



# Memorandum

**To:** The Board of Directors of Connecticut Foundation Solutions Indemnity Company, Inc. ("CFSIC")

**From:** Michael Maglaras, Superintendent

**Date:** September 10, 2020

**Re:** **Annual Report**

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I am pleased to provide you, in my firm's capacity as Superintendent of CFSIC, with CFSIC's second Annual Report summarizing our impact on the crumbling foundations natural disaster.

## **Date Range of Data**

Most of the data in this report is valid as of August 31, 2020, but also reflects additional data effective at the end of CFSIC's June 30, 2020 fiscal year. We will, at the end of September, supplement this report with infographics as we did last year.

## **Revenue to Date**

To date, CFSIC has received \$91,349,095 in revenue. This consists of a total of \$80,000,000 received in four \$20,000,000 tranches by way of allotments approved by the Connecticut Bond Commission and/or the Connecticut Department of Housing, \$10,601,209 in Healthy Homes surcharge funds, and \$747,886 in investment income.

We have also received several tax-exempt donations in smaller amounts, for which we are grateful.

## **Total Anticipated Additional Funding**

In addition to the actual revenue received as noted above, CFSIC has budgeted an anticipated \$105,500,000 in funding (not inclusive of investment income) projected to be received before its proposed new sunset date of June 30, 2030. As of this writing, while CFSIC's management has been assured that the current statutory June 30, 2022 sunset date will be moved legislatively to be June 30, 2030, and we have assumed for budgetary purposes that we will have access to funds through June 30, 2030, CFSIC's business model still partially reflects the existing June 30, 2022 sunset date, because the date has not been statutorily modified.

Of the total projected revenue noted above, \$20,000,000 is prescribed by statute as the remaining funding to be received from the Connecticut Bond Commission, in one remaining installment, at some point between the period July 1, 2021 and June 30, 2022.



With respect to the remaining \$85,500,000, CFSIC has budgeted approximately \$9,500,000 to be received at some point in June of 2021, and then subsequently the same projected amount in June of 2022 through June of 2030, in annual installments, from CFSIC's share of the \$12 per commercial homeowner insurance policy annual surcharge (Healthy Homes surcharge). We have budgeted this even though the first installment of the Healthy Homes surcharge received by CFSIC was \$10,601,209. CFSIC has traditionally adopted a conservative revenue budgeting scenario so as not to over-estimate our ability to respond to claimant needs. We believe and we hope that the remaining nine installments will each be in the neighborhood of \$10.6 million, as was the first installment, our more conservative budgeted revenue projections notwithstanding.

### **Current Financial Status**

CFSIC is statutorily insolvent. It is not a going concern.

CFSIC is on a July 1 through June 30 fiscal year. As of CFSIC's 8/31/20 unaudited financials, CFSIC carries negative equity of (\$43,570,509). This means that CFSIC is underwater by that amount, and therefore is entirely dependent upon future revenues to offset existing claim liabilities that represent verifiable individual homeowner foundation impairment.

From the standpoint of available cash versus commitments to construction expense, general expense, and foundation replacement reimbursements, CFSIC maintains, as of the date of this writing, a positive cash balance, and has done so since inception.

CFSIC has accomplished this by rationing its available cash through the use of periodic restrictions imposed on the countersigning of homeowner Participation Agreements by the Superintendent. CFSIC has already provided \$43.8 million in payments for construction and reimbursement to its claimants through the action of the Superintendent's countersigning of Participation Agreements.

CFSIC has gone into suspension periodically in order to ration its cash or to enable staff to manage the flow of application information correctly. In the fiscal year ending June 30, 2020, CFSIC went into application suspension twice: once on September 6, 2019 (for the taking of all applications...and where it came out of suspension on January 13, 2020, but only for the taking of Pending applications) and then subsequently again for the taking of all applications, including for Pending claimants, on June 30, 2020.

CFSIC is, as of this writing, actively engaged in the process of releasing and countersigning Participation Agreements for foundation remediation and will most probably continue to be until the third week of October 2020, at which point it will have committed almost \$30 million in recently received funding. At that time, CFSIC will have provided Participation Agreements to claimants holding places in the Participation Agreement line through February 26, 2020.

Booked unfunded claim liabilities carried on CFSIC's balance sheet greatly exceed CFSIC's assets. Booked liabilities consist of insurance company claim reserves, which



are commitments to individual homeowners for remediation or reimbursement when cash becomes available, and as a result Participation Agreements can be signed with those homeowners. These reserves are substantiated by individual applications from homeowners accompanied by verifiable points of written and photographic evidence.

