NAMIC Federal Issue Brief

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FINANCIAL REGULATORY REFORM

- **INSURANCE REGULATORY REFORM**
- **FEDERAL INSURANCE OFFICE (FIO)**
- **CONSUMER FINANCIAL PROTECTION AGENCY (CFPA)**

NAMIC
NATIONAL ASSOCIATION OF MUTUAL INSURANCE COMPANIES

EFFECTIVE ADVOCACY
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NAMIC Federal Issue Brief

REGULATION OF THE PROPERTY/CASUALTY INSURANCE INDUSTRY

There are continuing efforts to create a regulatory role for the federal government in the insurance arena, including the potential creation of an optional federal charter.

NAMIC OPPOSES the creation of a duplicative federal regulatory system or other federal/dual regulation for property/casualty insurance companies. Property/casualty insurance is highly dependent on local factors and NAMIC believes that the introduction of a federal regulatory structure, even on an optional basis, could have unintended consequences for the entire industry.

BACKGROUND

Mutual property/casualty insurance companies today are a critical component of the American economy. Property/casualty insurance companies on the whole are very well capitalized and are in no danger of insolvency. Their prudent management and conservative approach to long-term stability are particularly well suited to protecting consumers on Main Streets across America.

States have been the sole regulator of most insurance products since the beginning of the insurance industry in America. In adopting the McCarran-Ferguson Act in 1945, Congress recognized the central role of the states in the regulation of insurance.

State and local laws determine coverage and other policy terms. Reparation laws affect claims. Local accident and theft rates impact pricing. Climate – hurricanes, earthquakes, etc. – differ significantly from state to state. The state regulatory system recognizes and responds to these differences.

For years, the debate over insurance regulatory reform revolved around the creation of an optional federal charter (OFC). There were those in the industry that viewed the creation of an OFC proposal as a corrective to what they saw as a complicated and disjointed national regulatory structure for insurance.

There were also those that believed that effective modernization of the insurance regulatory structure could best be accomplished at the state-level. Those opposed to the OFC were concerned with the unintended consequences for the entire industry. They argued that allowing the federal government to set up a dual charter system for insurance had the potential to lead to costly, confusing, and duplicative regulations that could affect all insurers.

There are several important reasons why the federal government would not create a more effective regulatory regime for property/casualty insurers. In this political environment, creating new regulations at the federal level has the

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potential to go much further than necessary. What begins as an *optional* federal charter may well result in additional regulations and costs on the entire industry. Additionally, the property/casualty insurance industry remained stable and solvent throughout the financial crisis in part due to the state-based regulatory structure. Rather than simply creating an alternative regulatory scheme for those who seek it, the OFC could dilute the effectiveness of the current structure. For example, it is likely that the creation of an OFC would lead to the creation of a federal guaranty fund that would either replace the state guaranty funds or operate independently of them. In either case, this duplicative system would serve to damage all guaranty funds and threaten the solvency of the insurance industry.

On April 2, 2009, long-time supporters of an OFC, Reps. Melissa Bean, D-Ill., and Ed Royce, R-Calif., introduced H.R. 1880, the National Insurance Consumer Protection Act. The legislation would create an office located within the Department of the Treasury, that would have the authority to organize, incorporate, operate, regulate, and supervise national insurers, national insurance agents, and national insurance producers. It would also define national standards for company activities such as accounting, risk management, internal controls, investments, and reinsurance. The office would further be responsible for recommending to the new systemic risk regulator any insurance companies that would be required to be regulated at the federal level.

The bill would establish a division of consumer affairs with an office in each of the 50 states and a centralized call center would respond to consumer questions and complaints related to national insurers and producers. National insurers would also be required to appoint a consumer liaison to address consumer complaints or disputes. The creation of a duplicative federal insurance consumer protection system would be costly, confusing for consumers, and weaken existing consumer protections.

The legislation would also create a national guaranty fund financed by assessments on federally chartered insurers. In addition to participation in the federal guaranty fund, national insurers would be required to participate in state guaranty funds for every state in which they do business. This dueling set of national and state guaranty funds will weaken both systems. Interaction and coordination of the duplicative guaranty systems would confuse and delay settlements. The state guaranty fund system is a highly effective mechanism through which the industry polices and supports itself.

While H.R. 1880 is unlikely to be considered this Congress, there remains a significant constituency that continues to push for federal regulation of some kind. NAMIC however, believes that while the state-based system is far from perfect, continuing regulatory modernization efforts at the state level will ensure the best, most competitive future for the property/casualty insurance industry.

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NAMIC ONLINE

NAMIC REMAINS CONCERNED BY ONI POWERS IN DODD BILL

WASHINGTON (March 15, 2010) – The National Association of Mutual Insurance Companies (NAMIC) remains concerned about the latest version of financial services reform legislation unveiled by Sen. Chris Dodd, D-Conn., on Monday, specifically with regards to the powers granted to the proposed Office of National Insurance.

“While we remain concerned about some provisions in the bill, NAMIC applauds Sen. Dodd for his effort to address the problems in our financial regulatory system that contributed to the economic crisis we face today,” said Jimi Grande, senior vice president of federal and political affairs for NAMIC. “It is important to remember, however, that virtually every examination of the crisis has shown that property/casualty insurers played no role in creating the crisis and pose no systemic risk to the overall economy.”

A remaining concern for NAMIC is the broad subpoena authority granted to the proposed Office of National Insurance created by the legislation. Although the legislation states specifically that the ONI would not serve in any regulatory or supervisory capacity with regards to the industry, it would still grant it the subpoena authority to compel companies to produce data.

“Insurance is the most regulated industry in the country, and there is no shortage of data that would be available to the ONI either publicly or through the National Association of Insurance Commissioners,” Grande said. “The use of subpoena authority in this context could have unintended negative consequences by creating a duplicate and excessive process that would ultimately harm the consumer it seeks to protect.”

One area in which the new legislation has addressed NAMIC’s concerns is in the establishment of a new consumer protection agency, which under Sen. Dodd’s bill would be housed within the Federal Reserve. Echoing the version passed by the house, Sen. Dodd’s bill recognizes the strong consumer protections of the state-based regulatory system and excludes property/casualty insurance from the jurisdiction of this new federal agency.

“As with the stand alone agency that would be created by the House legislation, Sen. Dodd’s bill respects the strong regime of consumer protections with regard to property/casualty insurance at the state level,” said Grande. “This will help avoid regulatory confusion and ensure a more responsive consumer protection system.”

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NAMIC
ALERT

March 22, 2010

SENATE BANKING COMMITTEE PASSES FINANCIAL REGULATORY REFORM BILL

Today, the Senate Committee on Banking, Housing and Urban Affairs passed the Restoring American Financial Stability Act of 2010. Passed quickly and along a party line vote of 13-10, the bill was sent to the floor of the Senate for further consideration.

In an expedited procedure, Chairman Christopher J. Dodd, D-Conn., offered an opening statement outlining the many months of negotiation – both successful and failed – that led to this version of the bill. Ranking Member Shelby commented that he was disappointed that Chairman Dodd had to quickly move a bill because he believes bipartisan solutions on remaining conflicts are close at hand. However, he stated that much work remains to be done and hopes to solve those conflicts before a floor vote. The manager's amendment was then agreed to by a voice vote and the final vote reporting the bill out of committee taken and passed by 13-10.

Originally, more than 400 amendments to the legislation had been filed for the markup proceedings but Dodd struck a deal to have the fight on the Senate floor instead. This approach avoids considering the amendments in committee, which could have taken weeks. However, it also is viewed as a more partisan path and resulted in not a single Republican on the committee voting in favor of the legislation.

Chairman Dodd's manager's amendment incorporates 22 Democratic amendments and would jettison language allowing the Federal Reserve to use its emergency lending authority for a "financial market utility" such as payments and clearing systems, which opponents have argued was an unintentional bailout regime. It also would increase the Securities Investor Protection Corp.'s borrowing authority from Treasury from $1 billion to $2.5 billion; restricts auditors from receiving whistleblower awards and amends the Truth in Lending Act to cover transactions of up to $50,000 with adjustments for inflation.

Last week, Dodd unveiled a **second draft proposal** to reshape the nation's financial regulatory system. The draft significantly changed and built upon his initial draft released in November 2009. After months of negotiations, first with Banking Committee Ranking Member Richard Shelby, R-Ala., and then with Sen. Bob Corker, R-Tenn., Dodd decided to move forward without the support of the Republicans.

The legislation approved tonight would create a new federal systemic risk regulator, a massive expansion of the government's authority to resolve troubled financial institutions, create a Bureau of Consumer Financial Protection, and create a new federal office of insurance.

Since the financial crisis began in late 2008, NAMIC has been closely involved throughout the debate on financial regulatory reform legislation and has been able to achieve significant improvements to the legislation. These include ensuring that a proposed federal office to address insurance is strictly a non-regulatory information source, that a proposed new financial consumer protection agency does not have jurisdiction over the business of insurance, and that any new systemic risk regulation and federal resolution authority have little to no impact on any property/casualty insurer.

This is another important step in the Senate's financial regulatory reform debate, However, NAMIC will continue to work with the Senate on our remaining concerns. We will continue to keep you apprised as the debate continues through the legislative process.

COMMENTS: Please direct all requests or comments to Federal Affairs Manager Jon Bergner at **jbergner@namic.org**, or NAMIC Advocacy Alert, 3601 Vincennes Rd., Indianapolis, IN 46268.

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NAMIC ALERT

March 15, 2010

DODD UNVEILS PARTISAN FINANCIAL REGULATORY REFORM BILL

Today at 2 p.m., Senate Banking Committee Chairman Christopher J. Dodd, D-Conn., unveiled his latest draft proposal to reshape the nation's financial regulatory system. This draft significantly changes and builds upon his initial draft released in November 2009. After months of negotiations, first with Banking Committee Ranking Member Richard Shelby, R-Ala., and then with Sen. Bob Corker, R-Tenn., Dodd decided to move forward without the support of the Republicans.

