, cash equivalents and short-term investments	$141,781	$20,285

Management's Discussion and Analysis

Cash Flow (continued)

Cash and short-term investments increased $121.5 million in 2016 compared to 2015 due to:

Net cash from operations was $21.4 million in 2016 compared to $44.8 million in 2015 for a net change of ($23.4) million that was due to the following:

Description (in millions)	Cash Provided (Cash Applied)
Change in premiums collected is related to LCPIC'S depopulation efforts	(34.8)
Losses paid decreased primarily due to claims previously identified with Hurricane Katrina and because of new information determined in 2016, losses were ceded by LCPIC attributed to Hurricane Rita that previously had not been ceded.	4.9
Expenses paid decreased primarily due to the effect of depopulation on commissions and the ceded effect as described above for losses paid that also had a similar impact on LAE.	6.5
Net cash provided from items listed above impacting cash from operations	($23.4)

Net cash from investments in 2016 was $145.9 million compared to $23.4 million in 2015. The change in net cash relates to the cash inflows and outflows of the assessment revenue bond obligations as well as investments of operating cash. The increase in net cash from investments was primarily due to the investment activity related to LCPIC's bond obligations.

Cash provided from financing activities and miscellaneous sources increased $22.4 million in 2016 compared to 2015. Explanations of the change are displayed below:

Description (in millions)	Cash Provided (Cash Applied)
Change in borrowed money is primarily due to less principal paid in 2016 of $91.1 million compared to principal paid in 2015 of $128.7 million.	37.6
Change in accrued liability for restricted assessments as described in the Liabilities section on Page 350.2	29.9
Change in accrued liability for takeout premium payable as described in the Liabilities section on Page 350.1.	6.5
Change in excess emergency assessments over debt service as described in the Assets section on Page 350.1	(33.7)
Change in receivable for emergency assessments as described in the Assets section on Page 350.1	(20.8)
All other cash movements related to financing activities and miscellaneous sources	2.9
Net change	$22.4

Liquidity

All liquid funds held by LCPIC are kept in commercial bank accounts that are FDIC insured or 100% collateralized.

In addition to policyholder premiums, LCPIC has a much broader range of resources available to pay losses and repay debt obligations than does a typical insurer. Presently, LCPIC can institute a regular assessment up to approximately $250 million on the state insurance industry derived from 10% of their written premium for deficits each year, and an emergency assessment up to approximately $260 million derived from 10% of the premium written on property policyholders of the State of Louisiana for each calendar year of a storm to pay debt incurred in previous years. Emergency assessments levied in any calendar year can remain in place each year until any borrowings from that year have been repaid.

In 2015, LCPIC secured a $100.0 million line of credit with Regions Bank that matures in June 2017. The line of credit provides additional liquidity to the corporation.

In 2010, LCPIC instituted lockbox processing to reduce cash flow interruption in the event of a temporary closure of its office for a catastrophic event.

Management's Discussion and Analysis

Liquidity (continued)

In 2005, LCPIC did not have sufficient funds to pay 80,000 claims resulting from Hurricanes Katrina and Rita. In 2006, LCPIC issued $978.0 million of fixed rate assessment revenue bonds. On December 31, 2016, LCPIC had approximately $509.3 million of fixed rate assessment revenue bonds outstanding. The debt service of these bonds is paid through emergency assessments on property insurance policies written in the State of Louisiana. The emergency assessments are remitted quarterly to the bond trustee.

Pending Litigation

As of December 31, 2016 there were 180 open litigation matters against LCPIC. The majority of these lawsuits are first-party suits related to Hurricane Isaac. Unpaid loss and loss adjustment expenses are included on the balance sheet of approximately $3.1 million, excluding the Oubre class action suit described below. The balance of the litigated matters are related to first party losses, third-party bodily injury claims, subrogation or claims where the issue of coverage is in dispute.

Oubre v. Louisiana Citizens Property Insurance Corporation. The plaintiffs in this suit allege that LCPIC failed to timely initiate loss adjustment as required by Louisiana statutory law exposing LCPIC to penalties up to a mandatory limit of $5,000.00. On July 23, 2012 LCPIC settled the first phase of this class action suit with a payment of $104.7 million to the plaintiff counsel for distribution to the class members. LCPIC entered into a settlement with the class for the remaining Oubre claims. LCPIC has paid $109.8 million towards the final settlement as of December 31, 2016 and has a reserve of $30.8 million for the remaining settlement (included in unpaid losses on the balance sheet). LCPIC will continually review the reserve to ensure that it meets the anticipated settlement costs.

Future Plans

LCPIC had $650 million in total reinsurance and cat bonds in place for the 2016 storm season. The cat bonds include a $140.0 million four year catastrophe bond and a $100.0 million three year catastrophe bond. In addition to the reinsurance program and cat bonds, LCPIC has reinstatement premium protection and second event catastrophe coverage. The amount of reinsurance purchased by LCPIC is determined by many factors that include, losses projected by catastrophe models, insured values of the company, reinsurance market prices, and availability of cash. The reinsurance coverage, excluding cat bonds, described above expires on May 31, 2017. LCPIC is in the process of negotiating a new reinsurance program for the 2017 storm season.

To the extent that the above comments about future plans constitute forward-looking statements, these statements are not guaranties of future performance. Forward-looking statements are based on current expectations and projections about future events and are subject to risks, uncertainties and assumptions about LCPIC, economic and market factors, judicial rulings and the insurance industry, among other things. Actual events may differ materially from those expressed in forward-looking statements.