

January/February

2014

# Interim Report Card



**John W. Polak, CPCU**  
**General Manager**

**March 31, 2014**

March 31, 2014

To: Georgia R. Neblett, Chairman  
Richard Clifton Craig, Vice-Chairman  
Michael Gerik, Secretary/Treasurer  
Steven Lawrence Elbert  
William David Franklin, Sr.  
Lyndell Haigood  
Ron Lawson  
Michael O'Malley  
Eugene "Gene" Seaman  
Edward James Sherlock

**Re: *Bi-monthly Interim Report - Section 2210.107(b)***

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House Bill 3 became effective on September 28, 2011, and pursuant to Tex. Ins. Code, Section 2210.107(b), please find the bi-monthly interim report ("Interim Report Card") evaluating the extent to which the Texas Windstorm Insurance Association ("TWIA" or "Association") has met the objectives described by Section 2210.107(a), Texas Insurance Code for the two-month period preceding the date of the report (January and February 2014).

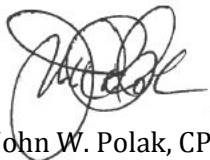
These interim report cards will be provided every 60 days as required by statute and will culminate in an Annual Report Card issued each June.

The initial report cards established the standards of performance for the Association to be reported against in subsequent report cards. Additional standards have been and will continue to be added as appropriate and as approved by the board of directors. Each interim report card serves as a snapshot in time of Association compliance with the standards with respect to each of the objectives.

The Association believes it is in full material compliance with all current standards of performance outlined in each of the following sections. This is the thirteenth interim report card to be issued by TWIA since the enactment of House Bill 3.

Should you have any questions, please feel free to contact me at (512) 899-4949.

Sincerely,



John W. Polak, CPCU  
General Manager

# Table of Contents

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|  |    |
|--|----|
| About This Report.....                           | 4  |
| Introduction.....                                | 5  |
| Standards of Conduct.....                        | 7  |
| State Auditor’s Office Examination .....         | 9  |
| Financial Statement.....                         | 9  |
| Board Composition.....                           | 11 |
| Open Meetings Act .....                          | 12 |
| Primary Board Objectives Reports .....           | 13 |
| Public Information Act.....                      | 13 |
| Issuance of Policies.....                        | 14 |
| Compliance with Building Codes.....              | 15 |
| Catastrophe Funding.....                         | 16 |
| Catastrophe Plan.....                            | 18 |
| Limits of Liability.....                         | 20 |
| Certain Appeals and Other Actions.....           | 20 |
| Compliance with the Plan of Operation.....       | 22 |
| Annual Evaluation of Association Management..... | 23 |

## About This Report

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In 2011, the 82nd Texas Legislature, 1st Called Special Session, passed House Bill 3 (“HB3”), modifying various aspects of the operations of the Texas Windstorm Insurance Association (“TWIA”). Amendments to Tex. Ins. Code, Section 2210.107 directed TWIA to report bi-monthly to the TWIA Board of Directors and report annually (“Report Card”) to the Commissioner, the Legislative Oversight Board, the Governor, the Lieutenant Governor, and the Speaker of the House of Representatives to the extent that TWIA met the objectives in Section 2210.107(a).

The primary objectives of the Board of Directors are to ensure that the Board and TWIA:

- (1) Operate in accordance with this chapter, the plan of operation, and commissioner rules;
- (2) Comply with sound insurance principles;
- (3) Meet all standards imposed under this chapter;
- (4) Establish a code of conduct and performance standards for Association employees and persons with which the Association contracts; and
- (5) Establish, and adhere to terms of, an annual evaluation of Association management necessary to achieve the statutory purpose, Board objectives, and any performance or enterprise risk management objectives established by the Board.

This Report Card has been developed to satisfy these reporting requirements and illustrates the measures and improvements taken to meet the objectives. The Report Card presents this information by referencing applicable sections of the TWIA governing statute in order of appearance.

## Introduction

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In 2008, the combination of Hurricanes Dolly and Ike resulted in over 100,000 claims and an estimated \$3 billion in losses. Concerns over claims handling led to TWIA being placed under Administrative Oversight by TDI and the passage of HB3 in 2011.

HB3 required numerous changes to TWIA operations. Among the improvements are new residential and commercial policy forms, more transparency via additional information on the TWIA website and live broadcasts of TWIA meetings, the funding of an ombudsman program, and the implementation of new claims handling procedures.

A new management team is now in place with a broader range of experience and a focus on accountability. In 2008, there were four members of senior management whose only insurance carrier experience was with TWIA, which was a very small company for most of their tenure. Today, not only does TWIA have significantly greater insurance carrier experience within its senior management ranks, but a greater portion of that experience is with larger carriers outside of TWIA. This bodes well for the future of the Association as it has not only greater depth of experience but a far greater breadth of experience in terms of skills and sophistication.

TWIA has undergone more than ten audits and examinations in recent years with varying areas of concentration, including four examinations by the Texas Department of Insurance (TDI), one of which is currently underway; two by Deloitte & Touche, LLP; and audits performed by Robert E. Nolan, KPMG, the State Auditor's Office, and Alvarez & Marsal. The Association has diligently developed and implemented corrective measures and created action plans to track and report the Association's progress in addressing the recommendations of each review.

TWIA has addressed 100% of the non-IT related recommendations outlined in the completed TDI audits, the Nolan report, the Deloitte audit, the Operations Improvement Plan, and the State Auditor's Office report. The KPMG audit of IT controls outlined 11 areas of primary concern due to faults of existing controls or potential vulnerabilities. The Association has completed 100% of the corrective actions for these areas. Only one IT related recommendation in the SAO report is pending at this time and completion is scheduled concurrently with implementation of the new Policy Center in 2014.

Current leadership is committed to fostering a culture of continuous improvement. TWIA has and continues to identify areas of improvement outside of audit observations to enhance processes and procedures and ensure the Association is in compliance with applicable statutes, regulatory guidelines, and industry best-practices. The new

management team has successfully implemented initiatives to address legislative changes, improve operational efficiency, create cultural transformation within the Association, and increase management controls and accountability. TWIA now has extensive controls and detailed financial and operational metrics in place to measure and evaluate the performance of every level of the Association, from the organization as a whole to individual departments and each individual employee. There are documented procedures and practices in place in all operational areas, and TWIA has greatly increased the level of transparency and communication between all levels of the Association and with outside stakeholders. The management team has begun a process of continuously refocusing the culture from task-based behavior to outcome-focused accountability.

