THE HOMEOWNERS' INSURANCE CRISIS: SOLUTIONS FOR HOMEOWNERS, COMMUNITIES, AND TAXPAYERS

FIELD HEARING

BEFORE THE

SUBCOMMITTEE ON
OVERSIGHT AND INVESTIGATIONS

OF THE

COMMITTEE ON FINANCIAL SERVICES

U.S. HOUSE OF REPRESENTATIVES

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WITNESSES

THURSDAY, JULY 2, 2009

APPENDIX

THE HOMEOWNERS' INSURANCE CRISIS: SOLUTIONS FOR HOMEOWNERS, COMMUNITIES, AND TAXPAYERS

Thursday, July 2, 2009

U.S. HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON OVERSIGHT
AND INVESTIGATIONS,
COMMITTEE ON FINANCIAL SERVICES,
Washington, D.C.

The subcommittee met, pursuant to notice, at 10 a.m., in the Commission Chambers, City Center, 401 Clematis Street, West Palm Beach, Florida, Hon. Dennis Moore [chairman of the subcommittee] presiding.

Members present: Representatives Moore and Klein.

Chairman MOORE OF KANSAS. Good morning. This field hearing of the Subcommittee on Oversight and Investigations of the House Financial Services Committee will come to order.

Our hearing this morning is entitled, "The Homeowners' Insurance Crisis: Solutions for Homeowners, Communities, and Taxpayers."

Before we get started, I want to say a word of thanks to the residents of West Palm Beach, Florida, for welcoming us here, as well as the people here at the City Center for letting us use your new facility for this field hearing today.

I would also like to thank Congressman Klein and his staff for their work in organizing this important field hearing.

At our last O&I Subcommittee hearing, we were forced to rush the proceedings because 28 roll call votes were called on the House Floor 5 minutes into the start of our hearing. The 28 votes actually turned into a day-long record of 53 roll call votes, but we had to wrap up the hearing very quickly, and the witnesses were kind of rushed to get their testimony in, with 2-minute statements each instead of the usual 5 minutes.

So to have a more robust discussion of the issues today, I decided to have our next hearing as far away from the Capitol as we could get during a work period so we wouldn't be interrupted by votes, but Congressman Klein should be forewarned that it won't preclude me from limiting him to 2 minutes. No, I'm teasing. I'm teasing.

In all seriousness, we will begin this morning's subcommittee hearing with members' opening statements up to 5 minutes per member, and there are two of us. And then we will hear testimony from our first panel of witnesses.

After that, members will have up to 5 minutes to question our witnesses and, if time permits, we may have a second round of questioning. We will then hear testimony from our second panel, have time for questions, and conclude with our third panel of witnesses testifying, with more time for questions.

Without objection, the opening statements of the members present will be made a part of the record. Without objection, I ask that written testimony from the Independent Insurance Agents and Brokers of America be entered into the record.

I now recognize myself for up to 5 minutes for an opening statement.

On May 4, 2007, at 9:45 p.m., Greensburg, Kansas, was hit by a Category 5 tornado. The tornado was estimated to be nearly 2 miles in width, and traveled for nearly 22 miles; 95 percent of that City was destroyed, with the other 5 percent severely damaged. The National Weather Service estimated winds of the tornado reached 205 miles per hour. I was invited by the Governor to go out and view the tornado just a couple of days after it happened. It was just unbelievable.

Thankfully, tornado sirens sounded in the City 20 minutes before the tornado struck, and a tornado emergency was issued, which undoubtedly saved many lives. This was the first tornado to be rated a Category 5 tornado since 1999. Former Kansas Governor Kathleen Sebelius, the HHS Secretary, as I said, took several of us out to view that disaster area.

Shortly after the storm, I joined my colleagues Congressman Jerry Moran and former Congresswoman Nancy Boyd on a visit there to meet with residents. We talked to people and heard what had happened.

During that visit, we attended local church services, had a meeting with local officials to discuss the successes and the problems with current relief efforts, toured the town to see firsthand the damage caused by the tornado, and participated in a USDA World Development Housing Rededication for the first facility to be rebuilt.

While the amount of damage was staggering, progress was already being made. In fact, I have been very impressed by how many people opened up their hearts and their wallets to help the people of Greensburg. That generosity has made a big difference in this little town in Kansas, and they were able to put their community and their lives back together.

It is a fact of life that catastrophic natural disasters will happen from time to time, and we need to be fully prepared. After the unacceptable response by FEMA to Hurricane Katrina, for example, we must ensure that our Federal Government is prepared to help in a time of need.

Hurricane Katrina caused $45.3 billion in insured losses. And, of the top 10 most costly insured catastrophes in the United States since 1989, 8 of the 10 were caused by hurricanes.

Today, we focus on how catastrophic natural disasters impact the affordability and the availability of homeowners' insurance, especially in places like here in West Palm Beach, Florida. This is a tough problem with no easy answers, but hopefully today's hearing will shed more light.

I appreciate the hard work of your Congressman Klein, who has put his thoughts and efforts into these issues. His work in carefully drafting the Homeowners' Defense Act is exhibited by the strong bi-partisan support the measure has received. I look forward to working with him in moving this legislature through this session of Congress.

I also look forward to hearing from our witnesses today, and the perspectives they bring to the table. We will hear from several different viewpoints of what these issues mean to real homeowners and to taxpayers.

We will also examine insurance industry coverage of catastrophic natural disasters, the withdrawal of insurance companies from offering policies in coastal areas, rising homeowners' insurance rates, premiums, and the resulting economic impact on State and local governments.

I will conclude by noting this is not just a Florida problem, by any means. California has had earthquakes; a number of States have been devastated by wildfires.

How these devastating tragedies impact the affordability and availability of homeowners' insurance is a national problem that demands a national response, in coordination with States that are most affected by these disasters.

I now recognize for 5 minutes a senior member of the subcommittee, and a leader in Congress on many financial issues, service issues, including the homeowners' insurance issues we are examining today, my colleague, representing the 22nd District of Florida, Representative Ron Klein.

Mr. KLEIN. I thank the chairman for your leadership, and thank you for taking time out of your schedule in Kansas to be with us during this week.

This is a great opportunity for those of us in our community to enter information into the record for Congress, for us to take back to Washington and give to our colleagues on the Committee on Financial Services and all the other committees, to give them the full balance of what is going on in the marketplace here in Florida.

But before I get into a couple of specifics, I would like to acknowledge and thank West Palm Beach Mayor Frankel and the City Commission for allowing us to use the building today, the chambers. I would also like to thank a whole number of people out in the audience, because many of you have been involved in the homeowners' insurance issue for many, many years now.

This is a great example of when people say, oh, things are developed in Washington with lobbyists and everything else. I will tell you the people who have been the biggest resource to me, and it is many of you in the audience here, as individuals, as individual homeowners, business owners, people who have had their own experiences.

We have come together with a whole lot of different meetings and task forces and study groups, and come up with a number of ideas which we have now taken to Tallahassee, and we are now taking up to Washington to try to solve a problem that, as the chairman said, is not just a Florida issue; it is a national issue in many capacities.

I just would like to do a little bit of overview. Many of us who are in the room today and live in our community did not live in West Palm Beach or Palm Beach County during Hurricane Andrew. Many people have moved here since then or have come from other places.

But—and surprising to say, for many people, that they are not aware that Hurricane Andrew was nowhere near West Palm Beach. It was in Florida City and Homestead. I live in Boca Raton; it was nowhere near us. And we had more damage from an unnamed storm after Hurricane Andrew came through than we did from Hurricane Andrew.

But the reality was, since that point in time, the insurance market in Florida has unfortunately become less and less stable. More and more companies have withdrawn, and we find ourselves in the position where the market is not what it should be, if at all available to the average consumer.

And one more note of history is after I was elected to the Florida Legislature right after Hurricane Andrew, so, I see Steve Geller here is someone I served with in the Legislature at the time, but we know that one of the first things we had to do was we had to come back in a special session and create something called the Joint Underwriting Association, the JUA, which was supposed to be a last resort agency, a government-backed agency for people who couldn't get private market insurance. Hopefully, it would go away in 2 or 3 years when the private market restored itself.

And yet, we find ourselves today in a place where the successor to the JUA, which is now called Citizens, which everyone knows what Citizens is, it is the largest underwriter of insurance in Florida. So it is supposed to have gone away, but it hasn't gone away. Unfortunately, we now have public-backed insurance as the largest scenario.

And that is exactly the opposite of where we want to be. We want private sector insurance coming in here.

Yet, at the same time, when I hear from consumers, I hear over and over and over again that if—I know that I paid my premium for the last 25 years to a particular insurance company, on time every single month, and yet when Hurricane Wilma came through, I had a $2,500 claim, and I had to call my insurance agent—and I appreciate the agents; they are the ones on the front lines. They are not making the decisions. But I had to call my agent so say if I file this, are they going to cancel me?

After paying tens of thousands of dollars in, a $2,500 claim, am I going to be canceled?

And in many cases, some of them were. Or some were canceled in the next insurance cycle. This is wrong. I think we all understand, you know, insurance companies are for-profit businesses, but we, as consumers, want to know that if we are doing our part on our side, that the insurance companies will stand behind us.

So I think there are a whole lot of issues out there that we can all hopefully work together and try to restore a market. What we have come up with in Washington, with a whole lot of input from many of you in this room here, and throughout the State and the country, is an idea which allows insurance to do what it is supposed to do—and, Mr. Chairman, I am hopeful that we are going to get a hearing on this as soon as we get back in the fall, after the August break—to literally pool insurance risk. But only among the States that want to do it. We are not going to obligate places in the United States where they feel like their insurance rates are just fine, the insurance markets are stable.

But there are 20-some States right now that have serious concerns, because insurance companies have pulled back. And I am just going to give quick examples. It is hurricanes, it is earthquakes—88 percent of the homes in California have no earthquake insurance. The California Earthquake Authority, which is a special group there, it is just too pricey, or they can't get it. It is just a very bad place, because when—it is not if, but when—the earthquake hits, we are talking about possibly $100 billion of recovery in that area.

Earthquakes, mudslides, firestorms, major ice storms, tornadoes, and it goes on and on. These are all areas where many insurance companies have withdrawn their coverage. So what we find is a lot of people going bare at a time when they need that coverage, their mortgage says they have to have that coverage.

So, Mr. Chairman, what we have tried to do is, in a bipartisan way, we put together a plan where we transfer that risk, for States that want to participate, over to an institutional bond arrangement where private investors fill that fund with their taking the risk on whether they will be repaid or not. They get interest, they get premium. We have tested this, and we believe that it is a viable solution to helping provide coverage on the upper highest end of catastrophe.

And, you know, for that, again, I appreciate the opportunity for us to take some testimony today, and to learn more about what people are saying so we can take this up to Washington, get it passed in the House, get it passed in the Senate, and present it to the President so we can get some relief around the United States.

Thank you, Mr. Chairman.

Chairman MOORE OF KANSAS. Thank you, Congressman Klein.

I am pleased to introduce our first panel of witnesses for this morning's hearing. First, we will hear from Dr. Ivan Itkin, a local resident from Fort Lauderdale.

Next, we will hear from Ms. Cynthia Shelton, president of the Florida Association of Realtors. Testifying next will be Mr. Joe Grillo—and please correct me if I mispronounce the name—senior vice president of Weekes & Callaway.

We also have Dr. Robert Detlefsen, vice president of public policy for the National Association of Mutual Insurance Companies.

And lastly, we will hear from Ms. Coleen Repetto, executive director of the Fair Insurance Rates in Monroe.

Without objection, your written statements will be made a part of the record, and you will each be recognized for a 5-minute statement summarizing your written testimony.

Mr. Itkin, you are recognized for 5 minutes, and please give us your testimony, sir.

STATEMENT OF IVAN ITKIN, RESIDENT OF FORT LAUDERDALE, FLORIDA

Mr. ITKIN. Thank you very much, Chairman Moore. And I would like to welcome you to south Florida.

Chairman MOORE OF KANSAS. Thank you.

Mr. ITKIN. We appreciate your coming and—

Chairman MOORE OF KANSAS. I am glad to be here.

Mr. ITKIN. —your concern that you have on this particular issue, which is a major concern for us. And I also want to thank Congressman Ronald Klein for his willingness to take on this issue, because it is extremely important for his constituents and for the other residents of Florida.

Having said that, I want to say good morning to you. I want to say good morning to you and to Congressman Klein, and hope that the House Financial Services Oversight and Investigations Subcommittee will be positive toward this issue as it bring this to the attention of our Members of Congress in Washington.

My name is Ivan Itkin. I live in a beachfront high-rise condominium building located at 3200 North Ocean Boulevard in the City of Fort Lauderdale. The building is 29 stories tall, with 220 residential units, and shares the 10-acre property with a similarly-sized building. The residents of the complex, like others in Florida, have great concerns over the availability of windstorm insurance.

With respect to my particular building, the condominium association has had great difficulty getting private hurricane insurance. Because of the possibility of hurricanes in our area, and the potential for causing significant and a widespread damage, private insurance companies are unwilling to insure against such outcomes.

Prior to the current policy year, we were able to obtain insurance from one carrier, QBE, which now refuses to insure our building unless impact glass is installed in all our windows and doors. Even installing hurricane shutters will not suffice, although the building was built to the code established just a few years ago.

As a consequence, we are forced to get insurance from the State-created insurer of last resort, Citizens Property Insurance Corporation, which is severely underfunded, and which will require large annual premium increases over a number of years from its policyholders.

The deductibles are so high that even if there is a major loss, there will be no recovery. For our building, the deductible is 5 percent of the building's appraised value of $85,243,600, which requires a loss to exceed $4.26 million before a single dollar can be recovered, even though our annual premium is $339,000.

It is quite obvious to us that we are not adequately protected. We need another solution. We need a catastrophic insurance program like National Flood Insurance, a program that will provide protection against all naturally occurring catastrophes.

I believe Congress needs to pass Federal NATCAT legislation.

Thank you for your attention, and I appreciate your taking the ball from here.

[The prepared statement of Mr. Itkin can be found on page 76 of the appendix.]

Chairman MOORE OF KANSAS. Thank you, Mr. Itkin, and I will say again to the witnesses, each of your written statements will be made a part of the record, and will be available to other Members of Congress as well. Ms. Shelton, you are next, please. Thank you.

STATEMENT OF CYNTHIA C. SHELTON, PRESIDENT, FLORIDA ASSOCIATION OF REALTORS

Ms. SHELTON. Thank you, Chairman Moore and Congressman Klein, for inviting me here today to speak before the Oversight and Investigations Subcommittee.

I am pleased to present the views of the Florida Association of Realtors on the issue of natural disaster insurance.

My name is Cynthia Shelton, and I am a Realtor from Lake Mary, Florida, which is the Orlando area. And I am current president of the Florida Association of Realtors. With me is our vice president and president for 2011, Pat Fitzgerald, from Jupiter, Florida.

The Florida Association of Realtors is the largest trade association in Florida. We represent more than 120,000 Realtor members—many of them are here in the room today—who are nvolved in all aspects of real estate including residential leasing, commercial investment property management, homeownership, appraisals, auctions, and much, much more, so we understand what our clients and customers and homeowners are going through.

The availability and affordability of property insurance is, at its core, a consumer issue. The importance of available and affordable insurance to homeowners, to commercial properties, to businesses, and to those who would like to own their home, investments, or place of business cannot be overstated. This is something that your constituents have long understood, since Floridians have dealt with the problem of insurance availability and affordability for many years.

Unfortunately, it is also something that is known to consumers nationwide, even those who are not in what we traditionally called disaster-prone areas. A strong real estate market is the linchpin of a healthy economy, one that generates jobs, wages, tax revenues, and the demand for goods and services.

In order to maintain a strong economy, the vitality of residential and commercial real estate must be safeguarded. Insurance availability and affordability concerns are not limited to Florida, or even to the Gulf Coast area. We have heard from Realtor colleagues from coast to coast, just like yourself, Chairman Moore, representing concerns about the availability and affordability of property insurance.

Like ours, their insurance concerns extend beyond homeowners' insurance, and include multi-family housing, businesses, and commercial property casualty insurance. It is no secret that insurance is a key component to the financing and purchasing of real estate. Without property casualty insurance, lenders will not lend. And when a policy is canceled or not renewed, property owners are typically in default of their mortgage terms.

The limited availability and high cost of insurance, therefore, not only threatens the ability of current property owners to hold onto their properties, but it also slows the rate of housing and commercial investment in these communities, and thus the economy. The inability to obtain affordable insurance is a serious threat to the real estate market, one we don't need any more than we have today. New home purchases, resale transactions, and housing affordability are affected in many of the following ways.

Homeowners' insurance is a necessary component in securing a mortgage and buying or selling a home. If a potential home buyer is unable to obtain or afford the required insurance, the sale will not be completed. As a result, potential home buyers are excluded from the market.

A home's value is another way. A home's value is directly tied to insurance cost. Homeowners are required by their mortgage lenders to not only pay for a full year in advance of closing on a home, but to maintain that homeownership regardless of what the ongoing costs are. And insurance that is expensive or unavailable devalues properties. Insurance costs impact renters and rent levels. Insurance costs incurred by multi-family property owners are ultimately passed on to their tenants through higher rents. This impacts housing affordability, particularly for low-income renters.

Our commercial members, of which I am one, have also experienced problems with commercial insurance, and availability and affordability of that insurance. Commercial property owners have experienced large increases in premiums, in some cases more than fourfold from the prior year, dramatically increasing the deductibles, as well, and, on top of that, less coverage.

Chairman MOORE OF KANSAS. Ms. Shelton, I will have to ask you to wind up your statement.

Ms. SHELTON. Yes.

Chairman MOORE OF KANSAS. Your time has expired, and your written statement will be made a part of the entire record—

Ms. SHELTON. Thank you.

Chairman MOORE OF KANSAS. —as well.

Ms. SHELTON. The glimmer of hope, we as Florida Realtors believe that it is time for Congress to consider a national natural disaster policy.

I cannot continue without acknowledging Congressman Klein and his support of prior bills, and of the one that is being introduced today.

Florida Realtors would like to see a healthy economy, and by having natural disaster insurance, I am sure that House Bill 2555 can address other issues that we will discuss, I am sure, at this hearing, such as mitigation and some other items that I think will help.

And we thank you, and the Florida Realtors and national Realtors are in support of this bill.

[The prepared statement of Ms. Shelton can be found on page 98 of the appendix.]

Chairman MOORE OF KANSAS. Thank you, Ms. Shelton. We will remind each of the witnesses, your statements will be received, obviously, for the record, but your written statements will also be a part of the record.

Mr. Grillo, you are next recognized for 5 minutes, sir.

STATEMENT OF JOSEPH A. GRILLO, CIC, SENIOR VICE PRESIDENT, WEEKES & CALLAWAY, INC.

Mr. GRILLO. I would like to also add my thanks for being invited to express my views today. I am representing that of a regional insurance agency. I am a senior vice president and sales manager, and part of the management team for Weekes & Callaway, which is a private agency. It has been in business since 1954, and is situated in Delray Beach. We have over 50 employees, and underwrite approximately $100 million in insurance premiums.

I have been a licensed agent in this State for 31 of the past 36 years, having only left it for a 5-year tour of duty in the State of Virginia. I did return, Congressman, before—just before Andrew, 2 weeks before Andrew occurred. So I have been here for most of the major events that have taken place.

Not that I should create panic, there are some small spots of bright news in that we have seen insurance rates, largely due to the mitigation credits, come down significantly over the past 2 years. However, this primarily takes care of the newer homes, and leaves out the older homes, which, obviously, need to be retrofitted. This is an area where I think the Federal or State Government can offer some relief and support in terms of grants, tax credits, and the like, to help other homeowners improve the risk. Improved risk will lead to better underwriting results, which should help to increase the affordability and availability of insurance.

The number of companies which have been underwriting in this State have actually increased in number, the private companies, although Citizens, as has already been pointed out, is by far the largest insurer in the State.

Well, that is just the good news. But the bad news is really more important. Our population growth has slowed significantly, and two of the main reasons have been property taxes and insurance. Florida is an area where a lot of retirees seek their final homes. And many have turned away, you know, for these very reasons. And we are now seeing the term half-back as a common reference, especially in the realty community.

Not that I am opposed to that. I am a vacation property owner in South Carolina myself.

However, having said that, insurance rates still remain at historical high levels. And the pressure is felt even more today with our problems with our economy on individuals and families as to affordability. Other than a handful of national insurers who will underwrite high-valued homes, we basically are void of all brand names in our marketplace. By brand names, I am talking about the State Farms, the Allstates, Hartfords, Travelers, and so forth.

We are left with a market consisting of start-up companies, most of whom have not been in business for more than 5 years, and who it might be questionable as to how well they could withstand a substantial hurricane, or perhaps even a less than substantial hurricane. We had seen, by benefit of our storms in 2004 and 2005, a number of those companies that couldn't make it financially as a result.

Obviously, this puts enormous pressure on our State catastrophe and guarantee funds, which ultimately leads back to the consumer. The few rated companies not Demotech rated, which is the rating given to those in business less than 5 years, who have been writing, are getting saturated with business. And this could very well threaten their future viability.

The good news of decreasing costs also carries some bad news, in that these companies, who are, in my opinion, marginally funded, will have less premium dollars to pay losses should a catastrophe occur.

There also remains severe restrictive underwriting in the V flood zones, and most of the companies that are writing are underwriting so on the basis of zip code saturation. So if you are fortunate enough to get into the company while there is open, you will get homeowners' insurance. Not speaking to the price, but availability. If they get saturated, they close it out, leaving a lot of people on the sideline.

In conclusion, we have availability and somewhat improved rates, but are sitting on a time bomb reliant on the weather; when and where will the wind blow. We do not have a long-term solution, and one can only imagine what would have happened here in Florida if Hurricane Ike had hit here instead of Texas.

Our key to the future, I think, is expanding our underwriting capacity, which must be done by having our brand names return to provide homeowners' coverage in our State. A free market competition economy will follow its own course, and lower costs over time, based upon underwriting results. This will only happen if they perceive they can control risk and have a reasonable expectation to earn a profit. This is where the Federal and State Government can and must provide vital support. As large as the insurance industry is, it is not sufficient to bear the entire risk. Catastrophic exposures due to population concentrations have become too significant.

If insurers are better able to measure risk with some caps on their exposure, through more affordable reinsurance, whether private or publicly sourced, they can assess their ability to put a portion of their assets at risk in such—in our catastrophic area, as well as others.

I do caveat, however, that regulation would be required, that the benefit of such a reinsurance plan is passed to the consumer and not retained in the profit coffers of the company.

Chairman MOORE OF KANSAS. Mr. Grillo, I am going to have to ask you to wind up—

Mr. GRILLO. Okay.

Chairman MOORE OF KANSAS. —your statement, sir.

Mr. GRILLO. Essentially, I am an open market person, but at the same time can see where the proposed legislation would have the Federal Government act as the conduit to better reinsurance costs.

With proper integration of the plan into the insurance mechanism, it is logical to believe that it would result in a better purchasing environment for the homeowner, which is what we all desire.

[The prepared statement of Mr. Grillo can be found on page 73 of the appendix.]

Chairman MOORE OF KANSAS. Thank you, sir. Dr. Detlefsen, you are recognized for 5 minutes, sir.

STATEMENT OF DR. ROBERT DETLEFSEN, VICE PRESIDENT OF PUBLIC POLICY, NATIONAL ASSOCIATION OF MUTUAL INSURANCE COMPANIES (NAMIC)

Mr. DETLEFSEN. Thank you, and good morning, Chairman Moore and Representative Klein.

I represent the National Association of Mutual Insurance Companies, a property casualty insurance association whose 1,400 members underwrite more than 40 percent of the property casualty insurance premium written in the United States.

Property insurance has, indeed, become more expensive and somewhat less available in the coastal regions of the United States. The reason for this is quite simple. The exposure of densely concentrated high-value property in certain geographic regions to relatively high levels of catastrophe risk means that property insurance in these regions will be expensive compared to regions that have lower levels of catastrophe risk.

Attempting to make property insurance in catastrophe-prone regions more affordable in high-risk areas, many States in hurricane-prone coastal regions, including Florida, impose rating and underwriting restrictions on property insurers that act as price ceilings on coverage.

While this rate suppression lowers the cost of insurance in the short term, it has long-term consequences that are far worse for insurance consumers. Government-mandated rate suppression lowers prices for people living in high-risk regions by requiring insurance buyers in low-risk regions to pay more, robbing Peter to pay Paul.

Further, inasmuch as higher insurance premiums serve as a powerful disincentive to further population growth and economic development in disaster-prone areas, insurance rate suppression perversely removes this disincentive. By distorting the public's perception of risk, rate suppression encourages the very phenomenon that created the problem in the first place, the growing concentration of people and wealth in high-risk regions.

Moreover, as the Wall Street Journal noted in an editorial published earlier this week, Florida's approach to insurance regulation "isn't even within a coastal mile of being actuarially sound. The State government acknowledges that in many high storm risk areas, the premiums are from 35 percent to 65 percent below what is needed to cover potential claims. That subsidy has made Governor Crist popular with many coastal residents, even as the State plays Russian roulette with the weather."

Rate suppression and underwriting restrictions are also largely responsible for the insurance availability problem in coastal areas. When government rate regulation prevents insurers from covering their costs, they may have no choice but to exit the market, as has happened here in Florida recently.

If the Florida approach is not the right way to solve the problem, what is? To answer that question, NAMIC has been working with a team of insurance experts at the Wharton School, as well as with a task force of its own members.

The Wharton team identified two key principles that should guide insurers and policymakers as they grapple with national disaster insurance issues. First, insurance premiums should be based on risk, to provide signals to individuals as to the hazards they face, and to encourage them to engage in cost-effective mitigation measures to reduce their vulnerability to catastrophes.

Second, any special treatment given to lower-income residents in hazard-prone areas who cannot afford the cost of living in those locations should come from general public funding, and not through insurance premium cost subsidies.