Consumer Financial Protection Agency

The biggest change in the draft addresses the most contentious issue of the overall package: the proposed creation of a new independent Consumer Financial Protection Agency (CFPA). The draft released today abandons the CFPA and instead would create a Bureau of Consumer Financial Protection to be located within the Federal Reserve Board. The newly created Bureau would have the ability to autonomously write rules for consumer protections governing all entities – banks and non-banks – offering consumer financial services or products.

Most importantly, all lines of property/casualty insurance are excluded from the purview and jurisdiction of the new Bureau.

Office of National Insurance

The draft released today does not make any changes to the section that proposes creating an Office of National Insurance, or ONI. Title V would create an Office of National Insurance within the Department of the Treasury. Similar to the comprehensive financial services regulatory reform legislation passed by the House last December, the new draft explicitly states that the ONI will not have regulatory or supervisory powers over the business of insurance. Additionally, the office will have little authority to preempt state laws dealing with insurance. However, the Dodd draft retains subpoena and enforcement provisions that were removed from the House legislation.

With respect to trade agreements, the discussion draft includes a savings provision that nothing in the legislation shall be construed to affect the development and coordination of U.S. international trade policy or the administration of the U.S. trade agreements program. Additionally, the Treasury secretary would be required to consult with the U.S. Trade Representative prior to initiating or concluding any international insurance agreements on "prudential measures," or measures concerning financial stability.

Lastly, the Office would be mandated to study insurance regulation and "how to modernize and improve the system of insurance regulation in the United States."

Systemic Risk Oversight

The Chairman's mark would create a new Financial Stability Oversight Council to focus on identifying, monitoring and addressing systemic risks posed by large, complex financial firms as well as products and activities that spread risk across firms. The nine member council would be comprised of the:

- Secretary of the Treasury, Chair
- Chair of the Board of Governors of the Federal Reserve
- Comptroller of the Currency
- Director of the Consumer Financial Protection Bureau
- Chairperson of the Securities and Exchange Commission
- Chairperson of the Commodity Futures Trading Commission
- Director of the Federal Housing Finance Agency; and
- An independent member appointed by the President confirmed by the Senate having insurance expertise.

The Council would be permitted to appoint technical and professional advisory committees, including an advisory committee of state regulators.

Specifically the Council would be tasked with identifying financial risks posed by large, interconnected bank holding companies or nonbank financial companies, responding to emerging threats and dispelling expectations that the government will back losses from financial institutions. Other duties include identifying gaps in regulation, acquiring information from regulators, recommending general supervisory priorities to functional regulators, facilitating information sharing, and identifying and requiring regulation of nonbank financial companies that pose a risk to the economy by the Board of Governors.

The Council may by a 2/3 vote, including an affirmative vote by the Secretary of the Treasury, require any U.S. non-bank financial company (including an insurer) to be regulated by the Board of Governors and be subject to heightened prudential standards if the entity is determined to be a risk to financial stability. Notice to affected companies must be provided in writing with an explanation of the rationale underlying the decision. The company would have the right to request a hearing within 30 days. Prior to a final determination the Council would be directed to consult with the primary functional regulator. Determinations would be subject to judicial review; however, final determination may be vacated only if they are held to be arbitrary and capricious. Designations must be reviewed annually and the designation may be rescinded by a 2/3 of vote of the Council with the concurrence of the Secretary of the Treasury.

In determining appropriateness for supervision the Council shall consider:

- the degree of leverage of the company;
- the amount and nature of the financial assets of the company;
- the amount and types of the liabilities of the company, including the degree of reliance on short-term funding;
- the extent and type of the off-balance sheet exposures of the company;
- the extent and type of the transactions and relationships of the company with other significant nonbank financial companies and significant bank holding companies;
- the importance of the company as a source of credit for households, businesses, and State and local governments and as a source of liquidity for the United States financial system;

- the recommendation, if any, of a member of the Council

Companies regulated under the new authority would be subjected to heightened prudential standards and increased liquidity standards; would be required to establish a risk committee and develop resolution or so-called "funeral plans:" undergo periodic stress tests; and be subject to early remediation. The Council would also be authorized to make recommendations to functional regulators for increased supervision standards for other entities. Regulators would be required to enforce the recommendations regarding activities of nonbank financial companies. If the regulator does not enforce the recommendations, it must notify the Council within 90 days of why the recommendations are not enforced.

The legislation would also create a new Office of Financial Research within the Department of the Treasury. The Director of the Office would serve as a non-voting member of the Council in an advisory capacity. The Council may direct the Office to directly request information from bank holding companies and nonbank financial companies. Information requests from the Office would be enforceable by subpoena upon certification that the information is necessary and that the Office has coordinated with the appropriate functional regulator.

In addition to its research and advisory functions, the Office would also be directed to provide certain data to financial industry participants and to the general public to increase market transparency and facilitate research on the financial system. The provision of such information would be subject to the caveat that intellectual property rights are not violated, business confidential information is properly protected, and the sharing of such information poses no significant threats to the financial system of the United States. The Office; however, is specifically directed to prepare and publish, in a manner that is easily accessible to the public, a financial company reference database and a financial instrument reference database.

Submission of data to the Council or Office would not constitute a waiver of applicable privilege. The Council and Office are directed to maintain the confidentiality of data and Title V, Freedom of Information provisions, including applicable exceptions, would apply to the data.

Resolution Authority

The bill establishes an orderly mechanism for the Federal Deposit Insurance Corporation ("FDIC" "Corporation") to liquidate or rehabilitate failing systemically significant financial companies, upon determination by the Department of the Treasury, Federal Reserve and FDIC. The legislation would allow most large financial companies to be resolved through the normal bankruptcy process. Insurance company and insurance subsidiary rehabilitation and liquidation would be "conducted as provided under [the] State law [of the domiciliary state]" and outside the new receivership system.

To facilitate the orderly dissolution of specified financial companies, the bill establishes a $50 billion "Orderly Liquidation Fund" within the U.S. Treasury. The fund would be pre-funded over a period of 5 to 10 years through risk-based assessments on bank holding companies with greater than $50 billion in consolidated assets and systemically significant nonbank financial companies supervised by the Federal Reserve. Additional assessments would be imposed if the fund experiences a loss during the initial capitalization period or fails to reach target funding level or as necessary to fully meet the obligations of the Corporation within 60 months of issuance. These additional assessments would be levied against a wider collection of financial firms, including nonbank financial companies, including insurance companies, with $50 billion or more in consolidated assets. Specific company assessments would be determined on a graduated risk-based basis, taking into consideration funds expended as a result of a state insolvency of one or more insurance companies.

NAMIC is continuing to wade through and analyze the almost 1,400 pages of the new draft bill to ensure there are not dangerous or unnecessary provisions slipped in anywhere. This draft reflects much of our work over the past 18 months and by and large recognizes that property/casualty insurers are fundamentally different from those in the financial services sector responsible for the financial crisis. The Dodd draft is slated to be marked up in the Senate Banking Committee during the week of March 22, and we will continue to bring you the latest updates as this debate develops. While this is a significant step in the evolution of the financial regulatory reform proposal, we still have several months of negotiating and fine tuning to work out some of our remaining concerns.

COMMENTS: Please direct all requests or comments to Federal Affairs Manager Jon Bergner at **jbergner@namic.org**, or NAMIC Advocacy Alert, 3601 Vincennes Rd., Indianapolis, IN 46268.

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NATIONAL ASSOCIATION OF MUTUAL INSURANCE COMPANIES

EFFECTIVE ADVOCACY
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FEDERAL INSURANCE OFFICE

Congress has proposed the creation of a federal office to provide expertise and information on the insurance industry to policymakers.

NAMIC BELIEVES that a properly crafted office within the Department of Treasury could play a vital role in the effort to streamline and modernize the state-based insurance regulatory system and provide essential information to Congress and the federal government. However, **NAMIC OPPOSES** the creation of a federal office that would have regulatory or supervisory authority over the property/casualty insurance industry.

BACKGROUND

The debate on the regulation of the insurance industry has increasingly focused on the creation of an entity within the federal government that would serve as a resource for Congress and the Administration in the designing and implementation of economic policy and trade negotiations.

Office of Insurance Information
Capital Markets Subcommittee Chairman Paul Kanjorski, D-Penn., introduced legislation establishing an Office of Insurance Information, during the 110th Congress. H.R. 5840, the Insurance Information Act, would have created an OII within the Treasury Department with jurisdiction for all lines of insurance except for health insurance to provide advice and counsel regarding domestic and international policy issues.

NAMIC worked closely with Chairman Kanjorski to shape the proposal to ensure that the legislation strictly prohibited the office from any regulatory authority over the business of insurance as well as significantly narrowing the scope of federal preemption. Preemption of state regulatory authority would only occur in the instance where a state treats a foreign insurer in a less favorable way than a domestic insurer.

H.R. 5840 was never debated by the full House of Representatives. However, in the 111th Congress – prior to the collapse of the financial markets – Subcommittee Chairman Kanjorski re-introduced the OII legislation as H.R. 2609.

Specifically, H.R. 2609 would collect and analyze data on insurance; advise the Secretary of the Treasury on major domestic and international policy issues; report to Congress every two years; establish federal policy on international insurance matters; and, ensure that state insurance laws remain consistent with federal policy in coordinating international trade agreements.

Administration-proposed Office of National Insurance

The administration proposed the creation of an Office of National Insurance (ONI) as part of a broader overhaul of the financial services regulatory sector. The ONI would be created within the Department of the Treasury. This new office was a significant departure from Kanjorski's OII. The ONI would have been tasked with monitoring all aspects of the insurance industry including gathering information, negotiating international agreements, and coordinating policy. Specifically, the office would gather information and identify any problems or gaps in regulation that could contribute to a future crisis. NAMIC expressed significant concerns about the powers that would be granted to this new entity, specifically the authority to issue subpoenas to insurers requiring them to submit data at any time, as well as the ability to pre-empt state law on regulatory matters.

