NATURAL DISASTER PROTECTION LEGISLATION: A LEGISLATIVE ANALYSIS

JANUARY 1995

PREPARED BY:

EARTH TECH
1420 King Street, Suite 600
Alexandria, Virginia 22314

PREPARED FOR:

THE NATIONAL ASSOCIATION OF REALTORS
700 Eleventh Street, N.W.
Washington, D.C. 20001-4507

Executive Summary

A succession of recent natural disasters, including Hurricanes Andrew and Iniki, and the Northridge earthquake in California, has resulted in record levels of property damage, insured property losses, and Federal disaster assistance. Hurricane Andrew and the Northridge earthquake resulted in over $16.5 billion and $7.2 billion of insured losses, and each resulted in nearly $30 billion in total damages. Disaster assistance for Hurricane Andrew was in the $8 billion range; for the Northridge earthquake, the total was $8.5 billion. As a result of the insured losses, some insurance companies were forced into bankruptcy, and other companies pulled out of the most affected markets, limited coverage, or raised premiums or deductibles. In parts of California, Hawaii, Louisiana, Florida and other areas of the U.S. and the Virgin Islands, insurance availability or affordability became a problem, and, in some cases, housing markets were affected. Future disasters could be even costlier. For example, a seismic event as strong as the 1906 San Francisco earthquake could cause over $84 billion in damages.

Several bills were introduced in the 103rd Congress to address the potential impacts of such catastrophic disasters. All but one of these bills died before reaching full committee markup. H.R. 2873, the "Natural Disaster Protection Partnership Act", was reported out of the House Public Works and Transportation Committee on October 7, 1994, but was not considered by the full Congress due to other pressing priorities. In addition, a bipartisan House task force issued a report that incorporated some key elements of H.R. 2873, as well as other proposals to address the natural disaster issue.

The legislation and the Task Force report share certain key elements. These elements are 1) establishment of a private, nation-wide, all-hazard insurance program, 2) implementation of mitigation programs, including funding to state and local governments, tied to stricter enforcement of building codes and emergency plans, and 3) development of a reinsurance program to limit insurers' losses when major disasters occur.

Although the efforts mentioned above share broad bipartisan support, action in this area will likely not occur until later in the 104th Congress, and the legislation will probably be substantially modified. Critics have focused primarily on the reinsurance provisions of the existing legislation, but also on the difficulty of setting rates that reflect actual disaster risks, and in encouraging sufficient participation to ensure insurance affordability.

While the goal of increasing the availability and affordability of disaster insurance is one that is supported by the real estate industry, it is not yet clear what the impact of the legislative proposals will be in many areas, because details have neither been defined or addressed. It is recommended that the current efforts to develop legislation in this area be supported. However, there are several concerns that deserve further attention:

- The magnitude, complexity, and potential economic impact of the proposed program must be considered. The current proposals would establish a program much broader than the National Flood Insurance Program, which has been developed incrementally over the last 27 years. A natural disaster protection program needs to be extensively debated and carefully crafted because the potential impacts are so great.

- There has been no real analysis of the cost of some of the mandates in the proposals. Some elements and their associated costs need to be better defined as well as the associated costs. In particular:

    - ★ ***Multi-Hazard Building and Safety Codes.*** Adoption and enforcement of building and safety codes which meet or exceed existing model building codes can significantly increase home prices. Codes need to reflect local conditions and disaster risks, and be cost-effective, i.e., the costs are commensurate with the reduction in risk achieved. Development and enforcement of codes at the state, rather than local level, could result in application of codes that are not appropriate to site-specific conditions.

    - ★ ***Inspections and Licensing.*** H.R. 2873 would study the feasibility of training and licensing home inspectors for natural disaster mitigation. Home disaster inspections could also be required, and could likewise increase the costs and complexity of real estate transactions.

Other concerns also exist. They include:

- ***Relationship of Premiums to Risks Incurred.*** Premiums should reflect actual risks incurred. In other words, residents of Minnesota should not subsidize Californians for earthquake risk. Rates need to reflect actual risk faced by homeowners.

- ***Viability of the Primary Insurance Program.*** There is a question as to how many homeowners would participate in the program even with mandatory purchase requirements for Federally-backed loans. Improved affordability of insurance can only result if enough individuals participate.