The TWIA Claims Department has experienced the most significant improvements. The new claims management team has developed a detailed catastrophe plan; improved communications with policyholders, adjusters, and agents; and ensured faster and more accurate claims handling using more modern technology and quality control measures. These changes have resulted in a measurable improvement in customer service. TWIA Claims has implemented an ongoing customer survey program with very positive results. Additionally, Claims has implemented a number of key performance metrics to provide an objective measure of the claims handling process, including:

- average number of days from receipt of claim to inspection,
- average number of days from inspection to receipt of report by TWIA, and
- average number of days from receipt of report to payment.

In addition, TWIA-controllable expenses were at or below budget from 2011-2013. TWIA expenses compare favorably both to the insurance industry as a whole and to other state residual market plans. TWIA is the second largest property insurance plan in the U.S., yet still maintains the second lowest cost per policy among the 37 property insurance plans in the U.S.

The initiatives management has implemented are indicative of a culture of continuous improvement and have better positioned TWIA to fulfill its mission of efficiently providing essential property insurance products and services for eligible Texas policyholders when no one else will. The State Auditor's Office final report confirms that TWIA has improved its claims processing and has implemented controls to produce accurate financial statements, ensure accountability of Association funds, and adequately support and authorize non-claims-related expenditures.

Most recently, the Texas Department of Insurance amended the terms of Administrative Oversight citing TWIA's operational improvements as a factor in TDI's decision to revise the conditions of Oversight.

## Standards of Conduct

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### **Ethics & Conflicts of Interest Policy**

TWIA developed and implemented a comprehensive Ethics & Conflict of Interest Policy (“Ethics Policy”) in February 2011. The policy was subsequently revised in September 2011 and April 2012, to incorporate changes mandated by House Bill 3 and to further describe prohibited employment relationships. All new employees, onsite contractors and board members are required to review the policy upon employment or appointment, sign the Ethics Certification, and complete the Required Relationship Disclosure Form listing any known potential conflicts of interest. The Ethics Policy is reviewed annually by all employees, onsite contractors and board members recertifying their commitment to ethical conduct and avoidance of the appearance of impropriety. Required relationship disclosures are required at the time of employment and are updated if new potential conflicts arise.

The majority of disclosed relationships that may give rise to a conflict occur in the Claims department, where contract claims examiners may have previous experience at an adjusting firm (or firms) with which TWIA/TFPA contracts. The Claims Department implemented monitoring and reporting processes to ensure that examiners do not work claims assigned to field adjusting firms where the examiner was formerly employed. Claims Quality Assurance further conducts quarterly audits of this issue by selecting a random sample of files to compare an examiner’s assignments to his or her disclosure form.

To ensure understanding and compliance with the policy, the Compliance Department, in conjunction with Human Resources, has developed a formal Ethics training class as part of a more robust and comprehensive orientation training for all employees, called TWIA 101. Annual training is scheduled for March of 2014 for all existing employees and will continue quarterly for new hires.

TWIA continues to monitor employees for compliance with the code of conduct. The Compliance Department has consolidated the tracking mechanisms for the annual ethics certification, required relationship and gift disclosures, and other required compliance training for all employees and contractors into a comprehensive database.

### **Fraud Reporting**

Section 2210.012 also mandates that “a board member or employee of the association who reasonably suspects that a fraudulent insurance act has been or is about to be committed by any board member or employee of the association shall, not later than the 30th day after discovering the conduct, report the conduct and identity of the person engaging in the conduct to the department and may report the conduct and the identity of the person engaging in the conduct to another authorized governmental agency. The department shall

forward a report received under this subsection to the authorized governmental agency in accordance with Chapter 701.”

To facilitate employee understanding and compliance with this Insurance Code provision and the Association’s Fraud Reporting policy, TWIA 101, scheduled for March 2014, will include a fraud reporting module.

Additionally, TWIA has implemented the initiatives described below to ensure compliance with applicable Insurance Code provisions.

### **Special Investigations Unit (SIU)/Fraud Abatement**

TWIA Claims continues to work closely with the SIU vendor, Veracity Research, to refine referral requirements, training programs, SIU reporting, and fraud abatement processes.

The following chart illustrates a sharp increase in fraud investigations and reports between 2010 and 2012, evidencing TWIA’s increased focus and responsibility on fraud abatement and reporting. With the utilization of Veracity Research, reporting levels moderated in 2012, reflecting a more sophisticated assessment by the vendor of the “reasonable suspicion of fraud” standard. In February, the Claims Department observed a higher than normal SIU referral rate driven by late reported claims, which appears to be driving a corresponding increase in referrals to the Department as well.

| Reports filed:  | 12/31/10 | 12/31/11 | 12/31/12 | 12/31/13 | 1/31/14 | 2/28/14 |
|-----------------|----------|----------|----------|----------|---------|---------|
| TDI Fraud       | 6        | 32       | 35       | 15       | 2       | 8       |
| TDI Enforcement | 5        | 7        | 24       | 9        | 0       | 0       |

TWIA is currently in the process of expanding the SIU and fraud abatement program to the Association’s underwriting functions as well.

To ensure TWIA stays abreast of current trends and information regarding insurance fraud, key personnel attend the Texas Department of Insurance Annual Fraud Conference. Additionally, key personnel with TWIA and TDI’s Fraud and Enforcement Units meet quarterly to discuss ongoing cases, trends, and issues. TWIA personnel will also be attending the April meeting of the Texas Committee on Insurance Fraud.

### **Whistleblower Policy**

As part of TWIA’s comprehensive Ethics Policy and commitment to creating a culture where unethical behavior is reported and properly addressed, TWIA created an anonymous Whistleblower Policy in February 2011. TWIA contracts with a third-party vendor to provide anonymous hotline reporting of fraud or ethics violations. Monthly reports are transmitted by the vendor to the Association’s General Counsel, Compliance Director, and General Manager. To date, we have received no Fraud or Compliance & Ethics



Reports.

## State Auditor's Office Examination

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Section 2210.058 states “the association is subject to audit by the state auditor and shall pay the costs incurred by the state auditor in performing an audit under this section.”

The State Auditor's Office (SAO) concluded in their August 1, 2012 final report that “the Texas Windstorm Insurance Association (Association) has improved its processing of claims. The Association also has controls to help produce accurate financial information, ensure accountability for Association funds, and adequately support and authorize non-claims-related expenditures.”

