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 2019 Annual Statement.

Major events occurring in 2019 for LCPIC were:

- LCPIC renewed its reinsurance program in May 2019 with storm coverage of $610 million and retention of $35.0 million that includes a traditional reinsurance program and cat bonds for an increased cost of approximately $1.6 million compared to 2018. The 2019 program provides for 1 in 303 year storm coverage compared to the 2018 program which provided 1 in 250 year storm coverage.
- LCPIC completed an thirtieth round of depopulation effective December 1, 2019 transferring 94 policies and approximately $17.1 million of exposure to the private insurance market.
- There were no significant catastrophes that occurred in 2019.

Financial Position

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

Balance Sheet (in thousands of dollars - 000)	2019	2018
Assets		
Bonds	$78,319	$84,186
Cash, cash equivalents and short-term investments	193,079	175,036
Total cash and invested assets	271,398	259,222
Uncollected and deferred premiums	6,723	7,162
Reinsurance balances	426	194
Long-term emergency assessments receivable	386,500	437,698
Excess emergency assessments collected over debt service	4,520	14,146
Other assets	15,170	15,116
Total assets	$684,737	$733,538
Liabilities and Policyholders' Surplus		
Unpaid loss and loss adjustment expenses	$16,001	$18,982
Borrowed money	405,304	462,803
Unearned premiums	30,434	32,656
Restricted assessments	36,080	34,434
Other liabilities	10,455	10,304
Total liabilities	498,274	559,179
Total policyholders' surplus	186,463	174,359
Total liabilities and policyholders' surplus	$684,737	$733,538

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Assets

Total assets decreased by $48.8 million in 2019 compared to 2018 primarily due to:

The decrease in bonds of $5.9 million in 2019 compared to 2018 is due to the use of proceeds from bond maturities and calls to purchase short-term bonds, cash equivalent bonds, and money market funds.

Cash, cash equivalents and short-term investments increased $18.0 million in 2019 compared to 2018 primarily due to a $15.7 million decrease in class action claim payments.

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 $51.2 million is due to a bond principal payment made in 2019 of $47.6 million and a $3.6 million cash draw down to partially cover the class action suit claim payment paid in 2019.

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 2019, excess emergency assessments decreased $9.6 million compared to 2018 primarily due to $67.6 million in emergency assessment income offset by $56.3 million in debt service costs.

Liabilities

Total liabilities decreased $60.9 million in 2019 compared to 2018 primarily due to:

Unpaid losses and LAE decreased $3.0 million in 2019. The decrease is primarily due to a settlement payment for the Oubre class action suit. IBNR reserves decreased $2.9 million primarily due to a payment made for class action suits. 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 a peer review 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 $57.5 million in 2019 compared to 2018 primarily due to the $47.6 million bond principal payment made in 2019 and $9.7 million reduction in unamortized bond premium.

The decrease of $2.2 million in unearned premiums is primarily from LCPIC's depopulation program.

Policyholders' Surplus

The increase in total policyholders' surplus of $12.1 million in 2019 compared to 2018 primarily due to a change in net income of $9.8 million. In addition to net income, $1.9 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.

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Results of Operations

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

Statement of Income and Ratios (000)	2019	2018
Premiums earned	$39,507	$43,225
Losses incurred	12,759	9,281
LAE incurred	6,324	5,793
Underwriting expenses	14,240	14,470
Underwriting gain (loss)	6,184	13,681
Net investment loss	(4,807)	(6,453)
Other Income	8,433	9,875
Net income	$9,810	$17,103
Loss Ratio	32.3%	21.5%
LAE Ratio	16.0%	13.4%
Underwriting expense ratio	38.2%	35.5%
Combined ratio	86.5%	70.4%

Net income in 2019 was $7.3 million less than 2018 due to:

Premiums earned decreased $3.7 million in 2019 compared to 2018 due to the following:

The multiple year effect of policies taken out from depopulation on the direct premiums earned.	($13.8)
The decrease in depopulation premiums earned due to the multiple year decreased in policies taken out.	8.3
The decrease in ceded premiums earned due to reinsurance cost savings in 2019 as compared to 2018. This cost savings is the annual savings booked from January through December as opposed to the program savings stated in the bullet on Page 350 which reflects the program costs period from June to May.	1.8
Net decrease in premiums earned	($3.7)

Losses and LAE incurred was $19.1 million in 2018 compared to $15.1 million in 2018 for a net change of $4.0 million that was primarily due to $2.7 million related to Hurricane Barry and 1.2 million related to the Oubre class action suit.