At all times, CFSIC must maintain a cash balance in excess of cash commitments to construction and reimbursement, in order to provide for unencumbered statutory capital and surplus of a minimum of \$225,000 and to provide for the payment of applicable operating expenses, in order to secure the continual flow of services so that if, at any point, further funding is not forthcoming, service providers can be terminated quickly and effectively, CFSIC's license as an insurer surrendered, and its operations terminated. Should CFSIC's operations be terminated, CFSIC would go into receivership, coming under the direct control of the Connecticut Insurance Department.

### **Operations**

CFSIC is regulated by the Connecticut Insurance Department, to which it is directly answerable for adherence to its original business plan and for its conduct as a licensed insurer.

CFSIC is managed on a day-to-day basis by outsourced service providers who carry out their duties directly under the supervision and management of CFSIC's Superintendent, with the exception of CFSIC's auditors, which report directly to CFSIC's board.

### **Expenses**

CFSIC's cost of operations includes the cost of claim adjustment, administrative services, legal services, actuarial services, accounting services, public outreach activities, audit fees, and liability insurance expense. CFSIC has no employees, as is traditional under the structure of a captive insurance company.

Its directors are volunteers who have agreed to contribute time to this effort as a public service.

CFSIC tracks its expenses on a calendar year basis, based on the advice of counsel with respect to the interpretation of the limitation contained in the original enabling legislation that CFSIC cannot expend more than 10% of all revenues received in any calendar year on administrative and operational expenses.

Since inception of operations, as of August 31, 2020, CFSIC has operated on a cash and accrual basis at an average of 2.9% of revenues on a calendar year basis.



**Claimant Activity; Total Outstanding Claim Liability; Total Claim Payments to Date**

What follows provides information as to the extent of application activity, outstanding claim liability, and paid claim liability to date, valued as of 8/31/20:

<b>Town</b>	<b>Total Active/Inactive/Pending Claimants Identified</b>	<b>Total Outstanding Claim Liability</b>	<b>Total Claim Payments to Date</b>
Amston	3	\$0	\$175,000
Andover	8	404,055	514,709
Ashford	33	2,347,457	1,429,321
Berlin	1	0	0
Bloomfield	4	157,484	17,500
Bolton	23	1,385,859	267,432
Branford	1	0	0
Bristol	2	0	0
Broad Brook	6	314,012	238,733
Burlington	1	0	0
Columbia	8	110,500	369,952
Coventry	76	2,791,368	3,252,445
Darien	1	0	0
Deep River	1	0	0
East Hartford	4	0	234,383
East Windsor	72	5,040,000	0
Eastford	1	0	40,956
Ellington	97	4,807,909	3,952,866
Enfield	31	816,169	1,436,147
Glastonbury	1	0	49,163
Granby	1	157,500	17,500
Hebron	3	170,433	304,885
Manchester	163	11,478,464	2,032,833
Mansfield	8	228,745	437,421
Middletown	1	0	0
Milford	1	0	0



Town	Total Active/Inactive/Pending Claimants Identified	Total Outstanding Claim Liability	Total Claim Payments to Date
Monroe	1	\$0	\$0
Naugatuck	2	0	0
New Britain	2	0	0
New Haven	2	0	0
Norwalk	1	0	0
Somers	40	1,418,826	1,031,385
South Windsor	148	8,726,463	5,991,464
Stafford/Stafford Springs	150	8,562,084	3,899,118
Storrs	11	567,685	516,016
Suffield	5	175,000	342,000
Tolland	220	12,027,829	8,757,786
Union	11	660,217	491,114
Vernon	370	18,317,683	4,333,980
Waterbury	2	0	0
West Hartford	1	0	0
West Haven	1	0	0
West Suffield	1	157,500	17,500
Willimantic	1	0	0
Willington	116	7,458,730	3,525,690
Windsor	1	0	0
Woodstock	2	172,300	175,000
<b>TOTAL</b>	<b>1,639</b>	<b>\$88,454,273</b>	<b>\$43,852,297</b>

Commentary:

1. The data in the CFSIC program changes daily, in fact in some cases hourly. This data is valid as of close of business on August 31, 2020.
2. Reserves are not held for Pending claimants; statutory reserves are posted for Active and Inactive claimants holding valid severity class codes.
3. Both booked and paid claim liabilities are reflective of claim activity for Type 1 and Type 2 claimants.



## **The Participation Agreement Process**

CFSIC holds Connecticut captive insurance license #29. Its charter and its operations are reflective of those of a licensed insurance company; however, CFSIC does not collect any premium and does not issue an insurance contract in the form of an insurance policy. As a result, CFSIC's operations resemble those of a captive insurer in some respects, and not at all in others.

