

THE SENATE SHOULD FOLLOW THE APPROACH OF BANKING COMMITTEE CHAIRMAN DODD ON NATURAL CATASTROPHE PREPAREDNESS AND ASSISTANCE

Four Bills Form the Cornerstones of a Solid Federal Policy

Senate Banking Committee Chairman Dodd has been at the forefront of efforts to adopt a realistic approach to catastrophic natural disasters that promise real relief for Americans. Senator Dodd's bills would:

- **Reauthorize the National Flood Insurance Program (S. 2284).** The NFIP has provided flood insurance for decades and currently insures approximately five million policy holders in 20,000 communities. The NFIP currently has a deficit of \$18 billion. S. 2284 would reauthorize the program and make modest, but positive, reforms. (Reported by the Banking Committee on November 1, 2007)
- **Help at risk homeowners protect their homes from damage (S. 2328).** This bill authorizes grants and loans to homeowners to "harden" their homes against hurricanes and other disasters. (Introduced by Chairman Dodd on November 8, 2007)
- **Help homeowners in financial need to purchase insurance in the private market (S. 2327).** This legislation helps existing, lower income, homeowners purchase insurance in the private market. (Introduced by Chairman Dodd on November 8, 2007)
- **Determine what additional measures, if any, are necessary (S. 2286).** Creates a national commission on natural catastrophe risk management and insurance. (Reported by the Banking Committee on November 1, 2007)

At the same time, the Senate should not follow the House in adopting two expensive, risky, and environmentally unsound bills:

- **Don't expand the NFIP to include wind damage.** Section 7 of the House-passed bill (H.R. 3121) will dramatically expand the NFIP to cover wind damage. This will divert attention away from the original focus of the NFIP and increase economic stress on a program that already is underfunded and overburdened. It also will increase the deficit and result in perverse incentives to build in unsafe and environmentally fragile areas, as well as discourage the provision of wind insurance by the private sector.
- **Don't pass "Nat Cat" legislation bailing out Florida's (and possibly other states') faulty programs.** The House-passed bill (H.R. 3355) would require the federal government to provide catastrophic loans to states if losses exceed 150% of state premiums assessed, would not require that the federal loans be repaid over a specific time period, and would not implement a penalty for a state's default. (S. 2310 includes a similar proposal.) The House-passed bill also would create a new Federal Natural Catastrophe Reinsurance Fund that would require the Treasury Department to sell reinsurance contracts providing coverage for 90% of insured losses that exceed the levels projected for a 1-in-200 year catastrophic event. Federal liability under these reinsurance contracts can amount to as much as \$200 billion.

THE SENATE SHOULD SUPPORT THE NFIP BILL (S. 2284) REPORTED BY THE BANKING COMMITTEE

Do Not Expand The NFIP to Include Wind Damage Insurance or Natural Catastrophe Loan, Insurance, or Reinsurance Programs

The National Flood Insurance Program (“NFIP”), which is operated by the Federal Emergency Management Agency (FEMA) and was established in 1968, provides flood insurance where the private market is unable to do so. NFIP currently insures approximately 5 million policyholders in 20,000 communities and has a deficit of \$18 billion. On November 1, 2007 the Banking Committee reported S. 2284, which would reauthorize and reform NFIP.

The House-passed NFIP reauthorization bill, H.R. 3121, however, includes a provision (Sec. 7) supported by Rep. Gene Taylor (D-MS) that would dramatically expand NFIP to provide wind damage insurance. The Senate should not follow in the footsteps of the House because it would:

- **Overwhelm the NFIP.** The program already has an \$18 Billion deficit and is struggling to resolve flood claims, manage fraud arising from Hurricane Katrina payouts, and prevent insolvency. Adding wind insurance will distract from the program’s mission and substantially undermine efforts to stabilize the program.
- **Result in incentives to build in unsafe or environmentally fragile areas.** Supporting wind insurance that encourages unwise construction in high risk areas sends the wrong message to communities regarding the environmental impact and danger of living in hazard-prone coastal areas and floodplains—areas that may be increasingly vulnerable given the potential impacts of climate change.
- **Cost taxpayers billions.** Experience with the NFIP shows and the American Academy of Actuaries confirms that adding federally backed wind insurance will not be actuarially sound—despite language to the contrary. Taxpayers nationwide will be left to pay the cost of wind damage, which would more than triple the government’s exposure under NFIP.
- **Discourage the provision of wind insurance by the private sector.**

Similar problems apply to the creation of new federal natural catastrophe programs that would require the federal government to provide loans intended to bail out state natural disaster catastrophe funds or require the federal government to provide government reinsurance for a state’s property and casualty insurance program. Therefore, if offered as an amendment to the NFIP bill, we urge you to oppose H.R. 3355 or its companion bill (S. 2310).

There are better ways to help people who already live in areas vulnerable to catastrophic storms—tax credits, loans, and grants to low and fixed-income property owners to encourage them to storm-proof and protect their homes and businesses.

THE SENATE SHOULD NOT ADOPT S. 2310 (CLINTON/NELSON)

National Catastrophe Risk Consortium Bill Protects Faulty State Programs, Not Homes

Although S. 2310 tries to address natural disaster catastrophic risk preparedness, the bill badly misses the mark. It would establish a National Catastrophe Risk Consortium of states that have created reinsurance programs for property and casualty insurers. The Department of Treasury would be required to provide catastrophic loans to states if insured losses exceeded 150 percent of the premiums assessed. Federal liquidity loans also could be issued to fill smaller shortages in state catastrophic reinsurance pools. (A similar House-passed bill, H.R. 3355, goes even further.)