The action items resulting from the SAO audit are 100% complete with the exception of one remaining IT-related finding scheduled for completion concurrently with implementation of TWIA's new Policy Center in 2014.

Additionally, TWIA was required to submit status reports to the State Auditor's Office. TWIA has submitted all reports requested by the SAO, including the status of the IT implementation due by 11/30/2012, 5/31/2013, and 11/30/2013; as well as the status of the Association-wide implementation plan on 2/1/2013.

## Financial Statement

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Section 2210.054 requires TWIA to file annually with the Department and the State Auditor's Office a financial statement summarizing the transactions, conditions, operations, and affairs of the Association during the preceding year.

In addition to complying with the Annual Statement requirements, TWIA also submits monthly statements to the Texas Department of Insurance and the Board of Directors. The following charts illustrate TWIA's most recent balance sheet and statutory income statement. The statutory balance sheet shows the financial position of TWIA at February 28, 2014 compared to February 28, 2013. The statutory income statement shows a comparison between YTD actual and budgeted revenues and expenses.

| <b>TEXAS WINDSTORM INSURANCE ASSOCIATION</b>      |  |                      |                        |                       |
|---|--|----------------------|------------------------|-----------------------|
| <b>Statutory Income Statement (000's omitted)</b> |  |                      |                        |                       |
|   | <b>for the two months ended February 28,</b> |                      |                        |                       |
|   | <b>Actuals - 2014</b>                        | <b>Budget - 2014</b> | <b>Variance - 2014</b> | <b>Actuals - 2013</b> |
| <b>Premiums Written:</b>                          |  |                      |                        |                       |
| Direct  | \$ 58,606                                    | \$ 61,138            | \$ (2,532)             | \$ 57,651             |
| Ceded   | 0  | 0                    | 0                      | 0                     |
| Net   | 58,606                                       | 61,138               | (2,532)                | 57,651                |
| <b>Premiums Earned:</b>                           |  |                      |                        |                       |
| Direct  | \$ 76,165                                    | \$ 76,717            | \$ (552)               | \$ 71,341             |
| Ceded   | 0  | 0                    | 0                      | (18,068)              |
| Net   | 76,165                                       | 76,717               | (552)                  | 53,274                |
| <b>Deductions:</b>                                |  |                      |                        |                       |
| Direct Losses and LAE Incurred                    | 7,617  | 7,672                | (55)                   | 17,122                |
| Direct Losses and LAE Incurred - Ike & Dolly      | 0  | 0                    | 0                      | 0                     |
| Ceded Losses and LAE Incurred                     | 0  | 0                    | 0                      | 0                     |
| Operating Expenses                                | 4,485  | 5,338                | (852)                  | 4,335                 |
| Commission Expense                                | 9,391  | 9,782                | (391)                  | 9,248                 |
| Ceding commissions / brokerage                    | 0  | 0                    | 0                      | 0                     |
| Premium / Maintenance Tax                         | 1,167  | 1,186                | (19)                   | 1,109                 |
| Total Deductions                                  | 22,660                                       | 23,978               | (1,318)                | 31,814                |
| <b>Net Underwriting Gain or (Loss)</b>            | <b>53,505</b>                                | <b>52,739</b>        | <b>766</b>             | <b>21,460</b>         |
| <b>Other Income or (Expense):</b>                 |  |                      |                        |                       |
| Gross Investment Income                           | 177  | 178                  | (1)                    | 212                   |
| Interest Expense on Debt                          | 0  | 0                    | 0                      | 0                     |
| Debt Issuance & Other Investment Expenses         | (25)   | (25)                 | 0                      | (6)                   |
| Sales Tax Refund and Other Income (Expense)       | 1,878  | 0                    | 1,878                  | 6                     |
| Total Other Income or (Expense)                   | 2,030  | 153                  | 1,877                  | 213                   |
| <b>Net Income (Loss)</b>                          | <b>\$ 55,536</b>                             | <b>\$ 52,892</b>     | <b>\$ 2,643</b>        | <b>\$ 21,673</b>      |
| <b>Surplus (Deficit) Account:</b>                 |  |                      |                        |                       |
| Beginning Surplus (Deficit)                       | 0  | 0                    | 0                      | (182,979)             |
| Net Income (Loss)                                 | 55,536                                       | 52,892               | 2,643                  | 21,673                |
| Change in Provision for Reinsurance               | 0  | 0                    | 0                      | 0                     |
| Change in nonadmitted assets & deferred taxes     | (1,237)                                      | 0                    | (1,237)                | (1,123)               |
| Other   | 0  | 0                    | 0                      | 0                     |
| Statutory Fund Cost                               | (54,299)                                     | (52,892)             | (1,406)                | 0                     |
| Ending Surplus (Deficit)                          | <b>\$ (0)</b>                                | <b>\$ 0</b>          | <b>\$ (0)</b>          | <b>\$ (162,429)</b>   |
| <b>Key Operating Ratios:</b>                      |  |                      |                        |                       |
| Direct:   |  |                      |                        |                       |
| Loss & LAE Ratio                                  | 10.0%  | 10.0%                | 0.0%                   | 24.0%                 |
| UW Expense Ratio:                                 |  |                      |                        |                       |
| Acquisition                                       | 18.0%  | 17.9%                | 0.1%                   | 18.0%                 |
| Non Acquisition                                   | 5.9%   | 7.0%                 | -1.1%                  | 6.1%                  |
| UW Expense Ratio                                  | 23.9%  | 24.9%                | -1.0%                  | 24.0%                 |
| Combined Ratio                                    | 33.9%  | 34.9%                | -1.0%                  | 48.0%                 |
| Net:  |  |                      |                        |                       |
| Loss & LAE Ratio                                  | 10.0%  | 10.0%                | 0.0%                   | 32.1%                 |
| UW Expense Ratio:                                 |  |                      |                        |                       |
| Acquisition                                       | 18.0%  | 17.9%                | 0.1%                   | 21.8%                 |
| Non Acquisition                                   | 5.9%   | 7.0%                 | -1.1%                  | 8.1%                  |
| UW Expense Ratio                                  | 23.9%  | 24.9%                | -0.9%                  | 29.9%                 |
| Combined Ratio                                    | 33.9%  | 34.9%                | -0.9%                  | 62.0%                 |