What eventually binds CFSIC and an individual homeowner contractually is a Participation Agreement, which outlines both the homeowner's and CFSIC's responsibilities, contractor or reimbursement payment schedules, and contractual commitments. Participation Agreements have been signed on a regular basis, permitting foundation remediation to be scheduled, and foundation reimbursements to be made, for approximately the past twenty months, except on those occasions during which PA suspensions occurred.

It is important to note that the actual schedule of remediation is up to the homeowner and the contractor in question in each case. When the Superintendent countersigns a Participation Agreement, this can literally mean that in some cases the remediation can commence in a few days, or in a few years, depending upon contractor and homeowner schedules. Once the Superintendent countersigns a Participation Agreement, CFSIC has in effect made a promise to make payment. It is for this reason that, even though CFSIC's sunset date may be moved to June 30, 2030, CFSIC will in essence be running off Participation Agreement commitments, to the extent it receives all of its funding, for at least four years after that date.

As of August 31, 2020, the Superintendent had countersigned 521 Participation Agreements, and almost 200 families had been put back in their homes with new foundations in place.

## **Application Process**

CFSIC's Underwriting and Claims Management Guidelines permit two types of claim activity.

A "Type 1" claim is a claim requesting assistance with the replacement of a foundation verifiably determined to be impaired through visual evidence of the manifestation of the presence of reactive pyrrhotite in the original aggregate used in the concrete composing that foundation, and where the homeowner has made, through the completion of an application and the provision of points of evidence, a valid claim for payment of enumerated allowable costs.

There are three classes of severity class code employed to reflect the degree of foundation impairment. These class codes provide a basic prioritization for the use of funds, beginning with Severity Class 3, which is a class code reflective of a severely impacted foundation.



A “Type 2” claim is a claim requesting assistance with reimbursement by CFSIC to a homeowner for the replacement of a foundation verifiably determined to have been impaired through evidence of the presence of reactive pyrrhotite in the original aggregate used in the concrete composing that foundation, but where that homeowner used personal resources to originally repair/replace such an impaired foundation prior to making application to CFSIC; and where the homeowner has subsequently made, through the completion of an application and the provision of points of evidence, a valid claim for reimbursement of enumerated allowable costs.

CFSIC’s Board of Directors has authorized a total of 100 such Type 2 paid claim reimbursements to be made during CFSIC’s statutory lifetime. As of August 31, 2020, CFSIC had engaged with 94 Type 2 claimants, where CFSIC had either completed or will shortly complete the reimbursement process for those families.

The application process gathers information for purposes of underwriting, claim prioritization, and eventual potential payment. On average, more than 150 pages of supporting documentation are collected with each application. The average time to process an application varies significantly, based on the ability and willingness of individual claimants to provide CFSIC with quantifiable and verifiable data, either at the precise point of application to the program or at some point thereafter.

CFSIC claimants are categorized as “Active,” “Inactive” or “Pending” with respect to both Type 1 and Type 2 claims. On January 13, 2020, the Superintendent announced the launch of the “Pending” class of claimant in order to permit claimants to register the existence of a verifiable impaired foundation...but with the clear understanding, repeated consistently on CFSIC’s website, that existing budgeted financial resources might be insufficient to respond to any Pending claimant at any point in the future.

CFSIC is doing its part to assist in a revitalization of the Northeast Corner real estate market. We have instituted a claim transfer process enabling Type 1 claimants who are registered with us as Active, Inactive, or Pending claimants, and where no remediation work has been done or started, to transfer their claim to the buyer of their home...where that buyer can assume the exact position of the original claimant in CFSIC’s register of claimants with no penalty.

### **CFSIC’s Effect on the Towns with Recorded Claimants**

CFSIC’s operations are having a direct and positive effect on the existing property tax abatement crisis in CT’s Northeast Corner.

The towns of Ashford, Coventry, East Windsor, Ellington, Manchester, South Windsor, Stafford/Stafford Springs, Tolland, Vernon, and Willington represent 90% of the total of our existing book of incurred claim liability.

CFSIC has been, for the past twenty months, improving the economies of the ten hardest hit communities, literally one home at a time, by identifying affected homes and beginning the process of restoring those homes, through foundation remediation, to original assessed value. By twelve months from the date of this writing we project that



CFSIC will have restored as much as 70% of the total of the current tax abatements for residential dwellings in these top ten hardest hit Connecticut communities.

### **The Extent of the Crisis**

In the past twenty months, CFSIC has collected a significant amount of data through the application and remediation processes. None of the data collected to date suggests that the crumbling foundations crisis currently or potentially affects as many as 35,000 homes in the 47 communities where CFSIC has applicants. Similarly, no data in CFSIC's possession provides evidence of a crisis on the magnitude of \$1 billion to \$2 billion, as has been widely reported.

However, the crumbling foundations crisis is a devastating economic and human crisis.