S. 2310 is the wrong answer to catastrophic preparedness goals. The bill would:

- **Promote the continuation of financially unsound state reinsurance programs.** Florida, for example, charges policyholders below-market premiums that do not reflect the risk of living in hurricane prone zones and are insufficient to cover claims in the event of a catastrophic event. The Casualty Actuarial Society notes that Florida has more than \$400 billion in exposure, but only receives \$3 billion in yearly premiums. Rather than encourage changes in Florida's programs, this bill encourages states to continue, adopt, or expand poorly conceived programs with the assurance that federal taxpayers will fix any shortfalls they experience.
- **Encourage subsidized development in unsafe and environmentally sensitive areas.** Environmental groups agree that S. 2310 should not be passed because it does not consider meaningful hazard mitigation, will jeopardize public safety, and will continue subsidized risky development in ecologically sensitive areas. The limited requirements of the bill, e.g., requiring that "new construction, substantial rehabilitation, and renovation" comply with applicable state codes, will not effectively reduce future development in high-risk areas or future casualty and property losses. S. 2310 does not require the implementation of adequate mitigation reforms—such as changes in building design and materials, and the physical siting of buildings—to limit damages in the event of natural disasters.
- **Set up the Federal Government for costly taxpayer bailouts.** Most state reinsurance programs would be eligible for the low-interest federal loans. But the bill provides no fixed repayment period and no penalty for a state's default. Responsibility for state insurance and reinsurance programs that pool natural disaster risks should remain with those states which have established such programs, rather than shifting the financing to the Federal government through such means as Federal loans or reinsurance.
- **Be geographically and demographically unfair.** Subsidies authorized by S. 2310 would, in effect, impose burdens on all taxpayers regardless of economic means, but generally benefit the more affluent.
- **Replace the functioning private reinsurance industry.** Since Hurricane Katrina, the reinsurance industry has infused more than \$26 billion into the catastrophic risk market and used state of the art equipment, actuarial experts, and top risk modeling programs that can assess and spread the financial risk associated with catastrophic storms. S. 2310 would establish a new, inexperienced entity to assist in managing billions of dollars in reinsurance pool resources. In an industry where slight miscalculations equate to billion dollar shortfalls, a Consortium-managed reinsurance market could leave taxpayers on the hook when it is time for homeowners to collect on valid claims.

There is a better way. Congress should make on-the-ground changes that would benefit homeowners (particularly working and middle class homeowners) and actually protect homes from damage. Congress should provide means-based tax incentives to promote mitigation efforts to "harden" homes (S. 2327) as has been done by the state of South Carolina, and should support private sector efforts to provide reinsurance at realistic and affordable rates (S. 2328).

**THE SENATE SHOULD SUPPORT THE
PROPERTY MITIGATION ASSISTANCE ACT OF 2007
(S. 2328)**

Mitigation Does Not Just Save Homes...It Saves Lives

On November 8, 2007, Senator Dodd (D-CT) introduced S. 2328 to help people protect their homes in areas at high risk for catastrophic storm damage. The need for mitigation is immediate. A recent study by The Wharton School's Risk Management and Decision Processes Center concluded that mitigation measures reduced damages from catastrophic storms by more than 50%. S. 2328 recognizes that investments in "hardening" homes through such actions as improved roofs, safe room construction, elevation of electrical systems, and the addition of storm shutters goes a long way to *saving* homes and, ultimately, to *saving* lives.

Moreover, experience shows that these investments pay dividends in reduced insurance costs as well as safety. For example, the State of Florida recently announced that participants in its mitigation program experienced average premium savings of more than \$150 per participating household, or approximately 15%. The Institute of Business and Home Safety has estimated that every dollar invested in mitigation yields four to seven times that in savings.

S. 2328 provides important tools in the fight against increasingly disastrous storms and would enable on-the-ground catastrophic preparedness, including:

- **Establishment of a Homeowner Mitigation Loan Program (HMLP).** HMLP, administered by the Federal Emergency Management Agency (FEMA), would provide pre-disaster grants to states. The state would then provide direct mitigation grants and non-compounding loans to property owners. A receiving state would be required to match not less than 10% of the grant amount received.
- **Focus on Low- and Moderate-Income Homeowners.** To ensure that those most in need are served by the legislation, the bill would limit grant eligibility to homeowners with incomes less than 50% of the area's median income and limit low interest loan eligibility to homeowners with incomes less than 120% of the limit. Regular loans are available to homeowners and businesses with incomes that exceed 120%.
- **Development of Long Term State Catastrophic Storm Preparedness Plans.** S. 2328 provides that states must submit to FEMA a mitigation plan in order to be considered for grant award. This provision encourages states to develop comprehensive plans that will improve the structural integrity of homes and the infrastructure within the state. For example, among those that received mitigation grants from Florida's My Safe Florida Home program, home strength increased by 36%. S. 2328 would, likewise, encourage similar protection in high risk areas.
- **Encouragement of Proper Insurance Coverage.** Homeowners and businesses are only eligible for mitigation assistance if they have home insurance and, where applicable, flood insurance for their property. This provision encourages property owners to utilize a multi-layered approach to protecting their property.