NAMIC's own statement of principles reflects these two key points, and identifies building codes and mitigation measures as two important additional ways to address disaster risk management issues. Thus, NAMIC supports two congressional bills, H.R. 2246 and H.R. 2592, that would encourage the use of strict building codes. We also support the mitigation grant provisions of Representative Klein's bill, the Homeowners' Defense Act. In fact, we would support more generous mitigation grants, because mitigation is one of the most effective ways both to reduce the individual's exposure to catastrophes, and to reduce his or her insurance costs. While NAMIC appreciates the work done by Representative Klein on this subject, we do not support the portions of the Homeowners' Defense Act that would build on State catastrophe funds, because such mechanisms invariably underprice the true risk-based cost of insurance.

We believe a better path would be to let the private market set risk-based insurance prices in order to create incentives for people to engage in risk mitigation and risk avoidance strategies. This leads to an important point. NAMIC recognizes that there are low-income people living in high-risk areas who simply could not afford risk-based premiums. Rather than distorting insurance markets to address this problem through rate suppression, NAMIC supports direct means-tested Federal subsidies to low-income residents of such areas, modeled on the Federal social welfare programs that provide Food Stamps and housing vouchers.

In conclusion, NAMIC realizes that property owners and insurers, mortgage lenders, Realtors, and home builders who live and do business in coastal areas will face serious challenges in the years ahead.

Congress can play a constructive role by reforming the National Flood Insurance Program, creating incentives for States to enact and enforce effective State-wide building codes, offering mitigation grants, and providing targeted subsidies that would enable low-income property owners to pay risk-based property insurance premiums.

Thank you for your kind attention—

Chairman MOORE OF KANSAS. Thank you.

Mr. DETLEFSEN. —and I would be happy to answer any questions you might have.

[The prepared statement of Dr. Detlefsen can be found on page 36 of the appendix.]

Chairman MOORE OF KANSAS. Thank you, sir. Ms. Repetto, please.

STATEMENT OF S. COLLEEN REPETTO, EXECUTIVE DIRECTOR, FAIR INSURANCE RATES IN MONROE (FIRM)

Ms. REPETTO. Thank you, Chairman Moore and Congressman Klein, for this opportunity.

My name is Colleen Repetto, and I am the executive director of FIRM, Fair Insurance Rates in Monroe, also known as the Florida Keys. We are a 501(c)(4) grassroots organization that began at a backyard barbecue in 2006, and has grown to more than 5,000 members countywide. We are run by volunteers, and we are funded by donations.

FIRM brought attention to the State-wide windstorm insurance prices by successfully challenging Citizens Property Insurance 2006 Monroe County rate filings. In 2004, a 1,900 square foot home, built to withstand 150-mile-an-hour winds, with hurricane protection, was paying $3,000 a year in windstorm premiums. By 2006, the same home was billed $15,900 for a 1-year premium, and had never had a wind claim.

As a result of our engineering, meteorological, geographical, statistical, and historical verified facts, which proved that our county had been charged excessive windstorm rates, the Office of Insurance Regulation rolled back our rates by 32 percent.

The rate was not the only issue. A Florida law allowing insurance companies to bill, and then file them for approval, was devastating to our policyholders. At the extremely high rates, people were receiving invoices from $9,000 to $25,000 for 1 year's premium on an insurance policy that, in the Keys, because we build to the highest, strongest building codes in the State, it was highly unlikely that the majority of our insureds would ever have damage greater than their deductible, and therefore, have no claim against the policy.

FIRM lobbied our State legislators to help repeal, although temporarily, the Use and File Law. Insurance companies currently must file their rates with the OIR before billing their policyholders. We continue to press to make File and Use a permanent law.

Contrary to popular perception, Monroe County is not a wealthy county. We have many low- and middle-income residents who could not afford this insurance, and were in distress at how they would provide the coverage that was required by their mortgages.

Currently, risk models used in setting rates do not separate wind and flood, and, therefore, do not accurately reflect probable maximum loss for each peril. There is no all-risk hurricane insurance. Wind is provided by State or private insurers, and flood is a Federal program. Claims can be delayed for years, until the damage is proportionately assessed, which cause additional financial burdens for property owners trying to get their lives back on track after a devastating storm.

We feel strongly that Federal funds, which are really all taxpayer dollars, should not be the first line of financial relief for natural disasters.

The National Climatic Data Center, a division of NOAA, tracks and evaluates natural catastrophic events that have great economic and societal impacts. In 2008 alone, $58,000,000,000 for insured and uninsured properties was spent in 44 States before the ice storms in the Northeast in December.

FIRM believes in personal responsibility, especially in high-risk areas. Property owners should strengthen their buildings to meet or exceed their regional perils, and buy insurance. All-risk policies could be provided by private insurance companies, capping their losses, followed by State catastrophe funds paying all-risk claims to their cap loss, with a Federal financial obligation guaranteed to kick in as a backstop.

Consumers need to be educated on the cost-savings benefits of strong building and mitigation, and offered low-interest loans or grants to better withstand the high risk.

Local governments have a responsibility to properly and appropriately develop land use regulations, and enforce building codes. Windfall tax dollars generated by rebuilding and repairs after a storm should be used to build State CAT funds—fund reserves, fund mitigation programs, and/or reduce premiums in the areas where they are collected. These unanticipated sales tax revenues should not be allowed to be deposited into general funds for use in any other way.

All in all, a comprehensive, multi-level, all-risk catastrophic insurance program needs to be implemented to preserve assets, protect the lives of our citizens, and maintain stable communities.

And we are very grateful to you to allow us to participate and tell our story.

Thank you.

[The prepared statement of Ms. Repetto can be found on page 82 of the appendix.]

Chairman MOORE OF KANSAS. Thank you, Ms. Repetto.

We would like to begin our questioning now. And, again, we are going to have limits here, because we have a couple of other panels who need to testify.

But, Mr. Itkin, I want to thank you for testifying, sir, and ask you a question. From your perspective, sir, who should bear the cost of disaster assistance after a natural catastrophe? Should it be the local residents, the insurance industry, the government, or some combination of the three?

Mr. ITKIN. Well, I think it has to deal with—that we have to pool our responsibilities for this particular situation, like a catastrophe, if it occurs.

You know, there are a lot of places around this country where they do have naturally occurring damages from tornadoes and from hurricanes. We tried to address at least people who had flood problems by enacting national flood insurance.

I think what is required is a national program which then can take control and provide for adequate premiums nationwide that will cover the costs of, you know, occasional damages that come in various locales.

I think it is just important. Like that is what basically insurance is. It is spreading the risk. And I think it is—in our situation, we don't have a—much yet, much tornado damage, and so—but there are people who do have tornado damage, and they suffer huge losses. So there has to be some way of combining people with their risk, having risk.

Chairman MOORE OF KANSAS. Thank you, sir. Ms. Repetto, do you have any additional comments on that question?

Ms. REPETTO. Well, we believe in a four-tiered approach. First of all, I think, because we are a consumer group, we always feel left out of the—when people talk about this.

The four-tiered approach is basically policyholders pay insurance companies for a product and a service. Before anyone else pays, when there is damage, we have to pay our deductible. So we kind of pay twice. We pay a premium for something we hope we never have to use, and I am sure the insurance companies feel the same way, but we, in our case, we had a homeowner who had her property insured, her building insured for $850,000. Now, that is a significant property. She had a 10 percent deductible with windstorm. Her premium, after she took the 10 percent deductible, was $18,000.

When you add the premium of $18,000, which is out-of-pocket, to a 10 percent deductible should she have a catastrophic loss, you are talking about this family having $103,000 out-of-pocket before they had ever filed.

So the four-tier approach is the policyholders, I absolutely believe everyone should buy insurance. You pay your deductible, you would pay—you would then go to the insurance company to pay the claim.

Beyond that, I think the insurance companies could have an all-risk policy that they cap the losses; then it could be a State catastrophe fund, cap loss; and then the Federal guarantee on top of that as a backstop.

Thank you.

Chairman MOORE OF KANSAS. Thank you very much.

Ms. Shelton, does the cost or availability of homeowners' insurance have an impact on home prices in your community across Florida?

Ms. SHELTON. Yes, sir, it does in many ways. And I will use an example right now. My daughter just bought a home in Tallahassee. The insurance policy on an 1,100 square foot home is—I had three quotes: one was $900; one was $1,200; and one was $1,500. The $900 is fairly less insurance, but if you look at that, that is over $100 a month on the average, if you use the middle ground there, that affects, on a $550 house payment, an additional $100 is going to go to insurance, not counting the tax base. So I would tell you that it affects probably the affordability of not only the average or affordable home price range, that is where it seems to get hit the hardest, but it also affects all across. Like we are still paying for Katrina right now. And so at some point, we have to realize, whether we are paying it for through taxes, through Congress in other ways, or, here in Florida, as an individual homeowner, I would tell you it is affecting the pricing of homes, as well as commercial properties across our State.

Chairman MOORE OF KANSAS. Thank you. And my time is about up. I am going to now yield to Congressman Klein for 5 minutes of questions.

Mr. KLEIN. Thank you, Mr. Chairman. And I thank all of you for coming today and taking time out of your busy lives to share with us your experience. As I was listening, Mr. Chairman, to the conversations here, if we were anywhere in the United States that has had insurance problems, it would probably be the Realtors, the insurance agents, the homeowners coming together—the home builders, all talking about building codes, and mitigation, and costs, and spreading the risk; it would be the same conversation. So I think this is somewhat representative of a problem that we see all over the United States, even though this particular meeting is taking place here in West Palm. I think we all share, and, Doctor, I think you had mentioned where we share the interest in mitigation and exposure.

As a Realtor, if you could just start out with telling me the kinds of impacts you think that mitigation—and that responsibility for mitigation. Do you think homeowners take that certainly? And, certainly, if insurance was incentivizing, taking responsibility, whether it is window issues, securing the trusses, all those kinds of things. Can you just share with us what your thinking is on how mitigation plays into stabilizing our insurance system?

Ms. SHELTON. Well, first of all, the mitigation plans that we are looking at right now, including the one that you are building, we believe you have to build strong homes. If you are going to build on the coast, you need to build a strong home on the coast, whether it is the shutters, or whatever it is going to take to protect, to prevent against loss. That is a cost, if you know up front, Congressman Klein, that you know is going to be an issue, you can plan. You know, I can't afford this property if the cost to build it to codes or mitigate it to be stronger is too expensive. I will look at other alternatives in other areas. What happens, though, is, currently, mitigation isn't really given credit on anything other than homes. If you start looking at the commercial properties, it doesn't matter how well you build it; you do not get a break on commercial properties.

Mr. KLEIN. Have we incentivized enough, I mean, from the insurance point of view, as—

Ms. SHELTON. No.

Mr. KLEIN. —a consumer, the investing? They are expensive propositions—

Ms. SHELTON. They are very—

Mr. KLEIN. —for retrofitting.

Ms. SHELTON. They are very expensive. And if you think about the average homeowner, just getting into a home in today's economy, to tell them—not new construction. I sincerely believe new construction, we have to build to better standards.

Mr. KLEIN. Okay.

Ms. SHELTON. Without a doubt. I do think some areas of the State have done that. Some have not. I think around the country, there are different things. If your house floods, why would you continue to build it in the same area? So I think there are things we have to take responsibility for individually. I do think the cost of mitigation for existing properties is astronomical. It is sometimes not worth taking that funds and put into it. You might as well set it aside and wait for the catastrophe to hit, and use it then, because it is just not practical to do so. I do think some of the credits have helped.

Mr. KLEIN. Can we—Mr. Grillo, can we, and should we, be doing more as a government, as a private sector, as an insurance underwriter, do more to incentivize investing in mitigation?

Mr. GRILLO. Absolutely. And that was part of my opening statements. The problem we have is those who are moderate- to higher-income can afford to take these steps in terms of the new construction, and also in terms of retrofitting of their homes. But we have people who are not necessarily low income. Take my daughter, for example. She is a teacher, and her husband, until a year-and-a-half ago, earned his living in the construction business, which is, of course, really underwater right now, so to speak. But if you look at just her salary as a teacher, she earned too much to gain much assistance from many of the programs currently available. Yet, when you take her salary and you net it down to what the net income is, it doesn't leave a lot left over to pay for major renovations of a home, of a retrofit of a roof; if it is an older home and didn't have the benefit of shutters, to invest in shutters. These are expensive propositions when people are trying to put food on the table.

Mr. KLEIN. Mr. Chairman, one more question?

Chairman MOORE OF KANSAS. Certainly.

Mr. KLEIN. Dr. Detlefsen, I share with you your—and I think most of us share the view on mitigation and reducing exposure. That is good for everyone. It is good for whomever is involved in this process: Homeowners, in terms of deductibles, and the insurance underwriters, as well as any government involvement. Where I differ, respectfully, with your view on the risk side is I would agree with your statement that we want to assess this based on risk. There have been proposals in Florida, if you follow the Florida Legislature, about deregulating insurance and letting the market go wherever it needs to go. There are a lot of problems with that, and certainly that doesn't provide, necessarily, the fact that insurance companies will sell in areas where we need insurance. And I think, as a public policy, we all understand the necessity for mortgages, and for people's peace of mind, you know, they can get insurance at a reasonable price, based on risk.

Here is my problem with just the comment about risk. Florida, a number of years ago, the Florida Legislature allowed I–95 to be an east/west point of demarcation for windstorm. If I could just finish this.

Chairman MOORE OF KANSAS. Certainly.

Mr. KLEIN. I appreciate that opportunity. I like to call that the I–95 Mountain Range. Now, the I–95 Mountain Range is not a real mountain range; it is a road that was constructed wherever they had the land to do it. But on the east side, there is presumably a higher risk on one side, and on the west side, there is a different risk. And yet, in the last four hurricanes we had in Florida, a lot more damage, because the hurricanes came from the west, than any kind of storm surge or anything on the east side. And it is not a question of more—higher property values or lower property values. It is an artificial designation. Now, risk is—how will we define it, you know? And most of the damage in Florida has been more inland. So just share with me, you know, how we get our arms around the risk. Because I think we agree on the assumption, but we are—you know, it is how you define it, and how you get to that point that people understand that you pay more if it truly is a higher risk.

Chairman MOORE OF KANSAS. And, Dr. Detlefsen, our time is up. So I am going to ask you to respond, if you can, within 30 seconds, and then submit whatever written statements you would like for the record. It will be part of the record.

Mr. DETLEFSEN. Representative Klein, I would agree with you that the I–95 divide is irrational and not an actuarially valid basis for distinguishing high-risk and low-risk regions. But, as you pointed out, that was an artificial construct that was created by the legislature.

Mr. KLEIN. Requested by the insurance industry. It was not—the Florida Legislature didn't come up with this on its own. It was the insurance industry that came and said we need this, that is the divide. I was there at the time.

Mr. DETLEFSEN. Well, but that is because they are not allowed to charge based on risk, and so with—in regard to individual areas that have high risk relative to other areas, and so they needed some way of being able to recoup the cost of insuring in the higher risk regions by charging more in other regions. And this apparently was what the legislature was willing to allow them to do. It is certainly not an ideal situation from the standpoint of the insurance industry.

Chairman MOORE OF KANSAS. I am going to have to close this panel down. I would invite each of you, if you have additional information you would like to provide to the members here, to submit written statements. They will be made a part of the record and considered. And I thank you very, very much for testifying. I excuse you, and I would like to invite the second panel to come up to testify. Please take your seats, and, again, thanks for testifying.

Ray Spudeck, if you would, please. I am pleased to introduce our second panel of witnesses for this morning's hearing. For this panel, we will hear from former Florida State Senator of the 31st District, and the former president of the National Conference of Insurance Legislators, the Honorable Steven Geller.

I am also pleased to introduce Dr. Ray Spudeck, chief economist in the Florida Office of Insurance Regulation.

Without objection, gentlemen, your written statements will be made a part of the record. You will each be recognized for a 5-minute statement summarizing your written statements. And, Senator Geller, you are recognized for 5 minutes, sir.

STATEMENT OF THE HONORABLE STEVEN GELLER, FORMER FLORIDA STATE SENATOR, AND FORMER PRESIDENT, NATIONAL CONFERENCE OF INSURANCE LEGISLATORS

Mr. GELLER. Thank you, Mr. Chairman. And I would love to spend an hour debating the gentleman from NAMIC.

Congressman Klein, I was the Chair of the Property and Casualty Subcommittee when Hurricane Andrew struck, so I am happy to go over that with you.

Good morning. I am Senator Steve Geller. Until I retired in November, I was the minority leader of the Florida Senate. I am past national president of the National Conference of Insurance Legislators, and chaired the Natural Disaster Subcommittee. I believe that a national natural disaster program of some type is absolutely critical. Some type of Federal backstop, such as the Terrorism Risk Insurance Act, is necessary for natural disasters. Expanding the National Flood Insurance Program to cover all natural disasters would also work.

I know from my days at NCOIL that many of my legislative colleagues asked why their constituents should pay so that a few wealthy people can live on the coast. It is not an issue of a few wealthy people living on the coast. Many of my former constituents in Century Village, Pembroke Pines, a senior community located much closer to the Everglades than to the ocean, will tell you that they can't make ends meet because of the high cost of windstorm insurance. Close to 80 percent of the population of the State of Florida lives in our 35 coastal counties. And no part of the State is more than 80 miles from the coast. And it is not just a Florida issue.

Mr. Chairman, I have a DVD that I would like to enter as a supplement to my remarks.

Chairman MOORE OF KANSAS. That will be received in the record.

Mr. GELLER. Thank you, sir. It is the introductions to 20 episodes of the Weather Channel television series, "It Could Happen Tomorrow." Each of the 20 episodes deals with natural disasters that could occur tomorrow, causing anywhere from hundreds of deaths to hundreds of thousands of deaths, from billions of dollars in damages to hundreds of billions of damage. And they are all over the country. They include wildfires, floods, earthquakes, hurricanes, a volcano, and tornadoes.

Mr. Chairman, it is a national issue. If any of the natural disasters that I mentioned occur, Congress will have to step in, or else face a collapse of the financial system. If a natural disaster costing $100 billion or more occurs, and Congress does nothing, the insurance industry will become insolvent. If the insurance industry can't pay off homeowners' policies on homes that have been destroyed, the banks that loaned money on those homes without insurance will fail. Is this starting to sound familiar?

The insurance industry is dealing with both actuarial risk and time risk. If there is a 1-in-100-year event that would cost $100 billion, the industry could charge $1,000,000 a year—I apologize. That would cost $100,000,000, the industry could charge $1,000,000 a year for 100 years for reserves, and that number will be actuarially sound. However, because of time risk, the insurance industry is trying to raise that hundred billion dollars as soon as possible, which raises rates to an impossible amount. And I don't blame the industry for trying to do this. Only the Federal Government can absorb the time risk while charging actuarially sound rates.

Let me give you some concrete examples of how great these savings could be if Congress steps in and eliminates the time risk.

In Florida, the State CAT fund charges rates approximately 78 percent to 90 percent less than private reinsurers. Because they have post-claim funding, they can eliminate the time risk. In Florida, over 50 percent of all windstorm dollars go directly to pay for reinsurance. In south Florida and other coastal areas, this number is much higher, up to 80 percent or 90 percent. Using simple math, we see that the total windstorm rates in south Florida could be reduced by 60 to 65 percent with an appropriate Federal program. I believe that the high cost of windstorm insurance is the single biggest issue in the State of Florida today. Many people pay more in homeowners' insurance than they do on their mortgage or property taxes. Businesses have to raise their prices to pay for the high cost of windstorm insurance.

The root of our current financial mess is the housing crisis. Congress has been working on ways to keep people in their homes. When people pay as much for homeowners' insurance as they do for their mortgage, a large reduction in their insurance rates helps far more than a cut in their mortgage payments. Let me repeat this. In many areas of the country, the single best thing that Congress can do to keep people in their homes is to pass a natural disaster bill. The best stimulus package that we can pass is not sending everybody $200. It is reducing their insurance premiums by hundreds or thousands of dollars a year. Let the consumer spend those savings in restaurants and stores, and we will have a much greater stimulus package than what Congress passed.

Chairman MOORE OF KANSAS. I am going to have to ask you to wind up, sir.

Mr. GELLER. Yes, sir, I will. And let's improve our balance of trade. The majority of the reinsurers are in foreign countries. Swiss Re, Hanover Re, Munich Re, Bermuda Lloyd's. Let's keep our American dollars in the American economy, instead of sending them overseas. No State can handle this alone. We have done our part.

Mr. Chairman, we thank you, and we hope that the Federal Government will help us out here.

[The prepared statement of Mr. Geller can be found on page 66 of the appendix.]

Chairman MOORE OF KANSAS. Thank you, Senator. Dr. Spudeck, you are recognized for 5 minutes, sir.

STATEMENT OF DR. RAYMOND SPUDECK, CHIEF ECONOMIST, FLORIDA OFFICE OF INSURANCE REGULATION

Mr. SPUDECK. Chairman Moore, Congressman Klein, on behalf of the Florida Insurance Commissioner, Kevin McCarty, I thank you for the opportunity to have the Office of Insurance Regulation testify before you today on what is probably the single most important issue to the Florida economy. My name is Ray Spudeck. I am the chief economist for the Florida Office of Insurance Regulation.

In addition to dealing with this issue on an ongoing basis for Florida, which is why I think I look pretty good for a 20-year-old man, I also have worked very closely in the national debate on this issue, both within the Federal Government and with agencies of the Federal Government, and with the National Association of Insurance Commissioners.

If I could, I think there are some things, as we talk about this issue, that we could agree on. First and foremost, we can't stop the ground from shaking, we can't stop the hurricanes from making landfall, and we can't stop the rivers from breaching. What we can do is ensure that we are prepared before that happens, that we are there, boots on the ground, ready to solve the problem immediately after it happens, and that we have a system that will speed the economic recovery.

Along those lines, it is Florida's loss, but I do believe it is the country's gain with Craig Fugate now moving to manage FEMA and direct FEMA. He is responsible for, I think, what we have as one of the best first responder systems that is available. And we have shared that with other States as they have needed it for natural disasters. That is first and foremost, and I think we can all agree on that.

Secondly, I would think most would agree that the economic recovery and the single most important thing that speeds an economic recovery is, in fact, the insurance mechanism. If people can't get their homes repaired, they can't come home, and they can't go to work. They also can't go to work if the building—if the place where they work hasn't been repaired, or if the schools are not repaired and being opened. Insurance is the engine that drives that, however that insurance is financed. So, critically, that is important, because there is a direct link between the risk of loss and repair of a specific building. It is much easier to talk about repairing your office building or repairing your home than it is saying, here is a bunch of money, here is a city; now, how do we want to repair it. We have seen signs of that economic recovery, both good and bad, in different cities around the country, around the Nation, over the last decade, and we will continue to see that.

Now, the question of how that is financed and the framework in which that insurance is provided leads to some discrepancies. As noted obliquely, we have entirely different systems for how we do this risk, and how we insure this risk, and how we create this insurance mechanism, depending on the type of risk. That, in turn, leads to how we recover for this type of risk. If the catastrophe is a hurricane, we insure that right now in the private sector, in some cases with help from the States, and what we notice is that claims do get paid, by and large, and economies can and communities do get recovered.

We do see some issues I will talk about with that market as I move forward, but that does seem to happen. If the next event, or if the major catastrophe is an earthquake, well, we are going to have an entirely different story. The good news is there won't be much insured loss, because, as Congressman Klein noted, since it is an optional cover in most insurance contracts, including those that, by the way, are guaranteed by the Federal mortgage agencies, there is not going to be much of an insurance loss. There is going to be economic devastation.

A modeling firm recently estimated that a repeat of the 1906 San Francisco earthquake would create—and the headlines all read—between \$50- and \$80,000,000,000 worth of insured losses. The next line of that report did not make the headlines, but suggested there would have been, actually, about \$250,000,000,000 worth of insured losses. And I am pretty sure we know how that is going to be recovered and that is going to get paid. It is going to get paid for by the American taxpayer.

In the case of flood insurance, every time the flood breaks, it costs somebody money. And, generally, it doesn't cost the people who have the floods themselves. And we see that different ways. I mean, we have a system currently; we are familiar with that in Florida. According to the Government Accountability Office, over the last 30 years, Floridians have paid in \$10,000,000,000 more than they have taken out in losses. We could have used that \$330,000,000 a year to do a lot of other things for our own markets.

Again, a huge limit on—a huge bill, and a huge bill for the American taxpayer.

So, in contrast to a lot of the critics of the work that you are trying to do, Congressman Klein, or the work that is trying to be done in the House this year, I would argue that the only publicly subsidized system that we have for dealing with catastrophic insurance risk is the one we currently have in place. Now, I think the private market works. I think there are issues, and I think there are areas where the government could get involved. And I will try and be brief. What we notice following a severe event is that there are disruptions to the marketplace. There is a volatility in the availability and pricing of insurance that in many cases makes it impossible. People are certainly saying that now.

In Florida, we were probably, most would argue, getting close to an equilibrium before the 2004–2005 hurricanes. That is completely gone now. In 2006, we saw, and this obliquely contradicts Dr. Detlefsen's question, surplus line companies, companies that are unregulated as to form and rate, actually canceling policies in mid-term, because they could no longer take the cover.

Nationally, as noted, the national insurance companies, the large insurance companies, have retreated from the coast. Not only the coast, they have retreated from catastrophic risk in all areas. Since 2000, the amount of insured exposure that has gone into residual markets nationwide has risen from $113,000,000,000 in 2000 to $670,000,000,000 in 2007. I am somewhat happy to report that, actually, Florida is reversing that trend. We are actually taking policies out of Citizens, and moving them in. What can the Federal Government do, I think, to try and close up—

Chairman MOORE OF KANSAS. Dr. Spudeck, I am going to have to ask you to wind up, and you can submit your written statement for the record, please, sir.