The ONI would also have had the responsibility of recommending to the Federal Reserve any insurance company that the office believes should be supervised as a top-tier financial holding company (Tier 1 FHC), which would be a company who's "failure could pose a threat to financial stability due to their combination of size, leverage, and interconnectedness." The ONI would also have assumed all existing responsibilities for the Terrorism Risk Insurance Program.

Although the ONI proposal did not call for the creation of a federal regulator for property/casualty insurers, it did leave open the possibility for Congress to create a federal insurance regulatory structure. The administration suggested that the US could achieve "increased [regulatory] uniformity through either a federal charter or effective action by the states."

Federal Insurance Office

Prior to a committee hearing in October of 2009, Rep. Kanjorski introduced a new version of his proposed OII legislation and renamed the new entity the Federal Insurance Office (FIO).

As in the 110th Congress, NAMIC worked closely with Rep. Kanjorski's staff and several positive changes that NAMIC advocated were made. First, it added language clarifying that the legislation does not establish a general supervisory or regulatory authority for the FIO or the Department of the Treasury over the business of insurance. Second, language ensuring that any non-publicly available information obtained would be treated as trade secrets and commercial or financial information obtained from a person would be treated as privileged or confidential and properly excluded from any FOIA requests. Third, the applicability of the Administrative Procedures Act was added, which would limit the preemption authority and provide judicial redress to maintain the integrity of the insurance system and to permit appropriate legal challenges to preemption. And finally, the new draft addressed the pre-emption issues, by providing a strong savings clause protecting state-based insurance regulation, providing for more state insurance regulator consultation, and creating a more reasonable data collection provision without broad subpoena power.

Although the name has been changed to the Federal Insurance Office, the new version strictly limits the office's ability to preempt state laws, does not grant the office subpoena authority, and explicitly maintains that the office will not have regulatory or supervisory authority.

Ultimately the FIO legislation was included into a larger package, H.R. 4173, the Wall Street Reform and Consumer Protection Act. H.R. 4173 passed the House of Representatives on December 11, 2009, by a vote of 223-202.

Senate-proposed Office of National Insurance

In the Senate, the financial regulatory reform legislation, the Restoring American Financial Stability Act of 2010, was released by Banking Committee Chairman Christopher J. Dodd, D-Conn. Included in the almost 1,400 page package was Title V which addresses the insurance industry. Title V would create an Office of National Insurance within the Department of the Treasury. Similar to the House-version, the discussion draft explicitly states that the ONI will not have regulatory nor supervisory powers over the business of insurance. Additionally, the office will have little authority to preempt state laws dealing with insurance. However, the Dodd draft restores the subpoena and enforcement provision that were removed from the House legislation.

With respect to trade agreements, the discussion draft includes a savings provision that nothing in the legislation shall be construed to affect the development and coordination of U.S. international trade policy or the administration of the U.S. trade agreements program. Additionally, the Treasury secretary would be required to consult with the U.S. Trade Representative prior to initiating or concluding any international insurance agreements on "prudential measures," or measures concerning financial stability.

Lastly, the Office would be mandated to study insurance regulation and "how to modernize and improve the system of insurance regulation in the United States." The ONI director must submit a report to congress no later than 18 months after the date of enactment.

The Restoring American Financial Stability Act was voted 13-10 out of the Senate Banking Committee and is awaiting debate by the full Senate.

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CONSUMER FINANCIAL PROTECTION AGENCY

A new federal agency to oversee consumer financial product safety should not regulate insurance products and duplicate state consumer protections.

NAMIC OPPOSES the inclusion of property/casualty insurance from the jurisdiction of the proposed Consumer Financial Protection Agency (CFPA).

BACKGROUND

One of the key elements of the financial services regulatory reform effort has been to ensure that taxpayers and consumers will be protected from another economic crisis. Included in the comprehensive regulatory reform legislation have been proposals to create a new federal office to oversee all consumer protection with regard to consumer financial products and services.

Insurance differs greatly from other financial products and services and insurance consumer protections are regulated very strongly by the states. In addition, there have been no consumer protection problems with regard to the property/casualty industry during the current economic crisis. For these reasons, NAMIC believes the resources and efforts to protect consumers should be focused on those segments of the financial services industry that led to problems.

NAMIC is concerned that a new federal consumer protection office with jurisdiction over property/casualty insurance will lead to dual regulation between the federal government and the states. Further, conflict between safety and soundness rules and the new office's consumer protection rules could occur.

Legislation creating an independent Consumer Financial Protection Agency was made part of the comprehensive regulatory reform legislation passed out of the House in December 2009. In part due to NAMIC's efforts, all lines of property/casualty insurance were specifically excluded from the jurisdiction of the CFPA because of property/casualty insurers' unique state-based regulatory regime and focus on policyholder protections.

On the other side of Capitol Hill, creation of the new consumer protection office was met with significant concern among senators from both parties. In an effort to create a bipartisan bill, Sen. Christopher Dodd, D-Conn., Chairman of the Senate Banking Committee, asked certain members of the committee to partner with

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senators of the opposite party to craft specific sections of the bill. Recognizing that consumer protections were the most contentious issue, Sen. Dodd partnered with Sen. Richard Shelby, R-Ala., Ranking Member of the committee, to debate options.

On February 26, 2010, Sen. Dodd began to circulate a new proposal that would create a consumer protection division within the Treasury Department rather than an independent agency. The proposed Bureau of Consumer Financial Protection would be given broad power to examine and enforce rules across financial services and products. However, this power would be significantly checked by the ability of a financial institution's primary safety and soundness regulator to appeal any decisions the new bureau would make. In addition, the bureau would have to consult with these regulators before proposing or finalizing any rules.

The business of insurance is also specifically excluded from the jurisdiction of the proposed bureau. On March 22, 2010, this new office was included in comprehensive financial service regulatory reform legislation that passed out of the Senate Banking Committee and is now heading for the floor.

NAMIC continues to work closely with the administration and Congress to adequately address concerns over consumer protection while ensuring the property/casualty insurance industry is excluded from federal consumer protection regulation and the state-based regulatory system maintained.

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NATURAL DISASTER LEGISLATION

- **NAT CAT (REP. KLEIN BILL)**
- **FLOOD REFORM**
- **BUILDING CODES**

NAMIC Federal Issue Brief

NATURAL CATASTROPHE

The high costs of recent natural disasters combined with the fear of future catastrophes have restricted homeowners' insurance, reduced availability, and raised affordability issues in disaster-prone regions.

NAMIC OPPOSES efforts to provide federal bailouts for state-sponsored insurance programs, which could create incentives for more states to create risky catastrophe plans similar to Florida, thereby increasing the federal government's financial exposure.

BACKGROUND

As the frequency of natural disasters rises, so increases the probability that a major catastrophe will strike the U.S. at a much higher cost than the reported $180 billion in insured losses and federal disaster relief as a result of the three 2005 hurricanes.

Simply put, the availability and affordability of property insurance in coastal regions is primarily a function of risk and higher property insurance prices in coastal areas have come in the wake of the recent storms. However, other variables, including actions taken by government, can also affect the supply and costs of insurance. Many states in catastrophe-prone coastal regions impose rating and underwriting restrictions on property insurers that act as price ceilings on coverage. This government rate suppression, which allows high-risk property owners to pay artificially low premiums, is the preferred solution of many regulators and state legislators to the property insurance "affordability problem" in catastrophe-prone areas. But rate suppression masks the real problem of rising costs – the growing concentration of people and wealth in high-risk regions – by forcing insurance buyers in low-risk regions to pay inflated prices in order to subsidize the insurance costs of those in high-risk regions.

In response to the increase in natural disasters, combined with the continued concentration of the population in vulnerable areas, NAMIC created the Task Force on Natural Disasters. The task force played a leading role in the development of solutions that address the issues associated with major catastrophic events such as hurricanes, earthquakes, windstorms, tornadoes, and wildfires. The task force formulated four general principles that serve to guide NAMIC members and staff as the natural disaster debate evolves.

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EFFECTIVE ADVOCACY
STRATEGIC PUBLIC POLICY
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The principles are:

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

In early 2009, the Florida Catastrophe Fund requested a line of credit from the Department of Treasury to shore up the fund since it would not be able to cover the amount for potential damages required by Florida state law. After the Treasury Department declined to issue a line of credit to the State Hurricane Catastrophe Fund in Florida earlier this year, Sen. Bill Nelson, D-Fla., introduced S. 505 to establish a consortium similar to that of a government sponsored enterprise that would give the Treasury Department authority to provide aid to any state that suffers a catastrophe. Additionally, S. 505 would create a National Homeowners Insurance Stabilization Program, providing loans to states after a catastrophe. This legislation is similar to S. 2310 which was introduced by Sen. Nelson in the 110th Congress.

Homeowners Defense Act

On May 21, 2009, Congressman Ron Klein, D-Fla., again introduced the Homeowners Defense Act, with several modifications from the 110th Congress. The Homeowners Defense Act was also introduced and subsequently passed in the House in the 110th Congress.

Rep. Klein's bill establishes the National Catastrophe Risk Consortium for state sponsored insurance funds to voluntarily pool their catastrophic risk, then transfer that risk to the private markets through the use of catastrophe bonds and reinsurance contracts. The creation of underfunded state catastrophe funds that subsidize insurance premiums will do much to distort the insurance markets.

The legislation would also establish a debt guarantee program in the Treasury Department that would authorize the federal government to guarantee debt issued by eligible state programs to assist in the financial recovery from natural catastrophes. NAMIC has reservations about this provision because of the advantage given to investors by the implicit federal backing.

H.R. 83, introduced by Rep. Ginny Brown-Waite, R-Fla., was included as part of this legislation in the last Congress and is again included in the Homeowners Defense Act. It would establish a federal natural catastrophic reinsurance fund that would be authorized to write reinsurance contracts for catastrophic events, defined as a 1 in 200 year event. NAMIC has serious reservations about what this provision could potentially do to reinsurance markets.