| <b>TEXAS WINDSTORM INSURANCE ASSOCIATION</b>      |                    |                    |
|---|--------------------|--------------------|
| <b>Statutory Balance Sheet (000's omitted)</b>    |                    |                    |
|   | <b>February-14</b> | <b>December-13</b> |
| <b>Admitted Assets</b>                            |                    |                    |
| Cash and short term investments                   | \$ 487,216         | \$ 439,193         |
| Premiums receivable & other                       | 1,086              | 1,039              |
| Amounts recoverable from reinsurers               | -                  | -                  |
| <b>Total admitted assets</b>                      | <b>\$ 488,301</b>  | <b>\$ 440,231</b>  |
| <b>Liabilities, Surplus and other funds</b>       |                    |                    |
| <b>Liabilities:</b>                               |                    |                    |
| Loss and Loss adjustment expenses                 | \$ 136,002         | \$ 132,959         |
| Underwriting expenses payable                     | 11,435             | 10,366             |
| Unearned premiums, net of ceded unearned premiums | 217,181            | 234,739            |
| Ceded reinsurance premiums payable                | 24,745             | 24,745             |
| Principal & Interest Payable - Debt               | -                  | -                  |
| Provision for reinsurance                         | -                  | -                  |
| Other payables                                    | 21,810             | 14,592             |
| Statutory fund payable                            | 77,129             | 22,830             |
| <b>Total liabilities</b>                          | <b>488,301</b>     | <b>440,231</b>     |
| <b>Surplus and others funds</b>                   |                    |                    |
| Unassigned surplus (deficit)                      | -                  | -                  |
| <b>Total liabilities, surplus and other funds</b> | <b>\$ 488,301</b>  | <b>\$ 440,231</b>  |
| <b>Balance in CRTF</b>                            | <b>\$ 187,050</b>  | <b>\$ 186,183</b>  |

| <b>TEXAS WINDSTORM INSURANCE ASSOCIATION</b>               |  |                      |                        |
|--|--|----------------------|------------------------|
| <b>Statement of Cash Flows (000's omitted)</b>             |  |                      |                        |
|  | <b>for the two months ended February 28,</b> |                      |                        |
|  | <b>Actuals - 2014</b>                        | <b>Budget - 2014</b> | <b>Variance - 2014</b> |
| <b>Cash flows from operating activities:</b>               |  |                      |                        |
| Premiums collected, net of reinsurance                     | \$ 65,823                                    | \$ 64,757            | \$ 1,066               |
| Losses and loss adjustment expense paid (1)                | (4,574)                                      | (31,795)             | 27,221                 |
| Underwriting expenses paid                                 | (15,141)                                     | (14,728)             | (414)                  |
| Other  | 1,878  | -                    | 1,878                  |
| Net cash provided by operating activities                  | 47,987                                       | 18,234               | 29,752                 |
| <b>Cash flows from nonoperating activities:</b>            |  |                      |                        |
| Statutory fund paid  | -  | -                    | -                      |
| Other  | (59)   | -                    | (59)                   |
| Net cash provided by nonoperating activities               | (59)   | -                    | (59)                   |
| <b>Cash flows from investing activities:</b>               |  |                      |                        |
| Sales and maturities of investments                        | -  | -                    | -                      |
| Net investment income                                      | 95   | 178                  | (83)                   |
| Net cash provided by investing activities                  | 95   | 178                  | (83)                   |
| <b>Cash flows from financing activities:</b>               |  |                      |                        |
| Borrowed funds   | -  | (25)                 | 25                     |
| Borrowed funds repaid                                      | -  | -                    | -                      |
| Net cash provided by financing activities                  | -  | (25)                 | 25                     |
| Net increase (decrease) in cash and short-term investments | 48,023                                       | 18,387               | 29,635                 |
| Cash and short-term investments, Beginning                 | 439,193                                      | 431,381              | 7,812                  |
| Cash and short-term investments, Ending                    | <b>\$ 487,216</b>                            | <b>\$ 449,768</b>    | <b>\$ 37,447</b>       |
| (1) Ike Loss/Lae payments                                  | \$ (1,226)                                   | \$ (26,323)          | \$ 25,097              |

## Board Composition

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Under Section 2210.102, the Board of Directors is composed of ten members (9 voting members and 1 non-voting member) appointed by the Commissioner, to include four public members from tier one counties, four members who must be representatives of the insurance industry, one member from a non-seacoast county, and one licensed engineer.

Insurers who are members of the Association shall nominate, from among those members, persons to fill any vacancy in the four seats reserved for representatives of the insurance industry. The Board shall solicit nominations from the member insurers and submit the nominations to the Commissioner. The nominee slate submitted to the Commissioner must include at least three more names than the number of vacancies. The Commissioner shall appoint insurance industry representatives from the nominee slate.

One Board position remained vacant during the reporting period. Alice Gannon, Secretary/Treasurer, resigned her position in August. TWIA staff received and forwarded three nominees to the Commissioner for consideration. The TWIA Board of Directors elected new officers at its quarterly meeting on February 18, 2014. The current membership and officers of the Board of Directors are:

| <b>Name</b>                                 | <b>Position</b>                           |
|---|---|
| Richard Clifton Craig, <i>Vice Chairman</i> | Public Member from Non-Seacoast Territory |
| Steven Lawrence Elbert                      | Public Member & Agent from Tier 1 County  |
| William David Franklin, Sr.                 | Non-voting Member, Licensed Engineer      |
| Michael Gerik, <i>Secretary/Treasurer</i>   | Member of the Insurance Industry          |
| Ron Lawson                                  | Member of the Insurance Industry          |
| Georgia R. Neblett, <i>Chairman</i>         | Public Member from Tier 1 County          |
| Michael O'Malley                            | Member of the Insurance Industry          |
| Gene Seaman                                 | Public Member from Tier 1 County          |
| Edward James Sherlock III                   | Public Member & Agent from Tier 1 County  |

## Open Meetings

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Section 2210.105 requires that, except for an emergency meeting, the Association shall notify the Department not later than the 11th day before the date of a meeting of the Board of Directors or of the members of the Association, and, not later than the seventh day before the date of a meeting of the Board of Directors, post notice of the meeting on TWIA's and TDI's websites. Section 2210.105 requires, except for a closed meeting authorized by Subchapter D, Chapter 551, Government Code (Texas Open Meetings Act), a meeting of the

Board of Directors or of the members of the Association to be open to the Commissioner or the Commissioner's designated representative and the public. Section 2210.105 requires that TWIA broadcast live on its Internet website, all meetings of the Board of Directors, other than closed meetings, and maintain on its Internet website an archive of meetings of the Board of Directors. A recording of a meeting must be maintained in the archive on the website up to the second anniversary of the broadcast. Section 2210.108 provides, except as specifically provided by Chapter 2210 or another law, TWIA is subject to Chapter 551 Texas Government Code, the Texas Open Meetings Act.

