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 2017 Annual Statement.

Major events occurring in 2017 for LCPIC were:

- LCPIC renewed its reinsurance program in May 2017 for the same storm coverage of $650 million and retention of $35.0 million that includes a traditional reinsurance program and cat bonds for a savings of approximately $7.6 million compared to 2016. The 2017 program provides for 1 in 157 year storm coverage compared to the 2016 program which provided 1 in 100 year storm coverage.
- LCPIC completed an eleventh round of depopulation effective December 1, 2017 transferring 8,724 policies and approximately $1.8 billion of exposure to the private insurance market.
- There were no significant catastrophes that occurred in 2017.

Financial Position

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

Balance Sheet (in thousands of dollars - 000)	2017	2016
Assets		
Bonds	$81,607	$984
Cash, cash equivalents and short-term investments	186,054	233,881
Total cash and invested assets	267,661	234,865
Uncollected and deferred premiums	9,594	12,727
Reinsurance balances	385	4,108
Long-term emergency assessments receivable	482,078	525,318
Excess emergency assessments collected over debt service	24,713	33,671
Other assets	16,164	18,714
Total assets	$800,595	$829,403
Liabilities and Policyholders' Surplus		
Unpaid loss and loss adjustment expenses	$40,487	$40,422
Borrowed money	518,360	574,019
Unearned premiums	35,071	48,402
Restricted assessments	32,512	31,857
Take out premium payable	7,246	8,735
Other liabilities	13,419	19,262
Total liabilities	647,095	722,697
Total policyholders' surplus	153,500	106,706
Total liabilities and policyholders' surplus	$800,595	$829,403

Management's Discussion and Analysis

Assets

Total assets decreased by $28.8 million in 2017 compared to 2016 primarily due to:

Bonds increased $80.6 million in 2017 compared to 2016 due to a change in investment strategy to maximize LCPIC's Louisiana premium tax investment credit. Effective January 1, 2017, LCPIC's cash on deposit no longer qualified as a Louisiana investment towards calculating the premium tax investment credit. Qualifying investments for the premium tax credit include bonds of the state, municipal, school, road, levee districts, or other political subdivisions of Louisiana. LCPIC's bonds of $81.6 million meet as qualifying Louisiana investments described in the previous sentence.

The decrease in cash, cash equivalents and short-term investments of $47.8 million in 2017 compared to 2016 is primarily due $80.0 million in funding the purchase of bonds as described above. Offsetting the decrease was $26.2 million in amounts recoverable from reinsurers and $6.2 million in net premiums in excess of claims and underwriting expenses.

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 $43.2 million is due to bond principal payment made in 2017.

Excess emergency assessments collected over debt service reflects the excess of either unrestricted bond funds or future debt service costs. The balance of this asset reflects the future debt service costs that exceed unrestricted bond funds. In 2017, excess emergency assessments decreased $9.0 million compared to 2016 primarily due to $63.5 million in emergency assessment income offset by $53.9 million in debt service costs.

Liabilities

Total liabilities decreased $75.6 million in 2017 compared to 2016 primarily due to:

Borrowed money decreased $55.7 million in 2017 compared to 2016 primarily due to the $43.2 million bond principal payment made in 2017 and $12.2 million reduction in unamortized bond premium.

The decrease of $13.3 million in unearned premiums is primarily from LCPIC's depopulation program.

Policyholders' Surplus

The increase in total policyholders' surplus of $46.8 million in 2017 compared to 2016 is primarily due to a change in nonadmitted assets of $22.6 million and net income of $19.9 million. The change in nonadmitted assets primarily resulted from the decrease in reinsurance amounts recoverable from reinsurers of $18.3 million that was collected during 2017. In addition to net income, $3.1 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)	2017	2016
Premiums earned	$55,401	$78,749
Losses incurred	14,717	(26,514)
LAE incurred	8,149	4,641
Underwriting expenses	14,815	18,930
Underwriting gain (loss)	17,720	81,692
Net investment loss	(9,200)	(47,361)
Other Income	11,394	49,697
Net income	$19,914	$84,028
Loss Ratio	26.6%	(33.7%)
LAE Ratio	14.7%	5.9%
Underwriting expense ratio	35.2%	30.7%
Combined ratio	76.5%	2.9%

Management's Discussion and Analysis

Results of Operations (continued)

Net income in 2017 was $64.1 million less than 2016 due to:

Premiums earned decreased $23.3 million due to LCPIC's depopulation efforts.

