

GENE TAYLOR  
4TH DISTRICT, MISSISSIPPI

COMMITTEE ON ARMED SERVICES  
COMMITTEE ON TRANSPORTATION  
AND INFRASTRUCTURE

<http://www.house.gov/genetaylor>

**Congress of the United States**  
**House of Representatives**  
**Washington, DC 20515-2404**

January 5, 2007

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The Honorable Barney Frank  
Chairman  
House Committee on Financial Services  
2129 Rayburn House Office Building  
Washington, DC 20515

Dear Chairman Frank:

I am writing to respectfully request that the House Financial Services Committee conduct a detailed investigation of insurance industry practices in the aftermath of Hurricane Katrina. I apologize for the extreme length of the letter, but I want to lay out a variety of insurance concerns in sufficient detail to give them justice.

First, however, I want to thank you for all of the assistance you have provided to me and my constituents since Katrina. Your efforts as Ranking Member of the Financial Services Committee helped build support for the homeowner assistance programs and flood insurance improvements that were approved in the 109<sup>th</sup> Congress.

The flood insurance buy-in bill that you helped me draft a few weeks after the storm led directly to the Mississippi and Louisiana homeowner assistance programs that were funded through the CDBG program. Although the House Republican leadership and the Bush Administration blocked our bill and Rep. Baker's proposal for Louisiana, Sen. Cochran was able to gain approval for homeowner assistance using CDBG funds. The Mississippi program is very similar to our bill, H.R. 3922, except that it took almost a year for HUD and the state to create and implement the new program. Our bill would have provided relief much more quickly by allowing homeowners to file flood insurance claims that would be funded with disaster appropriations.

As you know, that assistance was directed to homes that were not inside the special flood hazard areas on the federal flood insurance rate maps, yet suffered damage from Katrina's storm surge. In most cases, homeowners, insurance agents, lenders, and realtors relied on the federal maps to determine whether flood insurance was needed.

Despite the billions of dollars of federal assistance, South Mississippi's recovery is obstructed by the actions of private insurance companies. I ask that the Financial Services Committee conduct investigative hearings on two separate, but related, insurance problems: (1) the denial of thousands of Katrina wind claims wherever insurers

could blame flooding and (2) excessive premiums increases, market withdrawals, and other actions to force states to make concessions or to assume more coastal risks.

For thousands of destroyed properties in Mississippi, some insurers assigned all Katrina damages to flooding covered by the National Flood Insurance Program and none to their own windstorm policies. The Mississippi Coast suffered several hours of very destructive hurricane winds before inundation by the storm surge. Insurers paid billions of dollars of wind claims inland, where they could not possibly blame flooding, but assumed that flooding caused all the damage near the coastline.

In order to scrutinize Katrina claims practices in Mississippi, it probably would be helpful to separate the hurricane claims into four categories:

- Structures located north of the three coastal counties;
- Structures in the three coastal counties with no flood damage;
- Structures with wind and water damage that remained standing;
- Structures destroyed by some combination of wind and water.

All the evidence suggests that insurers paid wind claims without much dispute in the first two categories. They had no other choice. In the 79 counties north of the three counties on the Gulf, insurers paid more than 250,000 claims totaling more than \$3.5 billion. Claims were paid in every county in Mississippi, as far as 300 miles inland. The average claim above the Gulf counties was approximately \$14,300.

In the third category, it appears that most adjusters blamed flooding for all damage from the waterline down, but acknowledged wind damage above the waterline that could not be blamed on the surge. There are remaining disputes in some cases where insurers pay only for damage that homeowners can prove was caused by wind alone.

The fourth category is the source of most of the acrimony and also most of the lawsuits. Thousands of homes were battered by four or five hours of hurricane force winds before the surge inundation. Eyewitnesses across the Coast reported widespread structural damage before the surge, with the surge and the winds of the eyewall finishing off heavily damaged buildings. There is no place in Mississippi that suffered surge flooding without first experiencing hours of destructive winds.

Insurance claims data from the three Gulf Coast counties show that the National Flood Insurance Program and the Mississippi wind pool paid much more than did private insurers. These figures are the average claims amounts as of a few months ago.