The Association has met the requirements of the Texas Open Meetings Act by complying with posting requirements for meetings of the Board of Directors and its subcommittees. Pursuant to Chapter 2210.105, meetings are broadcast live and archived for later viewing on our website ([www.twia.org](http://www.twia.org)). The following meetings were held during this reporting period:

|                   |                         |
|-------------------|-------------------------|
| January 15, 2014  | Nominating Committee    |
| January 27, 2014  | Stakeholder Committee   |
| February 5, 2014  | Nominating Committee    |
| February 17, 2014 | Executive Committee     |
| February 18, 2014 | Quarterly Meeting       |
| February 21, 2014 | Clearinghouse Workgroup |

## Primary Board Objectives Reports

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Section 2210.107 requires the Association to report every two months to its Board of Directors and annually to the Governor, Lt. Governor, Legislature and TDI the extent to which the Association met the objectives outlined in the About This Report section. TWIA continues to comply with these requirements, most recently with the submission of the November 30, January 31, and March 31 Interim Report Cards.

## Public Information Act

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Section 2210.108 provides that, except as specifically provided by Chapter 2210 or another law, TWIA is subject to Chapter 552 Texas Government Code, the Texas Public Information Act ("the Act"). TWIA receives and responds to requests in accordance with the Act. The following table shows the number of requests received, withdrawn, and referred to the Office of the Attorney General (OAG) for a decision under the Act for 2011, 2012, 2013, and year to date 2014.

| Requests                  | Prior Years |      |      | 2014 |
|---------------------------|-------------|------|------|------|
|                           | 2011        | 2012 | 2013 | 2/28 |
| Total Received            | 108         | 182  | 162  | 38   |
| Withdrawn                 | 7           | 16   | 14   | 2    |
| OAG Rulings Requested     | 10          | 20   | 26   | 4    |
| % of Requests sent to OAG | 9%          | 11%  | 16%  | 11%  |

As illustrated in the table above, requests increased nearly 70% from 2011 to 2012. Requested decreased slightly more than 10% from 2012-2013; however, the Association filed 30% more requests for rulings from the Office of the Attorney General (OAG) than in 2012. This is attributable to an increase in requests from plaintiff attorneys regarding litigated or other protected matters.

## Issuance of Policies

Under Section 2210.203, if the Association determines that the property for which an application for initial insurance coverage is made is insurable property, the Association, on payment of the premium, shall direct the issuance of an insurance policy as provided by the plan of operation. A policy is issued for a one-year term and may be renewed annually on application for renewal as long as the property continues to be insurable property. Below are charts illustrating the number of policies currently in-force, the direct liability associated with those policies, and premiums written year-to-date:

### *POLICIES IN FORCE*

| Policy Type   | As of 2/28/13  | As of 2/28/14  | Change from Prior Year |
|---------------|----------------|----------------|------------------------|
| Mobile Home   | 888            | 947            | 6.6%                   |
| Residential   | 252,766        | 256,526        | 1.5%                   |
| Commercial    | 13,153         | 13,014         | -1.1%                  |
| <b>Totals</b> | <b>266,807</b> | <b>270,487</b> | <b>1.4%</b>            |

### *DIRECT LIABILITY*

| Policy Type   | As of 2/28/13           | As of 2/28/14           | Change from Prior Year |
|---------------|-------------------------|-------------------------|------------------------|
| Mobile Home   | \$41,835,632            | \$46,148,509            | 10.3%                  |
| Residential   | \$61,712,526,541        | \$64,509,440,477        | 4.5%                   |
| Commercial    | \$12,804,848,955        | \$12,335,789,890        | -3.7%                  |
| <b>Totals</b> | <b>\$74,559,211,128</b> | <b>\$76,891,378,876</b> | <b>3.1%</b>            |

*WRITTEN PREMIUMS (YTD)*

| <b>Policy Type</b> | <b>As of 2/28/13</b> | <b>As of 2/28/14</b> | <b>Change from Prior Year</b> |
|--------------------|----------------------|----------------------|-------------------------------|
| Mobile Home        | \$114,687            | \$111,411            | -2.9%                         |
| Residential        | \$42,114,439         | \$45,129,418         | 7.2%                          |
| Commercial         | \$16,067,267         | \$12,921,171         | -19.6%                        |
| <b>Totals</b>      | <b>\$58,296,393</b>  | <b>\$58,162,000</b>  | <b>-0.2%</b>                  |

## Compliance with Building Codes

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Sections 2210.251, 2210.258 - .260 set forth the building code and inspection requirements for eligibility in the Texas Windstorm Insurance Association and provide for limited exceptions. In accordance with these sections, TWIA requires a certificate of compliance (WPI-8) issued by the Texas Department of Insurance on all structures constructed, altered, remodeled, enlarged, repaired, or to which additions have been made on or after January 1, 1988. A noncompliant residential structure insured by the Association that has been approved for insurability under the approval process regulations in effect on September 1, 2009 is subject to an annual premium surcharge of 15% of the policy premium. These surcharges are deposited directly into the Catastrophe Reserve Trust Fund.

Prior to the passage of Senate Bill 1702 (SB1702), a residential structure that had not been certified might still be insured if the Department issued an alternative certification (WPI-12) after an inspector determined that at least one qualifying structural building component is in compliance with applicable building code standards.

On June 14, 2013 the 83rd Texas Legislature enacted SB1702, which amends the surcharge program for non-compliant structures and repeals the Alternative Eligibility Program. The bill also requires structures insured by the Association on or after December 31, 2015, to comply with the applicable windstorm building code standards.

The following tables show the number of TWIA policies currently in-force as of February 28, 2014 under the various compliance standards and the total surcharge amounts deposited into the CRTF each year, through February 28, 2014:

| <b>Compliance Standard</b>        | <b>Policies In-Force</b> | <b>Year</b> | <b>Surcharges</b> |
|-----------------------------------|--------------------------|-------------|-------------------|
| Certificate of Compliance (WPI-8) | 230,494                  | 2012        | \$7,408,157       |
| Approval Process                  | 26,848                   | 2013        | \$7,233,546       |
| Alternative Certification         | 13,145                   | 2014        | \$869,513         |

The deposits for this reporting period were \$420,604 and \$448,909 for January and February 2014, respectively.

