# 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 2020 Annual Statement.

Major events occurring in 2021 for LCPIC were:

- LCPIC renewed its reinsurance program in May 2021 with storm coverage of $545 million and retention of $35.0 million that includes a traditional reinsurance program and two cat bonds for an increase in cost of approximately $4.8 million for the 2021 through 2022 program period as compared to 2020 through 2021 program period. The 2021 – 2022 program provides for a 1 in 302 year storm coverage compared to a 1 in 303 year storm coverage for the 2020 – 2021 program.
- In 2021, LCPIC incurred losses from eight weather events where one hurricane, Hurricane Ida, resulted the majority of the incurred losses. The claims resulting from six of these weather events met coverage requirements under LCPIC's traditional reinsurance program.

## *Financial Position*

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

| **Balance Sheet (in thousands of dollars - 000)** | **2021** | **2020** |
|---|---|---|
| **Assets** | | |
| Bonds | $66,570 | $77,422 |
| Cash, cash equivalents and short-term investments | 206,278 | 156,685 |
| Total cash and invested assets | 272,848 | 234,107 |
| | | |
| Uncollected and deferred premiums | 12,052 | 7,086 |
| Reinsurance balances | 3,092 | 13,959 |
| Long-term emergency assessments receivable | 285,020 | 336,499 |
| Other assets | 16,137 | 14,812 |
| Total assets | $589,149 | $606,463 |
| **Liabilities and Policyholders' Surplus** | | |
| Unpaid loss and loss adjustment expenses | $9,775 | $11,174 |
| Borrowed money | 288,264 | 346,805 |
| Unearned premiums | 41,967 | 29,309 |
| Funds held by company under reinsurance treaties | 36,970 | 249 |
| Restricted assessments | 64,086 | 45,455 |
| Other liabilities | 13,460 | 11,533 |
| Total liabilities | 454,522 | 444,525 |
| Total policyholders' surplus | 134,627 | 161,938 |
| Total liabilities and policyholders' surplus | $589,149 | $606,463 |

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## Assets

Total assets decreased by $17.3 million in 2021 compared to 2020 primarily due to:

Bonds decreased $10.9 million in 2021 compared to 2020 primarily due to LCPIC temporarily suspending reinvestment of bond proceeds to partially offset claims paid due to Hurricane Ida.

Cash, cash equivalents and short-term investments increased $49.6 million in 2021 compared to 2020 primarily due to $74.2 million in reinsurance recoveries collected in advance in excess of net loss and loss adjustment expense payments due to Hurricane Ida. Offsetting the increase in cash was an increase of $10.3 million in claims management expenses, a decrease of $8 million in cash transferred from cash equivalents, and a $4.8 million increase in annual reinsurance expenses.

Uncollected and deferred premiums increased $5.0 million in 2021 compared to 2020 primarily due to an increase in policies issued during the fourth quarter.

Reinsurance balances decreased $10.9 million in 2021 as compared to 2020 primarily due to significantly greater collections from reinsurers for Hurricane Ida reinsurance recoverables as compared to uncollected reinsurance recoverables billed during the fourth quarter of 2020 for Hurricanes Laura, Delta, and Zeta.

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 $51.5 million is due to a bond principal payment made in 2021.

## Liabilities

Total liabilities decreased $10.0 million in 2021 compared to 2020 primarily due to:

Borrowed money decreased $58.5 million in 2021 compared to 2020 primarily due to the $51.5 million bond principal payment made in 2021 and $6.8 million reduction in unamortized bond premium.

Unearned premiums increased $12.7 million in 2021 compared to 2020 primarily due to the $16.7 million increase in direct written premiums.

Funds held by company under reinsurance treaties increased $36.7 million as compared to 2020 due to funds received from reinsurers to cover ceded incurred losses resulting from Hurricane Ida.

Restricted assessments of $64.1 million reflects assessment revenues held by the Bond Trustee for repayment of borrowed money. Restricted assessments includes excess emergency assessments collected over debt service. Restricted assessments increased $18.6 million in 2021 compared to 2020 primarily due to the $16.9 million increase in excess emergency assessments collected over debt service.

## Policyholders' Surplus

The decrease in total policyholders' surplus of $27.3 million in 2021 compared to 2020 primarily due to a net loss of $28.3 million.

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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) | 2021 | 2020 |
|---|---|---|
| Premiums earned | $35,382 | $36,166 |
| Losses incurred | 44,526 | 42,695 |
| LAE incurred | 5,816 | 6,667 |
| Underwriting expenses | 14,664 | 13,527 |
| Underwriting gain (loss) | (29,624) | (26,723) |
| Net investment loss | (6,093) | (6,034) |
| Other Income | 7,381 | 8,125 |
| Net income | ($28,336) | ($24,632) |
| Loss Ratio | 125.8% | 118.1% |
| LAE Ratio | 16.4% | 18.4% |
| Underwriting expense ratio | 30.5% | 38.6% |
| Combined ratio | 172.7% | 175.1% |

LCPIC experienced back-to-back years involving significant Hurricane catastrophes in 2021 and 2020. Also, until the fourth quarter of 2021, the amount of direct written premiums were recorded on a consistent basis in 2021 as compared to 2020. As a result, similar net income results occurred for premiums earned, losses incurred, and LAE incurred after ceded reinsurance. Net income in 2021 was $3.7 million less than 2020.