COUNTY	NFIP	Wind Pool	Other Insurance
Hancock	\$130,000	\$46,000	\$25,000
Harrison	\$157,500	\$37,500	\$25,000
Jackson	\$127,500	\$22,500	\$14,000

NFIP estimates it will pay approximately 18,000 flood claims in the three Mississippi Gulf Coast counties for a total of \$2.6 billion. That is an average of \$142,000 per claim, where the average policy was \$148,000. The state will pay an additional \$3 billion in CDBG funds to assist homeowners who did not have flood insurance.

As you know, GAO and the DHS Inspector General are examining the adjustment of Katrina wind and water claims. The Inspector General's investigation is similar to my amendment that was adopted by voice vote during consideration of the Flood Insurance Reform and Modernization Act. Thank you again for your role in making sure I would be allowed to offer my amendment on the House floor. Although the Senate did not act on the flood insurance bill, Sen. Lott was able to attach a similar provision to the Homeland Security Appropriations Act. That bill instructs the Inspector General to investigate whether insurance companies improperly assigned damages to NFIP that should have been paid by their windstorm coverage. That report is due by April 1.

I ask that you not wait until then to begin the committee's investigation. It is clear that the insurance companies have a conflict of interest when allowed to assign damages to the federal flood program rather than to themselves. It also is clear that NFIP does not provide sufficient oversight to determine whether insurers are fulfilling their contractual obligations to adjust flood claims by the same standards as their own claims and to provide proper adjustment of combined wind and water claims. In response to my inquiry, an NFIP official stated that oversight of insurance adjustment is a state regulatory function, and therefore outside FEMA and NFIP authority.

I am asking my constituents to provide photographs and documentation of cases of questionable conduct by insurers and their contractors. There are numerous reports of instances in which insurance companies or their contractors revised engineering reports or requested new reports if the original report found wind damage.

State Farm has used Haag Engineering and adjusters from E.A. Renfro to justify denials of wind claims. Both companies have a history of questionable actions, including a 2006 decision against State Farm's denial of 1999 tornado claims in Oklahoma. The Oklahoma jury found that State Farm acted with malice and recklessly disregarded its duty to act fairly and in good faith by employing Haag Engineering and E.A. Renfro.

One Haag report regarding Katrina declares that the NOAA Hurricane Research Division and the Naval Meteorology and Oceanography Command are both badly mistaken about strength of the winds and the timing of the storm surge. The Haag report instead uses a storm chaser's amateur video from a parking garage in Gulfport and questionable wind data from a portable tower in Escatawpa, 40 miles west of Gulfport and 10 miles inland, to conclude that the peak surge preceded the peak winds and that Katrina's winds were not strong enough to cause major structural damage.

E.A. Renfro has been placed in the Katrina spotlight by whistleblowers Cori and Kerry Rigsby, who were employed by Renfro to adjust claims for State Farm. The Rigsby sisters say that they were instructed to pay NFIP claims as quickly as possible,

while refusing to acknowledge any evidence of wind damage. The documents they copied include cases in which initial engineering reports identified wind damage, but State Farm or E.A. Renfro pressured the engineers to revise their reports. The whistleblowers also report that engineers who refused to revise their assessments did not receive additional assignments from State Farm.

I have long suspected that State Farm, Allstate, Nationwide, and a few other insurers agreed to aggressively deny Katrina wind claims as they had never done before. One company would not have been able to get away with blanket denials if the others had been paying claims. The manipulated assessments by firms such as Haag Engineering and E.A. Renfro suggest a much broader conspiracy to defraud consumers and taxpayers.

As you know, I intend to offer legislation to eliminate the antitrust exemption that was granted to the business of insurance by the McCarran-Ferguson Act. The insurance industry's actions in Mississippi provide ample evidence of widespread anticompetitive behavior that should be illegal. Those actions also provide proof that a small state such as Mississippi is not capable of adequately regulating the industry.

I question whether any state is capable of protecting consumers and taxpayers from heavy-handed insurance practices. Since Katrina, insurers have announced withdrawals from coastal areas of every Atlantic and Gulf state. The large insurers are in positions of strength to dictate their terms in high risk areas of every state. In recent decades, insurers have exacted concessions after every disaster – forcing state plans and state-sponsored pools to assume the highest risks and pressuring states to approve higher deductibles. The big companies stick to their “hard market” script. After every disaster, they act in concert to coerce states to allow them to shed risk even as they hike premiums.