Mr. SPUDECK. I will do that.

Chairman MOORE OF KANSAS. Thank you.

Mr. SPUDECK. If I can just—to finish up, there are things the Federal Government can do. Mitigation is important. We all agree on that. Federal—you guys—Federal Government guarantees a lot of mortgages. Why insurance isn't covered, why homes aren't built is not clear to me at all. Catastrophe reserves, the Internal Revenue Tax Code, you guys control that, not us. I think that can build reserves. And back up plans moving forward that don't disrupt the private market I think are important.

We look forward to working with you, and I am happy to answer any questions.

[The prepared statement of Dr. Spudeck can be found on page 103 of the appendix.]

Chairman MOORE OF KANSAS. Thank you. And I will recognize myself for 5 minutes for questions. And, again, each of you will have an opportunity to submit any additional comments you would like to make for the record. We would appreciate that.

What kind of impact, in terms of—well, what kind of impact is the present system going to have on property values in Florida if nothing is done by the Federal Government about what the Congressman and I are talking about here, something in that area? And I will direct first to you, Dr. Spudeck.

Mr. SPUDECK. Well, there are two things that are going to happen. First of all, as it becomes increasingly difficult to insure unmitigated homes, we recognize that if it continues the way it goes there are going to—there will likely be properties that are just: A, uninsurable; and B, unsalable. The average age of a home in Florida is between 24 and 25 years old. That predates most of the modern building codes. We tried to develop a mitigation program and a My Safe Florida Home Program. That has been very successful. The current economic situation has limited the amount of budget to that program from the State level. I think that is—otherwise, yes, I mean, we have an awful lot of older homes that aren't mitigated. These are interior homes, you know.

Chairman MOORE OF KANSAS. Do you agree, Senator, or have any additional comments, sir?

Mr. GELLER. Yes, Congressman. The current system is just devastating for home values, as you heard the Realtors talk. You are required to have insurance to purchase a home. If insurance is unavailable or unaffordable, then it devalues the home. Today, if you are—not even if you are on the water, if you are close to the water, if you are blocks and blocks away, you can be paying more, far more for your insurance than you are for your mortgage or your taxes. If you are close to the water, you could pay more for insurance than the two of them combined. People can't afford that. If they can't afford the home, they won't buy the home. That drives the value down.

And, again, we are not asking Congress to assume actuarial risk. Just assuming the time risk will solve much of this problem.

Chairman MOORE OF KANSAS. I am going to yield now to my colleague for 5 minutes for questions. Congressman?

Mr. KLEIN. Thank you, Mr. Chairman. And thank you, gentlemen, for being here today and sharing with us your experience. Let's start with Senator Geller.

One of the things that we are talking about is the whole risk assessment and whether doing something which helps to stabilize the insurance market encourages bad behavior. You know, people building in coastal areas. We know in Florida, and many parts of the United States, a large percent of our population, in the entire country, lives close to water.

Mr. GELLER. Yes, sir.

Mr. KLEIN. On the coast, and other places. So we have an existing issue. It is not like you can just wipe that away and pretend like it is not there and say, well, all those people just have to fend for themselves. We are trying to—we have a public policy that says that insurance is good, and we want to do that.

Can you just share with us whether your view of this is that there is a crowd-out issue here if we do something like create a national risk catastrophe pool.

Mr. GELLER. Not at all, Congressman. The problem here, as you pointed out, what some people say, oh, don't build near the water. All right. So let's eliminate Miami Beach, let's eliminate Fort Lauderdale, let's eliminate Palm Beach. That is not going to happen. And 80 percent of our population in Florida lives in the coastal counties. People living near the water today pay more. They should pay more. According to actuarial models, it is higher risk. Our problem isn't most hurricanes. Our problem is the unpredictable, 1-in-100-, 1-in-150-, 1-in-200-year disaster. That is the same reason you passed TRIA. You can't model for something that you can't predict. And you just can't predict the damages for a 1-in-200-year earthquake. You can't model for what is going to happen when the New Madrid Fault goes. And that is in the State right next to yours, Mr. Chairman. And so what's going to happen when all of these occur, it is impossible to model damages. We think that if you—the State and the private market can deal with the predictable 1-in-10-, 1-in-20-, 1-in-50-year events. All we are asking for is the unpredictable mega disaster, because right now, the insurance industry is trying to charge for an event that probably will not occur in the lifetime of anyone in this room.

Mr. KLEIN. Mr. Chairman, if I can just share with you a conversation I had with Steve Israel?

Chairman MOORE OF KANSAS. Certainly.

Mr. KLEIN. Steve Israel is a colleague of ours from Long Island in New York. And he got involved in our legislation because he started hearing from a lot of his constituents who were getting letters from a national insurance underwriter saying something to the effect of we are overdue for the big one, and—meaning a hurricane that sort of travels up the coast and hits Long Island—and, as a result of that, we are non-renewing, we are just canceling or not issuing new policies, and canceling old policies as they come up for renewal, in large scale in that area. So he all of a sudden was getting the same phone calls that we get here in Florida and other places where they couldn't get policies and national underwriters would come in. And here was just the speculation that maybe over time there is going to be a very bad storm.

Yes, and I think that is very helpful in understanding the question of crowd-out. Again, it is a matter of understanding risk. Everyone understands there are certain places in the country that are going to pay more. We get it. We are looking for stability, that there is a predictability and stability. We need to know that there is mitigation responsibility in homeowners, so the Category 1, 2, or 3, in the form of a storm like ours is probably not as damaging, other than trees falling over, maybe some minor damage. In California, if homes are built to earthquake standards, that many of the homes can be fortified and built to new standards. I am all for the building codes. And I think that is probably the right thing.

Mr. Chairman, if I can also, very briefly—

Chairman MOORE OF KANSAS. Certainly.

Mr. KLEIN. —acknowledge, there are a number of people in the audience who are elected officials and others. I just want to—since they are here, I want to acknowledge them. State Representative Kelly Skidmore is here. We also have Commissioner Mack Bernard from Delray Beach.

Chairman MOORE OF KANSAS. Yes.

Mr. KLEIN. And we have a representative from State Representative Joe Abruzzo's Office here. Barbara Zee and Ken Lassiter are here from COBRA. Long time friends, and people who have been very involved from the very beginning of these issues. I just wanted to acknowledge and thank them for their involvement and their interest.

Mr. GELLER. Mr. Chairman?

Chairman MOORE OF KANSAS. Yes, sir?

Mr. GELLER. May I briefly comment, 30 seconds or less, on what Congressman Klein—

Chairman MOORE OF KANSAS. 30 second or less, yes, sir.

Mr. GELLER. Congressman Klein, we found from COIL the most expensive natural—the most expensive hurricane won't hit Florida. It will hit New Jersey on its way up to New York. The same problems we are having here right now, Houston, coastal Texas, the entire Gulf Coast, as you mentioned, New York, New England. It is not a Florida issue. These same issues are occurring everywhere around the country. Not in California, simply because they are not buying insurance. But the most expensive natural disaster is clearly not in Florida.

Thank you, Mr. Chairman.

Chairman MOORE OF KANSAS. I thank the witnesses for their statements, and this panel is now excused. And I will invite our third and final panel to take their seats, please.

Good afternoon. I am very pleased to introduce our final panel of witnesses for this morning's hearing. For this panel, we will hear from retired Admiral James M. Loy, former Commandant of the United States Coast Guard, and former Deputy Secretary of the U.S. Department of Homeland Security.

And second, but certainly not least, we will hear from Ms. Vicki Williams, outreach coordinator for the My Safe Florida Home Program.

Without objection, I will state to the witnesses that your written statements will be made a part of the record, and you will each be recognized for a 5-minute statement summarizing your written statements.

Admiral Loy, you are recognized, sir, for 5 minutes. I appreciate your being here today.

STATEMENT OF ADMIRAL JAMES M. LOY, USCG (RET.), FORMER COMMANDANT OF THE U.S. COAST GUARD; FORMER DEPUTY SECRETARY OF THE U.S. DEPARTMENT OF HOMELAND SECURITY; AND NATIONAL CO-CHAIRMAN, PROTECTINGAMERICA.ORG

Admiral LOY. Thank you, Mr. Chairman, and thank you for your long service of effort focused on your constituents, and specifically your work on national preparedness.

Chairman MOORE OF KANSAS. Thank you.

Admiral LOY. Mr. Klein, your thoughtful and constant leadership on this legislation is important to all of us. With my 5 minutes, I am going to try to just do two things.

Chairman MOORE OF KANSAS. One moment. Can you just move the microphone a little closer, sir? Thank you.

Admiral LOY. Sketch quickly the ProtectingAmerica.org agenda, and then perhaps a couple comments on H.R. 2555, the Homeland Defense Act of 2009. PA.org is a national campaign co-chaired by my colleague, James Lee Witt, and myself. Our coalition now numbers about 300-plus organizations and over 20,000 individual members. We count the American Red Cross, the International Association of Fire Chiefs, insurance companies, emergency managers, small businesses, and Fortune 100 companies among our members, and we represent every State in the Nation. We came together in 2005 to raise the national awareness concerning our collective responsibility to prepare and protect American, and specifically American homeowners, from natural catastrophes. And especially, as, Senator Geller, on your last panel, focused in on mega natural catastrophes. We have discussed these issues with thousands of Americans, and have come to focus on two fundamental ideas.

First, we need a comprehensive and integrated public/private partnership to prepare and protect homeowners. It is not just about insurance, it is not just about mitigation, it is not just about public education, but all of those things, integrated together.

Second, we need affordable and available homeowners' insurance across our country. As to the first, the comprehensive solution, in my mind, needs to have four parts: A modified insurance construct along the lines that we have spoken about already this morning with your other panel members, that includes State and national level catastrophe funds; a strong mitigation effort that includes meaningful building codes, meaningful land use policies, and the strong enforcement of both; impactful public education programs that convince homeowners and convince families, and businesses, and communities to act decisively on these preparedness opportunities that are provided to them; and then first responder support, knowing full well that in any of these instances, first responders are our first challenge to deal with constructively. And I am happy to expand on any of those four program elements during our Q and A.

Second, recognizing that we are focused on catastrophic events, it is important to document that our domestic P&C insurance system has served us as a nation very well for over 200 years. What should simply be unacceptable is this build, destroy, rebuild, and hope cycle that we seem to have found ourselves in associated with catastrophic natural disasters. This is even truer today in these very difficult economic times when such an event actually threatens the wellbeing of our housing and lending sectors, as well as our insurance sector. The American people have simply lost their appetites for bailouts. Imagine their frustration in the wake of another 1906 San Francisco earthquake when the losses are estimated to be in excess of $450,000,000,000. Or another 1938 Long Island Express, as just discussed in the previous panel, which, if it should happen just 20 miles west of where it happened in 1938, would result in inestimable damage to New York City.

The key to better financial preparedness is a national CAT fund backing up those States which voluntarily establish State level funds keyed to their individual and unique exposures. This would create a privately financed and federally administrated layer of reinsurance to complement and stabilize private market reinsurance alternatives, and ensure our goal of greater availability and affordability of residential property insurance.

In the interest of time, I would like to comment on several ongoing discussions concerning H.R. 2555. First, some critics, and it has already been brought up this morning, suggest that the PA.org agenda would only encourage people to own homes in high exposure areas. I think such arguments, frankly, are the stuff of red herrings and straw men. The fact is, 57 percent of American citizens already live there. And if we never built another stick of housing on the East, West, or Gulf Coasts, or in America's heartland, 6 of 10 families would still be at risk, and we would owe them a better construct than they have today.

The PA.org agenda is instead a reasonable and actuarially sound approach that recognizes today's threat and sets private money aside to deal with it.

Second, regarding prevention and mitigation, we support the hybrid approach which keeps the mitigation program centered in HUD, but we have to connect it in some fashion to the privately financed CAT funds, which can spin off significant investment income to groups like the Red Cross and first responders, to strengthen their ability to deal with after those storms go by.

And, third, we look forward to further discussions with both of you regarding attachment points for State and national CAT funds, and the guarantee of loan concepts. The latter should be designed to be complementary, not substitutional, to the reinsurance fund. The lender or guarantor of last sort, that concept contained in last year's H.R. 3355 may very well be worth reconsidering.

Mr. Chairman, Mr. Klein, thank you again for the opportunity to discuss the PA.org agenda, and we look forward to working with you as you pass this important legislation for our country.

[The prepared statement of Admiral Loy can be found on page 77 of the appendix.]

Chairman MOORE OF KANSAS. Thank you, Admiral Loy. And I will now recognize Ms. Williams for 5 minutes, ma'am.

STATEMENT OF VICKI WILLIAMS, OUTREACH COORDINATOR, THE MY SAFE FLORIDA HOME PROGRAM

Ms. WILLIAMS. Chairman Moore, thank you. I am grateful to be here to discuss the success of the My Safe Florida Home Program.

First, let me explain the catalyst for the program, the creation in 2004 and 2005. The windstorms that blew over Florida inflicted $33,000,000,000 in insured losses on 2.8 million Floridian homeowners. There are approximately 4½ million single-family site built homes. The amount of insurance exposure is about $2.3 trillion. The average age of the homes that I am talking about, site built single-family homes, is about 24 years old in Florida.

In 2005, the National Institute for Building Sciences concluded that for every dollar invested in mitigation, there is a savings of $4. The legislature created the My Safe Florida Home Program to help protect property of Floridians and save money on insurance premiums. The goals that were set were to use $250,000,000 and provide free home inspections to 400,000 Floridians. This excluded manufactured housing, multi-family housing; all openings must be covered for the value to be there in the mitigation. And I can say that the values certainly are affected of these type of homes. The mobile home insurance is very difficult to obtain. Replacement value declines on those type of properties. And, frankly, there are no SHIP funds for those risky structures, as well. That is the First Time Homebuyer Grant funds. The providing matching grants part of the $250,000,000 was to give homesteaded Floridians up to

$5,000. And we thought there would be 35,000 Floridians that could be served.

I have provided a PowerPoint, of which you may have a copy in front of you; I am not certain. There is a map that shows a snapshot of the 400,176 inspections that were completed. It was based along the coastline. The results on the map are showing geographically where the inspections were done. As you can imagine, in the middle of the State, there weren't quite as many inspections; there are not as many people living there. The surveys of inspection customers after our services were provided, we asked for their feedback. They were motivated to get safety information. Tell me how I can protect my house the best way. And, also, of course, the insurance savings. About 40 percent of the people wanted safety info; about 30 percent of the people—39 percent of the people wanted that savings on their insurance. We found about a quarter of those people pursued getting their houses strengthened without using any grant funds, And 91 percent of the people who used the program found that they rated it as being an excellent or good program. The majority were willing to pay about $3,200 to match the grant that they received.

There is another map showing you geographically where the dollars went. A snapshot of 31,593 homes that used the grant money and hardened their house. I can tell you that number would be higher. I know many people that, as the economy turned, were unable to fund their part of the matching grant program. About 46 percent of the people who got the grants were from south Florida; 22 percent from the West Coast; 16 percent from the East Coast; and 15 percent from the Panhandle. Of the homes that were awarded grant funds to protect all the openings, the average increase in strength to the house went up 36 percent. As you are probably aware, there is a scale of zero to 100 on this inspection report, and the average hurricane rating was 44. On average, homeowners are seeing 27 percent reduction in premiums. That is an average. On our coastline in south Florida, I can tell you that amount went well over a third of the premium for most people in savings.

Here is the results. Jobs were created. The return on investment for this State of Florida program, retrofitting an average of 320 homes every week. This created about 1,000 jobs in every week. That is with an earmark of $160,000,000 for grants to perform retrofits. Of $120,000,000 that was paid out in grants to buy the materials and pay to get them installed, there was sales tax, 6 percent, that is $7.5 million in sales tax revenue.

More than 900 inspectors were trained to help perform $58,000,000 worth of inspections over a 2-year period of time. This inspection is valid for 5 years, and can be used again when the homeowner is shopping for renewal policies. One risk modeler suggested this program reduces catastrophic exposure by as much as 26 percent in Florida, and that Florida gets $1.50 return for every dollar invested. Intangibly, the peace of mind that people get knowing how they hardened their home, and the monetary relief to the family's budget, is priceless.

Thank you.

[The prepared statement of Ms. Williams can be found on page 116 of the appendix.]

Chairman MOORE OF KANSAS. Thank you, Ms. Williams. I am going to recognize myself for 5 minutes for questions.

As a former Deputy Secretary of DHS, Admiral Loy, I am interested in your views. Is there a role for the Federal Government, not just in the clean-up, but going one step further in dealing with these issues and how they impact the availability and affordability of homeowners' insurance?

Admiral LOY. There absolutely is, sir. As I think a number of your witnesses have already testified, the harsh reality is that this is a national problem and deserves national attention and a national solution. The notion of a national CAT fund as a backstop to those States which voluntarily put together their State level catastrophe funds is, in my mind, the right answer to this adjusted insurance construct. Beyond that, the existence of such funds, where one can mandate in the legislation that the invested income, in part, can be donated towards mitigation strategies, public education programs, and even equipment and training support for first responders where appropriate, allows a national solution to find its way towards these local challenges that are, as Senator Geller has already testified, a national reality, not just something that happens in the State of Florida.

Chairman MOORE OF KANSAS. Thank you, sir. Ms. Williams, the My Safe Florida Home Program sounds like a very effective one that is having a real impact. Other than participating directly in the insurance market, are there other steps the Federal Government can take or should take to reduce the cost and increase the availability of homeowners' insurance in disaster-prone areas?

Ms. WILLIAMS. The vision in our State agency would be that grant program partnerships could work the best, where our State matches Federal dollars. And insurance, as it gets harder to obtain, as groups such as Citizens Property Insurance are requiring roof inspections for renewals, tightening the guidelines for having a structure that is not risky, the impact will continue to assist homeowners in Florida. In 2005, the new building codes created a less risky structure and a significantly less premium for the same type of home.

Chairman MOORE OF KANSAS. Admiral Loy—

Admiral LOY. If I might add—

Chairman MOORE OF KANSAS. —do you have any thoughts on that?

Admiral LOY. —some thoughts.

Chairman MOORE OF KANSAS. Yes, sir, please.

Admiral LOY. One of the ideal strengths of the National Catastrophe Fund matched up with the State funds would be that the monies needed for the program you just described and were chatting with Ms. Williams about could very well be either a combination of grants on the Federal level and invested income yields from those State level catastrophe funds to be part of that matching system.

In other words, if we are dealing with an actuarially sound system to begin with, that is actually breeding dollars to do the good things that we want to do in the other areas of interest, mitigation, public education, first responders, that is what I mean by a comprehensive, integrated system, not just focusing on one element of it.

Chairman MOORE OF KANSAS. I see. I am going to recognize my colleague, Congressman Klein, for 5 minutes of questions, sir.

Mr. KLEIN. Thank you, Mr. Chairman. Thank you both for being here. Admiral Loy, thank you for your service to our country as a Commandant of the Coast Guard and our homeland security efforts. I think most people understand homeland security is not just about military security; it is about presenting also for the civil side of things. And we know that natural disasters, or man-made disasters, require planning in advance, and, of course, FEMA on the back side. And we are all pretty excited about having Craig Fugate as our new FEMA Director, who is a product of Florida, and many of us worked with him. And he really understands Florida's issues.

Admiral, let me just, if I can, one of the things that we have been talking about is whether the idea that we are presenting in this legislation really sort of distorts the public perception of risk, and will be adverse to people making decisions about whether they should live a certain place, live—build on the coast, live on the coast. I mean, again, I think you started out with your comment that a big percent of the people, if they didn't build another stick, you know, anywhere—

Admiral LOY. They are already there.

Mr. KLEIN. —on the coast or anywhere else, and also the recognition that a lot of the natural disaster damage occurs inland. It has nothing to do with the coast of the United States.

Can you just share with me whether you think this legislation helps or hurts that good public policy initiative.

Admiral LOY. Well, I think the key there is your last phrase, sir. This is about good public policy. And good public policy has to not only deal with what might be, but what is. And the harsh reality and the facts of the moment are that 6 out of 10 families already live in those exposed areas, with a dramatically higher exposure than elsewhere. If you match up that harsh reality with a system that is designed around actuarially sound premiums, then you are serving the national well-being, not trying to focus on whether or not somebody is going to make an individual decision to pick up and move to the West Coast of Florida just because they imagine there are affordable and available insurance rates there. The 60 percent of us all who are already there, or in the New Madrid Fault zone, or in the California earthquake zones, already exposed, deserve as much of our national attention as do anyone making an individual decision.

Mr. KLEIN. And then, too, that would argue that, particularly because we are asking them to shoulder the burden—

Admiral LOY. Absolutely.

Mr. KLEIN. —something that is actuarially sound—

Admiral LOY. That is the actuarially sound side of this whole equation, yes, sir.

Chairman MOORE OF KANSAS. Yes.

Mr. KLEIN. Ms. Williams, also, I am very much in favor of the My Safe Florida Home Program. I am a little disturbed that the money wasn't put into the last legislative session. But it has been very successful. And, again, one of the things we have in this proposed piece of legislation is to learn from that experience in Florida. Florida has been a little ahead of the curve because of some of the experiences we have had. But the idea of leveraging matching dollars or things like—just share with us, meaning for the chairman and for our record, why you think it is so important for us to have these kinds of programs, which of course will hopefully reduce the exposure.

Ms. WILLIAMS. Well, as you are aware, with the population, they have to go where the jobs are. And our urban site in Florida is coastline. Since there has been automation, there are not as many farming jobs, and that is what the middle of the State is primarily all about. But the matching grant program works so well with homeowners in the State of Florida. I believe that we are seeing the possibility, with the discussion of national catastrophe funds and how to allocate—every State has its own peril in disaster—but this would allow a State to effectively and creatively utilize a partnership based on the standards that we have used to train, have an infrastructure, to be certain that these reports were accepted.

To me, there was a lot of work done to create and build that program. That is part of where some of this funding had to go, to create it. So incorporating some Federal dollars into it would seem as if it is just the most advantageous to everyone, so you don't recreate a new program, spend new money on something that you have to start all over again.

Mr. KLEIN. And the last thing I would like to ask you is at a national level, I am constantly asked this as a sponsor of the bill, along with many co-sponsors around the area, why is this something that—is this being accepted? Are people around the country receptive to this, as opposed to previously this has been a Florida experience. You have been traveling.

Admiral LOY. Absolutely.

Mr. KLEIN. Can you share with us what sort of—what interior—what concerns the interior and other places?

Admiral LOY. Yes, sir, indeed. And I think there are a couple of just sort of metrics that you can look at real quickly, sir. First of all, your 50-plus cosponsors of the legislation represent 22 or 23 States at this point. It is not just a set of Representatives from the constituencies back home who are only in Florida. This is a very, very national reflection.

Second, we have spoken, I have gone and done editorial boards across the country, and the reality is that Americans are quite willing to pay that actuarially sound rate, and recognize that the system is designed to be there where the payment is attendant to the risk that you are willing to take for yourself and for your family.

That is the notion of actuarial soundness, which has been an underpinning of our insurance industry for a long time. What is unpredictable, to use, again, Senator Geller's words, is these mega catastrophes that come by, where the—the pinning of predictability is an attempt to associate with the kind of damages that are going to occur.

This extraordinary program that Ms. Williams is talking about, the My Safe Florida Home Program, is just one of those examples. And if you talk to Craig Fugate, if you talk to my counterpart and

Co-Chair, James Lee Witt, who was the FEMA Director during President Clinton's Administration, and if you talk to folks who have just left that particular position, they understand the national quest to do the right thing at the end of the day. James Lee Witt will talk about not only focusing on an individual homeowner and his home, which is a mitigation strategy attendant to building codes and the enforcement thereof, but also perhaps land use adjustments that are seeking national support for local solutions. And when you gain the national support for a local solution, you have in fact found yourself in the realm of serving the American public the way it needs to be served.

Chairman MOORE OF KANSAS. Thank you, sir. And I want to thank our witnesses in this panel and the other panels who have testified today. You have been very, very helpful, I think, in our understanding of some of the issues facing our country, and what we need to do, and maybe can address these.

Also, I am going to say by enacting creative solutions like Congressman Klein's Homeowners' Defense Act, we will begin to take steps to provide real solutions that will benefit homeowners, communities, and taxpayers.

I look forward to working with our witnesses and my Republican and Democratic colleagues in Congress on these important issues. The Chair notes that—and I want to thank Congressman Klein for being a host down here, number one, and number two, for his excellent questions and participation in this panel today.

If you have additional questions for this panel, you may submit those questions in writing, Congressman Klein. Without objection, the hearing record will remain open for 30 days for Congressman Klein and myself to submit additional questions, and we would ask that witnesses provide their written responses to those questions.

This hearing is adjourned, and I thank everybody for your participation.

[Whereupon, the hearing was adjourned.]

A P P E N D I X

July 2, 2009

Subcommittee on Oversight and Investigations
House Financial Services Committee
July 2, 2009

"The Homeowners' Insurance Crisis: Solutions for Homeowners, Communities, and Taxpayers"

Opening Statement from Chairman Dennis Moore [KS-03]

At 9:45 p.m. on May 4, 2007, Greensburg, Kansas was hit by a category 5 tornado. The tornado was estimated to be nearly 2 miles in width and traveled for nearly 22 miles. Ninety-five percent of the city was destroyed, with the other five percent severely damaged. The National Weather Service estimated winds of the tornado reached 205 mph.

Thankfully, tornado sirens sounded in the city twenty minutes before the tornado struck, and a tornado emergency was issued, which undoubtedly saved many lives. This was the first tornado to be rated a category 5 tornado since 1999. Kansas Governor Kathleen Sebelius and former President George W. Bush both declared Kiowa County a disaster area, which opened up the affected areas for national and international aid.

Shortly after the storm, I joined my colleagues, Congressman Jerry Moran and former Congresswoman Nancy Boyda, on a visit to Greensburg, Kansas, to meet with residents and check on the progress being made after the devastating tornado wiped out most of the town.