NAMIC does support the final provision of the Homeowners Defense Act, providing for a $15 million a year grant program to develop, enhance, and maintain mitigation programs that prevent and mitigate losses from natural catastrophes. However, NAMIC believes the program should receive more funding because the current level would not be large enough to have a substantial impact on people's behavior.

NAMIC was invited to testify at a July 2009 field hearing on natural catastrophe issues in West Palm Beach, Florida, and was the only insurance trade association to do so. Representing NAMIC was Dr. Robert Detlefsen, NAMIC's Vice President of Public Policy. He spoke before the House Financial Services Oversight and Investigations Subcommittee, emphasizing the fact that government intervention cannot be an effective substitute for the economic principles affecting the complex relationship between supply, demand and price. Detlefsen also outlined federal proposals which NAMIC supports in an effort to establish a proper balance between the roles of the private insurance sector and governments and 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 disasters.

The House Financial Services Subcommittee on Housing and Community Opportunity and Subcommittee on Capital Markets, Insurance, and Government Sponsored Entities also recently held a joint hearing entitled "Approaches to Mitigating and Managing Natural Catastrophe Risk." NAMIC submitted testimony, pulling from recent developments and displaying ways that states have started to manage their risk through making smart decisions at the state level. Many of these changes at the state level would not be incentivized if a federal backstop, such as the one that the Homeowners Defense Act would create, were in place.

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SUBMITTED TESTIMONY
ON BEHALF OF
THE NATIONAL ASSOCIATION OF MUTUAL INSURANCE COMPANIES

JOINT HEARING

SUBCOMMITTEE ON HOUSING AND COMMUNITY OPPORTUNITY

SUBCOMMITTEE ON CAPITAL MARKETS, INSURANCE, AND GSEs

OF THE COMMITTEE ON FINANCIAL SERVICES

U.S. HOUSE OF REPRESENTATIVES

“APPROACHES TO MITIGATING AND MANAGING NATURAL CATASTROPHE RISK: H.R. 2555, THE HOMEOWNERS’ DEFENSE ACT”

MARCH 10, 2010

Founded in 1895, NAMIC is a property and casualty insurance association, whose 1400 members underwrite over 40 percent of the property/casualty insurance premium written in the United States. NAMIC is grateful for the opportunity to submit testimony 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. While the private sector and government can and should work together to address problems of insurance availability and affordability in these areas, government intervention should not supplant the economic principles affecting the complex relationship between supply, demand, and price.

Understanding the Nature of the Problem

To understand the problem, we must begin with three simple facts:

1. The exposure of densely concentrated, high-value property to elevated levels of catastrophe risk in certain geographic regions means that property insurance in these regions will be relatively expensive compared to the regions that lack these attributes.

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 significantly increased population growth and commercial development at a time when the frequency and severity of catastrophic storms in these regions is increasing.

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.

Frequency and Severity of Major Coastal Storms

Higher property insurance prices in coastal areas have come in the wake of the three 2005 Gulf Coast hurricanes that killed more than 1,400 people and cost more than $180 billion in insured losses and federal disaster relief. But the trend was not caused by those hurricanes *per se*. Rather, insurance prices have increased because of what the 2005 hurricane season portends for the future.

Coastal Development and Population Growth

Greater frequency and severity of coastal storms would matter less if the affected areas were sparsely populated and contained few valuable assets. But in fact 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 is increasing 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 five years from now—Florida is projected to surpass New York as the nation's third most populous state.

Consider 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 $180,890,000,000 in damages, or 2,380 times the amount of damages caused in 1926.

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 cost of insurance in the short term, it has long-term consequences that are far worse for insurance consumers. First, rate suppression lowers prices for people living in high-risk regions at the expense of insurance buyers 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 removes a powerful disincentive – namely, higher insurance prices – to further population growth and economic development in disaster-prone areas. That may seem like a good thing to those that thrive on growth and development. But unfortunately, government rate suppression distorts the public’s perception of risk, thus encouraging—rather than discouraging—the very phenomenon that created the problem in the first place – the growing concentration of people and wealth in high-risk regions.

Federal and state governments then end up bearing the cost of the economically irrational decisions that result from rate suppression by paying for disaster aid to repair properties that might have never 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 and allows them to make a profit. Historically, profit margins in the highly competitive property/casualty insurance industry have been quite modest compared to other business sectors. But if government rate regulation prevents insurers from covering their claim costs, replenishing surplus reserves to pay future claims, and making a profit, they may have no choice but to exit the market or dramatically reduce exposure, as we have seen recently in Florida.

At the same time, NAMIC is not insensitive to the affordability issue, particularly for long-time, low-income residents and businesses of catastrophe-prone areas that have seen dramatic increases in their premiums related to new development and not to their behavior. NAMIC suggests that the best way to address the affordability issue is through direct governmental subsidies to needy individuals and businesses. Government programs for risk mitigation may also help. Such approaches would increase insurance affordability and availability without distorting the insurance mechanism that sends valuable signals as to the relative level of risk of living in a particular geographic area.

The Tide Is Beginning to Turn in Florida

In 2009 Florida lawmakers passed, and Governor Charlie Crist signed into law, HB 1495, allowing Citizens Property Insurance Corp. to increase premium rates by 10 percent for individual policyholders each year until actuarially sound levels are attained. Additionally, this bill also 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 Florida Citizens Property Insurance Corp., the state-run insurer, on a glide path to more appropriately matching rate to risk, it puts the entire state at the beginning of a path to better financial preparation for future storms.

A separate bill, HB 1171, 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. The bill would not have affected the state's ability to regulate against unfair discriminatory practices, insolvency, and insufficiency. The measure also included transparency, disclosure, and consumer provisions. The bill, which passed overwhelmingly, represented a greater understanding by 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, is so underfinanced that it couldn't possibly pay off claims in the event of major storm damages." Unfortunately, the governor chose to veto HB 1171 despite consumer and insurer support.

NAMIC would have preferred that this bill be applied to all insurers, and the 2010 versions – HB 447 and SB 876 - do just that. It remains to be seen if this year's session, which began in earnest just last week, will see success with consumer choice legislation in particular, but we have hope that the positive movement from last year will continue.

The Lack of Federal Backing Has Been an Incentive for States to Make Improvements

The likelihood that Florida and other disaster-prone states will move forward on the path toward more prudent catastrophe risk management depends in no small measure on the structure of incentives that Congress creates. If Congress enacts legislation that encourages coastal states to adopt and enforce stronger building codes, and to curtail further development of ecologically-sensitive coastal areas, it can slow the growth in coastal catastrophe risk exposure. The relatively small amount of damage caused by the huge earthquake in Chile, and in contrast the vast degree of damage caused in Haiti, are good examples of how natural catastrophe damage can be limited through stronger building codes. On the other hand, if Congress enacts legislation such as the Homeowners Defense Act, it will remove incentives for coastal states to adopt sensible risk mitigation and avoidance policies by creating mechanisms for spreading coastal zone catastrophe risk to insurance policyholders and taxpayers in other states.

Consider North Carolina, whose legislature and insurance commissioner worked together in 2009 to reform the state's troubled disaster insurance facility known as the "Beach Plan." A new law enacted in 2009 caps the insurance industry's non-recoupable assessment level for losses incurred by the Beach Plan at $1 billion, and lowers the plan's coverage limit from $1.5 million to $750,000.

Having the HDA in place would have discouraged these needed reforms. Under the HDA, bonds issued by the Beach Plan would be guaranteed by the federal government, and the plan would be eligible to participate in a new $200 billion federal reinsurance program. The discipline that state officials needed to enact the necessary reforms of the Beach Plan would have evaporated with the HDA's promise of a federal bailout.

If Congress enacts the HDA in 2010, the same dynamic will work to halt or even reverse the limited progress that other coastal states are making in better managing their catastrophe risk exposures. Indeed, the HDA would create a powerful incentive for coastal states that currently lack state-sponsored disaster insurance programs to create such mechanisms, potentially leading to a proliferation of state programs that artificially mask risk at the expense of federal taxpayers and insurance policyholders in states without such programs. Does the federal government and taxpayers in general, really want to be liable for paying huge sums of money for the failures of disaster-prone states to address their own problems?

The Commission Approach

The complexity associated with the issue of disaster-related legislation does not lend itself to a quick political fix. NAMIC supports a more measured approach through the creation of a commission to study the various facets of catastrophe risk management.

A number of proposals have been introduced in Congress aimed to reduce America's vulnerability to natural disasters. While some proposals have merit, each would benefit from the kind of rigorous, objective study that only an impartial commission of experts could provide. Moreover, there may be promising natural catastrophe-related measures that the federal government could undertake that have not yet been identified by Congress.

The commission approach would allow the development of a full menu of policy options that Congress could pursue and would bring together experts on catastrophe-related issues who would be given adequate time to study the issues in-depth and hold public hearings around the country to gather information from a host of constituencies affected by natural disasters.

Furthermore, several independent research organizations are currently engaged in major research projects whose purpose is to gather and analyze relevant data to allow policymakers to make informed decisions on these issues. Rather than rushing to vote on currently pending catastrophe bills, Congress should tap the growing body of knowledge and expertise that is available.

NAMIC is not seeking to be dilatory, just responsible. With all the work that has been done already in the private sector and that is in process, NAMIC believes a commission would probably only need nine-12 months to propose the best possible solutions. That time frame would leave ample time for the Congress to act swiftly.

We encourage the Congress to follow the measured approach of establishing a commission with a deadline that would facilitate prompt congressional action. NAMIC stands ready to work with Congress on such an approach and believes this would produce the best possible combination of private and public sector efforts to minimize the costs of addressing natural catastrophe risks for people who live in catastrophe-prone areas, for the states, and for the federal government and taxpayers.

Taking the Affordability Problem Seriously: A Different Approach

Last year, 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. As stated in the book, 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. We agree with the recommendation that 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.

This should not be all that difficult. 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, 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.
There is no reason why Congress could not 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.

Conclusion

The problems that natural catastrophes pose for the property/casualty insurance industry are not insoluble. The work that an impartial commission could do to bring needed clarity to some of these issues would surely benefit this discussion. We recommend that the next step be the creation of such a commission.