## Catastrophe Funding

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Subchapter B-1 of Chapter 2210 (Sections 2210.071 – 2210.075) describes the different sources of funding available to pay TWIA losses. Those sources are, in order:

- TWIA premiums and other revenue
- Available reserves and amounts in the Catastrophe Reserve Trust Fund (“CRTF”)
- Up to \$1 billion in Class 1 public securities, to be repaid by TWIA premiums
- Up to \$1 billion in Class 2 public securities, to be repaid by surcharges on coastal property policies and assessments of TWIA member companies
- Up to \$500 million in Class 3 public securities, to be repaid by assessments of TWIA member companies

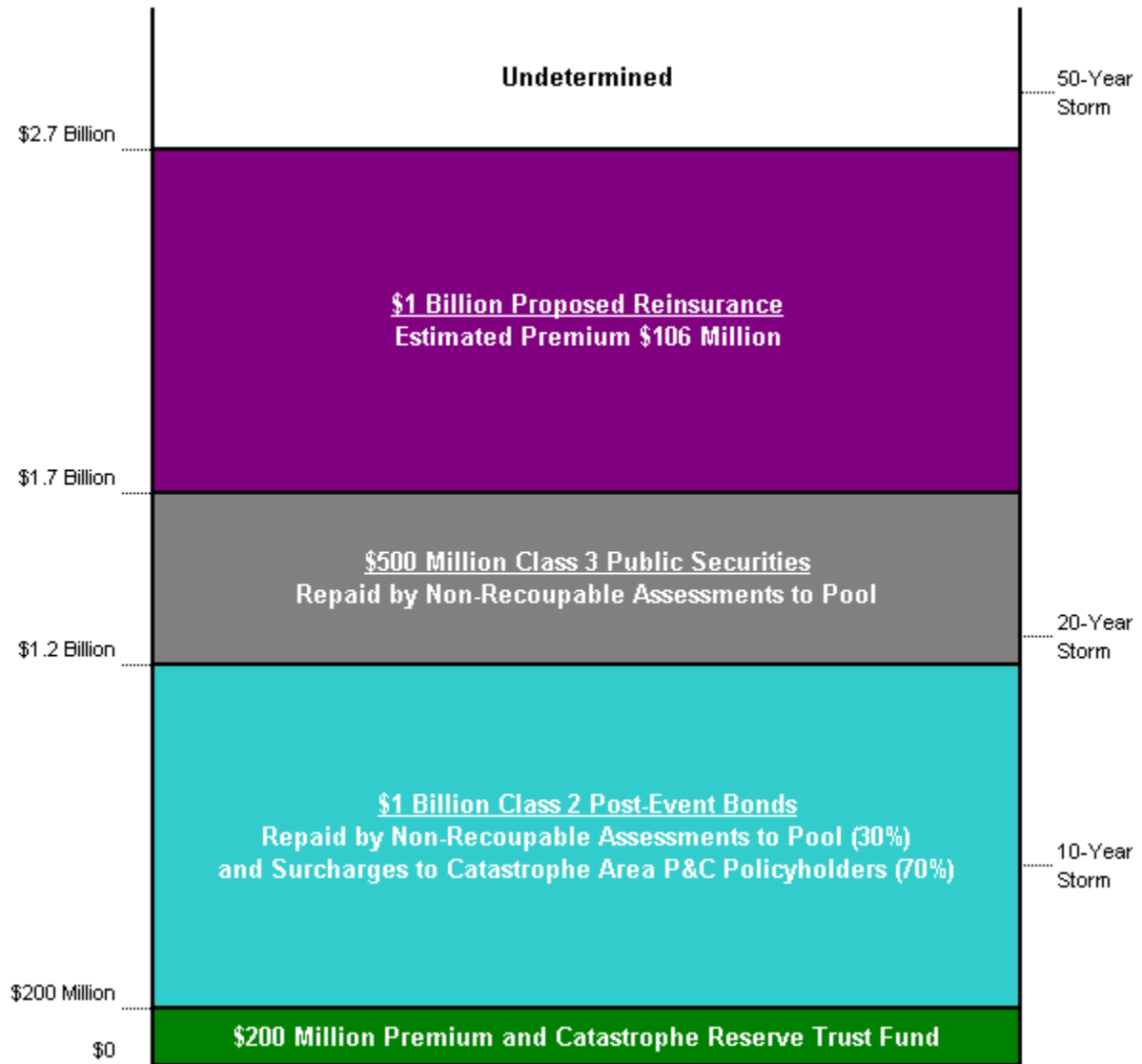
Additionally, reinsurance may be purchased in addition to or in concert with the trust fund and public securities.

TWIA is continuing to work with Commissioner Rathgeber and TDI staff on funding and liquidity options that might be available to TWIA.

TWIA successfully placed its reinsurance renewal effective June 1, 2013 in the amount of \$1B with an attachment point of \$1.7B for a total of \$2.7 B of coverage. TWIA is in the early stages of preparing to renew its reinsurance and will be updating its modeled loss exposures later in the first quarter of 2014.



Total funding for the 2013 hurricane season is illustrated by the following chart:



## Catastrophe Plan

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Section 2210.455 requires the Association, not later than June 1 of each year, to submit to the Commissioner, the Legislative Oversight Board, the Governor, the Lieutenant Governor, and the Speaker of the House of Representatives, a catastrophe plan covering the period beginning on the date the plan is submitted and ending on the following May 31.

The catastrophe plan must describe the manner in which TWIA will, during the period covered by the plan, evaluate losses and process claims after windstorms with a four, two, and one percent chance of occurring.

The catastrophe plan must include a description of how losses under Association policies will be paid, and how claims under Association policies will be administered and adjusted, during the period covered by the plan. The catastrophe plan submitted under this Section is for informational purposes only and does not bind the Association to a particular course of action.