Premiums earned decreased $784 thousand in 2021 compared to 2020 due to the increase in unearned premiums resulting from an increase in policies written during the fourth quarter as mentioned above.

Losses and LAE incurred was $908 thousand greater in 2021 as compared to 2020. LCPIC's net retained losses of $35 million was the same for both 2021 and 2020, and coupled with similar loss experience resulting from non-catastrophe related losses, the net incurred results reflected above is similar. On a direct basis, $492.6 million was incurred in 2021 for catastrophe claims as compared to $98.7 million incurred in 2020.

Underwriting expenses increased $1.1 million in 2021 as compared to 2020 primarily due to agents' commissions that correspond to the increase in policies written during the fourth quarter.

Combined ratio – the combined ratio in 2021 was 172.7% compared to 175.1% in 2020 primarily due to the decrease in underwriting expenses 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) | 2021 | 2020 |
|---|---|---|
| **Operations** | | |
| Premiums collected | $42,662 | $34,192 |
| Net investment income received (paid) | (3,225) | (3,751) |
| Miscellaneous income | 7,381 | 8,125 |
| Losses paid | (34,757) | (60,691) |
| Expenses paid | (19,987) | (20,384) |
| Net cash from operations | ($7,926) | ($42,509) |
| **Investment Activities** | | |
| Proceeds from investments sold, matured or repaid | $28,565 | $51,710 |
| Cost of long-term investments acquired | (20,450) | (53,390) |
| Net cash from investments | 8,115 | (1,680) |
| **Financing Activities** | | |
| Other cash provided (applied) | 49,405 | 7,796 |
| Net cash from financing activities and miscellaneous sources | 49,405 | 7,796 |
| **Change in Cash and Short-Term Investments** | | |
| Net change in cash, cash equivalents and short-term investments | $49,594 | ($36,393) |

Cash, cash equivalents, and short-term investments increased $86.0 million in 2021 compared to 2020 due to:

Net cash from operations was ($7.9) million in 2021 compared to ($42.5) million in 2020 for a net change of $34.6 million was due to the following:

| Description (in millions) | Cash Provided (Cash Applied) |
|---|---|
| Change in premiums collected is related to an increase in policies in force, 41,157 in 2021 as compared to 35,670 in 2020. | 8.5 |
| Change in net investment income received is related to a $.8 million decrease in bond interest and offset by a $1.1 million decrease in debt service costs in 2021 compared to 2020. | .3 |
| Losses and expenses paid increased primarily due to following: | |
| - Increase in amounts recoverable from reinsurers in 2020 for 2020 Hurricanes Laura, Delta, and Zeta claims | 13.5 |
| - Decrease in amounts recoverable from reinsurers in 2021 for 2021 Hurricane Ida and 2020 Hurricanes Laura, Delta, and Zeta claims | 10.9 |
| All other cash movements related to miscellaneous income and expenses paid | 1.4 |
| Net cash applied from items listed above impacting cash from operations | $34.6 |

Net cash from investments in 2021 was $8.1 million compared to ($1.7) million in 2020. The $9.8 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 bonds that matured during 2021. | (23.1) |
| Decrease in net cash related to LCPIC's growth in bonds purchased from 2020 to 2021. | 32.9 |
| Net cash applied from items listed above impacting cash from investments | 9.8 |

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Cash provided from financing activities and miscellaneous sources increased $41.6 million in 2021 compared to 2020. Explanations of the change are displayed below:

| Description (in millions) | Cash Provided (Cash Applied) |
|---|---|
| Change in funds held by company under reinsurance treaties is primarily due to funds provided to offset incurred losses stemming from Hurricane Ida. | 36.5 |
| Change in restricted assessments is primarily due to an increase of $18.6 million in excess emergency assessments collected over debt service in 2021 compared to an increase of $9.4 million in excess emergency assessments collected over debt service in 2020. | 9.2 |
| Change in receivable for excess emergency assessments collected over debt service in 2020 primarily due to the bond premium received from the 2016 bond refinancing. | (4.5) |
| Net change | $41.2 |

## 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 $275 million on the state insurance industry derived from 10% of their written premium for deficits each year, and an emergency assessment up to approximately $281 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 2021, LCPIC secured a $50.0 million line of credit with Regions Bank that matures in June 2023. 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, 2021, LCPIC had approximately $272.6 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, 2021 there were 246 open litigation matters against LCPIC. The majority of these lawsuits are related to first-party suits related to 2020 Hurricanes Laura and Delta. Unpaid loss and loss adjustment expenses are included on the balance sheet of approximately $7.0 million, excluding the Oubre class action suit described below. The balance of the litigated matters are 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 $145.5 million towards the final settlement as of December 31, 2020 and has a reserve of $3.7 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 $545 million in total reinsurance and cat bonds in place for the 2021 storm season which provided 1 in 303 year storm coverage. The cat bonds includes one $100.0 million three year catastrophe bond and one $125.0 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, 2022. LCPIC is in the process of negotiating a new reinsurance program for the 2022 storm season and it is anticipated to provide at least a 1 in 200 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.