Losses and LAE incurred was $22.9 million in 2017 compared to ($21.9) million in 2016 for a net change of $44.8 million that was due to the following:

Description (in millions)	**Increase (Decrease)**
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 had 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
In 2017, $3.6 million in Hurricane Ike losses were ceded without prior year ceded reserves.	(3.6)
All other decreases in incurred losses and LAE.	.5
Net decrease in losses and LAE incurred	$44.8

Combined ratio – the combined ratio in 2017 was 76.5% compared to 2.9% in 2016 is primarily due to the decrease in premiums earned and increase in 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.

Management's Discussion and Analysis

Cash Flow and Liquidity

Cash Flow

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

The cash flows of LCPIC are summarized as follows:

Cash Flow Statement (000)	2017	2016
Operations		
Premiums collected	$47,320	$64,447
Net investment income received (paid)	(8,788)	(47,606)
Miscellaneous income	11,394	49,697
Losses paid	7,241	(17,952)
Expenses paid	(24,069)	(27,219)
Net cash from operations	$33,098	$21,367
Investment Activities		
Proceeds from investments sold, matured or repaid	$425	$377,066
Cost of deficit long-term investments acquired	(82,125)	(231,119)
Net cash from investments	(81,700)	145,947
Financing Activities		
Other cash provided (applied)	774	(25,533)
Net cash from financing activities and miscellaneous sources	774	(25,533)
Change in Cash and Short-Term Investments		
Net change in cash, cash equivalents and short-term investments	($47,828)	$141,781

Cash, cash equivalents, and short-term investments decreased $47.8 million in 2017 compared to 2016 due to:

Net cash from operations was $33.1 million in 2017 compared to $21.4 million in 2016 for a net change of $11.7 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	(17.1)
Change in net investment income received is related to debt service costs that were greater in 2016 compared to 2017 as a result of the bond refinancing.	38.8
Change in miscellaneous income is primarily due to a decrease in assessment income required to offset debt service costs.	(38.3)
Losses paid decreased primarily due to losses ceded in 2016 and subsequently collected in 2017.	25.2
Expenses paid decreased primarily due to the effect of depopulation on commissions.	3.1
Net cash provided from items listed above impacting cash from operations	$11.7

Net cash from investments in 2017 was ($81.7) million compared to $145.9 million in 2016. The $227.6 million change in net cash relates to the cash inflows and outflows of the assessment revenue bond obligations as well as investments of operating cash. Explanations of the change are displayed below:

Description (in millions)	Cash Provided (Cash Applied)
Decrease in net cash related to LCPIC's bond obligations for the balance of common stocks reclassified to short-term investments in 2016.	(95.9)
Decrease in operating cash for purchase of bonds to maximize LCPIC's Louisiana premium tax investment credit.	(80.7)
Decrease in operating cash for the balance of common stocks reclassified to short-term investments in 2016.	(51.0)
Net cash applied from items listed above impacting cash from investments	(227.6)

Management's Discussion and Analysis

Cash provided from financing activities and miscellaneous sources increased $26.3 million in 2017 compared to 2016. Explanations of the change are displayed below:

Description (in millions)	Cash Provided (Cash Applied)
Change in borrowed money is primarily due to the 2016 bond refinance where additional bond principal was paid in 2016 of $45.5 million compared to 2017, offset by additional amortization of bond premium in 2016 of $36.4 million compared to 2017.	9.1
Change in accrued liability for takeout premium in 2016 due to the difference in timing of LCPIC's payment to assuming companies of the initial assumption for Round 10 in January 2017 and Round 9 in December 2015.	(8.3)
Change in accrued liability for restricted assessments in 2016 primarily due to cash used towards refinance of Series 2006C and Series 2012 Assessment Revenue Bonds.	45.0
Change in receivable for long-term emergency assessments – 2005 deficit primarily due to cash used towards refinance of Series 2006C and Series 2012 Assessment Revenue Bonds.	(64.6)
Change in receivable for excess emergency assessments collected over debt service primarily due to the bond premium received from the 2016 bond refinancing.	42.6
All other cash movements related to financing activities and miscellaneous sources	2.5
Net change	$26.3

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 $248 million on the state insurance industry derived from 10% of their written premium for deficits each year, and an emergency assessment up to approximately $259 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 2017, LCPIC secured a $50.0 million line of credit with Regions Bank that matures in June 2019. 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.

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, 2017, LCPIC had approximately $466.1 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.

Management's Discussion and Analysis

Pending Litigation

As of December 31, 2017 there were 107 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 $2.5 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, 2017 and has a reserve of $33.7 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 2017 storm season which provided 1 in 157 year storm coverage. The cat bonds includes two $100.0 million three year catastrophe bonds. 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, 2018. LCPIC is in the process of negotiating a new reinsurance program for the 2018 storm season and it is anticipated to provide 1 in 250 year storm coverage.

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.