During our visit, we attended local church services, had a lunch meeting with local officials to discuss the successes and problems with current relief efforts, toured the town to see first-hand the damage caused by the tornado and participated in a USDA Rural Development housing rededication of the first facility to be rebuilt.

While the amount of damage was still staggering, progress was already being made. In fact, I have been incredibly impressed by how many people opened up their hearts and wallets to help the people of Greensburg. That generosity has made a big difference to this little town in Kansas put their community and their lives back together.

It is a fact of life that catastrophic natural disasters will happen from time to time, and we need to be fully prepared. After the unacceptable response by FEMA to Hurricane Katrina, for example, we must ensure that our federal government is prepared to help in a time of need. Hurricane Katrina caused $45.3 billion in insured losses, and of the top ten most costly insured catastrophes in the United States since 1989, eight of the top ten were caused by hurricanes.

Today, we focus on how catastrophic natural disasters impact the affordability and availability of homeowners' insurance, especially in places like here in West Palm Beach, Florida. This is a tough problem with no easy answers, but hopefully today's hearing will shed more light on this issue and potential solutions that will help homeowners, communities, and taxpayers.

I appreciate the hard work Congressman Klein has put into these issues. His work in carefully crafting the Homeowners' Defense Act is exhibited by the strong bipartisan support the measure has received. I look forward to working with him to move this legislation forward in the process.

I also look forward to hearing from our witnesses today and the perspectives they bring to the table. We will hear from various viewpoints of what these issues mean for real homeowners and taxpayers.

We will also examine insurance industry coverage of catastrophic natural disasters, the withdrawal of insurance companies from offering policies in coastal areas, rising homeowners' insurance premiums and the resulting economic impact on state and local governments, as well as possible solutions to the homeowners' insurance crisis.

I will conclude by noting that this is not just a Florida problem, as some have suggested. At the opening of my statement, I described the devastating tornado that nearly destroyed an entire town in Kansas. All along the Gulf Coast and Atlantic Coast, other states have been ravaged by hurricanes. California has had earthquakes and a number of states have been devastated by wild-fires.

How these devastating tragedies impact the affordability and availability of homeowners' insurance is a national problem that demands a national response in coordination with states that are most affected by these devastating natural catastrophes.

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NATIONAL ASSOCIATION OF MUTUAL INSURANCE COMPANIES

Statement

of

Robert Detlefsen

Vice President – Public Policy

on behalf of the

The National Association of Mutual Insurance Companies

to the

Oversight and Investigations Subcommittee

of the Committee on House Financial Services

U.S. House of Representatives

"The Homeowners Insurance Crisis:

Solutions for Homeowners, Communities, and Taxpayers"

JULY 2, 2009

Good morning Chairman Moore, Ranking Member Biggert, and Members of the Subcommittee. My name is Robert Detlefsen. I am Vice President of Public Policy for the National Association of Mutual Insurance Companies (NAMIC). Founded in 1895, NAMIC is a property and casualty insurance association, whose 1400 members underwrite more than 40 percent of the property/casualty insurance premium written in the United States. I am grateful for the opportunity to testify this morning on a subject that poses an enormous challenge to the insurance industry and our nation as a whole.

It is widely acknowledged that property insurance has become more expensive and somewhat less available in the coastal regions of the U.S. The private sector and government can and should work together to address problems of insurance availability and affordability in these areas. However, we must be careful that any expansion of the federal government's role does not artificially suppress insurance rates, crowd out the private insurance market, and encourage unwise residential and commercial development in high-risk coastal regions.

The Problem of Coastal Insurance

Three simple facts help define the problem of coastal insurance:

1. The exposure of densely concentrated, high-value properties to elevated levels of catastrophe risk in certain geographic regions. This means that

property insurance in these regions will be relatively expensive compared to others with lower risk.

2. As population growth and commercial development in catastrophe-prone regions increases, the number of people and businesses faced with relatively high insurance costs will naturally increase as well.

3. The Atlantic and Gulf coastal regions of the U. S. have experienced increased population growth and commercial development at a time when the frequency and severity of catastrophic storms in these regions is increasing.

Factors Influencing the Availability and Affordability of Coastal Insurance

Simply put, the availability and affordability of property insurance in coastal regions is mainly a function of risk. But other variables, including actions taken by governments and *post hoc* reinterpretations of insurance contract language by courts, can also affect the supply and cost of insurance. The availability and affordability of coastal property insurance are particularly influenced by the following factors:

Frequency and Severity of Major Coastal Storms

In 2005 three Gulf Coast hurricanes killed more than 1,400 people and caused more than $180 billion in insured losses and federal disaster relief. Since 2005, property insurance prices in coastal areas have increased because of what the 2005 hurricane season portends for the future.

Coastal Development and Population Growth

The fact of the matter is that the areas most at risk of increased storm activity contain a disproportionate share of the nation's population, as well as its most valuable real estate. What is more, the movement of people and wealth from interior regions with relatively little catastrophe risk to coastal regions with the highest levels of catastrophe risk continues to increase even as the likelihood of severe coastal hurricane activity increases. According to the U.S. Census Bureau, Florida will experience significant population growth every year between now and 2030, by which time the state will have added more than 11 million new residents. That is equivalent to the entire current population of Ohio moving to Florida over the next 21 years. In 2015 —just six years from now—Florida will surpass New York as the nation's third most populous state.

Consider just this one dramatic example. The Great Miami Storm of September 18, 1926, a Category 4 hurricane with 145 mile per hour winds, caused $42 billion in economic damages (in today's dollars), according to the web site www.icatdamageestimator.com. Because of the enormous growth in population and wealth of Miami since then, were a similar storm to strike Miami today, the web site estimates that it would cause $180 billion in damages.

State Regulation

Many states in catastrophe-prone coastal regions, including Florida, impose rating and underwriting restrictions on property insurers that act as price ceilings on coverage. Many state officials believe that insurance rate suppression, which allows high-risk property owners to pay artificially low premiums, is the answer to the property insurance "affordability problem" in catastrophe-prone areas.

While rate suppression lowers the "price" of insurance in the short term, it has long term consequences that are far worse for consumers. First, rate suppression lowers prices for people living in high-risk regions at the expense of insurance consumers in low-risk regions, forcing people living in low-risk regions to pay inflated prices in order to subsidize the insurance costs of those in high-risk regions.

Second, rate suppression encourages rapid population growth and economic development by distorting the public's perception of risk. The growing concentration of people and wealth in high-risk regions will continue to drive up the cost of insuring those regions and further adding to the problem.

Federal and state governments end up bearing the cost by paying for disaster aid to repair properties that might never have been built in the first place. Risk-based insurance pricing alleviates this problem by sending accurate signals to consumers about the relative level of risk associated with particular regions and types of structures.

Rate suppression and underwriting restrictions are also largely responsible for insurance availability problems in coastal areas. Like any other business enterprise, insurers must charge a price that covers the cost of the good or service they provide. But if government rate regulation prevents insurers from covering their claim costs and replenishing surplus reserves to pay future claims, they may have no choice but to exit the market, as we have seen recently in Florida.

Litigation and the Viability of Insurance Contracts

For more than 30 years, the standard American homeowners insurance policy has contained a provision that excludes coverage for damage caused by flooding. Throughout this period, flood coverage has been provided almost exclusively by the federal government through the National Flood Insurance Program (NFIP).

Nevertheless, after every major disaster involving extensive flooding, attorneys take aim at the flood exclusion in homeowners policies, looking for ways to overcome decades of legal precedent. Sometimes they succeed, causing insurance companies to re-examine their policies and make adjustments so that the policy language is as clear and unambiguous as possible in stating that damage due to flood is not covered. They then file those policy contract forms with state insurance regulators and negotiate the terms until they can obtain official approval and issue them to policyholders.

Such was the case in Mississippi, Louisiana, and the other states hit by the 2005 hurricanes. And when it developed that many homeowners whose properties were damaged or destroyed by hurricane-related coastal flooding had not purchased federal flood insurance (or had not purchased enough to cover their losses), class action attorneys, joined in this instance by the Mississippi Attorney General, filed dozens of lawsuits in which they tried to persuade judges to abrogate the flood exclusion and force insurers to retroactively provide coverage for which they collected no premium. This type of litigation is a cost of doing business in certain areas and has an affect on the whether a company decides to serve those areas or not.

The Example of Florida

Florida lawmakers passed, and Gov. Charlie Crist signed into law, HB 1495, allowing Citizens to increase premium rates, by 10 percent, for individual policyholders each year until actuarially sound levels are attained. Additionally, this bill increases rates and lowers coverage amounts over time for the Florida

Hurricane Catastrophe Fund. The changes HB 1495 brings are encouraging. Not only does it put Citizens on a path to appropriately matching rate to risk, it puts the entire state on the path to better financial preparation for future storms.

However, Florida failed to pass HB 1171 which would have allowed Floridians the option to choose between rate-regulated property/casualty insurers and a select group of well-capitalized, mostly nationally recognized carriers exempt from price controls. While this bill should have been applied to all insurers, it was another step to improve the market in Florida.

Although Gov. Crist chose to veto the bill despite consumer support, the swift passage through the state legislature reflects the growing understanding of legislators of the importance in keeping a vibrant marketplace that provides choices for consumers. As reported in the *Tallahassee Democrat*, "New capital and new companies are important, because the state's insurer of last resort, Citizens Property Insurance Corp., is so underfinanced that it couldn't possibly pay off claims in the event of major storm damages."

The Wall Street Journal, in an editorial published on June 29, 2009, summarized the approach that Governor Crist chose when he vetoed HB 1171:

> Mr. Crist and the media portrayed the reform as a giveaway to the big insurers, and the Governor claims people can't afford "large and unpredictable" increases in premiums. The truth is large increases are

> precisely what is sometimes needed to cover the risk of living on coastal property. Mr. Crist's program makes the long-term losses much more severe because cut-rate insurance has encouraged overbuilding in coastal areas that are historically in the path of hurricanes. "We are one major hurricane away from an economic disaster in this state," says House bill sponsor William Proctor.

The state's opinion leaders agreed as well and in an editorial published on June 25, the *Tallahassee Democrat* urged the Florida Legislature to take the unusual step of coming back into session for the express purpose of overriding the governor's veto of HB 1171.

The Affordability Problem: What We Can Do

Last month, MIT Press published an important new book, *At War With the Weather: Managing Large-Scale Risks in a New Era of Catastrophes*, which has been hailed by Terri Vaughan, CEO of the National Association of Insurance Commissioners, as "essential reading for anyone searching for solutions to the problem of financing large-scale catastrophes." Authored by a team of distinguished insurance scholars from the Wharton School and Georgia State University, the book identifies "two key principles" that should guide insurers and policymakers as they grapple with natural disaster insurance availability and affordability issues. NAMIC believes that these principles provide Congress with a solid foundation from which to develop innovative solutions and avoid costly mistakes. The two principles are:

- *Risk-based Premiums:* Insurance premiums should be based on risk to provide signals to individuals as to the hazards they face and to encourage them to engage in cost-effective mitigation measures to reduce their vulnerability to catastrophes.

- *Dealing with Equity and Affordability Issues:* Any special treatment given to lower income residents in hazard-prone areas who cannot afford the cost of living in those locations should come from general public funding and not through insurance premium subsidies.

The book's authors recognize, as does NAMIC, that a market-based insurance pricing system in which premiums reflect the actual cost of insuring against catastrophic risk could result in significant premium increases for some property owners in high-risk regions. In lieu of cross-subsidization through rate suppression and taxpayer-funded government insurance schemes, policymakers should consider creating programs to provide direct government assistance, funded from general revenue, to particular consumers based on criteria established through a transparent decision-making process.

The federal government has a long history of designing and administering programs that provide grants and other forms of direct financial assistance to individuals on a means-tested basis for the purchase of essential goods such as food and shelter. For example, the government responds to the inability of some individuals to afford basic food staples, not by capping the price of groceries or creating government-run food stores, but by providing food stamps to low-income individuals that can be used to purchase food items from private vendors.

Congress could provide a similar form of aid to selected property owners for the purchase of insurance. Such an approach would have many advantages over the current system of generalized rate suppression and cross subsidization, not the least of which is that the assistance could be targeted to particular individuals based on financial need. Moreover, its availability could be limited to those currently residing in disaster-prone areas, and would thus avoid creating incentives for people not currently living in those areas to move into harm's way.

NAMIC's Reform Agenda and Federal Legislation

In 2006, a NAMIC Task Force issued a "Statement of Principles on Natural Disasters" (a copy of which is attached) that laid out an agenda for improving the ability of insurers, property owners, and government to manage and finance future natural disasters.

NAMIC readily acknowledges that a genuine mega-catastrophe comparable to the 1926 Miami hurricane striking heavily populated areas could potentially exceed private market capacity. To prepare for a disaster of this magnitude, it is appropriate for policymakers to consider whether government programs should be created to supplement the supply of private sector capacity. At the same time, we believe the Florida example should serve to caution lawmakers against creating a national catastrophe reinsurance program that unintentionally creates incentives for Americans to migrate from regions with relatively little exposure to catastrophe risk to coastal regions with the most frequent and severe hurricanes. The federal government should be careful not to subsidize states that enact disaster insurance "reforms" by transferring the cost of such measures to federal taxpayers.

The NAMIC Statement of Principles seeks to establish a proper balance between the roles of the private insurance sector and governments in order to send the proper signals to discourage development and/or mitigate its effects in dangerous areas while addressing affordability issues for low-income people already living in areas prone to natural catastrophes. The principles are as follows:

1. Market freedom and competitive pricing will lead to innovation in developing solutions to problems relating to disaster insurance and mitigation.
2. Competitive pricing and risk-based underwriting are essential to developing and maintaining a viable disaster insurance market.
3. Mitigation must be an indispensable aspect of any disaster risk management and insurance initiative.
4. The National Floor Insurance Program should be maintained, but must be reformed.

With the Congress absorbed with health care reform, energy, and financial regulatory reform legislation, there has been little time for consideration of natural catastrophe issues. As you know, it now appears as if the House and Senate will just extend, rather than reform, the NFIP this year.

Recently, Rep. Klein, D-D-Fl., introduced H.R. 2555, the Homeowners Defense Act of 2009. NAMIC commends Rep. Klein and the bill's cosponsors for keeping the Congress' attention focused on this important issue.

The bill would provide for mitigation grants to prevent and mitigate losses from natural catastrophes, which NAMIC believes is a key for property owners to reduce their exposure to catastrophe risk and a good way to reduce their insurance premiums. The larger the grant program, the more effective it will be.

NAMIC opposes the portions of the bill that seek to build on state catastrophe funds. As with Florida's programs, we believe such mechanisms invariably result in cross-subsidies by those not in risk-prone areas to those in risk-prone areas, under price the cost of insurance, and discourage private sector participation. To establish a federal debt guarantee program of obligations issued by state catastrophe funds on top of such a faulty floor would only aggravate the underlying problems.

NAMIC is also concerned that the federal natural catastrophe fund that the bill would create would crowd out the private reinsurance market; whether a 1 in 200 year event attachment point is high enough to warrant a federal reinsurance backstop; and whether a federal reinsurance program should be premised on flawed state reinsurance funds.

As for other legislative proposals, NAMIC strongly supports H.R. 2246, the Community Building Code Administration Grant Act, introduced by Congressman Dennis Moore, D-Kan and included as part of the climate change legislation passed by the House of Representatives on June 26, 2009. By providing $100 million a year for five years in federal grants to building departments, it will help local governments hire, train and equip code officials, including building and fire inspectors. More effective enforcement of building codes will improve safety for those residing in disaster-prone areas.

NAMIC also supports H.R. 2592, the Safe Building Code Incentive Act, introduced by Congressmen Mario Diaz-Balart, R-Fl, and Michael Arcuri, D-NY. The bill would amend the Robert T. Stafford Disaster Relief and Emergency Assistance Act to authorize the President to increase the maximum total contribution for a major disaster by 4 percent of the relief grant, if the affected state has in effect and is actively enforcing a nationally recognized statewide building code. As with H.R. 2246, this legislation would improve building safety for those living in disaster-prone areas.

Furthermore, the NAMIC Statement of Principles recognizes that there are low-income people living in such areas who simply cannot afford the premiums. Rather than distorting insurance markets to address this problem through rate suppression – and undermining the important signals sent by insurance pricing – NAMIC supports direct federal subsidies to existing low-income residents of such areas.

In conclusion, NAMIC realizes that the property owners, insurers, mortgage lenders, realtors, and home builders that live and do business in coastal areas will face serious challenges in the years ahead. We believe that the most effective mechanism for addressing these challenges is a private insurance market whose defining characteristics are open competition and pricing freedom. Congress can play a constructive role by reforming the National Flood Insurance Program, creating incentives for states to enact and enforce effective statewide building codes, and providing targeted grants that would enable low-income property owners to pay risk-based property insurance premiums.

NAMIC STATEMENT OF PRINCIPLES ON NATURAL DISASTERS

Introduction

The havoc wreaked by the 2005 Gulf Coast hurricanes has raised important questions about how Americans should prepare for and respond to natural disasters in the future. The likelihood of more frequent and severe natural disasters in the near term, combined with the continuing concentration of the country's population in areas vulnerable to natural disasters, pose significant challenges for government policymakers, insurers, realtors, home builders, mortgage lenders and property owners.

The National Association of Mutual Insurance Companies (NAMIC) will draw upon the experience, insight and expertise of its 1,400 member companies and professional staff to play a leading role in the development of solutions that address the issues associated with major catastrophic events such as hurricanes, earthquakes, windstorms and wildfires.

In December 2005, NAMIC formed a Task Force on Natural Disasters and invited representatives from 20 of its member companies to participate in a discourse on this subject. During the ensuing six months, the task force held regular meetings during which members were briefed by researchers, analysts, and practitioners from a variety of disciplines who were selected for their expertise in particular areas of disaster risk management and insurance. The task force also studied and discussed a sizable body of literature on natural disaster issues. Based on this process, the task force formulated four general principles that will serve to guide NAMIC members and staff as the natural disaster debate evolves.

The principles are:

1. Market freedom and competitive pricing will lead to innovation in developing solutions to problems relating to disaster insurance and mitigation.

2. Competitive pricing and risk-based underwriting are essential to developing and maintaining a viable disaster insurance market.

3. Mitigation must be an indispensable aspect of any disaster risk management and insurance initiatives.

4. The National Flood Insurance Program should be maintained, but must be reformed.

The following is an elaboration on the rationale behind each of the four principles.

1. **Market freedom and competitive pricing will lead to innovation in developing solutions to problems relating to disaster insurance and mitigation.**

    a) Insurance markets function most efficiently in the absence of government rate suppression and underwriting restrictions. A flexible regulatory environment in which insurers are free to price coverage based on risk will create incentives for property owners in high-risk areas to invest in loss mitigation measures. Likewise, risk-based pricing will create incentives for individuals, home builders and mortgage lenders to engage in risk avoidance strategies (such as refraining from purchasing or building homes in high-risk areas).

    b) Risk-based pricing will foster greater competition among insurers and increase the availability of property insurance in disaster-prone areas. Developing sufficient capacity to insure against losses caused by low probability/high consequence events is dependent on the ability of insurers and reinsurers to generate and hold capital. With an adequate rate of return, capital will flow into insurance markets.

    c) The private insurance market is best equipped to provide coverage for most types of natural disasters under most circumstances. Exceptions include flood insurance generally, and earthquake insurance in high-risk seismic zones. NAMIC recognizes that both recent and anticipated increases in the number and severity of natural disasters over the next decade has caused some observers to question whether primary insurers, reinsurers and the capital market will continue to have the ability to finance a "mega-catastrophe," or a series of high-consequence events occurring within a relatively short time frame.

    d) To date, the private marketplace has had the capacity to handle natural disasters. However, in jurisdictions with a restrictive regulatory environment, a significant increase in major storm frequency or the occurrence of a mega-catastrophe (e.g., an earthquake comparable to the 1906 San Francisco event, or a high-category hurricane striking heavily populated areas such as Miami, Houston, or New York City) could test or exceed private market capacity in high-risk regions. Such a mega-event could result in the inability of many insurers to meet their claim obligations and still offer protection on a going-forward basis. This is particularly true where insurers have established single-state companies as a way to manage their exposure. Therefore, consideration of state or federal programs designed to respond to these mega-events may be appropriate.

e) Disaster under-preparedness is not simply an insurance availability and affordability problem. Policymakers must recognize that human psychology strongly influences the decisions people make with respect to disaster risk management and insurance. Attention must be paid to the reasons why property owners as well as government officials tend to underestimate catastrophe risk and fail to prepare adequately for natural disasters. It is also important to acknowledge the tendency among many consumers to view insurance as a financial investment rather than as a protective measure. Studies indicate that this tendency leads people to discontinue coverage after a period during which they suffer no losses and file no claims, on the grounds that continuing to pay premiums "isn't worth it."

f) NAMIC supports the concept of amending the federal tax code to allow insurers to set aside a portion of premium income in tax-exempt policyholder disaster protection funds. NAMIC also supports the concept of allowing homeowners to create tax-free catastrophic savings accounts similar to health savings accounts which could be used to pay hurricane deductibles and costs associated with retrofitting properties.

2. Competitive pricing and risk-based underwriting are essential to developing and maintaining a viable disaster insurance market.

a) Open and competitive property markets are ultimately in the best interest of consumers. Lawmakers and/or regulators sometimes impose rating and underwriting restrictions on property insurers that allow high-risk property owners to pay artificially low premiums, forcing lower-risk property owners to subsidize the insurance costs of high-risk buyers by paying inflated premiums. NAMIC believes that using the insurance pricing mechanism to create hidden cross-subsidies among risk classes is not good public policy.

b) A market-based insurance pricing system in which premiums reflect the actual cost of insuring against catastrophic risk could result in significant premium increases for some property owners in high-risk regions. Policymakers may consider creating programs to provide direct government assistance, funded from general fund revenue, to low-income and other groups according to criteria established by the unit of government providing assistance. In designing such programs, care should be taken not to reduce risk mitigation incentives.

c) In discussions of insurance price regulation, the term "actuarially sound" is often used without definition. This term must be carefully defined, as there is no common definition shared by all participants. For example, many have used "actuarially sound" to mean prices that solely reflect the expected value of the loss costs. However, a definition of "actuarially sound" that is based on expected value pricing cannot apply to catastrophe exposed coverages. This is because "actuarially sound" pricing for catastrophe exposed coverages must also include compensation for the unusually large call on capital that is required to pay catastrophic losses. The call on capital that results from the highly correlated large-scale losses typically associated with extreme events may well be several times greater than the total annual "expected loss" of the coverage. In other words, the term "actuarially sound" should be understood to include not just the insurer's expected loss costs and expenses based on yearly averages. It should also include an adequate "risk load" that takes into account the call on capital.

d) Lawmakers, judges and the general public must recognize the cyclical nature of property insurer profits, how profits relate to surplus, and the role of surplus in ensuring that insurers are able to meet their contractual obligations to policyholders. Using return on equity as the universal benchmark for measuring company profitability, economists have found the return on equity of insurance companies to be lower than that of most other industries. Regulatory decisions and judicial rulings that require insurers to pay disaster-related claims irrespective of the terms of the insurance contract could cause availability problems at best and widespread failures in the market at worst.

3. Mitigation is an indispensable aspect of disaster risk management and insurance.

a) Effective mitigation efforts including the development of strong building codes as well as responsible land-use planning have been shown to greatly reduce the level of property damage and human suffering caused by natural disasters.

b) Government policymakers, insurers, builders, realtors, mortgage lenders and other stakeholders have a shared responsibility to help Americans who live in harm's way understand the nature of catastrophic risk and the threat it poses to their property and personal safety. Government-imposed rate suppression and reliance by private insurers on actuarially unsound government reinsurance programs can have the effect of distorting public perceptions of risk. Risk-based insurance pricing, on the other hand, sends accurate signals to consumers about the relative level of risk associated with particular regions and types of structures.

c) NAMIC supports the concept of federal legislation that would create financial incentives to encourage states to adopt and enforce strong, statewide building codes. With respect to existing properties, NAMIC supports government initiatives to create mitigation grant programs to enable homeowners in high-risk areas to invest in risk mitigation measures.

4. The National Flood Insurance Program should be maintained, but must be reformed.

a) The National Flood Insurance Program (NFIP) has provided flood insurance coverage to homeowners across the country since 1968. While Hurricane Katrina revealed shortcomings in the program, NAMIC believes the NFIP should continue to operate, but it must adopt significant reforms.

b) NFIP premiums must be actuarially sound for all covered structures. The current method for setting premiums, which is based on average annual losses, has been called "unsustainable" by the Congressional Budget Office. This approach has prevented the NFIP from accumulating the surplus necessary to pay claims during periods when loss costs are above average.

c) The borrowing authority of the NFIP must be increased so that program administrators will not be required to seek special appropriations from Congress each time a natural disaster involving major flooding occurs.

d) Additional federal funds should be allocated to the national flood hazard mapping program. Updating and improving flood maps should be a priority within NFIP also in those communities that will benefit most from updated flood maps.

e) Stiffer penalties should be imposed on financial institutions that either fail to require flood insurance coverage for mortgages on properties in flood-prone areas, or allow the policies to lapse.

f) The NFIP needs additional resources and a renewed mandate to improve and expand its public education programs to ensure that more people are made aware of the program and the benefits of having flood insurance coverage to protect their properties.

g) NAMIC urges policymakers and other interested parties to work together to develop additional improvements to the National Flood Insurance Program.

INSURANCE

New laws and policies in the wake of Hurricane Katrina seem intended to scapegoat insurance companies rather than protect the public.