Combined ratio – the combined ratio in 2019 was 86.5% compared to 70.4% in 2018 primarily due to the decrease in premiums earned and increase in losses and LAE 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 losses and expenses paid, cost of investments acquired, and debt service costs.

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The cash flows of LCPIC are summarized as follows:

Cash Flow Statement (000)	2019	2018
Operations		
Premiums collected	$38,174	$43,509
Net investment income received (paid)	(2,231)	(3,956)
Miscellaneous income	8,433	9,875
Losses paid	(16,325)	(30,091)
Expenses paid	(19,698)	(20,743)
Net cash from operations	$8,353	($1,406)
Investment Activities		
Proceeds from investments sold, matured or repaid	$16,064	$5,435
Cost of long-term investments acquired	(12,671)	(10,545)
Net cash from investments	3,393	(5,110)
Financing Activities		
Other cash provided (applied)	6,297	(4,502)
Net cash from financing activities and miscellaneous sources	6,297	(4,502)
Change in Cash and Short-Term Investments		
Net change in cash, cash equivalents and short-term investments	$18,043	($11,018)

Cash, cash equivalents, and short-term investments increased $18.0 million in 2019 compared to 2018 due to:

Net cash from operations was $8.4 million in 2019 compared to ($1.4) million in 2018 for a net change of $9.8 million was due to the following:

Description (in millions)	Cash Provided (Cash Applied)
Change in premiums collected is related to LCPIC'S depopulation efforts	(5.3)
Change in net investment income received is related to an increase in bond interest and lower debt service costs in 2019 compared to 2018.	1.7
Change in miscellaneous income is primarily due to a decrease in assessment income required to offset debt service costs.	(1.4)
Losses and expenses paid increased primarily due to following:	
- Class action suit settlements ($5.6 million paid in 2019 versus $21.3 paid in 2018)	15.7
- Loss and LAE paid for Hurricane Barry claims	(2.7)
- All other cash movements related to expenses paid	1.8
Net cash provided from items listed above impacting cash from operations	$9.8

Net cash from investments in 2019 was $3.4 million compared to ($5.1) million in 2018. The $8.5 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)
Increase in net cash related to LCPIC's bonds that matured during 2018.	10.6
Decrease in net cash related to LCPIC's growth in bonds purchased from 2018 to 2019.	(2.1)
Net cash applied from items listed above impacting cash from investments	8.5

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Cash provided from financing activities and miscellaneous sources increased $10.8 million in 2019 compared to 2018. Explanations of the change are displayed below:

Description (in millions)	Cash Provided (Cash Applied)
Change in borrowed money is primarily due to additional bond principal paid of $3.2 million in 2019 compared to 2018, offset by the decrease in amortization of bond premium in 2019 of $1.3 million compared to 2018.	(1.9)
Change in accrued liability for takeout premium due to the increase in policies included in LCPIC's take out program, 94 policies in 2019 as compared to 32 policies in 2018.	7.2
Change in accrued liability for pending escheatment payable due to a multiple year decline in outstanding checks that are greater than 6 months after the issue date.	1.0
Change in receivable for long-term emergency assessments – 2005 deficit is primarily due to $3.2 million in additional bond principal paid and $3.6 million cash draw down to partially cover the class action suit claim payment paid in 2019.	6.8
Change in current emergency assessments receivable - companies is due to a decline in state insurance industry written premium in 2018 used to calculate the receivable.	(1.0)
Change in receivable for excess emergency assessments collected over debt service primarily due to the bond premium received from the 2016 bond refinancing.	(1.0)
All other cash movements related to financing activities and miscellaneous sources	(.3)
Net change	$10.8

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 $253 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 2019, LCPIC secured a $50.0 million line of credit with Regions Bank that matures in June 2021. 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 approximately 80,000 claims resulting from Hurricanes Katrina and Rita. In 2006, LCPIC issued $978.2 million of fixed rate assessment revenue bonds. On December 31, 2019, LCPIC had approximately $374.1 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.

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Pending Litigation

As of December 31, 2019 there were 55 open litigation matters against LCPIC. The majority of these lawsuits are first-party suits related to first party losses, third-party bodily injury claims, subrogation or claims where the issue of coverage is in dispute. Unpaid loss and loss adjustment expenses are included on the balance sheet of approximately $6.4 million, excluding the Oubre class action suit described below. The balance of the litigated matters are first-party suits related to Hurricanes Katrina and Isaac.

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 $136.7 million towards the final settlement as of December 31, 2019 and has a reserve of $9.4 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 $610 million in total reinsurance and cat bonds in place for the 2019 storm season which provided 1 in 303 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, 2020. LCPIC is in the process of negotiating a new reinsurance program for the 2020 storm season and it is anticipated to provide 1 in 300 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.