We believe that this crisis involves most probably 4,000 to 6,000 homes in total, which will require remediation between the date of this writing and the end of 2030 in two distinct waves of remediation activity, as described below. To be clear, the negative economic impact on the communities and the citizens of the Northeast Corner of Connecticut is quantifiable, verifiable, and cannot be disputed.

It is important to emphasize what we firmly believe to be the manageable size of this crisis. We also believe that the key to raising additional funding from state and federal sources will in fact be the understanding of just how manageable this crisis is, through the adoption of realistic and verifiable assessments of the impact of the crisis.

CFSIC's database is the only credible database in existence on the extent of this crisis.

As a result of what CFSIC's data now suggests, we maintain that this crisis is now and will continue to be a crisis that is manageable in what we project is two potential "waves" of impairment manifestation: the first one that began on January 10, 2019 and will run through approximately June 30, 2024...and a second one, which will begin then and end at some point after 2030, resulting in the need for as many as 6,000 potential foundation replacements.

### **CFSIC's Challenges**

CFSIC faces a number of challenges as it heads into its 2021 fiscal year.

I'm happy to report that one of these challenges is not the receipt of our original planned funding. Governor Lamont and his administration have worked hard to understand what CFSIC does and its mission. While it is clear that CFSIC needs more funding than it is budgeting in order to do its job well, the irregularity of funding, as was reported at this time last year, has largely become a thing of the past, and we are grateful to Governor Lamont and his team for their confidence in our efforts.



Other continuing challenges are:

1. Additional funding: CFSIC needs an additional \$100 million. If it gets, over the next nine years, an additional \$100 million, our data suggests that the crisis would be largely put to rest for a minimum of fifteen years.
2. Politics: A significant challenge to CFSIC is its potential for politicization. CFSIC is an independent company. It is a private company. It is a federal tax-exempt corporation, and it is not a branch of state government. Firm representations have been made by management to CFSIC's insurers that it will be operated consistent with good governance rules at all times, and that it will remain a private company. Its success lies in its independence, because it is a fiduciary and must at all times act as one, and where no action should be taken that even suggests or hints at a conflict of interest or an underlying political motive. As CFSIC's success becomes more apparent, and as its impact on the Northeast Corner more profoundly felt, it is vitally important that everyone associated with CFSIC maintain high standards of fiduciary responsibility and, most importantly, independence in all their considerations.
3. Privacy: The Superintendent's office and all CFSIC's service providers maintain strict privacy standards with respect to claimant information. There continue to be challenges to that privacy standard. Claimant information should at all times be maintained as confidential. Claimants sign their applications, and when they do they attest to the correctness and truthfulness of their application information, and they reveal to us elements of their personal lives and financial condition, to which no politician, no official, no member of CFSIC's board, and no concrete activist should have access. When they sign those applications, they submit themselves to the force of severe penalty under law for anything they attest to that is untruthful. In return, we owe them the duty of privacy. CFSIC's success in the future will lie with the public's trust. Under CFSIC's current management, we will assure that that trust is not misplaced.

CFSIC's challenges, oddly enough, are not about its underwriting and claims management program, not about the claim adjustment process, and not about its operations...its challenges remain as noted above. I urge all members of the public to recognize these challenges for what they are, and I urge CFSIC's board to enforce strict adherence to the principles noted above.

### **Offering Thanks**

I would like to close by acknowledging that what we have achieved in the past twenty months is as a result of a team effort.

About a dozen people work behind the scenes on the CFSIC project on a daily basis in one capacity or another. These people support the office of Superintendent by quietly doing a job each day that very few people would take on. These people are my teammates, and they recognize the terrible toll that this crisis has taken on people's lives. I'm proud of my teammates. They have acted patiently with victims whose lives



have been turned upside down by this crisis, and occasionally they have endured personal abuse, harassment, and in some cases worse in the course of duty.

When I took this assignment I was instructed by many people to expect the anger, the frustration, and the impatience of claimants to manifest itself. My team and I have gotten all of that in the course of this assignment. As Superintendent, however, when people have crossed the line into abuse or personal threats, I have also been clear that I will remove them from consideration to receive funds should they refuse to respect the dignity and humanity of my team members. I have been clear that whatever the source of their anger, CFSIC has never been the problem; CFSIC has always been the solution.

On a positive note, we continue to get many emails and phone calls thanking us for what we have done and are doing. Many of those calls end with tears of happiness. Some of those calls end with tears of happiness on both ends of the telephone.

Respectfully submitted,

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Michael Maglaras, Principal  
Michael Maglaras & Company, Superintendent of CFSIC

Sources of Data:  
CFSIC August 31, 2020 Incurred Loss Run  
CFSIC August 31, 2020 Unaudited Financials  
CFSIC Internal Construction Tracking Data Reports