NAMIC believes that the surest way to increase the supply of insurance in catastrophe-prone coastal regions is to remove government restrictions on pricing and underwriting, immediately making the market attractive for new entrants. Also, the best approach to the affordability issue is through direct governmental subsidies to needy individuals and businesses as described above. Such an approach would increase insurance availability without distorting the insurance mechanism that sends valuable signals as to the relative level of risk of living in a certain area.

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March 9, 2010

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

Honorable Spencer Bachus
Ranking Minority Member
House Committee on Financial Services
B371A Rayburn House Office Building
Washington, DC 20515

Dear Chairman Frank and Ranking Member Bachus:

On Wednesday, March 10, 2010, the House Financial Services Subcommittees on Capital Markets and Housing will hold a hearing on the Homeowners Defense Act, H.R. 2555. While the National Association of Mutual Insurance Companies (NAMIC) is encouraged that Members of Congress are working to develop a comprehensive natural disaster plan to address concerns about coastal insurance affordability and availability, we are concerned that this legislation would expand the federal government's role to a point that the private insurance market could be crowded out. The result would likely be to encourage unwise residential and commercial development in high-risk coastal regions, such as the Atlantic and Gulf coasts of Florida.

The high costs of recent natural disasters combined with credible projections of future catastrophes have led to restricted homeowners' insurance coverage, reduced availability, and affordability issues in disaster-prone regions. The Homeowners Defense Act attempts to address these issues, but NAMIC believes it fails in this attempt. We believe it would instead artificially and unnecessarily alter private insurance markets and create a federal backing that would place taxpayers at risk for paying catastrophe losses through an implicit federal guarantee, thereby potentially adding billions of dollars to the federal deficit.

NAMIC strongly believes that we should build on the incentives to avoid and mitigate risk that the private sector provides through supply, demand, and price. A variety of other approaches would establish a proper balance between the roles of the private insurance sector and governments. This end result can be accomplished through sending proper signals to discourage development and/or mitigate its effects in dangerous areas and also by addressing affordability issues for low-income people already living in areas prone to natural disasters.

In sum, this legislation would create a permanent federal role in the private insurance markets that would be detrimental to people living in catastrophe-prone areas. NAMIC opposes this approach. We urge you to oppose the Homeowners Defense Act in the upcoming hearing and subsequent markup and, instead, support proposals that would couple private sector signals with government incentives to encourage proper uses of catastrophe-prone lands.

Sincerely,

Jimi Grande
National Association of Mutual Insurance Companies
Senior Vice President, Federal and Political Affairs

cc: Members of the House Financial Services Committee

Homeowners' Defense Act
Myths vs. Realities

MYTH. The Homeowners' Defense Act will help all states that face natural disasters.

FACT. **The Homeowners' Defense Act will actually hurt taxpayers in most states to benefit only those in a handful of states.** Currently, only Florida and California would benefit from the guarantees contained in the bill. In fact, under the bill, by reinsuring underfunded state insurance funds in California and Florida, taxpayers across the country would be on the hook for billions of dollars in insurance losses. Most Americans would lose financially under this bill.

MYTH. The Federal government already pays for natural disaster losses.

FACT. **The Federal government does not currently pay for the costs transferred to taxpayers under this bill.** After disasters, insurance payments and federal allocations have different purposes. The bulk of federal spending covers emergency response, public infrastructure, aid to local governments and cleanup. In contrast, insurance payments are used for home replacement and repair. A comparison of FEMA and private market insurance payments for U.S. hurricanes from 1994 through 2006 shows insurers paid out more than $100 billion while FEMA paid a little more than $16.3 billion to individuals. Under this bill, the Federal government would still pay all clean up, temporary assistance, and repair of public infrastructure, as well as insurance claims.

MYTH. This bill will lower people's insurance costs.

FACT. **There is absolutely nothing in this bill to ensure that homeowners' insurance costs will decrease** or that insurance will be more readily available. In fact, in the state of Florida, homeowners insured by the state are paying 40 – 60% of actuarial rates. Lowering the premiums any further would substantially increase the costs of this bill on the American taxpayer. Under Florida's current system, many consumers pay artificially low, subsidized premiums regardless of their income. All policyholders, including charities, school districts, low-income car owners and businesses are taxed on their insurance policies to subsidize coastal properties insured by the state fund. This bill would perpetuate this problem by making all US taxpayers, regardless of income, subsidize insurance for Florida's coastal residents.

MYTH. This bill will help low-income families.

FACT. **This bill requires low and moderate income taxpayers countrywide to subsidize the homes of wealthier coastal residents.** There are absolutely no income level or home value restrictions on who receives subsidies under the bill and the Florida system provides deep subsidies to those that own homes up to $2 million, including vacation and second homes. Sen. Al Lawson, D-Tallahassee, criticizes the Florida insurance program that HR 2555 would guarantee and reinsure, saying "You're robbing from the poor to take care of the rich…to subsidize these million-dollar homes built on the coast." While lower income residents may also receive some subsidies, the largest subsidies go to wealthier homeowners. A Florida State University study found that "policyholders closer to the coast are paying relatively less for insurance than those further inland." The Homeowners' Defense Act establishes a regressive tax where Americans of all income levels are forced to pay for these subsidized insurance policies.

MYTH. The cost of this bill is minimal.

FACT. **Under the Homeowners' Defense Act, American taxpayers could be on the hook for hundreds of billions of dollars.** Independent research shows that the federal reinsurance in this bill could cost over $200 billion—CBO has not scored that portion of the bill. Though CBO has said that the guarantee program has a minimal cost, under budget scoring rules, they must assume the guarantees will be paid back. Budget rules in this case mask reality. Like the National Flood Insurance Program (NFIP), which is $19 billion in debt as a result of deep subsidies and lack of reserves, Florida's program provides deep subsidies, has insufficient reserves, and fails to charge premiums for catastrophic events. Under this bill, the Federal government would guarantee state insurance programs like it does for the debt of the NFIP.

MYTH. This bill is the only solution to Florida's problem.

FACT. **Florida can take concrete steps to put its insurance program on the path to solvency without seeking a taxpayer bailout.** Florida's state Catastrophe Fund does not buy private reinsurance and, instead, plans the largest municipal bond issue in U.S. history if it runs out of money. The Cat Fund currently has $8 billion in claims payment ability and a potential liability of $28 billion. Capital exists in the private market to easily cover this gap. In fact, international reinsurers have announced at least $15 billion in planned 2010 share repurchases because they have capital they cannot deploy effectively. Likewise, Citizens subsidizes the homes of the wealthy. Florida could limit subsidies in its program to those who have affordability issues and could require its catastrophe fund to purchase private reinsurance.

MYTH. The bill does not incentivize development in environmentally sensitive areas.

FACT. **If this bill is passed, Florida will continue to further lower insurance rates, creating a false sense of security, and helping to encourage development and re-development of sensitive coastal areas and wetlands.** HR 2555 would undermine market signals to developers of properties in high risk areas including barrier islands, in floodplains, and on the coast. Like the NFIP, which the courts have determined enables development in threatened and endangered species habitats, HR 2555 would promote development in environmentally sensitive areas by subsidizing insurance rates through federal guarantees and reinsurance. The Intergovernmental Panel on Climate Change projects that sea level will rise 7 to 23 inches by 2100, yet many states including Florida do not yet take into account sea level rise in their coastal management and coastal development policies. HR 2555 does nothing to change this or to otherwise ensure wise land-use planning that better protects people and the environment

MYTH. There are strong mitigation provisions in the bill.

FACT. **The Homeowners' Defense Act contains much weaker mitigation provisions than other legislation that would help to strengthen homes in at-risk areas.** Though HR 2555 contains some funding for strengthening homes, it is dwarfed by the amount of money that will be spent to help people develop in sensitive areas through subsidized insurance rates.

MYTH: The states seeking federal guarantees financially support their own insurance funds.

FACT. **Neither Florida nor California guarantee, provide their own full faith and credit or financially back their state insurance funds** although they are asking Federal taxpayers to do so.

MYTH: The guarantees provided have precedence as the Federal government guarantees municipal bonds.

FACT: **The $400 billion per year muni bond market has no Federal guarantees.** HR 2555 would provide guarantees for state insurance funds thus providing preferences over bonds of states and cities, school districts, hospitals, universities, and all other government and quasi-government entities.

NAMIC Federal Issue Brief

FLOOD INSURANCE

The National Flood Insurance Program (NFIP) is currently financially unsustainable, and requires significant reforms in order to continue providing flood protection to homeowners and businesses alike.

NAMIC SUPPORTS a long term extension with common sense reforms for the program, such as the phasing-out of subsidies for pre-FIRM structures, the phasing-in of actuarially sound rates for non-residential properties and non-primary residences, and the updating of floodplain maps.

NAMIC STRONGLY OPPOSES the addition of windstorm coverage to the NFIP, which would significantly increase the program's costs and liabilities at the expense of a competitive private market.

BACKGROUND

In the aftermath of Hurricane Katrina and other storms in 2005, the NFIP incurred over $20 billion in debt to the Treasury. As it currently is constituted, the program will never be able to repay the debt. If Congress does not reform and reauthorize the program, its long-term solvency is at risk.

NAMIC has worked with members of Congress to bring attention to the bipartisan legislation of the 110th Congress that would have provided meaningful reforms to the NFIP. Among the key reforms included in the proposal that NAMIC supported are:

- Updates of flood maps and elevation standards to include mapping of the 500-year flood plain for future use.
- Phase-in of actuarial rates for non-residential properties and non-primary residences.
- Increased penalties on financial institutions that do not control customer compliance with mandatory coverage.
- Provide additional money for mitigation programs.
- Maximum coverage limits would be increased to $335,000 for structure, $670,000 for non-residential structure, and $135,000 for contents.
- Placing the program on a sound financial footing by eliminating the NFIP debt.