Facing Mother Nature

BY MARTIN F. GRACE AND ROBERT W. KLEIN
Georgia State University

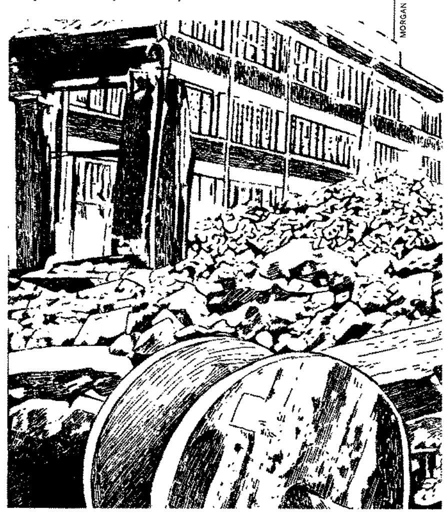
Changes in insurance markets that followed the flurry of hurricanes in 2004-2005, capped by Hurricane Katrina, have been met by a storm of criticism in Congress and state capitals. Rather than addressing the economic realities of increasing catastrophe risk with informed discussion and sound proposals and policies, politicians are attacking its messenger – the insurance industry.

Political attacks on the insurance industry are not a new phenomenon. But the current assault may rank among the most severe, misguided, and damaging campaigns ever waged, with potentially disastrous consequences for many Americans. Government's mismanagement of catastrophe risk is rooted in a climate of public ignorance and distrust of the insurance industry. That enables politicians to weave a fiction that plays well with their constituents as it sows the seeds of their and others' exploitation. There is a pressing need to correct several fallacies that infect the current debate and educate the public about the economics of catastrophe risk, the dangers posed by the current course of policy, and better solutions.

MOTHER NATURE VS. HUMANITY

One common fallacy is the belief that catastrophe perils are like other insured perils. The reality is that catastrophe perils have unique characteristics that are highly relevant to managing the risk they pose. Perils such as auto accidents are relatively stable and predictable (based on historical experience), but catastrophe perils are highly variable and impossible to predict with any degree of confidence.

The occurrence of hurricanes is determined by both long-term and short-term weather patterns. Weather scientists cannot predict exactly how many hurricanes will strike the Unit-


MORGAN BALLARD

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ed States in a given year, but they can calculate the probabilities of various hurricane scenarios over any defined period of time. The scientists are telling us that we are currently in a cycle of greatly increased hurricane activity, and the probability of one or more severe hurricanes occurring in a given year is much higher now than it was two decades ago.

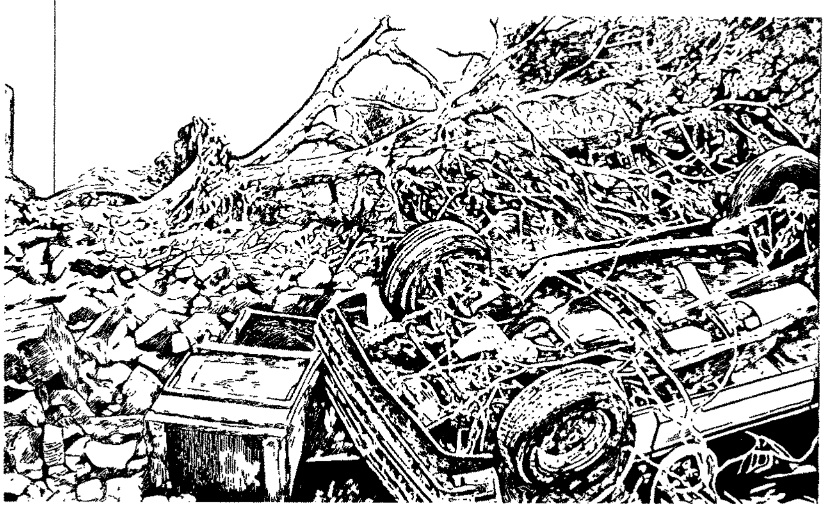
The actual occurrence of hurricanes is analogous to Mother Nature rolling weighted dice. But recent history is consistent with the scientific analysis of how the dice are weighted. Figure 1 displays the number of hurricanes striking the United States by decade for 1920-2004 and also distinguishes the number of more severe – Category 3-5 – hurricanes. Hurricane frequency and intensity increased over the first three decades of this period and then fell during the next three decades. Storm activity intensified again starting in the late 1980s and continues today. Figure 1 also reflects the variability of the number and severity of hurricanes that actually occur from year to year within any given multi-year cycle of increased (or decreased) hurricane activity.

Property losses from hurricanes are a function of both hurricane activity and the value and vulnerability of structures in their path. Because of increases in those factors, the probability of higher hurricane losses is rapidly increasing; this is reflected in historical data on insured catastrophe losses shown in Figure 2. While catastrophe losses vary greatly from year to year, it is clear that catastrophe losses on the whole (even measured in constant dollars) have increased dramatically since 1990, with several "bad years" resulting from one or more severe disasters in those years.

Total insured catastrophe losses (in 2006 dollars) were $29.3 billion in 2004 and $63.9 billion in 2005 – primarily caused by hurricanes striking the Southeast. Hurricane Katrina alone generated $41.9 billion in insured losses – almost twice the amount caused by Hurricane Andrew, which had been the most costly natural disaster prior to Katrina. As devastating as Katrina was, experts are concerned about the significant possibility of a much larger disaster that could cost in excess of $100 billion in insured losses alone.

GROWTH AND LOSSES The dramatic increase in U.S. coastal development has contributed to the rise in hurricane losses. During the previous active storm cycle of 1920-1950, coastal areas were less developed, so storms striking those areas caused less property damage. During the next three decades there was considerable economic growth in those areas, but storm activity had lessened and did not impede growth.

A 2004 National Oceanic and Atmospheric Administration study estimates that 153 million people lived in coastal counties in 2003, representing 53 percent of the U.S. population but only 17 percent of the nation's land mass. From 1980 to 2003, 33 million people were added to the coastal population, representing a 28 percent increase overall. The pace of growth has been much higher along the southern Atlantic and Gulf coasts where hurricane risk is the greatest. The NOAA study predicts further strong population growth in Southeastern and Gulf coastal areas. Indeed, Florida coastal population growth, alone, has increased by more than 11 percent just between 2000 and 2005. We should also note that Hawaii



faces significant hurricane risk as evidenced by Hurricane Iniki in 1992 and the near miss of Hurricane Flossie in 2007.

Hence, considerable development occurred when hurricane losses were relatively low and property insurance was relatively cheap. That development has continued, even after hurricane activity increased. A myopic sense of security has contributed to large movements of people and the associated property development that is now at significant risk from intensified hurricane activity. At the same time, little attention has been paid to hazard mitigation (e.g., building hurricane-resistant homes). The result is a substantial increase in the potential and actual property losses from hurricanes.

THE ROLE OF INSURANCE

It is important to review some basic principles of insuring catastrophe risk and address several fallacies that permeate the current debate. Those fallacies include:

- The pooling of risk exposures (e.g., homes) within an insurance mechanism implies that everyone in the pool should pay the same premium. Profits from insuring low-risk exposures should cover losses from high-risk exposures.
- Insurers and insurance markets are immune from competition. Unless closely regulated, insurers can charge excessive prices that will generate excessive profits. In this context, insurers are deliberately over-estimating the risk of hurricanes to support inflated prices and other actions that they are taking.
- Insurers have earned excessive profits. The fact that they have earned any profits at all means that they should not be raising their prices and managing their exposures in hurricane-prone areas.
- Insurers intentionally seek to "underpay" claims, i.e., pay less than what they are obligated to pay under the terms of the policies they issue. This further contributes to their excessive profits.

Property owners exposed to hurricane risk can manage this risk in different ways. Many prefer (or are forced by their lenders) to do so by transferring their risk to insurers. Fundamentally, any legitimate insurance arrangement to cover potential losses from a given peril must be financed with risk-based premiums that cover insurers' full cost of providing coverage, including their risk-adjusted cost of capital. This means that the premium paid by any insured should cover his or her "actuarially fair share" of the costs, i.e., high-risk insureds must pay higher premiums than low-risk insureds. This is essential to control adverse selection and moral hazard that will otherwise destroy any insurance arrangement that is not subsidized by government funds. Further, fierce competition prevents private insurers from charging higher rates to low-risk insureds to subsidize the rates for high-risk insureds or raising rates in future years to recoup losses from prior years.

Insuring catastrophe losses presents special challenges that are not associated with other kinds of perils. Insurers must deal with the fact that catastrophe losses are highly variable from year to year and the possibility that they could suffer very high losses in a given year that could easily bankrupt them. Insurers manage their catastrophe risk by controlling their exposures (e.g., avoiding large amounts of exposures in high-risk areas), holding extra capital earned in "good years" to help fund "bad years," and diversifying their risk through the use of reinsurance and other financial instruments to cover especially large losses.

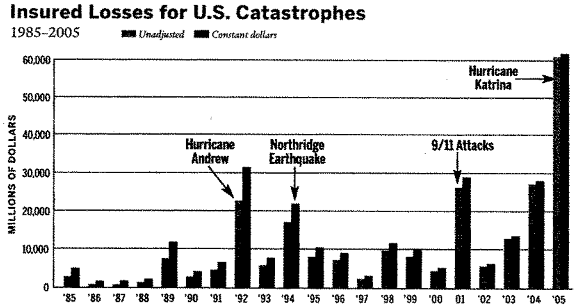
Hence, in order for private insurers to be willing to commit capital to underwrite catastrophe risk, they must be allowed to manage their risk and charge what they perceive to be adequate risk-based premiums to cover all their costs, including the cost of financial diversification and the relatively high cost of capital associated with underwriting a very volatile peril. This leads to two economically desirable outcomes: the supply of private capital is maximized, and the incentives of those who benefit from coastal property are properly aligned by paying the full cost of risk for coastal property.

Contrary to popular opinion, insurers are not immune from competition. In fact, insurance markets tend to be highly competitive because of the large number of insurers and low entry barriers to insurance markets. While it is true that loss shocks and/or the reassessment of hurricane risk can cause short-term tightening of the supply of insurance, over the long term insurers cannot sustain excessive prices. Any insurer that sought to do so would lose business to opportunistic competitors who would offer lower prices and still earn reasonable profits.

Figure 2

Insured Losses for U.S. Catastrophes

1985–2005

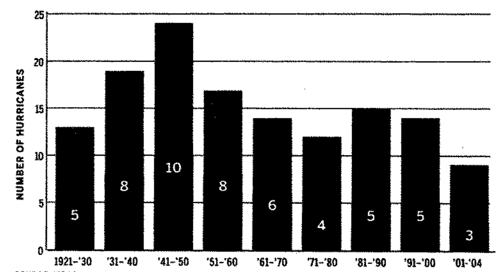


SOURCE: *Insurance Information Institute*

Figure 1

U.S. Hurricane Strikes by Decade

1821–2004 ■ *All* ■ *Category 3-6*



SOURCE: *NOAA*

Estimating and pricing catastrophe risk is a speculative enterprise that requires the use of sophisticated but inherently imperfect mathematical models. The models are plagued by considerable "parameter uncertainty" – modelers and insurers cannot be sure that they have exactly measured the "true" risk of hurricanes. Criticism of the models is one of the tactics used by politicians and their allies to challenge insurers' actions. While no model should be considered perfect and error-free, the firms that are putting their capital on the line need to be the arbiters of what they use to estimate and price the risk they underwrite. Ultimately, market forces and competition will drive insurers to use the most "reasonable" estimates of hurricane risk to price and manage their exposures. Several new companies have formed to mine carefully certain market niches, but the fact that venture capitalists have not jumped in to write large amounts of property insurance in hurricane-prone areas is telling in terms of their assessment of the current market price for the business.

Prior to Hurricane Andrew in 1992, insurers paid little attention to the growing risk posed by hurricanes, so insurance was relatively cheap and readily available. They generally did not use catastrophe models and did little to control their catastrophe exposures. Hurricane Andrew was a wake-up call to the insurance industry, which quickly and dramatically responded to the message. Using catastrophe models to assess their risk, insurers sought to raise their rates and adjust their exposures to reflect the new reality. However, political resistance only allowed gradual adjustments by private insurers and subsidization of government-provided insurance further undermined market price signals, especially in Florida.

By 2004, insurers believed that their overall rates and exposures were close to where they needed to be, with the exception of continued regulatory constraints on rates in the highest-risk areas. Their experience in 1992–2004 was consistent with the models they were using at that time. However, the very active storm seasons of 2004–2005 made them realize that their current models had substantially underestimated the risk they now faced. At the same time, weather scientists were warning that the hurricane cycle that had started in the late 1980s was intensifying and the probability of severe hurricanes was now much higher than it was at the beginning of the cycle.

Catastrophe models were revamped based on new information. Insurers sought to raise their rates further and cut their exposures in high-risk areas to attain new, economically sustainable positions. Coastal property owners and other interest groups vociferously protested the rate hikes – the new rates that were going into effect had finally reached a level that was negatively affecting the value of real estate in coastal areas. Politicians in Florida responded by attempting to create an insurance Disneyland (i.e., a return to the "good old days") by rolling back rates and expanding government subsidization of coastal property risk.

Florida is subject to the greatest problems because of its extensive development and its high exposure to hurricanes. But other states along the Gulf and Atlantic coasts are feeling the pinch of increased hurricane risk. Insurers are seeking to adjust their exposures and raise rates in all of these states, but not to the degree they are doing so in Florida. Northern coastal states face a significant but lower level of hurricane risk than southern coastal states. Still, coastal states besides Florida are facing increasing market and political pressures, and there is a significant danger that some may attempt to follow Florida's legislative and regulatory lead; they have already joined in calling for federal help.

MAKING TOO MUCH MONEY?

So-called consumer advocates and many politicians have strongly criticized insurers' actions, insinuating that the industry earns excessive profits and, hence, does not need to raise rates and control its catastrophe exposure. But most experts believe that insurers have under-priced catastrophe insurance historically based on models that underestimated the risk of hurricanes, and their recent actions are understandable in light of the risks they face. This is reflected in insurers' relatively low rates of return on their overall operations and their negative long-term earnings in high-risk lines like property insurance in Florida. While insurers' historical performance should not be the only basis for evaluating their management of catastrophe risk, it is symptomatic of the catastrophe risk problem.

According to industry analysts, the historical average return on equity (ROE) for the insurance industry is 14 percent, approximately the same as the *Fortune 500*. However, over the last 10 years the insurance industry's ROE was 7.0 percent compared to the *Fortune 500's* ROE of 13.4 percent. Property-casualty insurers have substantially under-performed relative to less risky industries, and homeowners insurance has been one of the worst-performing lines of insurance.

One of the important fallacies we cited above is the common view that insurers' "book of business" is one big pot and that, as long as they are earning profits on their nationwide operations for all lines of business, they do not need to raise rates or manage their exposures in high-risk lines and geographic areas. However, this view is contrary to how insurers and other firms must run their business. In essence, each product line and "block of business," e.g., homeowners insurance in Florida, must be economically viable. Just as any firm would have to jettison or change an unprofitable product line, insurers must make sure that their operations in a particular line and area will earn a fair rate of return over the long term. Otherwise, it becomes a drag on an insurer's performance that owners and investors will not tolerate.

According to regulatory estimates, cumulative homeowners insurance profits in Florida have been negative for the period 1990–2005. Figure 3 shows that profits as a percentage of premiums varies from year to year, but the cumulative sum of profits in Florida is negative for both homeowners insurance and all lines of coverage. The few bad years have more than wiped out any profits that insurers earned in good years. Also, we should note that several Florida insurers went bankrupt or were seized by regulators after the 2004–2005 storms because they did not have national operations to bail out their Florida losses.

Writing homeowners insurance in Florida has been a losing proposition that is getting worse, not better. Hence, it is not surprising that insurers are not enthusiastic about writing large amounts of property insurance on Florida's coasts. For example, State Farm recently announced its decision to drop 50,000 policies in Florida, though regulators are challenging that decision. The reason that most have stayed at all is the size of Florida's auto insurance market and the hope that things will eventually turn around for property insurance. However, public officials are making it much harder for property insurers to stay and wait for better days.

Finally, we need to comment on insurers' payment of hurricane-related claims. Insurers are committed to satisfying their legal obligations to pay claims arising from their contracts because that is the purpose of the business they are in, and because deliberate attempts to underpay claims will result in severe regulatory and other legal sanctions, as well as reputation losses. That said, insurers also do not want to pay any more than they are legally obligated to pay, and disputes between insurers and claimants on how much should be paid are inevitable in some situations.

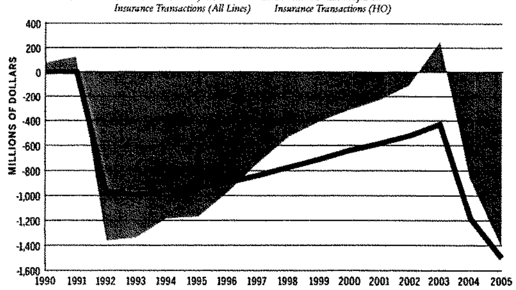
Settling claims arising from a hurricane that causes significant flooding, like Katrina, creates some special problems for claims settlement. First, the large number of claims strains insurers' claim-adjustment resources. Second, when a home suffers damages from both wind and flooding (or flooding alone), the potential for disputes significantly increases. Wind damage is covered under most homeowners insurance policies but flood damage (including storm surges from hurricanes) is excluded because of a government-industry understanding that it should be covered by the federal flood insurance program. However, most homeowners do not buy flood insurance unless forced to by lenders who hold a mortgage on their property. Hence, the many claimants without flood insurance are motivated to ascribe all or most of their damages to wind, while insurers are motivated to just pay for wind damage.

Disputes will naturally arise when the post-storm evidence does not clearly reveal the cause(s) of damage beyond any factual challenge that could be raised. Insurers are not infallible and likely have made some errors or too narrowly construed the cause of losses in some cases. However, this problem is much less significant than the allegation that insurers have deliberately and systematically sought to underpay hurricane claims on a wide scale. The more than $40 billion in insured losses from Hurricane Katrina indicates that insurers have made substantial claims payments even if some claimants do not believe they have been paid enough.

Figure 3

Cumulative Real Profit on Insurance Transactions in Florida

1990–2005 — *Cumulative Real Profits on Insurance Transactions (All Lines)* — *Cumulative Real Profits on Insurance Transactions (HO)*



SOURCE: *National Association of Insurance Commissioners*

FLORIDA'S LEGISLATIVE DISASTER

The last fallacy that warrants correction is that the government can substantially lower the cost of hurricane insurance without large subsidies from non-coastal property owners and taxpayers. This was demonstrated by the fact that Florida's insurance subsidization schemes required substantial assessments on all insurance consumers and taxpayers in the state to cover deficits arising from the 2004–2005 storm seasons. Despite that experience, in early 2007 Florida enacted legislation and implemented policies that further expanded and subsidized government-sponsored coverage and tightened constraints on private insurers.

The major changes in Florida essentially allow the state's insurer of last resort, Citizens Property Insurance Corporation (CPIC), to compete directly with private insurers. In the past, the CPIC's prices were mandated to be the highest in the state and its eligibility requirements were structured so that the CPIC would not undercut the private provision of insurance. Under the 2007 changes, its rates have been rolled back and a homeowner will be allowed to obtain insurance from the CPIC if its rate is lower than what the homeowner can obtain from a private insurer.

Prior to the new legislation, the CPIC had been growing rapidly in terms of the number of policies in force and exposure to loss (amount of insurance coverage written). It will grow much larger because of its restructuring. It had been projected that the new legislation will increase the CPIC's growth to a level of 1.36 million policies and over $400 billion in exposures by the end of 2007, but it now appears that this projection will be substantially surpassed. Hence, the CPIC will account for more than one-third of the state's property insurance market, but a much higher proportion of the state's high-risk coastal exposures.

In addition, the state, through its unique Florida Hurricane Catastrophe Fund (FHCF), is offering reinsurance to insurers at below-market rates through its power to assess (tax) homeowners, commercial, and auto insurance policyholders to pay for any future deficit. If significant losses occur, the FHCF can sell bonds and tax all insurance consumers, regardless of where they live in the state, to cover the deficit. A large catastrophic loss will require recapitalization, and current and future taxpayers of Florida will have to pay for the losses. Florida insurance regulators are also tightening their constraints on insurers' rates and requiring insurers to lower their rates based on the lower, subsidized cost of reinsurance from the FHCF (even if they do not buy reinsurance from the FHCF).

Florida further prohibited insurers from establishing Florida-only subsidiaries of national insurers. This prohibition is intended to extract subsidies from insurers' non-Florida operations, which is a flawed idea as we have previously explained. The purpose of single-state subsidiaries is to preserve a parent insurer's option to recapitalize a subsidiary after a major storm (or not) and make an insurer's Florida performance more transparent. While Florida has had a number of insolvencies after Andrew and the 2004–2005 seasons, none of the subsidiaries of national insurers have failed nor have they been abandoned. However, the new legislation and the attitude of the legislature may make insurers rethink their commitment to the Florida market.

The net effect of Florida's legislative and regulatory changes is to arbitrarily lower the cost of risk to Florida consumers (with coastal property owners getting the greatest benefit) and shift the additional risk to consumers of other insurance products as well as Florida taxpayers. The new policies will increase the state's reliance on smaller, unaffiliated insurers and government-subsidized insurance. This is a recipe for an economic disaster when the next major storm hits the state.

CONGRESS: BAIT AND SWITCH

Florida is not alone in assaulting the insurance industry. Many federal legislators from coastal states have attacked the industry and sought subsidies from non-coastal areas. They have criticized insurers for the settlement of Katrina claims, rate increases, and their actions to limit their catastrophe exposures.

Beyond criticism of the industry, there has been the discussion of what the federal government should do. Proposals include eliminating the industry's special antitrust status, constraining insurers' actions through state and/or federal regulation, and establishing some kind of national catastrophe plan. The most prominent proposal would make the federal government serve as a "reinsurer" to augment private insurance/reinsurance and state insurance/reinsurance funds. One objective of the plan would be to encourage more states to establish state reinsurance mechanisms like the FHCF. There is a heated debate among insurers and others as to the need for and soundness of such a plan, but there are many federal legislators who appear to be favoring the scheme.

Government insurers are notorious for failing to charge adequate, risk-based rates because of political pressure. That is why they often run deficits that are covered by people who buy insurance in the private market and by taxpayers. Indeed, one Florida ex-legislator has been quoted as saying that he expects the federal government will bail out Florida's unique hurricane reinsurance fund because of the state's political clout – a factor he suggested figured positively into the Florida's legislature's expansion of the fund. Inadequate self-funding is the all-too-common experience at both the state and federal levels. The two most prominent federal insurance programs – crop insurance and flood insurance – have continued to generate deficits that have been covered by general fund appropriations. Government insurance programs are often sold with the fiction that they will reduce the need for taxpayer-funded disaster aid. The unfortunate reality is that we get the worst of both worlds – taxpayer-subsidized insurance (i.e., a contractual entitlement) and more disaster aid. A recent working paper by David Cummins, Michael Suher, and George Zanjani estimates that the net present value of the federal government's liability for disaster aid related to natural catastrophes (over a 75-year period) is between $1.2 and $7.1 trillion.

The net effect of the federal proposals would be excessive coastal development, reduced motivation to build hurricane-resistant structures or strengthen existing ones, and a reduced supply of private insurance. Taxpayers would end up subsidizing the cost of the additional increase in the risk of hurricane losses because of federal and associated state policies.

A BETTER COURSE

The supply of catastrophe reinsurance has increased since 2005. There has also been rapid growth in securitizing catastrophe risk with other financial instruments, but the amount of such financing has fallen far short of its potential. Even at the primary level, insurers are seeking to move to a new, sustainable equilibrium and some insurers are considering cautious expansion of their operations in hurricane-prone areas. It is not a problem of supply – investors are happy to invest in insurers, reinsurers, or catastrophe securities at the right price. The problem is one of demand. If the federal and state governments are willing to supply under-priced insurance and reinsurance as well as constrain insurers' rates, who will be motivated to pay for adequately priced private capital?

The quickest and best solution would be to remove the constraints on private markets. The government could help by allowing insurers to set aside reserves to fund future catastrophe losses with the same kind of tax treatment that other kinds of loss reserves receive (most European countries allow catastrophe reserves). It also could make it easier to issue financial instruments (e.g., cat options, cat bonds, etc.) in the United States to cover catastrophe risk with the kind of appropriate tax treatment that they receive in other countries.

For those committed to the idea of a government reinsurer (whether its need is demonstrated or not), one might propose that it issue pre-event catastrophe bonds rather than engage in post-event borrowing and assessments that run a greater risk of taxpayer subsidies. Government purchase of catastrophe options also might be more feasible given that its portfolio of exposures would be aligned with the parametric triggers (e.g., total losses for a region or the United States) that would be used for such options. Private insurers and reinsurers could help to facilitate the aggregation of exposures (servicing policies as well as underwriting lower layers of risk) and ceding higher risk layers through adequately priced excess-of-loss reinsurance contracts with a government reinsurer.

The primary advantage of this approach would be that the government would pay for the cost of issuing catastrophe bonds (and/or options) up front, which in turn should be reflected in the premiums paid by those (e.g., property-owners) who ultimately receive the protection. There is precedent outside the United States for this approach: pre-event financing is used by the multi-country Caribbean Catastrophe Risk Insurance Facility. We can learn from innovations such as this and from the policies and institutions of other countries. Indeed, proposals for alternative plans have already begun to surface that may offer more economically sound approaches to pooling and diversifying catastrophe risk.

CONCLUSION

Homeowners insurance, especially in light of recent trends in hurricane frequency and severity, must be priced in accordance with the insured risk and associated costs. Further, any legitimate insurance arrangement, public or private, must manage its catastrophe exposure so that it can afford to pay its claims obligations if a disaster occurs. State and federal legislators do not appear to acknowledge this reality. In fact, Florida's insurance woes will not be solved unless and until the government allows private insurers to manage their risk and price coverage in a manner that will achieve a viable and sustainable property insurance market.