TWIA's Catastrophe Plan is a living document continually updated with information learned from real and modeled events with the goal of constantly improving the Association's capacity and ability to respond promptly and effectively to catastrophic claims situations. The level of detail in TWIA's current catastrophe event planning has exponentially increased over that of 2008 and prior years. Prior to Ike, leadership provided only a high level review. The catastrophe plan was updated infrequently and lacked detailed information about available resources and ability to scale for larger events. The current Claims leadership team conducts annual catastrophe planning meetings to achieve the goal of continuous improvement. The result is a dynamic document designed to provide detailed information regarding:

- roles and responsibilities for Claims and other departments;
- information regarding available resources;
- details for scalability for larger events including pre- and post-event loss projection and staffing modeling tools; and
- operational guidelines and directives for TWIA's response to a catastrophe.

A complete copy of the 2013 TWIA catastrophe plan was included in the Annual Report Card submitted May 31, 2013. The 2014 catastrophe plan will be presented in the May 31, 2014 Annual Report Card.

TWIA has activated the catastrophe plan six times since January 1, 2012 for localized wind and hail events. Leadership's commitment to planning and the proficient execution of that

plan is evidenced by TWIA policyholder satisfaction levels. TWIA’s Customer Care Survey was initially implemented in April 2012. Since June 2012, TWIA payment letters have included QR codes that link policyholders to the Customer Care Survey. The survey is also accessible through the Association’s website, [www.twia.org](http://www.twia.org). The following exhibits illustrate policyholders’ positive reactions to the improvements management has implemented.

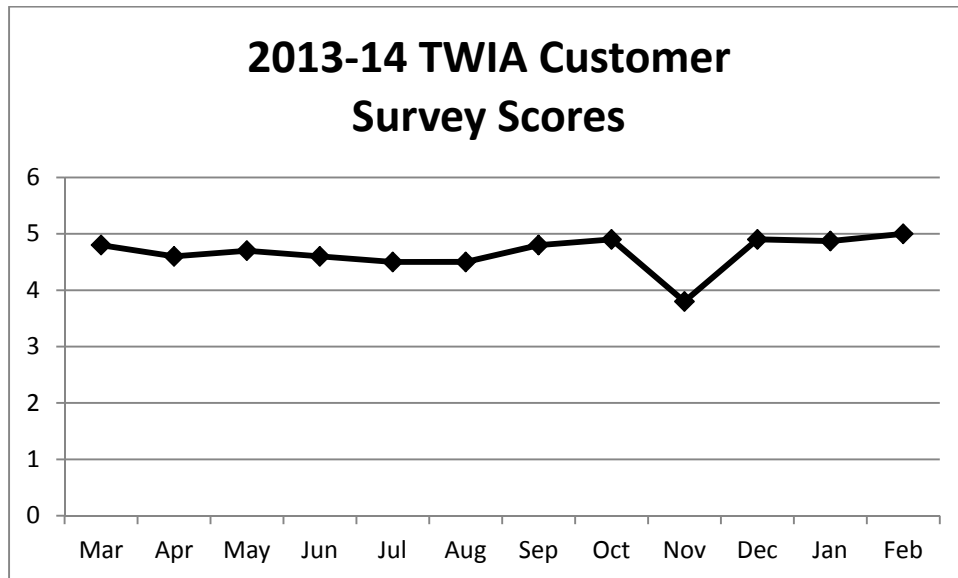
### 2013-14 TWIA Customer Survey Scores

Policyholders are surveyed on their experience in various parts of the claims process. The short survey consists of the following five questions:

1. Reporting my claim to TWIA was easy
2. A TWIA employee explained the claims process to me
3. The TWIA adjuster who came to my home was professional, courteous, and helped me with my claim
4. The outcome of my claim was clearly explained to me
5. I am satisfied with the overall handling of my claim to TWIA

*AVERAGE SCORE BY MONTH*

| Mar | Apr | May | Jun | Jul | Aug | Sep | Oct | Nov | Dec | Jan  | Feb |
|-----|-----|-----|-----|-----|-----|-----|-----|-----|-----|------|-----|
| 4.8 | 4.6 | 4.7 | 4.6 | 4.5 | 4.5 | 4.8 | 4.9 | 3.8 | 4.9 | 4.87 | 5.0 |



## Key Performance Indicators

The following table lists the year to date Key Performance Indicators for TWIA claims as of 2/28/14:

|   |       |
|---|-------|
| Number of Claims Received                                       | 463   |
| Number of Claims Closed With Payment                            | 1,255 |
| Claims Closure Rate   | 271%  |
| Average Number of Days From FNOL to Inspect Property            | 1.5   |
| Average Number of Days From Inspect Property to Receipt by TWIA | 1.6   |
| Average Number of Days From Receipt by TWIA to Payment          | 3.7   |
| Number of TDI Complaints  | 2     |
| TDI Complaints as a Percentage of Total Claims Received         | 0.43% |

## Limits of Liability

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Under Subchapter K of Chapter 2210 (Sections 2210.501 – 2210.504), TWIA is required to propose inflation adjustments to the maximum liability limits under a windstorm and hail policy. At the August 13, 2013 quarterly meeting of the Board of Directors, proposed adjustments to the maximum limits were approved as follows:

|   | Current<br>2013 | Proposed<br>2014 |
|---|-----------------|------------------|
| Dwellings and individually owned townhouses         | \$1,773,000     | \$1,816,000      |
| Contents of an apartment, condominium, or townhouse | \$374,000       | \$383,000        |
| Commercial structures and associated contents       | \$4,424,000     | \$4,514,000      |

A filing to increase the limits of liability was made September 30, 2013 and a public hearing was held October 30, 2013. The Texas Department of Insurance denied the request to increase the maximum liability limits, citing the cumulative increases in TWIA limits since January 1, 2005 in concluding that the filed increases in limits were not necessary at the time. Current limits will continue and be applicable to all policies issued in 2014.

## Certain Appeals and Other Actions

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### Claims: Settlement and Dispute Resolution

HB 3 made significant changes to both the process by which insureds can dispute the decisions of the Association relating to the payment of, the amount of, or the denial of a claim, and the remedies available to the insured. Section 2210.014 made Insurance Code

Chapters 541 (bad faith) and 542 (Prompt Pay Act) inapplicable to TWIA claims, and Section 2210.572(c) made the Deceptive Trades & Practices Act inapplicable to TWIA. These were three of the main causes of action asserted by insureds who sued TWIA alleging claims were underpaid or settled in bad faith. New provisions of Chapter 2210, Subchapter L-1, provide the process for claims decisions, payments, and disputes.