In 2007, Representative Maxine Waters, D-Calif., introduced legislation (H.R. 3121) that would raise the borrowing authority of the NFIP while also reforming the program. This bipartisan legislation was strongly supported by the insurance industry and was almost

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identical to legislation passed by the House of Representatives in 2006. The legislation had enjoyed significant bipartisan support with almost no controversy until a highly controversial proposal by Rep. Gene Taylor, D-Miss., to add wind coverage to the NFIP was included as part of the bill. H.R. 3121 passed the House of Representatives in September 2007.

In October 2007, the Senate Banking Committee marked up a separate version of flood reform legislation, which NAMIC strongly supported. S. 2284, the Flood Insurance Reform and Modernization Act of 2007, similar to the House bill, contained many of the same significant reforms. Additionally, the Senate bill, unlike the House bill, included a provision that would forgive the NFIP's more than $18 billion debt that had been incurred at the time. By eliminating this debt, the NFIP would be in a healthier financial situation. Currently, the NFIP pays about $900 million a year to the Treasury in the form of interest.

Unable to come to an agreement, the two chambers have instead passed a series of short term extensions, often for no more than a few months at a time, and have not yet taken up the issue. In December of 2009, the program was allowed to expire for roughly nine hours when an extension failed to win approval for before the deadline. And again in February 2010, the program was allowed to expire for nearly 2 days before Congress temporarily extended the program.

In the 111th Congress, no NFIP reauthorization and reform legislation has been introduced. However, Rep. Gene Taylor, D-Miss., has introduced H.R. 1264, the Multiple Peril Insurance Act, stand-alone legislation to include wind coverage as part of the NFIP. NAMIC strongly opposes this legislation.

Congress created the NFIP in 1968 to address the increasing costs of taxpayer-funded disaster relief for flood victims and the increasing amount of damage caused by floods. With private insurers unable to underwrite the risk of massive floods, it became clear that a federal program's creation was essential. The program was designed so that the premium dollars taken in every year are used to pay out any flood losses incurred by policyholders. More than 90 percent of all flood policies are written through Write Your Own (WYO) carriers. The WYO Program allows participating property/casualty insurance companies to write and service the Standard Flood Insurance Policy. The companies receive an expense allowance for policies written and claims processed while the federal government retains responsibility for underwriting losses.

While the program was designed so that the premium dollars collected are used to pay flood losses incurred by policyholders, the flood losses have been so great in recent years that the program is currently $20 billion in debt.

CONTACT INFORMATION

For more information please contact Kathy Mitchell, federal affairs director, at (202) 580-6744 or kmitchell@namic.org.

April 9, 2010

The Honorable Harry Reid
The Honorable Mitch McConnell

The Honorable Nancy Pelosi
The Honorable John Boehner

Dear Leadership:

On behalf of the undersigned associations, we are writing to respectfully underscore the importance of a reauthorization of the National Flood Insurance Program (NFIP) as the current program expired on March 28, 2010. Moreover, it is critical that such reauthorization is retroactive to address the gap in protection resulting from the hiatus. Failure to reauthorize the NFIP expeditiously when Congress returns will severely harm real estate markets, putting consumers at risk of uninsured losses and potentially putting additional tax money at risk to cover relief efforts.

Five and a half million taxpayers depend on the NFIP as their main source of protection against flooding, the most common natural disaster in the United States. Without quick retroactive reauthorization of the NFIP, residential and commercial real estate transactions in flood zones across the country will be further adversely impacted, as federally-backed mortgage loans cannot be secured without this critical protection.

If Congress fails to reauthorize the NFIP, it will still be paying for post-disaster relief for flood victims, yet it will be unable to collect premiums for renewing current flood insurance policies, which amounts to $2.85 billion annually. Devastating storms in the northeast underscore the need for Congressional action to reauthorize the NFIP immediately.

We also urge Congress to consider a long-term extension. This is the second time in recent months in which Americans have not been able to count on the NFIP because the program's authorization has been allowed to lapse.

The NFIP is critically important to Americans and the U.S. economy. We urge Congressional action now to reauthorize this program and avoid the costly consequences that would result from a failure to do so.

Respectfully,

American Insurance Association
National Association of Mutual Insurance Companies
Property Casualty Insurers Association of America
The Financial Services Roundtable
Independent Insurance Agents and Brokers of America
Mortgage Bankers of America
National Association of Realtors
National Association of Home Builders

Secretary
U.S. Department of Homeland Security
Washington, DC 20528

Homeland Security

April 24, 2009

The Honorable Barney Frank
Chairman
Committee on Financial Services
U.S. House of Representatives
Washington, DC 20510

Dear Chairman Frank:

This letter provides the Administration's views on reauthorization of the National Flood Insurance Program (NFIP). During the 110th Congress, the House of Representatives passed H.R. 3121, the *Flood Insurance Reform and Modernization Act of 2007*. The Senate amended that bill with a complete substitute. A conference on the competing versions did not take place, and Congress ultimately authorized a seven-month extension of the program until March 6, 2009 (Public Law 110-329). Since then, the program has been reauthorized through September 30, 2009 by the *Omnibus Appropriations Act of 2009* (Public Law 111-8).

The Administration supports meaningful reforms to the NFIP and reauthorization of the NFIP through Fiscal Year 2014. The Administration strongly believes that any legislative measures aimed at reforming the NFIP must address the debt incurred from Hurricanes Katrina, Rita, and Wilma in 2005. The Administration has serious concerns with provisions in the bills passed last year that mandate Federal Emergency Management Agency (FEMA) participation in state-sponsored mediation programs, the establishment of an unnecessary flood insurance advocate, as well as the additional provision for multiple-peril insurance contained in the House bill. These concerns are discussed in detail below.

The Administration supports the following elements, which were contained in the Senate and House bills:

- Phase-in actuarial rates for nonresidential properties, non-primary residences, and repetitive loss properties;
- Raise the cap on chargeable annual increases in premiums from 10 percent to 15 percent;
- Authorize an ongoing program to review, update, and maintain flood insurance program maps; and
- Reestablish the Technical Mapping Advisory Council, the duties of which would include developing recommendations for improvements to the flood mapping program.

NFIP Debt Forgiveness

The Administration strongly supports forgiveness of the current debt resulting from the 2005 hurricane season. As of January 31, 2009, the NFIP had incurred a debt of $19.2 billion. The National Flood Insurance Fund (NFIF) has and continues to make interest payments from both premium and borrowed funds and, as indicated in previous testimony before the Senate Banking, Housing, and Urban Affairs Committee and House Financial Services Committee, it is unlikely that the NFIP will ever be able to retire this debt. The debt load has had a significant impact on NFIP financial operations. Had the program not been obligated to make interest payments, the NFIP could have covered all losses from events subsequent to the 2005 hurricanes, including the 2008 floods and hurricanes, without having to borrow the $1.68 billion to pay losses from these events. The result is that the program has had to borrow more to pay interest on the debt, further compounding the situation.

As originally conceived, the NFIP was the means to encourage communities and citizens to understand their risk from flooding and mitigate against future flood damage. Congress provided the incentives to do this by encouraging community participation, discounting premiums for Pre-FIRM structures (structures built prior to the issuance of Flood Insurance Rate Maps), mandating the purchase of flood insurance in Special Flood Hazard Areas, and authorizing grant programs to mitigate repetitively damaged structures. The NFIP's flood risk identification and floodplain management land use and building standards will have reduced the costs and consequences of flooding by a conservative estimate of $16.3 billion from 2000 through 2010. This amount does not include the considerable savings achieved as a result of the program prior to 2000. It would be difficult to comprehend how enormous the costs of flooding would be for all levels of government and citizens if these standards were not in place.

The NFIP's financial position is similar to the Nation's financial position, by which its obligations exceed its income. This can be dealt with in a systematic way through debt forgiveness or the debt can continue to grow until all of the NFIP's income must be used to service the debt. The Administration is asking for debt forgiveness because the size of the current debt creates an unstable financial situation for the NFIP and the subsidized insurance premium structure does not and will not allow the NFIP to collect enough to service the debt or repay it. Without continuing to borrow to service the debt, the NFIP cannot pay the expenses of operating the insurance program, fund map modernization efforts, or support flood mitigation programs.

Because Congress chose to provide a subsidy to Pre-FIRM structures, the NFIP's premium rates are by statutory definition inadequate. Over the long term, the Program should expect to need to borrow from the Treasury from time to time. Those times would generally occur after major catastrophic flooding events such as Hurricane Katrina. While those incurred debts could possibly be repaid during periods of moderate flooding activity, such as the period from 1985 to 2004, such periods should be expected to be temporary. Once the debt has reached a very high level—such as the current debt of close to $20 billion—there is no realistic prospect that the NFIP could ever repay it.

Should debt forgiveness be included in any legislation reauthorizing the NFIP, an appropriation should be made to FEMA in the amount of the current market value of the loans to be forgiven, which would then be transferred to the U.S. Department of the Treasury. This transaction would make the cost of the debt forgiveness transparent and will ensure that this cost is properly accounted for by FEMA. This would have no budget scoring impact because it would simply be an intra-governmental transfer.

If the debt were forgiven, the Administration would propose tying future borrowing authority to insurance exposure, so the Program's authority to borrow would be related to its contingent liabilities, not to the arbitrary amount that was included in the original legislation. The Administration supports indexing the borrowing authority cap to 0.5 percent of the total amount of NFIP insurance-in-force at the prior fiscal year's end. This formula would result in a current borrowing authority cap of about $5 billion based on the approximately $1 trillion of insurance-in-force. This suggested percentage is based on our review of expected losses during a period of increased hurricane activity and would provide a sufficient borrowing margin so that requests for increases in the cap should rarely be needed, while still allowing a reasonable opportunity for the NFIP to retire any incurred debt up to that level. The Senate version of the reform bill that was before the last Congress contained a provision that restored the borrowing authority to $1.5 billion.