Florida's response to the increased frequency and severity of hurricanes has been to effectively ignore or grossly underestimate the risk. As a result of Florida's policies, hurricane losses will be further understated and regulated prices will be lower. Again, this short-sighted approach will likely yield even greater potential losses and a resulting loss of private market willingness to underwrite catastrophe risk in the state, with rippling adverse effects on other types of insurance. Other states may follow Florida's lead.

Federal legislative efforts in natural disaster financing may encourage the states to take on even more risks. According to a recent survey, state government assumption of exposures has grown from $57 billion in 1990 to $600 billion in 2007. The growth may be partially based on the states' hope for a federal program to bail them out after a disaster. That hope will likely grow if a flawed federal catastrophe program is enacted.

There are private market solutions to the problem of managing and insuring catastrophe risk. Private catastrophe financing would work better if the government did not constrain and compete against it. Tax-deferred catastrophe reserves like those European insurers employ to manage their long-term catastrophic risk would encourage private market participation, as well as the encouragement of catastrophe risk financing instruments. Allowing insurers to earn long-term profits consistent with the risks they face would also encourage insurers to increase the supply of insurance.

Private market solutions should be fully exploited before government financing of natural disaster risk is considered. Further, any government financing mechanisms that are instituted should be confined to fill a gap that private markets cannot fill (if such a gap is clearly demonstrated). Those mechanisms should be fully financed by risk-based premiums paid by those who receive the benefit of government protection, not subsidies from other insurance buyers and taxpayers. Such policies would promote more efficient management of catastrophe risk and avoid subsidies of excessive risk-taking in coastal areas. R

Readings

- "After the Storms: Property Insurance Markets in Florida," by Martin F. Grace and Robert W. Klein. Georgia State University working paper, Dec. 18, 2006.
- "Facing Mother Nature: Economics v. Politics," by Martin F. Grace and Robert W. Klein. Georgia State University working paper, June 26, 2007.
- "Federal Financial Exposure to Catastrophic Risk," by J. David Cummins, Michael Suher, and George Zanjani. Working paper, July 31, 2007.
- "Increased Hurricane Risk and Insurance Market Responses," by Martin F. Grace, Robert W. Klein, and Zhiyong Liu. *Journal of Insurance Regulation*, Vol. 24 (2005).
- "The 2007 Review of the Insurance Securitization Market," by Morton N. Lane and Roger G. Beckwith. *Trade Notes* (Lane Financial LLC), April 20, 2007.

Tallahassee's Homepage
Tallahassee.com

June 25, 2009

Our Opinion: Override this veto

Lawmakers should revive consumer choice

|

The Florida Department of Insurance Regulation has been claiming that, since 2006, 40 new property insurance writers have brought $4 billion in capital to Florida to cover homeowners in the event a heartbreaker of hurricane turns coastal properties into a rubble.

This new business and big capital coming into the state was, ostensibly, a reason that Gov. Charlie Crist on Wednesday vetoed the Consumer Choice Bill, which might well have made State Farm strongly consider returning to Florida to cover homeowners who have long been loyal customers. State Farm said it was leaving the state following an ugly showdown with the governor two years ago over its homeowner rates.

The veto should be subject to a legislative override, however, and Sen. Mike Bennett, R-Bradenton, said Wednesday afternoon that this is definitely on the table.

An override is a serious move, and a big one requiring lawmakers to come back into session, but property insurance — or the lack of its reliable availability — is a serious, big issue in our state, and hurricane season is well under way.

Along with Mr. Bennett's desire to see Insurance Commissioner Kevin McCarty resign "for making misleading statements and bending facts ... because he has a personal vendetta against State Farm," Mr. Bennett said it's in the Legislature's purview to reaffirm, though an override, this legislation that won strong bipartisan support in both chambers during the session.

New capital and new companies are important, because the state's insurer of last resort, Citizens Property Insurance Corp., is so underfinanced that it couldn't possible pay off claims in the event of major storm damages.

Yet, according to Department of Insurance financial documents obtained Wednesday by the *Democrat*, that $4 billion in new capital is not going to fortify the everyday Floridian who has property insurance despair.

That's because $3.8 billion of that $4 billion is coming from what are known as surplus lines.

What it means

Rep. Bill Proctor, R-St. Augustine, co-sponsor of the vetoed measure, described surplus lines as "companies that operate on a permit rather than a license and typically pick up facilities no one else will insure, like a $4 million house on a key, or a condo high rise on the beach."

"Surplus lines have no regulation on cost, no limits on the upper rates, and they won't be insuring the average homeowner with a home in Live Oak," Mr. Proctor said. "If you're going to drive major companies out of the state on the condition that you've got these budding new companies that will fill the gap, but in reality $3.8 billion of that $4 billion is in surplus line companies, well, that's not money that protects the average homeowner."

The vetoed legislation (HB 1171/SB 2036) would have deregulated rates for large, well-capitalized insurers, perhaps 20, allowing them to charge higher rates provided they made the transactions transparent with respect to fully regulated policies. The bill recognized free-market choices consumers want and are willing to pay for when service and security are at stake.

"When you look at the statewide polling, the broad support from every caucus, the Chamber, Associate Industries," said a frustrated Mr. Bennett, "I think the governor's staff gave him bad advice." He said supporters are talking to other members "to see what the appetite for an override is."

Conversely, said OIR spokesman Ed Domanski, "Commissioner McCarty knows that Gov. Crist carefully considered this bill and has done what is best for the people of Florida."

As we've said before, the "people's governor" should let the people make the decision about who will insure their homes and what they're willing to pay.

He took away this option in vetoing the Consumer Choice Bill. Lawmakers should reconvene and reaffirm support for homeowners by overriding the veto.

Hurricane Charlie
The Republican Barney Frank.

Florida Governor Charlie Crist is running for the U.S. Senate next year, and we wonder if one reason is that he doesn't want to be in Tallahassee when the next hurricane hits his state. His veto of a hurricane insurance reform bill last week all but guarantees a state disaster on top of any wrought by Mother Nature.

The bill would have trimmed the cost of a state-run enterprise that insures homeowners against storm damage. The program has an $18 billion unfunded liability and has taxpayers on the line for tens of billions in property losses from the next major hurricane. The Republican legislature tried to reduce those future losses, but Mr. Crist sounded like Barney Frank rolling the dice on Fannie Mae in declaring there's nothing to worry about.

By way of background, two years ago Mr. Crist gave a big gift to coastal property owners by converting the state of Florida into one of the world's largest property insurers. The Citizens Property Insurance Corporation provides below market-rate insurance policies directly to homeowners. Meanwhile, the Florida Hurricane Catastrophe Fund (CAT) regulates how much private insurers can charge homeowners and requires companies to purchase low-cost reinsurance from the government. Mr. Crist didn't invent these programs, but he vastly expanded their reach -- to about one million policies today. He transformed Citizens from insurer of last to first resort.

Here's the problem: This system isn't even within a coastal mile of being actuarially sound. The state government acknowledges that in many high-storm risk areas the premiums are from 35% to 65% below what is needed to cover potential claims. That subsidy has made Mr. Crist popular with many coastal residents even as the state plays Russian roulette with the weather.

The reform, which passed with wide margins, would have allowed large private insurers to compete with Citizens and charge whatever premiums they wish. This would give homeowners a wider range of choices, and it would let private insurers spread hurricane risk around the world through reinsurance. The big and well-capitalized insurers -- including Allstate, Nationwide and most recently State Farm -- have either curtailed operations or withdrawn from the Sunshine State because they can't make money charging subsidized rates. The companies could be bailed out under the CAT reinsurance program, but the fund may run out of money when a big one hits.

Mr. Crist and the media portrayed the reform as a giveway to the big insurers, and the Governor claims people can't afford "large and unpredictable" increases in premiums. The truth is large increases are precisely what is sometimes needed to cover the risk of living on coastal property. Mr. Crist's program makes the long-term losses much more severe because cut-rate insurance has encouraged overbuilding in coastal areas that are historically in the path of hurricanes. "We are one major hurricane away from an economic disaster in this state," says House bill sponsor William Proctor.

Mr. Crist is also pushing a federal disaster-insurance fund, probably because he knows the risks he's taking and wants all American taxpayers to bail out his Florida schemes when future hurricanes hit. Meantime, he continues to perpetuate the myth that Florida property owners can have billions of dollars of subsidized insurance at little expense or risk. It's this kind of something-for-nothing economics that gave us the debacle of Fannie Mae. With that philosophy, Mr. Crist would feel right at home in Washington.

Printed in The Wall Street Journal, page A11

Good Morning. I'm Senator Steve Geller. Until I retired from the Florida Senate in November, because of Term Limits, I was the Minority (Democratic) Leader of the Florida Senate. I'm past National President of the National Conference of Insurance Legislators (NCOIL) and chaired their Natural Disaster Subcommittee. I served on the Insurance committees in the Florida House and Senate for 17 years. I was Chairman of the Property and Casualty Insurance Subcommittee of the House of Representatives when Hurricane Andrew struck. During my tenure as NCOIL President, one of my top two priorities was the issue of Natural Disaster insurance. I was the first State Legislator to push this issue at meetings of the National Association of Insurance Commissioners (NAIC). I've worked with the insurance industry on Natural Disaster insurance, although the industry remains deeply divided. I've spoken across the Country on the issue of Natural Disaster insurance.

I'm not here today to speak specifically on Congressman Klein's bill, although I think that it's a good bill. I leave the specifics up to Congress. What I can tell you is that a National Natural Disaster program of some type is absolutely critical. Some type of Federal Backstop, such as TRIA (Terrorism Risk Insurance Act) is necessary for natural disasters. Expanding the National Flood Insurance Program (NFIP) to cover all Natural Disasters would also work.

NCOIL supported the formation of TRIA. I served as Vice-Chair of the newly created Terrorism Insurance Select Committee of NCOIL in the days following 9/11. The feeling in NOIL and Washington was that it was impossible to charge an adequate premium for an unknown risk, and that without insurance coverage, many of our major buildings would be unable to operate. I believe that the same principle applies to Natural Disasters, that is, an inability to charge an adequate premium for an unknown risk. Many people, including Members of Congress, suggested that TRIA be extended to cover Natural Disasters.

One of the main arguments against including Natural Disaster coverage with TRIA was the argument that Natural Disasters could be adequately priced based on historical losses, while insured damages due to terrorism could not be adequately predicted. Mr. Chair, since TRIA was enacted in 2002, this argument has proven to be false. The insurance industry in general no longer looks at historical data to price Natural Disaster insurance; it now uses modeling to set rates. I would submit that the damage from a one in one hundred fifty year earthquake or hurricane is as unquantifiable and unpredictable as the damage from a terrorist attack.

Some people, including Members of Congress, have suggested that the NFIP be expanded to include all Natural Disasters. I certainly feel that this would also be an appropriate method of spreading the risk, which is the purpose of insurance. There are issues which would need to be considered here. First, NFIP is primary insurance, not reinsurance, which would lead to greater involvement by the Federal Government, and also mean that people that purchased homeowners insurance but not a Natural Disaster policy would not have any Natural Disaster coverage. Also, most flooding from lakes or rivers is predictable based on historical data, while other types of rare Natural Disasters may not be. The NFIP has required certain mitigation to be eligible for coverage. This mandatory mitigation could help reduce the costs in the event of certain natural disasters.

I know from my days at NCOIL that many of my legislative colleagues, especially those from the center of the country, have asked why their constituents should pay so that a few wealthy people can live on the coast and have their homes repeatedly destroyed. They're confusing windstorm with flood insurance. Unlike areas near major rivers, which flood repeatedly, or coastal communities, where homes on the beach were destroyed and rebuilt more than once, that simply doesn't happen in Florida with any frequency. Although there is a good chance of a hurricane striking somewhere in Florida, the chances of a hurricane hitting any particular area or home are quite small. We simply don't have the problem of homes being repeatedly destroyed by hurricanes and being rebuilt again and again.

It's also not an issue of a few wealthy people living on the Beach. Many of my former constituents in Century Village Pembroke Pines, a senior community located much closer to the Everglades than the Ocean, will tell you that they can't make ends meet with the high cost of windstorm insurance. They'll tell you the same thing in Hollybrook, another senior community, and throughout South Florida. I don't think that anyone is seriously suggesting that we should abandon Miami Beach or Fort Lauderdale, Hallandale Beach or Hollywood. They're all coastal cities. Close to 80% of the population of the state of Florida lives in our 35 coastal counties, and no part of the state is more than 80 miles from the coast. And it's not just a Florida issue.

Mr. Chair, I have a DVD that I believe will be fascinating viewing, and that I'd like to enter as a supplement to my remarks. Although its 15 minutes long, if time permits at the end of my remarks, I request permission to play about 2 minutes of it. With the permission of the Weather Channel, it's the introductions to 20 episodes of their television series *It Could Happen Tomorrow*. Each of the 20 episodes deal with natural disasters that could occur tomorrow, causing anywhere from hundreds of deaths to hundreds of thousands of deaths, from billions of dollars in damage, to hundreds of billions of damage. This list includes wildfires in Austin, San Diego, and Los Angeles, Flooding in Boulder and Sacramento, Earthquakes causing tsunamis in Hawaii and the Pacific Northwest, Hurricanes in New York City, Savannah, and Houston, Earthquakes in San Francisco, New Madrid Missouri, Seattle and Las Vegas, a Volcano in Washington State and F4 or F5 Tornados in Washington, DC, Dallas and St. Louis. Mr. Chair, it's a National issue. The most expensive hurricane wouldn't hit Florida, it would hit New Jersey on its' way to New York City. The most expensive natural disaster wouldn't be a hurricane; it would be a volcano, or an earthquake, probably an earthquake hitting the center of the country at the New Madrid fault.

I will add that of those 20 natural disasters, the only ones that would be covered by the Federal Government are the ones involving flood, which would be covered, to the extent that people purchase insurance, by the NFIP. This committee knows that the Flood program operates at a deficit. What you may not know, while the rest of the country says that Florida should deal with its own issues, is that almost every state runs a deficit, while one state pays far more into the flood program than it receives. That state is Florida, which subsidizes the natural disasters in the rest of the country.

If any of the natural disasters I mentioned occurs, Congress will have to step in, or else face a collapse of the financial system. If a natural disaster costing $100 billion occurs, and Congress does nothing, the insurance industry will become insolvent. If the insurance industry can't pay off homeowners policies on homes that have been destroyed, the banks that loaned money on the homes without insurance will fail. Even if the insurance companies stay afloat, many banks won't. In California and many other states, banks don't require insurance coverage for earthquakes. Because of the high cost of earthquake insurance, it's estimated that less than 12% of California homeowners have purchased earthquake insurance. Does this sound familiar? I've been predicting it for years.

The insurance industry is trying to protect itself from potentially devastating claims by charging enough to cover 1 in 100 year or more claims. By definition, those claims are not likely to occur in the lifetime of anyone in this room, or anyone paying insurance. The insurance industry is dealing with both actuarial risk and time risk. If there's a 1 in $100 year event that would cost $100 million dollars, on an actuarial basis, and ignoring taxes or earnings, the industry could charge $1 million a year for 100 years for reserves, and that number would be actuarially sound. However, because of time risk, the insurance industry is trying to raise that $100 million as soon as possible, or else buy re-insurance to cover it. That raises rates to an impossible amount. Only the Federal Government can absorb the time risk, while charging actuarially sound rates.

Let me give you some concrete examples of how great these savings could be if Congress steps in and eliminates the time risk. In Florida, the state catastrophe CAT fund charges approximately $6.50 per hundred dollars of insurance coverage up to about $16 billion dollars of total coverage, which is about a 1 in 33 year event. The private sector charges about $30.00 per hundred, or about 4 ½ times as much. In the layer of reinsurance over $16 billion dollars, the CAT fund charges approximately $2.50 per hundred dollars of insured coverage, while the private sector charges about $25.00 per hundred. This is about ten times as much. The public sector (CAT) numbers work out to percentage savings of 77.7% to 90%.

In Florida today, as far as we can tell on a statewide average, over 50% of all windstorm dollars go directly to pay for reinsurance. In South Florida and other coastal areas, this number is much higher, up to 80% or 90%. Using simple math, if 80% of the windstorm premium in South Florida goes to reinsurance, and if the blended rate charged by the private sector is only an 80% savings, than total windstorm rates in South Florida could be reduced by 60-65%. Mr. Chair, we're talking about cutting windstorm rates by over 60% here in South Florida with an appropriate Federal program.

It is also very difficult for the Insurance industry to build the reserves that they would need to pay claims. As the Members of the Financial Services Committee know, the United States is one of the very few countries in the world to charge a tax on the income generated from natural disaster reserves. Because of the negative impact that changing this would have on the U.S. Treasury, I do not expect this change to be made in the foreseeable future.

I believe that the high cost of windstorm insurance is the single biggest issue in the State of Florida today. Many people pay more in homeowners insurance than they do on their mortgage or property taxes. Businesses have to raise their prices to pay for the high cost of windstorm insurance. And Florida is the Canary in the coal mine here. The same problems are starting in New York and New England, and the Gulf states.

There is no prediction on how much homeowners and businesses would save Nationwide with a Federal program. There are many, many variables. Would the Federal program be primary, like NFIP, or be reinsurance? If reinsurance, what would be the attachment points, limits, and co-pays? Reinsurance rates vary by region and type of disaster. The rates vary every year. For example, in Florida, reinsurance rates are scheduled to increase this year by about 15%. They vary by company, and who they purchase reinsurance from. In Florida, for example, State Farm buys reinsurance from the State Farm parent company, purportedly at lower rates than they could from other companies. They vary based on what level companies begin to reinsure at, and up to what levels. Some companies choose to reinsure to a one in one hundred year event, while others may reinsure to a one in two hundred fifty year event. There are many other variables as well. What we do know is that a Federal program of either reinsurance or direct insurance would generate major savings on Natural Disaster insurance, probably in the range of 25% to 50%. The savings can be calculated reasonably well once the parameters of the plan are established. I gave you examples earlier that were South Florida specific, and assumed a program similar to our state CAT fund.

Although this issue has been important for years, it's particularly important now. President Obama campaigned in Florida on a promise to enact a Natural Disaster program. And the current fiscal crisis raises the stakes even more.

The root of our current financial mess is the housing crisis. Congress has been working on ways to keep people in their homes. When people are paying as much for homeowners insurance as they are for their mortgage, a 25%-50% reduction in their insurance rates helps fare more than a 20% cut in their mortgage payments. Let me repeat this. In many areas of the country, the single best thing that Congress can do to keep people in their homes is to pass a Natural Disaster insurance bill. The best stimulus package we can pass is not sending everybody $200 dollars; it's reducing their insurance premiums by hundreds or thousands of dollars a year. Let the consumers spend those savings in restaurants and stores, and we'll have a much greater economic stimulus than Congress passed. And let's improve our balance of trade. The majority of the reinsurers are in Foreign countries. Swiss Re. Hanover Re. Munich Re. Bermuda. Lloyds. Let's keep our dollars in the American economy instead of sending them overseas.

About two and a half years ago, I was primarily responsible for drafting that portion of major insurance legislation that increased the amount of reinsurance that the Florida CAT fund would issue. We passed this despite concerns that we were overextending our risk because we knew that our constituents simply could not continue to pay ever increasing premiums. As a result of this legislation, Florida companies reduced the amount of reinsurance purchased from foreign reinsurers. A friend of mine that was in Bermuda when this occurred advised me that there was rending of clothes and gnashing of teeth in Bermuda, because we were keeping more of our money here.

No state can handle these massive natural disasters alone. In Florida, we've done our part, with out CAT fund, and stronger building codes. We know that the Federal Government will step in after a major catastrophe occurs in this nation. By passing legislation in advance, Congress can act and prepare for the worst, instead of having to react. This preparation will also dramatically reduce insurance premiums, and benefit taxpayers all across the nation. I will leave up to the wisdom of this committee what type of program would work best, whether that be a TRIA type program, a NFIP type program, or simply having the Federal Reserve guarantee low cost loans to pay off Natural Disaster claims, thus dealing with the time risk issue. I like Congressman Klein's bill. We're not asking for a handout, just a hand. Mr. Chair, we need your help.

Thank you.

Thank you for the opportunity to express myself before this subcommittee. My comments will attempt to convey the views of a regional insurance agent who faces the daily routine of serving the homeowner community in Florida. Comments will be restricted to views of the Florida situation as that is the basis of my experience.

I have been a licensed insurance agent in this state for 31 of the past 36 years only interrupted for a period of 5 years when I worked in VA. I have personally seen and been part of a number of insurance crises in the state ranging from the Workers Compensation and Medical Malpractice crises of the 70's, the insurance capacity crunches of the 80's and 90's; and, most importantly, the homeowners' crisis that has essentially remained since Hurricane Andrew in 1993 and the evolution of insurance in the state to where we are today. All of this is now profoundly affected by the current economic crisis which is integral to our daily lives.

I overviewed some of the prior testimony and know you have heard from regulators and political leaders and have been provided statistics in support. I do not have actuarial promulgations but rely on history which repeats itself in one way or another and hands on experience.

Contrary to some reports:

- Insurance rates have been reducing significantly over the past two years thanks mostly to mandated Mitigation credits. Many consumers have, where possible, improved their own risk via hurricane shutters and new roofing up to code for example. The newer construction is not the issue but the older homes and the ability of those homeowners to afford improvements is. This is an area where State and Federal government can look to assist via tax credits, grants and the like. Better risks can only serve to enhance underwriting results which in turn affects pricing and availability.
- The number of companies has increased who are writing homeowners coverage in the state although Citizens remains the primary underwriter of such a risk.

This is good news! The bad news is:

- Florida's population growth has slowed significantly in recent years with property tax and insurance cited as key causes of retiring individuals to looking elsewhere and actually causing some residents to leave Florida. The term "halfback" has become common.

- Insurance rates are still higher than historical levels and the pressure is heavily felt on individuals and families due to the economy.
- Lowering insurance costs at this point in time would have limited affect on improving the housing markets and local economy – it is the economy which is having the most profound impact on the housing market.
- Other than less than a handful of national insurers who specialize in high valued homes, we no longer have any "brand" names writing homeowners insurance in this state.
- The market consists almost entirely from start up companies many of whom will not be able to sustain a substantial or perhaps less than substantial hurricane. This will place enormous pressure on state catastrophe and guaranty funds which ultimately will lead back to the consumer.
- The few rated companies (not demotech) who have been writing are getting saturated with business which could well threaten their future viability.
- The good news of decreasing cost carries some bad news in that these companies will have less money to pay losses which threatens future viability.
- There remains restrictive underwriting in "V" flood zone areas where coverage is either Citizens or Excess & Surplus Lines who have no rate restriction.
- We encounter seasonal and "Zip" code saturation where insurers attempt to avoid overextending in an area which does not help remaining homeowners.

Conclusion: We have availability and somewhat improved rates but are sitting on time bomb reliant on the weather - when and where will the wind blow. We still do not have a long term solution to the problem.

Keys to our future:

- Expand underwriting capacity which must be done by having "brand" names return to provide homeowners coverage in our state. A free market competition and economy will follow its own course and lower costs over time bases upon underwriting results. This will only happen if they perceive that they can control risk and have a reasonable expectation to earn a profit.

  - This is where Federal and State governments can and must provide vital support. As large as the insurance industry is, it is not sufficient to bear the entire risk. Catastrophic exposures due to population concentrations have become too significant. If insurers are able to better measure the risk due to a cap on their liability via affordable reinsurance whether private or public sourced, they can better risk a portion of their assets to write in a catastrophic area based upon perceived profits.
  - I would caveat that some regulation would be required to ensure that the benefit of such reinsurance plan is passed to the consumer and not retained in the profit coffers of insurers.
- While an insurer should still be subject to making a profit or loss based upon their underwriting prowess, they should not be punished by assessments for risks they do not underwrite. This is the greatest deterrent for an insurer to enter a market. Such type of volume assessments causes a pass through to the consumer and is reflected in insurer rate structures. Where it cannot be reflected, an insurer is discouraged from underwriting in a given state.
- Current private reinsurance which I believe has already been well publicized, views risk on an annual basis and prices accordingly but all recognize that catastrophic events occur over a longer period. The upward price reaction to a poor result year creates an uneven and volatile marketplace which culminates in sometimes severe pricing swings to the consumer. Additionally, there is often significant lag time in reinsurance payments to insurers which further pressures the primary provider. A plan which can level this process would prove most beneficial to the consumer.
- Essentially, I am an open market person but at the same time can see where the proposed legislation would have the Federal government act as a conduit to better reinsurance costs. With the proper integration of the plan into the insurance mechanism it is logical to believe it would result in a better purchasing environment for the homeowner.

Respectfully submitted,

Joseph A. Grillo, CIC
Senior Vice President
Weekes & Callaway, Inc.

TESTIMONY BY IVAN ITKIN BEFORE THE HOUSE FINANCIAL SERVICES OVERSIGHT AND INVESTIGATIONS SUBCOMMITTEE
July 2, 2009
West Palm Beach City Center
401 Clematis Street
West Palm Beach, FL 33401

Good morning, members of the House Financial Services Oversight and Investigations Subcommittee. My name is Ivan Itkin. I live in a beach-front, hi-rise condominium building located at 3200 N. Ocean Blvd. in the city of Fort Lauderdale. The building is 29 stories tall with 220 residential units and shares the 10-acre property with a similarly-sized building.

The residents of the complex, like others in Florida, have great concerns over the availability of windstorm insurance. With respect to my particular building, the condominium association has had great difficulty getting private hurricane insurance. Because of the possibility of hurricanes in our area and their potential for causing significant and widespread damage, private property insurance companies are unwilling to insure against such outcomes.

Prior to the current policy year, we were able to obtain insurance from one carrier, QBE, which now refuses to insure our building unless impact glass is installed in all our windows and doors. Even installing hurricane shutters will not suffice, although the building was built to the code established just a few years ago.