- ***Reinsurance Provisions.*** Failure to limit Federal liability could expose the Federal government to large potential losses. This could ultimately impact interest rates and general economic well-being.

SECTION 1.0
PURPOSE AND METHODOLOGY

The purpose of this study is to discuss the status and provisions of various legislative proposals addressing catastrophic natural disaster response, and to analyze the potential impacts on the real estate industry. In addition, this study recommends strategies or positions that the real estate industry may wish to pursue during the legislative debate.

This section describes the purpose and methodology of this analysis.

Section 2.0 of this report discusses briefly the situation that generated the current legislative debate: the insurance availability and reinsurance problems created by a recent series of catastrophic natural disasters. The potential for even costlier future disasters is also discussed.

Section 3.0 presents a brief history of the various legislative proposals introduced during the 103rd Congress. Also discussed are the recommendations of a bipartisan task force on natural disasters and an interagency Administration task force.

Section 4.0 presents a section-by-section analysis of H.R. 2873, also known as the Mineta Bill, because Norman Mineta was the sponsor of the legislation. Included in this analysis is a discussion of the potential impacts of some of the key provisions on the real estate industry.

Section 5.0 identifies the political positions of the proponents and opponents of natural disaster legislation. Concerns and recommendations of these groups are discussed.

Section 6.0 discusses the legislative outlook for natural disaster legislation in the 104th Congress.

Section 7.0 discusses the conclusions of the analysis and recommendations for further action.

The information for this report was gathered from interviews with key individuals and published reports from the following organizations:

- The Senate Committee on Commerce, Science, and Transportation;
- The House Committee on Transportation and Public Works;
- Congressional staff for Senators Inouye and Pressler and Representatives Mineta, Shuster, Durbin and Emerson;
- The Bipartisan Task Force on Disasters;
- The Congressional Research Service;
- The General Accounting Office;
- The Congressional Budget Office;
- The Federal Emergency Management Agency;

- The Interagency Task Force on Natural Disasters;
- The Natural Disaster Coalition and the insurance industry;
- The National Association of Homebuilders;
- The Mortgage Bankers Association; and
- The National Association of Realtors.

SECTION 2.0

BACKGROUND: THE RISING COST OF NATURAL DISASTERS

The spur for Congressional activity on natural disaster legislation has been a series of recent devastating natural disasters, that have caused tens of billions of insured losses, and which have seriously stretched the capacity of insurance companies and the Federal government to respond. Prior to 1989, the U.S. had never experienced a natural disaster causing more than $1 billion in insured losses; in 1992 alone, insured losses totalled $23 billion and were greater than those of the seven previous years combined. Figure 2-1 depicts the rising cost of natural disasters in the U.S.[1]

The costliest of these disasters has been a series of major hurricanes and earthquakes that struck major populated areas from 1989 to 1994. In 1989, Hurricane Hugo struck the Virgin Islands and South Carolina, causing more than $4 billion in insured losses.[2] Shortly thereafter, a major earthquake struck the San Francisco area, resulting in widespread damage that helped raise total 1989 losses to $7.6 billion.[3] During 1992, Hurricane Andrew in Florida, and Hurricane Iniki in the Pacific contributed to the record $23 billion in insured losses for that year.[4] Hurricane Andrew alone resulted in $16.5 billion in insured losses, and $30 billion in total losses. Andrew cost 300,000 state residents their jobs, destroyed 8,000 businesses and ruined more than 32,000 acres of farmland.[5] Finally, in January 1994, the Northridge earthquake in Southern California caused losses that are now estimated to be almost $30 billion; the insured portion of that total was $7.2 billion.[6]

In addition to record insured losses, these events resulted in record levels of Federal disaster assistance to partially cover uninsured losses. In California, for example, only 25% of homeowners carry earthquake coverage. Over the past six years, special supplemental appropriations for disaster relief have totaled $34 billion, or nearly $300 for each individual

---

[1]Natural Disaster Coalition, Fact Sheet: "Important Facts About Natural Disasters."

[2]CQ Researcher, Congressional Quarterly, Inc., "Disaster Response: Does the Country Need a New Natural Strategy?" October 15, 1993, Volume 3, Number 38, page 891.