The current market for windstorm insurance on the Mississippi Gulf Coast is a prime example of the insurance industry's hard market tactics. Unlike Florida or Texas or Louisiana, Mississippi's coastline is only about 75 miles long. We can go a decade or more without a significant storm, but when a major hurricane hits Mississippi, all of the coastal area is hit. There are no other large regions of the state paying high-risk premiums but not filing claims.

In 1987, two years after Hurricane Elena, the State created the Mississippi Windstorm Underwriting Association, commonly called the wind pool. The wind pool provides last resort windstorm coverage in six counties – the three counties on the Gulf and the three counties directly above them. The wind pool board purchases reinsurance against hurricane risk. If claims exceed the amount of reinsurance, the property insurers in the state are assessed according to their market share. Because insurers are the backstop for the pool, the state gives company representatives five of the eight seats on the board. The other three are local insurance agents appointed by the Governor.

In order to encourage companies to provide wind coverage in the coastal counties, the state gives those who do so a 1.4 to 1 credit against their wind pool assessments. The state also allows insurers to apply a hurricane deductible of up to two percent of the

policy in the coastal counties. Several states were forced to permit hurricane deductibles in the mid-1990s when insurers threatened to leave markets following Hurricane Andrew.

At the time of Katrina, the Mississippi wind pool carried \$1.8 billion in risk and had reinsurance to \$175 million, which was believed to be a 250-year event. Katrina losses to the wind pool exceed \$700 million, and the wind pool assessed approximately \$545 million to insurers. State Farm, Nationwide, Allstate have the largest shares of the Mississippi market, but they covered wind on the coast, so they received credits against their assessments to the wind pool. Of course, this forced other insurers in the state to pay more on their assessments to the pool.

Shortly after Katrina, the wind pool board voted to require the pool to buy more reinsurance. This transfers more risk to policyholders rather than to assessments on insurers. The wind pool purchased \$350 million reinsurance for the incomprehensible premium of \$43 million. Even after Katrina, no loss history or risk model could justify a premium that high. However, reinsurance appears to operate as a cartel rather than as a competitive market. There were no bids or competition for the reinsurance policy. Several reinsurers simply divvied up shares of the \$350 million.

The wind pool then requested state approval of a 398% increase in residential premiums. Gov. Barbour proposed and received HUD approval to use \$50 million in CDBG funds to subsidize the residential wind pool premiums for the next two years. That allowed Insurance Commissioner George Dale to approve an increase of *only* 90% in residential premiums.

The Mississippi legislature is considering proposals to use state tax funds to subsidize commercial premiums, which have increased 268%. However, now that the large insurers are no longer writing new wind policies near the coastline, more and more properties will be covered by the wind pool. The wind pool board should be expected to increase the amount of reinsurance.

I do not know which companies reinsure the wind pool, but I assume they are among the many located in Bermuda and other tax havens. The current trend, supposedly to transfer more risk to overseas reinsurers, opens up many opportunities for profiteering, fraud, and tax evasion. In 2004 testimony before the Senate Committee on Government Affairs, Eliot Spitzer warned about collusion in the reinsurance market:

We have found that a small group of brokers and insurance companies essentially control the market, having created a network of interlocking connections and secret payments which ensure that the bulk of business goes to certain insurers, and that profits remain high.

Spitzer recommended that the federal government should take responsibility for oversight of off-shore capitalization and investment by insurance companies. He also suggested that the federal government establish basic standards of accountability for the insurance industry.

As we have discussed, I am drafting legislation to create a natural disaster insurance program that would provide coverage all perils. I am convinced that investigations into the insurance problems that were exposed by Katrina will make a convincing case for all perils disaster insurance. Homeowners should be able to purchase insurance and know that their losses will be covered. Thousands of South Mississippians had purchased all the insurance that was available to them – homeowners, windstorm, and flood – yet found themselves with large uncovered losses.

Thank you again for all of your assistance to me and to the residents of the Gulf Coast. I look forward to working with you on these and other issues.

Sincerely,

A handwritten signature in cursive script, appearing to read "Gene Taylor".

GENE TAYLOR  
Member of Congress

GT:jbm

cc: The Honorable Nancy Pelosi  
The Honorable Steny Hoyer  
The Honorable James Clyburn  
The Honorable John Conyers  
The Honorable Paul Kanjorski  
The Honorable Maxine Waters  
The Honorable Mel Watt  
The Honorable Charlie Melancon  
The Honorable William Jefferson