As a consequence, we are forced to get insurance from the state-created insurer of last resort, Citizens Property Insurance Corp., which is severly under funded and which will require large annual premium increases over a number of years from its policyholders. The deductibles are so high, that even if there is a major loss there will be no recovery. For our building, the deductible is 5% of the building's appraised value of $85,243,600 which requires a loss to exceed $4.26 million before a single dollar can be recovered, even though our annual premium is $339,090.

It is quite obvious to us that we are not adequately protected. We need another solution. We need a catastrophic insurance program like national flood insurance, a program that will provide protection against all naturally occurring catastrophes. I believe Congress needs to pass federal NATCAT legislation.

Thank you.

PROTECTING . . .
AMERICA.org
PREPARING FOR AND PROTECTING AMERICA FROM CATASTROPHE

Admiral James M. Loy, National Co-Chair
Former Deputy Secretary, Department of Homeland Security
Commandant, U.S. Coast Guard (Retired)

James Lee Witt, National Co-Chair
Former Director, Federal Emergency Management Agency
Former Chief Executive Officer, International Code Council

STATEMENT OF

JAMES M. LOY
ADMIRAL, USCG (Ret.)

NATIONAL CO-CHAIRMAN
PROTECTINGAMERICA.ORG

Before the
House of Representatives Committee on Financial Services
Subcommittee on Oversight and Investigations

July 2, 2009

Statement for the Record

Thank you to the members of the committee present and to Congressman Klein for your leadership on this very important issue. I appreciate the opportunity to appear before you today in my capacity as co-chairman of ProtectingAmerica.Org, an organization committed to finding better ways to prepare and protect American families from the devastation caused by natural catastrophes.

My fellow co-chairman is James Lee Witt, the former director of the Federal Emergency Management Agency. Our coalition's over 300 organizational members include first responder groups, including the American Red Cross, the International Association of Fire Fighters, emergency management officials, insurers like State Farm and Allstate, municipalities, small businesses, Fortune 100 companies and more than 20,000 individual members. The membership is broad and diverse and represents virtually every state in the nation.

ProtectingAmerica.org was formed in 2005 to raise the national awareness about the important responsibility we all have to prepare and protect consumers, families, businesses and communities from natural catastrophes. We have built a campaign to create a comprehensive, catastrophe management solution that protects homes and property at a lower cost, improves preparedness, and reduces the financial burden on consumers and taxpayers – all in an effort to speed recovery, protect property, save money and save lives.

Though we come from all walks of life, we share a common belief that the current system of "destroy, rebuild and hope" in the aftermath of extraordinary natural catastrophes is fatally flawed. Even more importantly in these difficult economic times, we cannot afford to face the threat of another large shock to our weakened housing and lending sectors.

A catastrophic event, be it an earthquake under one of our American great cities, or a massive hurricane making landfall near any of the metropolitan areas from New York to Houston, would cause such enormous damages that our economy would be rocked, private resources would be quickly depleted and a federal bailout of potentially hundreds of billions of dollars would be required. The American taxpayers have lost their appetite for bailouts. They would be far better served by a program that uses private insurance dollars to pre-fund coverage for the eventuality of a catastrophic natural catastrophe.

To that end, we believe that a comprehensive, integrated plan linking a national catastrophe fund with support to first responders and strong provisions for education and mitigation would best address the threat of the next mega-catastrophe. A national catastrophe fund will create a privately financed and federally-administered layer of reinsurance to complement and stabilize private market reinsurance alternatives and ensure greater availability and affordability for consumers of residential property insurance. It will do so by acting as a backstop for state catastrophe funds, which will protect the private market from collapse and ensure that resources are available to rebuild after a major catastrophe. Specifically, it will save constituents additional money on their homeowners' insurance and help states better manage the risk associated with mega-catastrophes, which are essentially uninsurable in the private market due to the timing risk.

Qualified state funds would be able to purchase re-insurance from the national program. Rates for this coverage would be actuarially based and would only be available to state programs that have established the prevention and mitigation funding. In the event that a catastrophe strikes, private insurers would be required to meet all of their obligations to their policyholders. Should catastrophic losses exceed those obligations, the state catastrophe fund would be utilized. In the event of an extraordinary catastrophe, the national backstop program would provide benefits to the state and help pay remaining claims.

Because this is a state-by-state program based entirely on risk, the likelihood of a taxpayer subsidy is virtually eliminated. This approach requires pre-event funding and relies on private dollars from insurance companies in the areas that are most exposed to catastrophe. As this program relies on the traditional private market for paying claims, the inherent inefficiencies and bureaucracy in a government-run program are eliminated.

This approach is far preferable to the de facto bailout we have witnessed with natural disasters in recent memory. Studies in the aftermath of Hurricane Katrina suggest that after-the-fact recovery funding for catastrophes results in an enormous taxpayer subsidy for uninsured and underinsured properties. In fact, a Brookings Institution study on the Katrina cost found that of the first $85 billion in taxpayer dollars spent on Katrina recovery efforts, more than $10 billion covered losses for uninsured or underinsured properties.

We believe a national catastrophe fund would actually buffer the already fragile housing and lending markets during this time of economic downturn. The proposed approach would reduce the threat of insurer insolvency and enhance the industry's capacity to pay claims. This in turn creates an important measure of stability to the catastrophic insurance industry and mitigates the shock to the US economy that a major natural disaster might otherwise produce.

ProtectingAmerica.org strongly believes in complementary readiness, preparedness and mitigation provisions. Ideally, the plan would require the national and state catastrophe funds to dedicate a significant portion of their investment income to local communities and non-profits to support mitigation efforts like building code development/enforcement; preparedness initiatives, such as those offered by the American Red Cross to improve education and training to ensure that citizens and organizations in their community are better prepared for natural catastrophes, and the equipment and personnel needs of first responder agencies, such as local fire departments.

When catastrophe strikes, our after-the-fact response programs and protocols do a remarkable job in getting victims into shelters and in mobilizing emergency supplies and personnel so that the situation does not worsen. All Americans, regardless of whether or not they have been victimized by catastrophe, owe our first responders an enormous debt of gratitude. Their service is invaluable.

Clearly, programs that would improve preparedness, increase public education, enhance prevention and mitigation programs, and augment support for first responder programs would improve our national capability to prepare and protect those of us who live in harm's way.

Public education programs would help homeowners to make necessary plans and be prepared in advance of an emergency. Mitigation programs such as strong, enforceable building codes and effective retrofitting programs would improve the integrity of catastrophe-prone structures so that damage would be minimized if catastrophe strikes. An increase in first responder funding would help finance these critical programs that too often get shortchanged in the give-and-take of local budgeting.

ProtectingAmerica.Org believes that in addition to minimizing the extent of catastrophic losses through prevention and mitigation programs, we must also reduce the taxpayer subsidy of recovery efforts, ensure the adequacy of recovery dollars, and improve the delivery of those critical funds to homeowners. To that end, we strongly advocate that the consumer savings provisions of the proposed legislation are maximized and receive every consideration.

Congressman Klein, thank you for your leadership on this important issue. Your continued persistence on behalf of all homeowners has given this issue the attention it deserves in Congress. Your current legislation, HR 2555, takes significant steps towards a comprehensive disaster preparedness policy for the federal government. As we have discussed, there are three key points that are critical to any comprehensive solution to the homeowners' insurance crisis and we welcome the opportunity to work with you going forward.

The National Reinsurance Program: Our goals are to generate additional capacity, bring more stability to the market, make high-quality insurance more available and ensure that consumers realize significant cost-savings on their homeowners insurance. The best way to accomplish this is to enable and encourage more states to create well-structured, actuarially-sound catastrophe funds and to supplement the reinsurance protection for the current state catastrophe programs in Florida and California.

To deliver meaningful premium savings for consumers and to allow for the maximum use of the reinsurance by differing programs in multiple states, reinsurance provisions should allow more flexibility on the attachment point (e.g. the Florida Hurricane Catastrophe Fund caps out at a lower point, approximately a 1-70 year event). In addition, it may be worthwhile to consider alternative means to fund the reinsurance program other than upfront appropriations of the entire potential liability since the odds of incurring this liability are very small. We believe a lower attachment point provides a seamless level of protection for policy holders.

Stabilization Provisions: We fully support provisions from HR 3355 to provide for liquidity loans as an additional option for states that qualify. We believe this is a key element to be included in a comprehensive program.

Prevention and Mitigation: We applaud you for making sure that better prevention and mitigation needs to be part of a comprehensive program. Our team of experts, on behalf of the

American Red Cross and other first responders, can serve as a useful resource to consider ways in which to enhance these provisions.

I would also like to address a common argument that making homeowners' insurance more affordable and available in high risk states would only encourage people to own homes in those areas. Under scrutiny and under present circumstances, I think you will reject those arguments as we have. The fact is that 57 percent of the American people already live-in areas prone to natural disasters. If we never built another stick of housing on the East or Gulf Coasts, anywhere in California or anywhere across the heartland, almost 6-in-10 families would still be at risk. This approach is instead a reasonable and actuarially sound approach that recognizes the reality of the threat and sets aside the money to deal with it. Moreover, we also advocate effective land use policies be adopted and enforced to protect undeveloped areas going forward.

I would also like to address another frequent criticism that is misplaced. Opponents of this legislation to include reinsurers suggest that homeowners or taxpayers in non-exposed areas will have to pay for the risks assumed by residents of exposed areas. The fact is under this approach, each state is left to assess the magnitude of catastrophic risk confronted by its residential property owners. States not susceptible to mega-catastrophes can opt-out of participation. As a result, taxpayers in those states would no longer be required to subsidize certain federal disaster relief efforts.

I am optimistic that now is the time to affect significant change in the way we address the threat of natural catastrophes. In fact, the political environment has never been more favorable. While campaigning in Florida last fall, then-Senator Obama made a full and public commitment to enacting the Homeowners' Defense Act of 2007. Florida Governor Charlie Crist has made the creation of a national catastrophe backstop a top priority and has worked with federal officials from both parties to make it a reality. Texas Governor Rick Perry and Louisiana Governor Bobby Jindal are both strong advocates of this approach. Senator Bill Nelson, who has brought a deep understanding of insurance issues to the Senate, has been a leader on this issue as well.

This needs to continue to be a top national priority. It reflects strong leadership to act before the next crisis. We believe it is time for the federal government to take action on this important issue and that with your assistance, and with the support of the Obama Administration, together we can get this critical legislation passed into law.

Congressmen Klein and Moore, I want to thank you again for taking the time to consider and discuss this important subject. I would be happy to answer any questions that you may have.

Submission of your Testimony

Statement – S. Colleen Repetto (FIRM)

I am the Executive Director of FIRM (Fair Insurance Rates in Monroe) from Monroe County, FL, aka The Florida Keys. We are a 501c4 grassroots organization that began at a backyard barbeque in 2006. FIRM has grown to 5000+ members countywide, we are run by volunteers, and funded through donations.

FIRM brought attention to the statewide windstorm insurance crisis by successfully challenging Citizens Property Insurance 2006 Monroe County rate filings. In 2004, a 1900 sq. ft. home built to withstand the 150mph winds with hurricane protection was paying $3000 a year in windstorm premiums. By 2006 this same home was billed $15,900 for a one year premium and had never filed a wind claim. As the result of FIRM's engineering, meteorological, geographical, statistical and historical verified facts which proved that our county had been charged excessive windstorm rates, the Office of Insurance Regulation rolled-back our rates by 32%.

The rate was not the only issue. A Florida law allowing insurance companies to use or bill rates and then file them for approval was devastating to our policyholders. At the extremely high rates, people were receiving invoices for $9,000 to $25,000 for one year's premium on an insurance policy that, in the Keys because we build to 150 mph winds, it was highly unlikely that the majority of insureds would ever have damage greater than their deductible, and therefore have no claim against their policy. FIRM lobbied our state legislators to help repeal, although temporarily, the use and file law. Insurance companies currently must file their rates with the OIR before billing their policyholders. We continue to press to make file and use a permanent law.

Contrary to popular perception, Monroe County is not a wealthy county. We have many low and middle income residents who could not afford this insurance and were in distress at how they would provide the coverage that their mortgages required.

Currently, risk models used in setting rates do not separate wind and flood and therefore do not accurately reflect probable maximum loss caused by each. There is no "all risk" hurricane insurance. Wind is provided by state or private insurers, and flood is a federal program. Claims can be delayed for years until the damage is proportionately assessed which cause additional financial burdens for property owners trying to get their lives back on track after a devastating storm. We feel strongly that federal funds, which are really all taxpayer dollars, should not be the first line of financial relief for natural disasters.

The National Climatic Data Center (a division of NOAA) tracks and evaluates natural catastrophic events that have great economic impact. In 2008 alone, $58 billion for insured and uninsured properties was spent in 44 states before the ice storms in the Northeast in December.

FIRM believes in personal responsibility especially in high risk areas. Property owners should strengthen their buildings to meet or exceed their regional perils and buy insurance. “All risk” policies could be provided by private insurance companies capping their losses followed by state catastrophe funds paying “all risk” claims to their cap loss, with a federal financial obligation guarantee to kick in as a backstop.

Consumers need to be educated on the cost/savings benefits of strong building and mitigation and offered low interest loans or grants to better withstand the high risk. Local governments have a responsibility to properly and appropriately develop land use regulations and enforce strong building codes.

Windfall tax dollars generated by rebuilding and repairs after a storm should be used to build state cat fund reserves, fund mitigation programs and/or reduce premiums in the areas where they were collected. These unanticipated tax revenues should not be allowed to be deposited into general funds for use in any other way.

All-in-all a comprehensive multi-level “all risk” catastrophic insurance program needs to be implemented to preserve assets, protect the lives of our citizens, and maintain stable communities.

We are grateful to participate and tell our story. Thank you.

Information about You

S. COLLEEN REPETTO
806 Corte del Sol -- Marathon, Florida 33050 – (305) 743-5348

PROFILE
PROFESSIONAL EXPERIENCE

FIRM (Fair Insurance Rates in Monroe) **2006-Present**
Board Member and Executive Director

- Assisted to bring about significant changes in windstorm insurance in Monroe County
- Raise funds by donations to support our 501C4 non-profit organization
- Represent Monroe County residents' insurance issues to the state legislature
- Make presentations to County residents on windstorm insurance issues
- Continue to work on residential, commercial-residential and commercial windstorm issues
- Appointed Funded Consumer Liaison to the National Association of Insurance Commissioners
- Present consumer issues to a variety of government insurance committees or departments, such as the Florida Commission on Hurricane Loss Projection Methodologies, the Florida Office of Insurance Regulation, the Governor's office, the Florida Consumer Advocates Office, and other government entities.
- Assist consumers with their insurance complaints and claims resolution

My insurance education consists of volunteering to work with FIRM as a start-up, grassroots organization to bring about fair, equitable and non-discriminatory windstorm rates for the residents and property owners of Monroe County. It's been an on the job learning process and our success is testament to our facts and our resolve.

FIRM, nor I, receive any federal grants and do not have, or have had, any federal contracts.

FIRM was founded in 2006 at a backyard barbeque. It quickly turned into an organized group of dedicated residents who raised funds to help hire experts to provide the facts and figures to show why Monroe County should not be paying the exorbitant rates used by Citizens Property Insurance Corporation in 2006. We are a 501c4 organization, funded by donations and staffed by volunteers. We have 5000+ members countywide. FIRM has never received any federal grants and has never had any contracts with the federal government.

FIRM
FAIR INSURANCE RATES IN MONROE
www.FIRMKeys.org

"The Homeowners' Insurance Crisis: Solutions for Homeowners, Communities, and Taxpayers"

A Presentation to the
Subcommittee on Oversight and Investigations
Field Hearing
West Palm Beach, FL

S. Colleen Repetto, Executive Director, FIRM
(Fair Insurance Rates in Monroe)
Thursday, July 2, 2009

Who is FIRM?

FAIR INSURANCE RATES IN MONROE
www.FIRMKeys.org

- FIRM is a 501c 4, grassroots organization founded in Key West with 5,000+ members countywide, run by volunteers and funded through donations
- Brought attention to statewide windstorm insurance crisis
- FIRM successfully challenged Citizens Property Insurance Corporation (CPIC) 2006 Monroe County FL windstorm rate filings
- The Office of Insurance Regulation therefore rolled-back Monroe County residential rates by 32% resulting in an effective rate of $13.44/$1,000 of coverage
- FIRM has worked with a coalition of consumer groups around the state of Florida for insurance reform

Residents' Dilemma

FIRM
FAIR INSURANCE RATES IN MONROE
www.FIRMKeys.org

- 1900 sq. ft. home with Class A Shutters paid $3,000 in 2004 for windstorm insurance
- The same1900 sq. ft. home with Class A Shutters billed $15,900 in 2006 for windstorm, never having filed a claim
- 2006 rates meant that the average residential property owner paid $610 a month in windstorm premiums alone excluding other related fees and surcharges
- 2006 windstorm premiums represented 17% of the median household income on average
- Entry level home ownership was out of reach for most young families and rents rose dramatically
- Recruitment and retention of teachers, healthcare workers, police, firemen, hourly workers in the tourism industry, and retirees and long-term residents living on fixed incomes were driven out of the county because they could no longer afford to live in the community
- Escalating insurance premiums devastated real estate market as windstorm insurance premiums were becoming a "deal-breaker" in real estate transactions
- Citizens 2006 rate increase represented $35 million dollars of lost disposable income with a proposed 37% increase representing a potential $79 million dollars out of our pockets

The Hurricane Insurance Challenge

FAIR INSURANCE RATES IN MONROE
www.FIRMKeys.org

- Two simultaneous perils – wind and water
- Wind insurance is provided by private insurers and Citizens Property Insurance Corp.
- Flood insurance is a federal program
- Current risk models do not separate the perils and, therefore, do not accurately reflect probable maximum loss for damage caused by each
- "All risk" policies would eliminate this problem

Delays are Costly to the Consumer

FIRM
FAIR INSURANCE RATES IN MONROE
www.FIRMKeys.org

- Currently, policyholders' claims can be delayed by each insurer until hurricane damage is assessed proportionately to wind and flood
- Repair and rebuilding delays cause considerable additional financial burdens
- Lifestyle is continuously interrupted
- It can take years to properly settle claims

National Climatic Data Center (NCDC - Division of NOAA)

- "Nations Scorekeeper" when addressing severe natural catastrophic events in their historical perspective
- NCDC tracks and evaluates climate events in US and globally that have great economic and societal impacts
- US has sustained 90 natural disasters over the past 29 years in which losses, insured and uninsured, exceed $700 billion
- In 2008 alone, an estimated $58 billion was spent on weather related events in 44 states before accounting for the Northeast ice storms in December

Source: National Climatic Data Center (NOAA)

Layered Insurance Coverage

FAIR INSURANCE RATES IN MONROE
www.FIRMKeys.org

- If in fact, a majority of states suffer from natural catastrophic events, then high risk areas should have 4 levels of "all risk" insurance coverage
- Level 1-Individual "all risk" policyholder pays premium *and* deductible
- Level 2-Private insurance "all risk" policy pays claims to cap loss
- Level 3-State Catastrophe Fund pays "all risk" claims over private insurance to cap loss limit
- Level 4-Federal Catastrophe Insurance Plan provides a catastrophic financial obligation guarantee to state for amounts over the state's cap loss limit

Taxpayers are the State and Federal Governments

FIRM
FAIR INSURANCE RATES IN MONROE
www.FIRMKeys.org

- All taxpayers are picking up the tab now for hurricane damages caused by flood ***and wind*** on properties without insurance
- Taxpayers who buy wind and flood policies are taking responsibility for their choices
- Every property owner needs to be motivated and able to take personal responsibility for their property and the welfare of their family members

Building and Mitigation Education and Accounting

FAIR INSURANCE RATES IN MONROE
www.FIRMKeys.org

- Property owners need to know the cost/savings benefits of strong building and mitigation in their own high risk area
- Civic groups, insurance brokers, mortgage brokers, the real estate industry and others could provide 'high risk area specific' mitigation seminars to educate consumers
- Low interest loans, grants, and premium credits should be available to help consumers strengthen their properties
- Counties and municipalities have a critical responsibility to the public welfare when developing land use regulations and enforcing building codes
- Models used to predict PML should account for variables in building codes by area

Personal Responsibility

FAIR INSURANCE RATES IN MONROE
www.FIRMKeys.org

- Tax incentives could be provided to owners who take personal responsibility, harden their properties, and buy underlying insurance
- Private insurance company policies could eliminate exclusions but cap losses on “all risk” policies
- State catastrophe funds should be required before tapping federal guarantees
- Federal assistance should be limited to providing financial help to property owners who mitigate for risk and/or buy underlying insurance, in the states that provide a catastrophe fund

A Source of Funding, albeit After the Fact

FAIR INSURANCE RATES IN MONROE
www.FIRMKeys.org

- Property rebuilding and repair purchases (labor and materials) are a result of natural disasters
- Most states charge sales tax on purchases which, for these expenses, provides a state "windfall" tax revenue stream
- Unanticipated state sales tax revenue could be used to build reserves in state catastrophe funds and/or to fund mitigation programs, such as My Safe Florida Home
- The "windfall" income should never be available to any state's general revenue fund
- The funds result from catastrophic events and should be available to offset future catastrophic claims

Sound Public Policy

FAIR INSURANCE RATES IN MONROE
www.FIRMKeys.org

Why COGA (The Catastrophe Obligation Guarantee Act) merits the support of public officials:

- **COGA** will meet the ongoing common need of established state programs such as those in California, Florida, Louisiana, and Texas for reliable, adequate private financing
- Dependence on the fluctuating and heavy cost of private reinsurance creates less predictable premium affordability
- Federal guarantees of state programs' post-event debt will provide existing state programs, and any other qualifying state program, with dramatically enhanced debt-market access, across all market conditions, at much lower borrowing costs

Summary

FIRM
Fair Insurance Rates in Monroe
www.FIRMKeys.org

- Unaffordable insurance premiums create havoc for homeowners, taxpayers, communities and the overall economy.
- Uninsured risks equal delayed repairs, taxpayer exposure, and potential blights on neighborhoods devaluing comparable repaired or rebuilt properties.
- Mitigation strengthens buildings to withstand natural disasters, limiting damage and causing less lifestyle disruption. Better protection lowers claims which should attract more private insurers, make insurance premiums more affordable, and lessen government funding liability.
- Consistent state insurance regulation equals rate stability and protects consumers.
- Public insurance programs need access to reasonably priced capacity to meet high level risk exposures.
- Consumer education creates public awareness of the cost/savings benefits of insuring assets and the safety of your family.
- Appropriate land use regulations and strong enforcement of building codes lead to greater public safety as well as lower insurance expenses.

STATEMENT
OF

CYNTHIA C. SHELTON

ON BEHALF OF THE FLORIDA ASSOCIATION OF REALTORS®

"The Homeowners' Insurance Crisis: Solutions for Homeowners, Communities and Taxpayers"

U.S. House Financial Services Committee

Subcommittee on Oversight and Investigations

Field Hearing

West Palm Beach, Florida

July 2, 2009

Introduction

Thank you Chairman Moore and Congressman Klein for inviting me here today to speak before the Oversight and Investigations Subcommittee. I am pleased to present the views of the Florida Association of REALTORS® on the issue of natural disaster insurance.

My name is Cynthia Shelton. I am a REALTOR® from Lake Mary, Florida, and I am the current president of the Florida Association of REALTORS®. The Florida Association of REALTORS® is the largest trade association in Florida, representing more than 115,000 members involved in all aspects of the residential and commercial real estate industries.

The availability and affordability of property insurance is, at its core, a consumer issue. The importance of available and affordable insurance to homeowners, commercial property owners and those who would like to own their own home or place of business cannot be overstated. This is something that your constituents have long understood since Floridians have dealt with problems of insurance availability and affordability for a number of years. Unfortunately, it is also something that consumers nationwide – even those who are not in what have traditionally been considered "disaster-prone" areas – now know all too well.

Residential and Commercial Properties at Risk

A strong real estate market is the linchpin of a healthy economy, generating jobs, wages, tax revenues and a demand for goods and services. In order to maintain a strong economy, the vitality of residential and commercial real estate must be safeguarded.

Insurance availability and affordability concerns are not limited to Florida or even the Gulf Coast region. We have heard from our REALTOR® colleagues from coast to coast expressing concerns about the availability and affordability of property insurance. Like ours, their insurance concerns extend beyond homeowners' insurance and include multifamily rental housing and commercial property casualty insurance.

It is no secret that insurance is a key component to financing the purchase of real estate. Without property casualty insurance, lenders will not lend, and when a policy is canceled, or non-renewed, property owners are typically in default of their mortgage terms.

The limited availability and high cost of insurance, therefore, not only threatens the ability of current property owners to hold onto their properties, but it also slows the rate of housing and commercial investment in these communities. The inability to obtain affordable insurance is a serious threat to the real estate market.

New home purchases, resale transactions and housing affordability are affected in the following ways:

- **Homeowners' insurance is a necessary component in securing a mortgage and buying and selling a home.** If a potential homebuyer is unable to obtain or afford the required insurance, the sale will not be completed. As a result, potential homebuyers are excluded from the market.

- **A home's value is directly tied to insurance costs.** Homeowners are required by their mortgage lenders to maintain homeowners insurance, regardless of its cost. And insurance that is expensive or unavailable devalues property.
- **Insurance costs impact rent levels.** Insurance costs incurred by multi-family property owners are ultimately passed on to tenants through higher rents. This impacts housing affordability, particularly for low-income renters.

Our commercial members, of which I am one, have also experienced problems with commercial insurance availability and affordability. Commercial property owners have experienced large increases in premiums-- in some cases more than four-fold while at the same time experiencing dramatically increasing deductibles and decreases in coverage -- and in some cases, a complete lack of availability. These changes put the property owner at greater financial risk to recover from losses, while also affecting property values since dramatic insurance increases often cannot be passed on to commercial tenants.