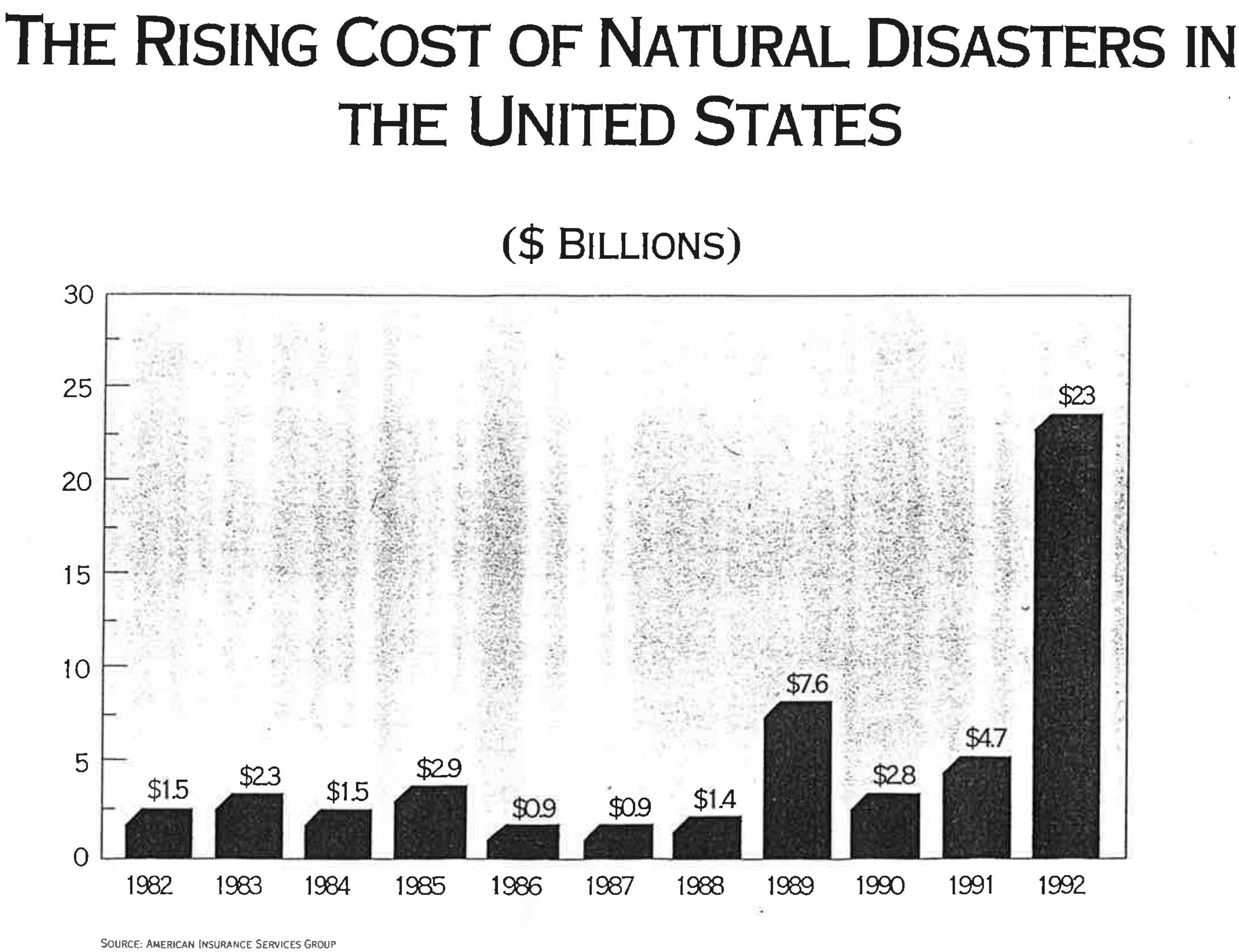
[3]Ibid.

[4]Rawle King, Insurance Markets After Hurricane Andrew, "Congressional Research Service, April 21, 1993.

[5]CQ Researcher, op. cit., page 902.

[6]The Journal of Commerce, "California Quake Loss Estimate Raised", August 5, 1994.

