PARAGON

Reinsurance Administration & Asset Recovery Solutions

MEMORANDUM

To: Jack Nicholson, Martin Hegelstad

From: Andrew J. Rapoport, FCAS, MAAA

Date: 06/05/2008

Subject: FHCF Bonding Need Review: 05/31/08

I Loss Projections

We project the following estimates for ultimate loss and loss expenses to be paid by the Florida Hurricane Catastrophe Fund ($ Billions). Note that industry paid, outstanding and reported losses are the industry losses in the FHCF layer.

These are the values we recommend the FHCF use in calculating outstanding losses for May 31, 2008.

Contract Year	Industry Reported Paid	Industry Reported Outstanding	Industry Reported Losses	FHCF IBNR Losses	FHCF Ultimate Losses
2004	3.797	0.055	3.852	0.098	3.950
2005	4.428	0.445	4.873	0.327	5.200
Total	8.225	0.500	8.725	0.425	9.150

This is an increase of $200 million to ultimate 2005 contract year losses.

These were the values we recommend the FHCF use in calculating outstanding losses for April 30, 2008.

Contract Year	Industry Reported Paid	Industry Reported Outstanding	Industry Reported Losses	FHCF IBNR Losses	FHCF Ultimate Losses
2004	3.796	0.052	3.848	0.102	3.950
2005	4.405	0.432	4.837	0.163	5.000
Total	8.201	0.484	8.685	0.265	8.950

At December 31, 2007, the corresponding values were:

Contract Year	Industry Reported Paid	Industry Reported Outstanding	Industry Reported Losses	FHCF IBNR Losses	FHCF Ultimate Losses
2004	3.752	0.077	3.829	0.121	3.950
2005	4.227	0.541	4.768	0.032	4.800
Total	7.979	0.618	8.597	0.153	8.750

For Fiscal Year End June 30, 2007 the corresponding values were:

Contract Year	Industry Reported Paid	Industry Reported Outstanding	Industry Reported Losses	FHCF IBNR Losses	FHCF Ultimate Losses
2004	3.722	0.076	3.798	0.152	3.950
2005	3.918	0.408	4.326	0.174	4.500
Total	7.640	0.484	8.124	0.326	8.450

Based on losses reported to and paid by the FHCF through December 31, 2007, we have increase our prior estimate of contract years 2005 ultimate losses by $400 million to $5.2 billion. We have not changed our contract year 2004 estimate of $3.950 billion.

We increased concerns regarding adequacy of company reported reserves. Overall FHCF IBNR is now approximately 83% of industry reported outstanding losses in the FHCF layer. Actually allocation by contract year may vary from our current selections.

Based only on loss information, our current ultimate loss selections are $800 million higher than when the FHCF bonded in 2006. Based on demand deposit account balance of $187 million and outstanding losses of $925 million our bonding need would be $738 million (compared to $538 million based on April 30 estimated losses. Current industry reported losses of $8.725 billion are $375 million higher that our ultimate loss estimate of $8.350 billion used for bonding purposes in 2006.

II Observations of Loss Emergence

We have included exhibits showing comparison of industry loss reporting from 2005 to 2008 for the 2004 and 2005 contact years. We have included both the April and the May comparisons.

In April we saw the following. The 2005 year (hurricane Wilma losses) shows significantly higher development than the 2004 year (4 hurricanes). The FHCF layer development the first 12 months post hurricane year were very similar (11.8% for 2004 and 10.8% for 2005). The second year was flat for 2004 but produced 13.2% development for 2005. On a calendar year basis, both contract years have had more losses reported in the last 12 months than in the prior 12 months.

In May , the patterns were similar except first year post hurricane development was lower for 2005 (1.045) and then for 2004 (1.107). But second year development was still significantly higher for 2005 (1.134) vs. (.999) for 2004. On a calendar year basis, both contract years also still had more losses reported in the last 12 months than in the prior 12 months, but 2005 had over twice as many new losses.

Citizens has reported in their 12/31/07 actuarial opinion that they are continuing to see new reports and reopened claims for Hurricane Wilma. A follow-up conversation with Citizen's actuary on June 4, indicated they continue to see more reopened claim and that they do not have a specific estimate on the magnitude of the future losses from these reopend claims.

One other company with a large share of 2005 losses increased their reported losses this month accounting for most of the increase for the month. We have not yet had a follow up with a representative from this company regarding the increase.

We have also observed that for the industry Hurricane Wilma has more commercial habitational losses than the 2004 hurricanes. These losses develop slower and have longer settlement periods due to the much greater average size loss.

We recommend maintaining the additional $100 million of reserves ($3.95 billion ultimate) for 2004 to cover potential changes in coverage from audits. With four hurricanes, changes to exposure bases can affect up to 4 retentions for a company. We recommend again increasing the ultimate loss level for 2005 to $5.2 billion from $5.0 billion. These selections imply total FHCF IBNR (anticipated industry reporting of $425 million, about 83% of industry reported outstanding reserves of $500 million. It is likely the allocation between years will shift over time.

There is no precedent for anticipating additional reportings to the FHCF. Intuitively we would expect that reportings should decrease year to year, but we have seen increases over the last 12 months for both contract years.

From cash flow considerations the FHCF needs to bond to continue making timely payments. Because of the considerable uncertainty in final loss reportings, at least two tranches should be used. The first tranch should at minimum cover known reported losses to the FHCF. This will provide additional time to get a more accurate evaluation for a second (and hopefully final) tranche.

We have also included new paid projections based on the revised ultimate estimates to assist in estimating cash flow. These exhibits need some additional formatting for their final versions but should provide some insight into when the next bonding tranche would be needed.

We have prepared bonding projections and payouts with 2005 ultimate losses at $5.0 billion and $5.2 billion (labeled 600 and 800 for overall ultimate reserve increases since first bonding).

Considerable uncertainty and variability are inherent in excess property catastrophe reserve estimates, and accordingly, the subsequent development of those reserves may not conform to the assumptions inherent in their determination and, therefore, may vary from the foregoing estimated amounts. No warranty is expressed or implied that this will not occur, or that such development will not exceed the ranges provided.

cc: Budde, Cook, Mackenthun, Fix