Catastrophic Natural Disasters are a National Issue

As a result of the 2004 and 2005 hurricanes, attention over the past few years has focused more heavily on Florida and the Gulf Coast states, but other areas of the country are also susceptible to large-scale natural disasters. Devastating floods in the Midwest are certainly catastrophic to the property owners affected. Wildfires out west are no less catastrophic to the family or business that is wiped out by the tragedy.

The glimmer of hope for that flood victim is that they were given the opportunity to buy their disaster insurance in the form of flood insurance. The government chose to insure flood when the private market evaporated more than 30 years ago and then the private market decided flood was not a peril they wanted to insure. We believe strongly that the federal government has a role in writing the wind risk as well.

Elements of Natural Disaster Insurance

Florida REALTORS® believe that now is the time for Congress to consider a NATIONAL natural disaster policy. I cannot continue however, without acknowledging the hard work of you, Congressman Klein, in taking on this issue in the last Congress and actually getting your bill through the U.S. House of Representatives. Thank you.

The lack of a national natural disaster policy has had a measurable direct impact on the availability and affordability of property casualty insurance in many parts of the country. The inability to obtain affordable homeowners' insurance is a serious threat to the residential real estate market – and thus, our entire economy.

Homeowners and commercial property owners need insurance to protect themselves, their families and their property in case of catastrophe.

Proposed Legislative Approaches

Florida REALTORS® would like to see healthy and vigorous debate during the current Congress that leads to sound and productive legislation on natural disaster insurance. I am very proud that Congressman Klein introduced The Homeowners' Defense Act of 2009 with more than 40 co-sponsors from 21 states. We certainly share the goal of ensuring the availability and affordability of homeowners' insurance coverage for catastrophic events.

H.R. 2555 is a new and refreshing approach in providing not only more than thirty states with the opportunity to pool their risk of natural disasters, but we are very excited about the HUD program to provide grants to eligible entities to develop, enhance, or maintain programs to prevent and mitigate losses from natural catastrophes. The Florida REALTORS® have long advocated increased mitigation efforts at the state and federal level. Florida REALTORS® have made our support of your good legislation known – in a vocal way – to our national colleagues.

To this distinguished panel I will admit that I do not believe there is a single silver bullet solution to our property insurance crisis in the United States. We can work to advance efforts on many fronts with regard to a national disaster program whether that is getting H.R. 2555 through Congress, folding wind into the National Flood Insurance Program, more efficient and less expensive mitigation techniques, giving tax credits to property owners who harden their buildings, stronger building codes, growth management policies in coastal areas that anticipate wind events…there are so many pieces to this puzzle.

Conclusion

Thank you again for inviting me to present the views of the Florida Association of REALTORS® today. Passage of an appropriate comprehensive national disaster policy is a top legislative priority for REALTORS®. We stand ready to work with you and others in Congress to develop a responsible natural disaster policy that addresses the needs of consumers, the economy and the nation.

I would be glad to answer any questions that you may have.

Testimony of
Raymond Spudeck, Chief Economist,
Florida Office of Insurance Regulation

Before the
Subcommittee on Oversight and Investigations
Of the
House Committee on Financial Services

Regarding:
"The Homeowner's Insurance Crisis: Solutions for Homeowners, Communities, and Taxpayers"

July 2, 2009
Commission Chambers, City Center
401 Clematis Street
West Palm Beach, Florida

Testimony of Raymond Spudeck
Chief Economist
Florida Office of insurance Regulation

Chairman Moore, Ranking Member Biggert and members of the Subcommittee on Oversight and Investigations, on behalf of Florida Insurance Commissioner Kevin McCarty, I thank you for the opportunity to testify here today regarding the homeowner's insurance crisis resulting from catastrophic natural disasters and I applaud you for your leadership on this critical issue.

My name is Raymond Spudeck, and I am the Chief Economist for the Florida Office of Insurance Regulation. In addition to my ongoing work with the Florida homeowner's insurance market, I have also been deeply involved in the national debate with the Property & Casualty Insurance Committee of the National Association of Insurance Commissioners (the "NAIC") as well the Committee's Catastrophe Insurance Working Group.

Our Current System for Catastrophic Natural Disaster Insurance

In your invitation to provide testimony, you asked a number of penetrating questions that are central to the ongoing debate regarding the correct system for insuring against catastrophic losses resulting from natural disasters. As the debate continues and as your questions suggest, the one central fact is that the insurance contract is the engine that provides for economic recovery for individuals, communities and regions following a large scale natural disaster. Individuals cannot return home unless their damaged properties are repaired. Moreover individuals may not be able or willing to return to their homes unless their places of employment are returned to operating condition, and schools and social infrastructure repaired. Insurance payments for legitimate insured losses make all of this happen. We have examples from over the last five years, in

Florida, and elsewhere along the coastline of the United States, of where this system works, and sadly, where it does not.

It is also important to recognize that the framework that provides the necessary insurance is an important part of the recovery process. As we meet today, the ability of housing markets and local and regional economies to withstand and recover from natural catastrophes depends critically on what type of peril creates the disaster, where the disaster occurs, and the severity of the disaster event. The different types of catastrophic natural disasters are managed very differently within our current insurance framework. This, in turn, can lead to highly different outcomes.

Wind events, including tornados and hurricanes, are considered a basic covered peril in the vast majority of homeowner's insurance policies. Flood, on the other hand, is only rarely written by the private insurance industry for residential property; since 1968 the National Flood Insurance Program (NFIP) has been the public solution to managing this risk. Finally seismic events, especially earthquakes, are not considered a standard covered peril, and aside from the California Earthquake Authority, there is no public mechanism to underwrite the risk, so coverage is restricted to being an optional coverage, where available, in the private insurance market.

If the natural catastrophe is a significant hurricane, in most cases claims will be paid in a timely fashion. There are sometimes delays in being able to physically get to a property to assess the damage and adjust the claim. There are also sometimes disputes regarding the source of the damage, wind versus water. Following the disaster, as claims are paid, if the hurricane generates sufficiently large losses, it may well be the case that some insurers find themselves in financial distress and possibly unable to continue to underwrite insurance.

As well, following a major hurricane, individual property owners may witness the all too common phenomenon of finding insurance difficult, sometimes impossible, to find, as well as likely seeing budget-busting rate increases. Frequently, following a significant hurricane, there is increasing pressure on residual markets to provide the mandated insurance. This has been especially true since 2004 as many of the "major" national property insurance companies have made the decision to curtail their exposure to natural catastrophe risk. According to the Insurance Information Institute, nationally the amount of residential property exposed to catastrophic risk insured in residual markets has grown from $113 billion in 2000 to $670 billion in 2007.

Experience from the Florida Market

The property insurance market in Florida had, for all intents and purposes, reached equilibrium by 2004 from the shocks created following Hurricane Andrew in 1992. The four land falling hurricanes in 2004 followed by the subsequent four hurricanes in 2005 served not only to disrupt this equilibrium but to put significant stresses on the market that are still in evidence today. Private insurance companies rely heavily on reinsurance acquired in the global marketplace. By 2006, this reinsurance was in many cases either unavailable or only available at rates that were economically unfeasible. Direct writers who could still acquire reinsurance were seeing rate increases in high double digits, sometimes even triple digits. Others who could not find insurance in the private market were forced into Citizens Property Insurance Corporation, our residual market mechanism, which at one point had over 1.2 million policyholders, a number that has since abated as we develop a domestic market.

As this passed through to homeowner's policies and commercial property policies, the result was devastating to the Florida economy. Real estate transactions were being delayed, forestalled or cancelled. Business expansion and development plans were either scaled back or cancelled. Individuals, facing in some cases a doubling of their insurance cost, if they were able to find coverage, were forced into making tough economic choices, including at the extreme whether to buy homeowner's insurance, food or prescription medicines. This squeeze in disposable income was felt throughout the Florida economy, and this ripple effect continues today along with the other economic issues facing our citizens.

With the current financial turmoil, our Florida Hurricane Catastrophe Fund entered into 2009 unsure that it would be able to obtain financing in the municipal bond market if needed, despite its Aa rating. That situation has only recently eased somewhat

If the natural catastrophe is a significant flood event, the ability of the affected areas to recover is going to depend critically on the degree to which affected properties were insured with the NFIP. Unfortunately, recent evidence from 2004 and 2005 suggests that far too many properties damaged by flood were uninsured; either they were outside of the mandatory flood plains as dictated by antiquated maps, or they were in the mandated flood zones, but were uninsured anyway. A recent study by the Rand Corporation provides evidence that suggests that the rate of take-up (that is how often the coverage is purchased) outside of the mandated zones is around 5%, and the take-up rate in mandated zones is only about 75%. Following the event, taxpayers are likely to face a bill to subsidize the NFIP losses. Florida knows this all too well. According to the GAO, over the last thirty years Floridians have paid in almost ten billion dollars more in premium than they have received in benefit; an amount of subsidy that is a magnitude large than the next largest subsidizing state, California.

If the natural catastrophe is an earthquake, the ability of the affected regional economy to recover is going to largely depend on the degree of disaster relief coming from the federal government and the American taxpayers. The reason is really quite simple; the majority of residential property in earthquake prone areas is not insured for this very real risk. In California, for example, it is estimated that the take-up rate for optional earthquake insurance has fallen to about 12% or less. The same take-up rate is frequently suggested to be true in the earthquake prone areas in the Midwest's New Madrid area, and along the eastern seaboard's seismically active areas.

As you can see, what is lacking in our current system is a comprehensive approach to managing the devastating effects of catastrophic natural disasters. Our current policy relies heavily on the American taxpayer through the Federal government for most types of natural disasters. As generous and compassionate as the American people are, the current system leaves much to be desired. While it is true that our current reliance on federal payments for large-scale disaster does spread the cost of these events across a broad pool, the American taxpaying public, it does so rather ineffectively. At the other extreme, our current system of insuring large scale disasters in the case of hurricanes can and frequently does create unwanted and unneeded volatility in the marketplace, which adversely affects property owners.

Perhaps more problematic is that precious little of this money is being invested in programs or projects to prevent this sort of scenario from repeating. Our current system is largely based on an after the fact reaction. I would argue that a more proactive system that prepares the public and mitigates the potential for catastrophic damage following such an event is more practical, and in the long run less expensive to both affected individuals and the public at large.

Moreover, while the recent focus has been on coastal insurance issues, the broad problem is also one that is national, not regional, in scope. Also in the documents attached to my testimony, you will find maps of the catastrophic exposure to natural disaster facing each state. As these maps show, very few Americans are not moderately or severely exposed to the effects of a natural disaster.

<u>Other Approaches to Managing Disaster Risk and Insurance</u>

What then could be done to create a comprehensive plan? Both within the US and across other developed economies a variety of programs have been created to manage the economic consequences of catastrophic events. These programs differ in their structure based on underlying premises regarding the nature of the risk. As such, the resulting roles of the private insurance market and government entities vary considerably across programs. The Government Accountability Office report "U.S. and European Approaches to Insure Natural Catastrophe and Terrorism Risks," GAO-05-199 published in February 2005, provides a thorough description of these various approaches.

Public policy frequently enters the debate as to whether or not a natural catastrophe is an insurable risk. Here in the US, it was decided in 1968 that flood was not an insurable risk with the creation of the National Flood Insurance Program. Interestingly, other countries consider flood an insurable risk.

Using the same premise, both France and Spain have created risk pools for mandated natural catastrophe coverage that result in the state assuming the risk on an unlimited basis.

On the other hand, many natural catastrophes are considered insurable as a matter of public policy, and government is used sparingly to facilitate the private sector mechanism. Perhaps the most common tool provided under this premise is the insurer's ability to set aside reserves to pay for catastrophic losses on a tax-deferred basis. While differences do exist in how these reserves are structured and monitored, they are common throughout the world. As a measure of their perceived importance, a recent International Accounting Standard ruling (accounting guidance followed by most of the rest of the world except the US at this point) would have done away with this reserving mechanism. Virtually all European nations, along with a number of other jurisdictions, chose not to adopt this new rule.

The US does not allow for the creation of tax-deferred reserves by insurers, although a number of variants of a tax-deferred reserve have been developed and proposed since Hurricane Andrew in 1992.

A second tool found in many nations is a risk pool funded by private insurers but managed by the government. In Switzerland, for example, coverage for all natural catastrophes, except earthquake, is mandated in property insurance policies. Private insurers as well as state-owned canon specific insurers, pool these risks together and an average actuarial rate is determined and charged by all insurers.

Federal Support of Disasters and Disaster Insurance

As we observed from Hurricane Katrina, the Indian Ocean tsunami, and the 2005 earthquake in Pakistan, federal governments globally will always become involved if there is a national catastrophe that affects its citizens. One important policy question is whether this support is provided before or after an extreme event. It is like the old television commercial featuring the auto mechanic telling the camera "You can pay me now, or you can pay me later." It is almost always more inexpensive to finance disaster recovery before a catastrophe occurs, rather than after-the-fact. This is precisely the purpose of insurance --- to pay prior to the accident, to provide an economic cushion to survive the adverse event.

Although I believe this Subcommittee should carefully consider the cost/benefit of all options for federal involvement, it is important to stress the solution to handling natural catastrophes, and ensuring a stable insurance market, does not necessarily begin or end with a massive federal program. In its Constitutional powers of taxation and interstate commerce, Congress' powers directly and indirectly affect state insurance markets. The loan conditions put on federal mortgages, the tax treatment of insurance company's reserves, economic incentives for individuals to retrofit their homes, improved building codes, and even upgrading our nation's infrastructure are all areas Congress can address to positively impact the insurance marketplace. In the following section, I will attempt to summarize a few of the key ideas that I believe would be worthy of consideration.

Improve Disaster Preparedness and Disaster Response

Disaster planning and disaster response are the very first steps to saving lives and protecting communities. The sad evidence from Hurricane Katrina bears solemn testament to this fact. The recently released study of community disaster preparedness by the Department of Homeland Security suggests there is still much to be done around the country. The report states the "current catastrophic planning is unsystematic and not linked within a national planning system." It states that, "this is incompatible with 21st century homeland security challenges..." It goes on to suggest, "the need for a fundamental modernization of our Nation's planning processes." Not only is this a key priority for us in Florida, insurance regulators around the country agree. To that end, the NAIC has endorsed disaster planning as a top priority and maintains disaster preparedness manual for use by all states.

Build Better Homes

We cannot stop natural disasters, but there are measures we can take to mitigate damage. The first component of any comprehensive national strategy must be mitigation. By mitigation I mean preemptive measures taken to reduce or eliminate risk to property from hazards and their effects. In practical terms, this involves toughening building codes for new structures by making them more resistant to hazards such as wind, flood, and earthquakes. It also means stricter state and local guidelines to limit construction in highly hazardous areas.

The insurance mechanism can reinforce this mitigation through its pricing. The insurance industry, or whoever provides the insurance, can and should incentivize property owners to take the personal responsibility to protect themselves from catastrophic loss through mitigation by providing meaningful premium discounts for mitigation investment. We have implemented such measures in Florida

The federal government can positively impact these decisions by predicating federal loan decisions through the Federal Home Association (FHA) and Rural Development Home Program to only allow the purchase of homes that meet the most stringent building code standards. If a home does not meet these standards, a procedure for requiring the retrofitting of the home must be enforced.

Mitigation techniques work, are cost effective, and we have seen their successful utilization. In Florida, the Florida Department of Financial Services provided $2.3 million to develop four model "hurricane houses" with advanced building techniques to withstand 140mph winds. In 2004, the eye of Hurricane Frances, a category 2 hurricane, passed over one of these houses located in Ft. Pierce. The house survived with no appreciable damage. In Tulsa, the development of education and marketing to extol the value of "saferooms" has met with tremendous success, significantly increasing the demand for this tornado mitigation safety device.

Although strengthening building codes for new structures will improve the housing stock on a going-forward basis, this will have a minor impact on the entire book of business for property insurers in the short-run. The majority of the housing stock in the US is already built. This is true even in rapidly growing states; the average age of a house in Florida is 24 years. Many of these houses were built prior to any building code standards, much less the most recent, even in areas where building codes are in place.

In 2006,, the Florida Legislature passed the Florida Comprehensive Hurricane Mitigation Program, which provides for free home inspections, as well as 50% matching grants of up to $5,000 to encourage single-family homes to reduce vulnerability to hurricane damage. The response was overwhelming. The Florida Department of Financial Services received over 65,000 applications for the free home inspections that would alert consumers how to harden their homes. Regrettably the target for the year was to inspect 12,000 homes based on resource constraints, but this illustrates the interest homeowners have in protecting their homes when the proper financial incentives are provided. The current economic environment has curtailed expansion of the program right now, but as the economy recovers I expect the program will return as its importance is recognized by all.

Mitigate by Improving Infrastructure

Another element of improving the homeowners market is to improve our nation's infrastructure. This includes dikes, levees, tunnels, bridges, solid waste facilities, transportation facilities, and roads. Let us recall during the Hurricane Katrina tragedy in New Orleans, many of the structures withstood the initial damage of the storm, only to be destroyed due to the failed levee system. The American Society of Civil Engineers' March 2005 Report Card showed deteriorating conditions in 13 of the 15 infrastructure areas surveyed. Insurers are becoming reluctant to insure structures in areas with outdated or outmoded infrastructure risks. A commitment to improving our infrastructure, especially as it relates to structures that place homes in greater risk during a catastrophic event, will help prevent or mitigate damages to homes.

Expand the Capacity of the Insurance Marketplace

The current system of insurance is very good at handling the "normal" disasters ranging from car accidents, to storms, and even to large hurricanes. Catastrophic natural disasters, especially the prospect of mega-catastrophes (i.e. the "big one" hitting California, a category 3 or 4 hurricane hitting New York, major seismic activity along the New Madrid Fault in the Midwest), create risks that could simply destroy an insurance company or potentially the entire industry. This risk of ruin will likely keep the private sector from offering sufficient capacity for entirely rational reasons. No potential rate of return is going to be worth the risk of losing the entire company.

Following major events, disruptions and shocks in availability and pricing also serve to limit the consistent delivery of insurance at rational prices.

I believe there are a number of possibilities that could expand and stabilize the capital flows into the market to ensure sufficient capacity and stabilize pricing. These would include:

Consider Natural Catastrophe Reserves for individuals or, on a tax deferred basis to insurance companies to provide an economic cushion for likely future events. Allowing U.S. companies to join companies in most other industrialized nations, and granting them the ability to set aside tax-deferred reserves specifically for catastrophes, when structured appropriately so as not shelter income, could provide additional capacity for the market. As well, at least some of the "boom or bust" cycle in the property insurance market could be smoothed to everyone's benefit

Consider a Federal Backstop for Catastrophic Risk

For the creation of a federal backstop, a number of innovative ideas have been suggested. It is important to note that these ideas, if deemed appropriate, do not, contrary to some public opinion, necessitate a public subsidy. In fact, actuarial pricing to expected loss seems to be a consistent theme.

One concept is to have the federal government, through the U.S. Treasury Department, implement a reinsurance program offering reinsurance contracts sold at regional auctions. One variation of this proposal would be to allow private insurers to obtain reinsurance contracts.

Other proposals would restrict these reinsurance funds to authorized state catastrophe funds, similar to our Florida Catastrophe Fund, or the California Earthquake Authority.

More recently, there has been discussion of limiting the role of the federal government to providing credit guarantees to state or regional funds which would be repaid over an intermediate term after a qualifying event.

Working with states or regions, there is the possibility of the federal government coordinating products and designs for state or regional groups to obtain financing in the alternative markets, especially through securitizations.

National Catastrophe Reinsurance

Currently, the United States is one of the only industrialized nations in the world not to have a federal comprehensive catastrophe plan. A comprehensive plan should include planning for the disaster, building resistance to the disaster, and economically efficient financing of the disaster. The role of the federal government should be limited to those areas where individuals, private markets or state governments cannot affect a better solution on behalf of the American people. Clearly there are a number of forward thinking ideas that need further consideration, but they should be framed to first answer the question, "Will this make insurance for individuals and businesses more available, and more affordable, with fewer burdens on the American taxpayer than the current system?" We will work with this Subcommittee to find the right answers to that question. The lessons of recent catastrophes may be the only warning we get to start making those decisions, so I thank you for holding this hearing, for inviting me here today, and for your continued interest and leadership on this crucial issue. I'd be happy to answer any questions you have.

MY SAFE FLORIDA HOME PROGRAM

Creation of My Safe Florida Home Program

- 2004 and 2005 hurricanes inflicted **$33 billion in insured losses** on **2.8 million** Florida homeowners.
- There are approximately **4.4 million single-family, site-built homes** in Florida representing $2.3 trillion in insurance exposure. Average age of these homes is **24 years** old.
- In a 2005 study, the National Institute for Building Sciences concluded that **for every dollar invested in mitigation, there is a savings of $4**.

MY SAFE FLORIDA HOME PROGRAM

Florida Legislature created My Safe Florida Home to:

- **Help Floridians better protect their property**
- **Help Floridians save money on insurance premiums**

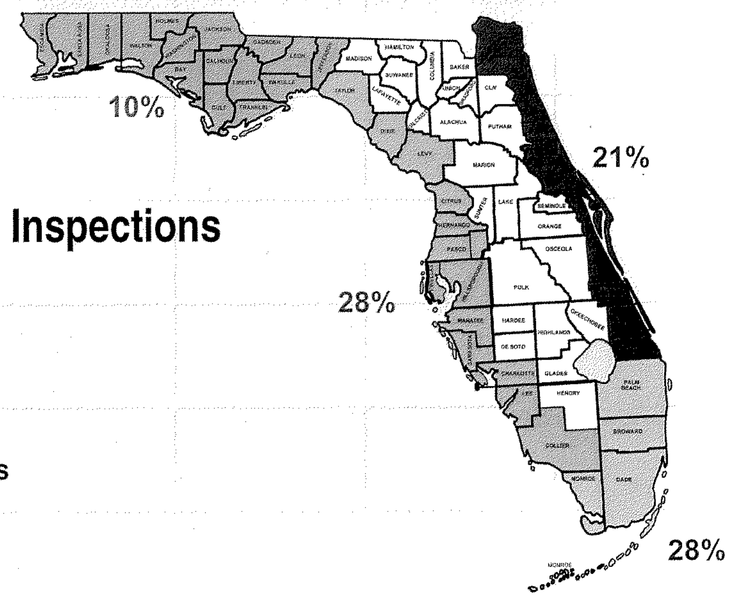
Goals Set by the Legislature with $250 million:

- **Provide free home inspections to 400,000 Floridians**
- **Provide matching grants up to $5,000 to 35,000 Floridians**

MY SAFE FLORIDA HOME PROGRAM

Snapshot:
400,776 Completed Inspections

- 28% from South Florida
- 28% from the West Coast
- 21% from the East Coast
- 13% from Interior Counties
- 10% from the Panhandle



MY SAFE FLORIDA HOME PROGRAM

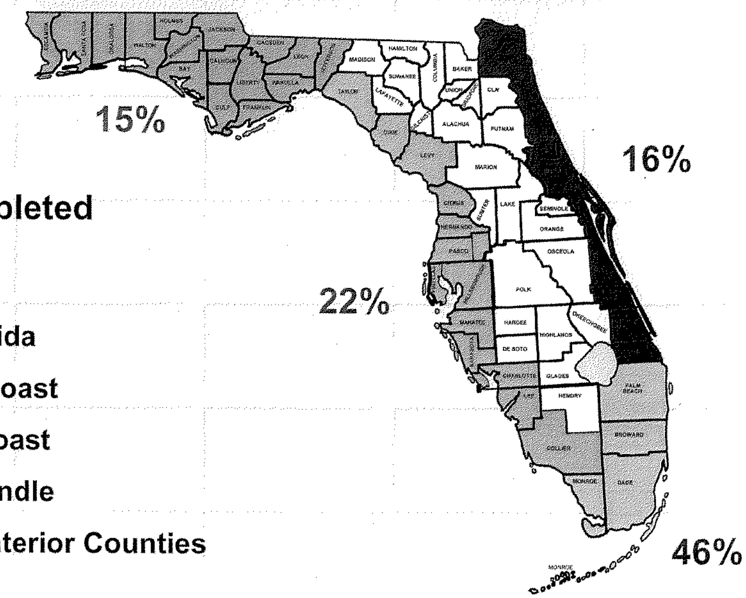
SURVEYS OF INSPECTION CUSTOMERS

- Motivated to get safety information (40%) and insurance savings (39%).
- 26% are pursuing improvements without grant funds.
  - More than one-third choosing to do opening protection.
- 91% rated their experience with My Safe Florida Home as Excellent or Good.
- Majority willing to pay about $3,200 to match.

MY SAFE FLORIDA HOME PROGRAM

Snapshot of 31,593 Homes Completed with Grants

- 46% from South Florida
- 22% from the West Coast
- 16% from the East Coast
- 15% from the Panhandle
- Less than 1% from Interior Counties



MSFH – Hardening Homes, Reducing Insurance Costs

MY SAFE FLORIDA HOME PROGRAM

Of homes awarded grant funds to protect all openings, the average increase in strength to the home as measured by the hurricane-resistance rating scale is 36% (or 16 points).

Average hurricane rating of a home determined at inspection is 44 on a scale of 0 to 100.

On average, homeowners are seeing a 27% reduction in their hurricane premiums as a result of retrofitting their homes.

MY SAFE FLORIDA HOME PROGRAM

Return on Investment

The My Safe Florida Home program retrofitted an average of 320 homes every week, effectively creating nearly 1,000 jobs in a given week. That's with an earmark of $160 million for grants to perform retrofits.

Of $120 million paid out in grants to buy materials and pay for installation services. At an average sales tax rate of 6 percent, approximately $7.2 million in sales tax revenue was generated.

More than 900 inspectors helped perform $58 million dollars worth of inspection work over a 2-year period.

One risk modeler has suggested this program will reduce catastrophic exposure in Florida by as much as 26%.

That same modeler estimated that Florida is getting a $1.50 for every $1 invested by My Safe Florida Home.