Participation in State Disaster Claims Mediation Programs

The Administration has significant constitutional concerns regarding provisions in the bills that would require FEMA claims adjustors to participate in state-sponsored mediation at the request of state insurance commissioners. The Constitution carefully allocates power among the branches of the Federal Government and between the states and the Federal Government, and it does not permit Congress to confer upon state officials the authority to compel agents and programs of the Federal Executive Branch to be subject to states' authority. Stated differently, this provision would violate constitutional principles, articulated by the Supreme Court, prohibiting Congress from delegating Federal executive power to individuals outside of the executive branch.

Flood Insurance Advocate

There are also constitutional concerns regarding the provision in the Senate bill that would require a "National Flood Insurance Advocate" to provide reports directly to Congress without any prior review by executive branch officials. By precluding review and approval by the FEMA Administrator, the Secretary of Homeland Security, and the Office of Management and Budget, the provision would interfere with the President's authority under Article II of the Constitution to supervise and control the internal operations and procedures of the Executive Branch (see *Myers v. United States*, 272 U.S. 52, 132-34 (1926)). Although the Senate bill did not prohibit contemporaneous review of the report by the President, this does not change the constitutional analysis. The constitutional concerns with this provision are heightened insofar as the National Flood Insurance Advocate's report may contain legislative recommendations. Moreover, to the extent that the powers and authorities given to the National Flood Insurance Advocate under the bill—most notably the authority to "enter into contracts" of various types with appropriated Federal funds—would entail the exercise of delegated sovereign authority, the provision for his or her appointment would conflict with the requirements of the Appointments Clause of the Constitution.

Additionally, this provision would add a new, expensive bureaucracy within FEMA, paid for directly from the NFIF without collecting offsetting revenues from policyholders and would be duplicative of processes already available to policyholders through the NFIP's formal appeals process as set forth in 44 C.F.R. § 62.20(f) and in the in the *NFIP Flood Insurance Claims Handbook.*

Multiperil Coverage for Flood and Windstorm

The Administration strongly opposes the provision in the House bill establishing insurance coverage for multiple perils. The Administration objects to this coverage for a number of reasons:

- Coverage is available in the private sector and through state wind pools. Property owners are served by the private market, which provides catastrophic windstorm coverage without the need for Federal aid. The Administration opposes extending the Federal Government's role and increasing its liability for an insurance program that is readily available in the private sector and through state insurance plans. Many carriers in Florida have told the state's insurance regulator that they would write the wind policies of insurers withdrawing from the state.
- Voluntary Federal wind coverage would create significant problems involving coordination of benefits and adversely affect competition and selection among the various public and private wind programs.
- Wind coverage would greatly increase the NFIP's exposure to catastrophic risks at a time when the program has a growing debt and accrued interest of over $19 billion;
- The legislation requires Federal wind insurance to be actuarially sound, as it should; hence, the insurance offered through a Federal program will not be less expensive than what is available in the private insurance market.
- The requirement to discontinue the multi-peril coverage whenever borrowing occurs could lead to shutting down the program.
- Unless communities adopt the international building codes without amendments, FEMA would be forced to review thousands of community building codes every three years and continuously monitor them to ensure compliance.
- Building codes and standards do not dictate land use and zoning requirements, which have always been reserved for states to decide what is appropriate. The term 'windstorm' includes any hurricane, tornado, cyclone, typhoon, or other wind event, yet American Society of Civil Engineers Minimum Design Loads for Buildings and Other Structures (ASCE 7-05), and the Nation's model building codes do not address tornadoes.

In summary, the Administration looks forward to working with Congress to reform and strengthen the NFIP for the benefit of policyholders and taxpayers. The Administration believes that any reform or reauthorization legislation should address the NFIP's debt and financing and avoid expanding the program to cover new non-flood-related areas. Any National Flood Insurance Program reform should include a phase-in of actuarial rates, subsidy reduction, an increase in the annual premium rate cap, authorization of a mapping program, and re-establishment of the Technical Mapping Advisory Council as core elements.

Thank you for the attention to the views in this letter. An identical letter has been sent to the Ranking Member of the House Committee on Financial Services, and the Chairman and Ranking Member of the Senate Committee on Banking, Housing, and Urban Affairs. Should you wish to discuss this matter further, please do not hesitate to contact me at (202) 282-8203.

Yours very truly,

Janet Napolitano

NAMIC Federal Issue Brief

BUILDING CODES

Stronger, safer buildings for Americans and their families during natural disasters can save lives, reduce property loss, and reduce public disaster aid.

NAMIC SUPPORTS Congressional action to encourage the adoption and enforcement of strong building codes. Legislation providing increased post-disaster aid for those states that have adopted and currently enforce nationally recognized, statewide building codes can serve as a powerful incentive to state and local governments.

BACKGROUND

The Louisiana State University Hurricane Center estimated that of the $10 billion in wind damage to homes in Louisiana as a result of Hurricane Katrina, modern building codes would have spared 80 percent of the damage. Standardized building codes and adequate enforcement of those codes play an increasingly important role in public safety and loss prevention, even in states that do not have a major natural disaster catastrophe exposure. In addition to saving lives and reducing property loss, statewide building codes based on nationally recognized standards can:

- reduce the need for public disaster aid
- promote a level and consistent playing field for design professionals, suppliers, and builders
- create a minimum standard upon which consumers can rely
- contribute to the durability of structures; and, in some locations, favorably affect the affordability and availability of insurance
- protect the environment from waste caused from rebuilding after disaster

Since there are such great benefits to implementing and enforcing building codes, it is critical to develop federal incentives, encouraging states to adopt appropriate statewide building codes. One such way to do this is by increasing the amount of post-disaster mitigation aid a state can receive following a natural disaster based upon whether that state has adopted stronger statewide building codes.

NAMIC formed the Building Code Coalition (BCC) to develop federal legislation that would provide this kind of incentive to states to create or better enforce statewide building codes. Under current law, FEMA provides federal assistance for mitigation efforts by the states under the provisions of the Robert T. Stafford Disaster Relief and Emergency Assistance Act. The amount of funding available is

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NAMIC
NATIONAL ASSOCIATION OF MUTUAL INSURANCE COMPANIES

EFFECTIVE ADVOCACY
STRATEGIC PUBLIC POLICY
VALUABLE MEMBER SERVICES

limited to 7.5 percent of the total disaster grant awarded the state by FEMA, as long as the state has a standard mitigation plan. However, if a state has an enhanced mitigation plan, it is currently eligible for 20 percent in post-disaster mitigation. NAMIC and the BCC support the creation of a separate financial incentive of 4 percent additional funds for states that have adopted and enforce statewide building codes. This approach would provide a new incentive for states to adopt statewide building codes. For those states that commonly experience natural disasters, this financial incentive could be very desirable. But for those states choosing not to adopt and enforce statewide building codes, no penalty or mandate would be in place.

During the 110th Congress, the BCC actively educated members of Congress and their staffs on a legislative proposal to provide federal incentives for states to pass statewide building codes, resulting in the introduction of legislation in October 2007. Reps. Doris Matsui, D-Calif., and Mario Diaz-Balart, R-Fla., introduced, H.R.3926, the Building Code State Incentive Act of 2007. The Building Code State Incentive Act was included as part of H.R. 6658, the Disaster Response, Recovery and Mitigation Enhancement Act of 2008, which was passed out of the House Transportation and Infrastructure Committee in July of 2008.

On May 21, 2009, Reps. Mario Diaz-Balart, R-Fla., and Michael Arcuri, D-N.Y., introduced H.R. 2592, The Building Code State Incentive Act. This legislation is almost identical to legislation introduced in the 110th Congress and would increase the amount of federal monies available to states that enact and enforce nationally recognized statewide building codes. Specifically, it would add 4 percent to the money a state would be eligible to receive under current disaster relief legislation.

The adoption of building code incentives is a common-sense approach that Congress can soon adopt. NAMIC looks forward to working with members of Congress to help shepherd this bill through the legislative process.

CONTACT INFORMATION

For more information please contact Kathy Mitchell, federal affairs director, at (202) 580-6744 or kmitchell@namic.org.

BUILDING CODE COALITION
Washington, DC

ALLSTATE INSURANCE COMPANY ▪ AMERICAN INSURANCE ASSOCIATION ▪ COUNCIL OF INSURANCE AGENTS AND BROKERS ▪ FARMERS INSURANCE GROUP OF COMPANIES
FEDERAL ALLIANCE FOR SAFE HOMES ▪ FINANCIAL SERVICES ROUNDTABLE ▪ INSTITUTE FOR BUSINESS AND HOME SAFETY ▪ INDEPENDENT INSURANCE AGENTS AND BROKERS OF AMERICA
INTERNATIONAL CODE COUNCIL ▪ LIBERTY MUTUAL INSURANCE ▪ METLIFE ▪ NATIONAL ASSOCIATION OF MUTUAL INSURANCE COMPANIES
NATIONAL FIRE PROTECTION ASSOCIATION ▪ NATIONAL READY MIXED CONCRETE ASSOCIATION ▪ NATIONWIDE INSURANCE ▪ NEIGHBORWORKS AMERICA ▪ PROFESSIONAL INSURANCE AGENTS
PROPERTY CASUALTY INSURERS ASSOCIATION OF AMERICA ▪ REINSURANCE ASSOCIATION OF AMERICA ▪ SIMPSON STRONG-TIE CO
SOLUTIA ▪ ST. PAUL TRAVELERS ▪ STATE FARM INSURANCE COMPANIES ▪ THE HARTFORD ▪ USAA

November 5, 2009

The Honorable Nancy Pelosi
Speaker of the House
H-232, US Capitol
Washington, D.C. 20515

The Honorable Steny Hoyer
House Majority Leader
H-107, US Capitol
Washington, D.C. 20515

Speaker Pelosi and Majority Leader Hoyer:

The Building Code Coalition (BCC) was created to encourage and incentivize the adoption and enforcement of statewide building codes. As members of this coalition, we are encouraged by recent actions of the House Transportation and Infrastructure Committee and urge timely consideration of H.R. 3377, the *Disaster Response, Recovery, and Mitigation Enhancement Act of 2009*, by the House of Representatives. This legislation strengthens our nation's ability to prepare and respond to major natural disasters.