All claims personnel have been trained on the new claim-handling procedures and deadlines included in HB 3. Claims decision letters have been revised to provide clear notifications of the portions of a claim the Association has accepted or denied in full or in part, as required by Section 2210.573(d). Claims decision letters also include brief descriptions of the procedures to dispute accepted or denied claims and provide forms that insureds can use to begin the dispute resolution process, as required by Section 2210.573(e)-(g).

Below is a table listing data, as of February 28, 2014, regarding claims subject to the HB 3 dispute resolutions.

| Disputed Claims   |                 |                      |                 |       |                         |           |                        |
|-------------------|-----------------|----------------------|-----------------|-------|-------------------------|-----------|------------------------|
| Dispute Frequency |                 |                      | Type of Dispute |       |                         |           |                        |
| Total Claims      | Disputed Claims | % of Disputed Claims | Appraisals      | Suits | LORs (not in Appraisal) | Mediation | TDI & Other Complaints |
| 13,030            | 119             | 0.91%                | 70              | 7     | 18                      | 4         | 20                     |

| Appraisals |                      |                    |                           |           |            |
|------------|----------------------|--------------------|---------------------------|-----------|------------|
| Total      | Open/Pending         | Appraisal Complete | Appraisal Process Stopped |           |            |
| Appraisals | Appraisal In Process | Appraisal Award    | Settled with Supplement   | Withdrawn | Ineligible |
| 70         | 19                   | 21                 | 20                        | 6         | 4          |

## Appraisal and Rule-Making

All disputes regarding a claim that is accepted by the Association must be submitted to an appraisal process pursuant to Section 2210.574. The Department adopted rules to govern this appraisal process. TWIA continues to work with TDI to implement the rules regarding the appraisal process.

## Ombudsman Funding and Program

Section 2210.582 directed the Department of Insurance to establish an Ombudsman Program to assist TWIA policyholders in understanding and navigating the claims process. The Department established the Coastal Outreach and Assistance Services Team (“COAST”) Program and adopted rules relating to its function on March 19, 2012. Even before the formal adoption of the rules, at 28 TAC §5.4201, TWIA revised its claims correspondence to advise insureds of the program and provide contact information in English and Spanish. TWIA fully funds the COAST program based on the budget provided by the Department each March.

TWIA has established a positive working relationship with the Ombudsman. Through cooperative efforts, we have been able to answer policyholder questions before concerns are escalated to the Department’s complaint division, and to assist in education efforts promoted by the COAST Team.

## Compliance with the Plan of Operation

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The Plan of Operation is a series of administrative rules found in the Texas Administrative Code, Title 28, Chapter 5, Subchapter E. Administrative rules must be proposed by an agency (TDI in this case) and adopted pursuant to statute. The Texas Department of Insurance proposed the following rules during the reporting period regarding TWIA loss funding:

| Subject   | Section Number  | Filed   | Published |
|---|---|---------|-----------|
| Subchapter E. Texas Windstorm Insurance Association.<br>Proposed Repeal Regarding Loss Funding      | <a href="#">5.4131 and 5.4132</a>   | 1/30/14 | 2/14/14   |
| Subchapter E. Texas Windstorm Insurance Association.<br>Proposed New and Amended Loss Funding       | <a href="#">5.4101, 5.4102, 5.4121, 5.4123-5.4128, 5.4133, 5.4135, 5.4136, 5.4141-5.4147, 5.4148, 5.4149 and 5.4164</a> | 1/30/14 | 2/14/14   |
| Subchapter E. Texas Windstorm Insurance Association.<br>Proposed Repeal Regarding Premium Surcharge | <a href="#">5.4183</a>  | 1/30/14 | 2/14/14   |
| Subchapter E. Texas Windstorm Insurance Association.<br>Proposed Amendments to Premium Surcharge    | <a href="#">5.4171-5.4173, 5.4182, 5.4184-5.4187, 5.4189-5.4192</a>   | 1/30/14 | 2/14/14   |

The existing loss funding rules were adopted to implement HB 4409, 81st Legislature, Regular Session, 2009. Proposed rules would repeal existing rules and replace them with rules implementing HB 3, 82nd Legislature, First Called Session, effective September 28, 2011.

Proposed rules affect TWIA loss funding, specifically the issuance and repayment of Class 1, 2, and 3 public securities. Some of the changes affecting loss funding in general include the ability to issue Class 1 public securities prior to a catastrophic event and to permit the issuance of Class 2 and Class 3 public securities if TPFA is unable to issue all or any portion of the Class 1 public securities. Current statute authorizes the Commissioner to order the issuance of Class 2 public securities if the Commissioner finds that all or any portion of the total principal amount of Class 1 public securities cannot be issued.

Proposed rules also revise the procedures for making and assessing premium surcharges required to repay Class 2 public securities. HB 3 restricted the types of policies subject to surcharge from “all property and casualty lines of insurance” with limited exceptions to only property and auto policies.

TDI states in their introduction to the proposed rules that the amendments do not impose any requirement not already required by the statute and do not directly affect rates.

## Annual Evaluation of Association Management

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The fifth objective outlined in 2210.107(a) is to establish, and adhere to terms of, an annual evaluation of Association management necessary to achieve the statutory purpose, Board objectives, and any performance or enterprise risk management objectives established by the Board.

Since January 1, 2012, TWIA’s annual budget has been based upon department level budgets for which department management and their staffs are accountable. Individual performance standards have been established for each position within the organization. These standards reflect accountability as well as objective metrics appropriate to the individual employee’s responsibilities. The 2014 budget was presented to the Board at its December 10, 2013 meeting. The budget was approved subject to an evaluation and final determination of the Executive Committee regarding the compensation and performance of the General Manager and the senior management team.

The Finance Department has prepared budget conformance reports at the department level to monitor performance beginning with 2012 first quarter results. Under the current

management team, TWIA has consistently performed at or below budget for controllable expenses in nearly every area. Controllable expenses through February 28, 2014 are at budget and below the comparable period in 2013.

TWIA staff is evaluated against a set of performance standards, including objective performance measures based upon their department and their individual role within their department. Each department head is accountable for his or her individual budgets, and these measures comprise a portion of the standard of performance against which they are evaluated on an annual basis. Staff within each department has similar, although not identical, objective measures against which to evaluate performance. Performance Evaluation documents reflect these areas of accountability.

Risk Management Objectives have been established in the form of Business Continuity planning, Catastrophe Claims planning, Reinsurance, and other funding mechanisms to effectively manage the financial and human resources of the organization in meeting its established purpose.