



Association of Bermuda Insurers and Reinsurers

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March 9, 2010

Honorable Barney Frank
Chair
Committee on Financial Services
U.S. House of Representatives
Washington, D.C. 20515

Honorable Spencer Bachus
Ranking Minority Member
Committee on Financial Services
U.S. House of Representatives
Washington, D.C. 20515

Subject: HR 2555

Dear Chair Frank and Ranking Member Bachus:

On behalf of the largest providers of catastrophe reinsurance to the United States – the 23 members of the Association of Bermuda Insurers and Reinsurers (ABIR) – we write to express our opposition to HR 2555 which would replace private sector risk bearing capital with government reinsurance and government guarantees of state debt. The effect of HR 2555 would be to force US taxpayers countrywide to subsidize the insurance costs of state catastrophe funds in those states most exposed to hurricanes and earthquakes. Seventeen of the 23 ABIR members have US subsidiary insurance companies which employ nearly 16,000 people in the United States. The ABIR members write insurance and reinsurance in the US through their subsidiaries, including catastrophe exposed risk; and write the bulk of their catastrophe reinsurance in their Bermuda parent companies.

Private sector reinsurance capacity is reliable, growing and abundant in today's market. Time and time again as record setting US catastrophic events have tested the private sector's ability to pay for catastrophic risk, the reinsurance industry has stepped forward and raised capital to provide the increased supply of private sector reinsurance needed by our US customers. US capital providers have expressed their confidence by providing capital to reinsurance companies and by directly assuming catastrophic risk through securitization instruments. The securitization of catastrophe risk is expected to continue its dramatic growth in the coming years and legislation is not needed to encourage this market action. It is estimated that about \$8 billion in private catastrophe bonds to support US risk will be issued in 2010. This amount is expected to increase by 25% annually in the next five to ten yearsⁱ. US catastrophic risk is unique in its size and scope and thus US consumers benefit from the ability to pool this risk with European windstorm, Japanese earthquake and typhoon risk and the growing catastrophic risk that is emerging in Latin America and Asia.

The current US (re)insurance market is characterized by an oversupply of capital which has led to a "soft market" – lower consumer prices generally in US commercial insurance (including reinsurance) markets. As a result Bermuda and U.S. publicly traded insurers and reinsurers are returning an estimated \$7.2

billion in capital to their shareholders via stock buybacksⁱⁱ. This illustrates, for many of those companies, capital that could be used to support US catastrophe risk -- in the event market demand called for it.

The Bermuda insurers and reinsurers have supported US insurance consumers by:

1. Paying 24 % of the claims of the 2005 hurricanes--Katrina, Rita and Wilma; Bermuda's insurers and reinsurers paid \$22 billion in claims for the US hurricanes in 2004 and 2005
2. Paying enough in Hurricane Katrina claims to help rebuild 87,000 homes in Louisiana and Mississippiⁱⁱⁱ
3. Paying 66 % of the claims from Texas' Hurricane Ike in 2008 (as illustrated in the claims payments of the Texas Windstorm Insurance Association (TWIA)) -- an estimated \$1 billion of the \$1.5 billion TWIA reinsurance program payment; another \$1 billion in claims outside of TWIA from Ike were paid for by Bermuda's insurers and reinsurers
4. Providing roughly 40% of the reinsurance coverage for the California Earthquake Authority (an equivalent of \$1 billion in reinsurance)
5. Supplying approximately 40% of US property catastrophe reinsurance (as an illustration of our global diversification – we supply 40% of the (broker placed) European windstorm and flood insurance coverage).

Those that support HR 2555 are primarily focused on the incorrectly perceived high cost of insurance in local markets and argue that enactment of HR 2555 will lead to lower prices for insurance supplied by state catastrophe funds. As the experience with the National Flood Insurance Program (NFIP) has illustrated, it is not sound public policy for the US Congress to subsidize catastrophic insurance rates. The likely consequence of such action is to increase coastal development (the NFIP is now \$20 billion in debt) and put more people and property in harm's way thus increasing exponentially the future risk and debt facing the federal government. Subsidized federal reinsurance will inevitably replace private sector risk capital with government debt. It will inevitably lead to outsized catastrophic risk in California and Florida being subsidized by taxpayers from Denver to Des Moines to Bangor.

The true away to address insurance costs is to bring down the cost of hurricane and earthquake claims. The scientific way to do this is to focus on "storm proofing" and earthquake hazard mitigation efforts. Excellent local programs in California, Florida and South Carolina exist which document the true consumer costs savings that can be achieved through hazard mitigation programs. These hazard mitigation programs not only lower future insurance claims costs, but they also save lives and protect people from life threatening injuries.

Hazard mitigation is a common sense public policy approach that has a common base of support in all 50 US states. Statistics document that for every one dollar spent on hazard mitigation an additional four dollars will be saved.^{iv} Studies from Hurricane Ike^v and Hurricane Charley^{vi} document the value of tough building codes in reducing property damage and protecting people—claim frequency can be reduced as much as 60% with current building codes and claims severity can be reduced by more than 40%. Rather than spending scarce federal resources on subsidizing state insurance programs, a better use of that money would be to support successful state and local hazard mitigation programs (already in place) which produce long term results rather than one year premium relief. ABIR supports pending hazard mitigation legislation including HR 3026 and HR 3377.

HR 2555 will replace much of this private sector risk bearing capacity with debt guarantees and federal reinsurance to prop up state government funds; it will replace – not augment – private reinsurance and securitizations. There are other ways in which unwise US public policy proposals can diminish private sector risk bearing. Another example is HR 3424 that would impose a punitive tax on affiliated reinsurance transactions between US insurance companies and their foreign parents or affiliates. Research by the Brattle Group and Wharton Professor Dr. David Cummins has shown that HR 3424, if enacted, will lead to a 20% reduction in US reinsurance supply. ABIR and the Coalition for Competitive Insurance Rates oppose HR 3424^{vii}.

We are members of the Smarter Safer Coalition and support the views presented in its letter to the Committee. We appreciate the opportunity to express these views.

Sincerely,

A handwritten signature in cursive script that reads "Bradley L. Kading".

Bradley L. Kading
President and Executive Director
Association of Bermuda Insurers and Reinsurers (ABIR)

Copy: Members of the House Financial Institutions Committee

ⁱ John Seo, Fermat Capital Management, Speech, October 2009

ⁱⁱ Insurance Insider, March 2010, report

ⁱⁱⁱ Analysis of the Economic Impact in the US of Bermuda's Insurers and Reinsurers, GSP Consulting and ABIR, November 2007

^{iv} Congressional Budget Office 2007, \$1 spent on mitigation leads to reduction in future spending by \$3; 2005 Multi-hazard Mitigation Council, \$4 savings for every \$1 spent

^v Insurance Institute for Business and Home Safety, IBHS, Hurricane Ike, Nature's Force vs. Structural Strength, recommendations include, state wide building codes, home inspections to ensure compliance, better flood mapping, training for inspectors, assistance for low income consumers with housing retrofits

^{vi} Insurance Institute for Business and Home Safety, IBHS, 2004, Benefits of Modern Wind Resistance Building Codes on Hurricane Claim Frequency and Severity, Claim frequency from Hurricane Charley down 60% for houses built under current building codes; claims severity down 42% for houses built under current building codes

^{vii} The Impact on the US Insurance Market of a Tax on Offshore Affiliate Reinsurance: an Economic Analysis, May 2009, www.keepinsurancecompetitive.com