The BCC is particularly encouraged to see the inclusion of H.R. 2592, the *Safe Building Code Incentive Act*, in H.R. 3377. This specific provision encourages states to adopt and enforce nationally recognized model building codes for residential and commercial structures, allowing states to qualify for an additional four percent of funding available for grants, post-disaster.

The benefits of building codes are well-documented. According to the Louisiana State University Hurricane Center, up to 80 percent of the approximately $10 billion in wind damages to homes and contents in Louisiana as a result of Hurricane Katrina could have been avoided with modern building codes. In addition, a 2005 National Institute of Building Sciences study concluded that for every one dollar spent on mitigation at the federal level, the American taxpayer saves four dollars in disaster assistance. Given these facts, it is imperative that we create an environment that encourages the use of sound, practical building codes to mitigate the damages and prevent losses caused by natural disasters.

BCC members have seen first-hand the benefits of strong building codes and the damages, both personal and property, that can be avoided through the utilization of strong building codes. Given our experience, we applaud Chairman Oberstar, Congressman Arcuri, and Congressman Diaz-Balart's efforts to see the *Safe Building Code Incentive Act* introduced and included in H.R.3377, which unanimously passed out of the House Transportation and Infrastructure Committee on November 5, 2009.

We, as a coalition, stand behind this effort and look forward to working with you on the passage of this legislation in the House.

Sincerely,

Allstate Insurance Company

American Insurance Association (AIA)

Council of Insurance Agents and Brokers (CIAB)

Farmers Insurance Group of Companies

Federal Alliance for Safe Homes (FLASH)

Financial Services Roundtable (FSR)

Institute for Business and Home Safety (IBHS)

Independent Insurance Agents and Brokers of America (IIABA)

International Code Council

Liberty Mutual Insurance

MetLife

National Association of Mutual Insurance Companies (NAMIC)

National Fire Protection Association

National Ready Mixed Concrete Association

Nationwide Insurance

NeighborWorks America

Professional Insurance Agents (PIA)

Property Casualty Insurers Association of America (PCIAA)

Reinsurance Association of America

Simpson Strong-Tie Co

Solutia

St. Paul Travelers

State Farm Insurance Companies

The Hartford

USAA

BUILDING CODE COALITION

Washington, DC

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FEDERAL ALLIANCE FOR SAFE HOMES ▪ FINANCIAL SERVICES ROUNDTABLE ▪ INSTITUTE FOR BUSINESS AND HOME SAFETY ▪ INDEPENDENT INSURANCE AGENTS AND BROKERS OF AMERICA
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Allstate Insurance Company

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National Fire Protection Association

National Ready Mixed Concrete Association

Nationwide Insurance

NeighborWorks America

Professional Insurance Agents (PIA)

Property Casualty Insurers Association of America (PCIAA)

Reinsurance Association of America

Simpson Strong-Tie Co

Solutia

St. Paul Travelers

State Farm Insurance Companies

The Hartford

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Promoting Safety and Protecting Property

BUILDING CODE COALITION
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BUILDING CODE LEGISLATION--FAST FACTS

Overview

- Model building codes govern all aspects of construction and help to protect homes and buildings from hurricanes, tornadoes, earthquakes, floods, fire, ice storms and other natural catastrophes.
- A uniform statewide adoption and enforcement of model building codes by states will help to eliminate long-term risks affecting people, property, the environment, and ultimately the economy.
- With billions of dollars paid by the federal government and the private sector for disaster relief and rebuilding communities, legislation would enhance the Federal Emergency Management Agency's (FEMA) goal of making sure our cities and towns are better equipped to "prepare for, prevent, respond to and recover from disasters."
- 2005 National Institute of Building Sciences' study concluded for every $1 spent on mitigation at the federal level, the American taxpayer saves $4 in diaster assistance.

Legislative History

- In the 110th Congress, H.R. 3926, the "Safe Building Code Incentive Act of 2007," was introduced and was included as part of H.R. 6658, the Disaster Response, Recovery and Mitigation Enhancement Act of 2008, which was passed out of the House Transportation and Infrastructure Committee in July of 2008.

House Action—111th Congress

- H.R. 2592, the "Safe Building Code Incentive Act of 2009," May 21, 2009
- Sponsored by Representatives Mario Diaz-Balart (R-FL) and Mike Arcuri (D-NY)
- Introduced with 6 original co-sponsors and referred to the House Transportation and Infrastructure Subcommittee on Economic Development, Public Buildings, and Emergency Management
- Would amend the Stafford Act to enhance existing mitigation programs by encouraging states to adopt and enforce nationally recognized model building codes for residential and commercial structures to qualify for an additional 4 percent of funding available for grants, post-disaster.
- Administered by FEMA
- Included as part of HR 3377, the Disaster Response, Recovery, and Mitigation Enhancement Act, introduced by Chairman Oberstar (D-MN), which passed unanimously out of the Transportation and Infrastructure Committee on November 5, 2009

NAMIC Federal Issue Brief

CREDIT BASED INSURANCE SCORING

Credit-based insurance scores are a proven predictor of loss without a discriminatory effect - and the barring or limiting of their use by insurers would harm consumers.

NAMIC OPPOSES any attempt to restrict or prohibit the use of credit-based insurance scoring, which would deprive insurers of the use of a statistically proven underwriting tool and result in higher premiums for consumers.

BACKGROUND

Credit-based insurance scoring has been repeatedly proven to be a strong predictor of insurance loss that better enables companies to underwrite and rate their business – and provide their customers with the best rates available.

Consumers benefit from insurance scoring because it keeps the insurance marketplace competitive – which results in lower prices, better service, and more product choices. Insurance scores are used with other information to better predict the likelihood of future claims and the cost of those claims.

Importantly, insurance scores are not credit scores. Credit scores predict the likelihood that an individual will default or be delinquent in paying back an extension of credit. An insurance score predicts the likely "loss ratio relativity" of an individual. A loss ratio is the amount paid out by an insurance company in claims divided by the amount collected in premiums – thereby predicting whether an individual will experience more or fewer losses than average.

Insurance scores are only one of more than two dozen factors that are used by insurers to make an underwriting or rating decision about an individual. Other factors typically include an individual's motor vehicle report, claims history, or the condition of one's home.

In recent years states have begun enacting laws and regulations for insurers to follow in using an individual's credit information. In 2002, the National Conference of Insurance Legislators (NCOIL) created a "Model Act Regarding Use of Credit Information in Personal Insurance," which became the basis for additional legislation in other states. Today, 47 states have laws or regulations pertaining to credit-based insurance scoring.

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STRATEGIC PUBLIC POLICY
VALUABLE MEMBER SERVICES

In addition to state oversight, numerous studies have found that credit-based insurance scores have no discriminatory effect, either directly or by proxy, on consumers. Between 1996 and 2007, there have been 18 studies on the use of credit-based insurance scoring conducted by the Federal Trade Commission, the Federal Reserve Board, state regulators and others, and they have consistently found a strong relationship between an individual's credit score and incurred losses for both personal auto and homeowners policies without discriminatory effects. In fact, House Financial Services Committee Chairman Barney Frank, D-Mass., has recognized that credit-based insurance scoring has been statistically proven to be effective.

Currently, the FTC is in the process of conducting a comprehensive study on the impact that insurance scoring has on homeowners insurance premiums. NAMIC is confident the study will reach the same positive conclusions as the many others.

While no legislation restricting or prohibiting the use of this valuable underwriting tool has been introduced in the 111th Congress, on March 24, 2010, the House Subcommittee on Financial Institutions and Consumer Credit held a hearing examining the overall issue of credit scores during which insurance scores were discussed. A second hearing focusing specifically on insurance scores will be held mid-May.

NAMIC continues to work with the administration, Members of Congress and their staffs to highlight the benefits this important underwriting tool provides to both insurers and consumers alike.

CONTACT INFORMATION

For more information on please access our NAMIC Policy Briefing on credit-based insurance scores at http://www.namic.org/insbriefs/090306InsuranceScoring.pdf or contact Dylan Jones, federal affairs director, at (202) 580-6741 or djones@namic.org.

NAMIC Federal Issue Brief

TAXATION OF SMALL PROPERTY/CASUALTY COMPANIES

The investment income election for small property/casualty insurance companies (Internal Revenue Code Section 831(b)(2)) must be changed to reflect the inflationary impact since its enactment in 1986.

NAMIC SUPPORTS the expansion of Internal Revenue Code Section 831(b)(2) to reflect the inflationary impact since its enactment 24 years ago. Many small companies are approaching the current $1.2 million limit and both they and their customers will be adversely impacted if it is not raised and tied to an annual adjustment in the cost of living.

BACKGROUND

There are many small property/casualty insurers organized as mutual companies. These companies were originally formed to offer insurance coverage to specific groups, often in rural areas, that may not have otherwise been able to obtain affordable coverage. Many of these small mutual companies serve farming communities and rely on the tax benefit to provide additional surplus and cash flow so that all available financial resources can be used solely for paying claims.

Since the Tax Reform Act of 1986, Section 831(b) of the Internal Revenue Code has allowed property/casualty insurance companies with direct or net written annual premiums not exceeding $1.2 million to elect to be taxed on their net investment income.

However, this election level has not been adjusted since the Code went effect in 1986. For instance, what was once $1.2 million in 1986, after 24 years of inflation, would now be $2.028 million. Thus, while a company's annual costs have increased over the years with inflation, the investment income election level has not.

Because these small, mutual property/casualty insurance companies have such limited financial resources, all of their assets must be preserved for claims paying to ensure their important niche market is protected. Providing these small insurers with this tax election accomplishes that goal.

In the 111th Congress, Reps. Earl Pomeroy, D-N.D., and Paul Ryan, R-Wisc., introduced H.R. 3301. The legislation would increase Section 831(b) investment

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income election under the Internal Revenue Code from the current $1.2 million to $2.025 million with an annual cost-of-living index for future years.

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