Figure 2-1 The Rising Cost of Natural Disasters in the United States



taxpayer.[7] Disaster assistance for Hurricanes Andrew and Iniki and Typhoon Omar was $11.1 billion; for the January 17, 1994 Northridge earthquake in California, the bill was $8.5 billion, making it the largest appropriation for a single disaster.[8] Federal disaster assistance, however, typically only covers a small portion of total losses suffered; in a worst case situation it may cover only up to $40,000 in losses.[9]

The record insured losses have created disruption in insurance markets, resulting in bankruptcy, limits on coverage or deductibles, hikes in premiums, or, in the worst case, inavailability of coverage. In the aftermath of Hurricane Hugo in the Virgin Islands, many insurers pulled out of the market. The limited coverage now available has increased substantially as have deductibles. The typical premium for a homeowners policy has risen from to a level five times that of pre-Hugo rates, and many first-time homeowners are being locked out of the housing market due to lack of coverage, and the resulting inability to secure mortgage financing.[10]

The stories were similar in the wake of Hurricane Iniki in Hawaii and Hurricane Andrew in Florida, and the Northridge earthquake in California. In Hawaii, it was estimated in 1993 that the "impairment of the Hawaii property insurance market is about 40%, causing hardships to many consumers. There are approximately 218,000 homeowners policies... of these, 70,700 are or will be non-renewed by the end of the year."[11] In Florida, high losses drove nine insurance companies into insolvency and forced dozens of property insurance companies to either withdraw from the Florida property insurance market or reduce their underwriting exposure by not renewing policies.[12] Nearly 900,000 Floridians were in danger of either losing their coverage or being forced to insure through the state's more expensive Joint Underwriting Association.[13] In California, the state's three largest insurers, and many smaller insurers stopped writing new homeowners coverage during 1994. Governor Pete Wilson acknowledged that the lack of insurance availability could dampen real estate sales and slow the state's economic recovery.[14]

---

[7] Jack Weber, Natural Disaster Coalition, Testimony before the House Committee on Public Works and Transportation. February 23, 1994.

[8] House of Representatives Committee on Public Works and Transportation, "Report on the Natural Disaster Partnership Act of 1994," Report 103-848, October 7, 1994.

[9] House of Representatives, Hearing before the Subcommittee on Water Resources and Environment of the Committee on Public Works and Transportation. February 23, 1994, page 57.

[10] Ibid., page 6.

[11] Linda Chu Takayama, Insurance Commissioner, State of Hawaii, letter to J. Robert Hunter, National Insurance Consumer Organization. March 19, 1993.

[12] Rawle King, op. cit.

[13] The CQ Researcher, op. cit., page 902.

[14] The Daily News, "Another Aftershock". July 5, 1994.

As bad as these disasters were, there is a potential, indeed a likelihood of even costlier catastrophes in the future. For example, if Andrew had struck only twenty miles further north, through the heart of Miami, it could have caused $50 billion in damages.[15] New meteorological data indicate that the East Coast is entering a cycle where intense hurricanes are likely to strike Florida and the East Coast more frequently. At the same time, the amount of insured property in Gulf and Atlantic coastal counties has increased 64 per cent over the level in 1980, to $1.86 trillion.[16]

The same is true for earthquake risk. The Northridge earthquake only registered a 6.7 on the Richter Scale; the San Francisco earthquake of 1906 was 200 times more powerful. A 1992 report by the U.S. Geological Survey predicts a 50% chance of severe earthquake on the West Coast within five years (the Northridge earthquake was only a moderate earthquake).[17] It has been estimated that a repetition of an event of the magnitude of the 1906 San Francisco earthquake would cause over $84 billion in damages.[18] In Memphis, Tennessee, where most homeowners are not even aware they face an earthquake risk, an earthquake as powerful as the 1811 New Madrid earthquake could cause nearly $70 billion in damages.[19] Figure 2-2 shows the probable cost of future natural disasters.

The rising toll of natural disasters, the drain on the Federal budget in terms of disaster relief, insurance availability and affordability problems, and the need for better mitigation and disaster response prompted the Congress to act. The next section describes the legislation that was drafted in the 103rd Congress to address these problems.

[15]CQ Researcher, op. cit., page 891.

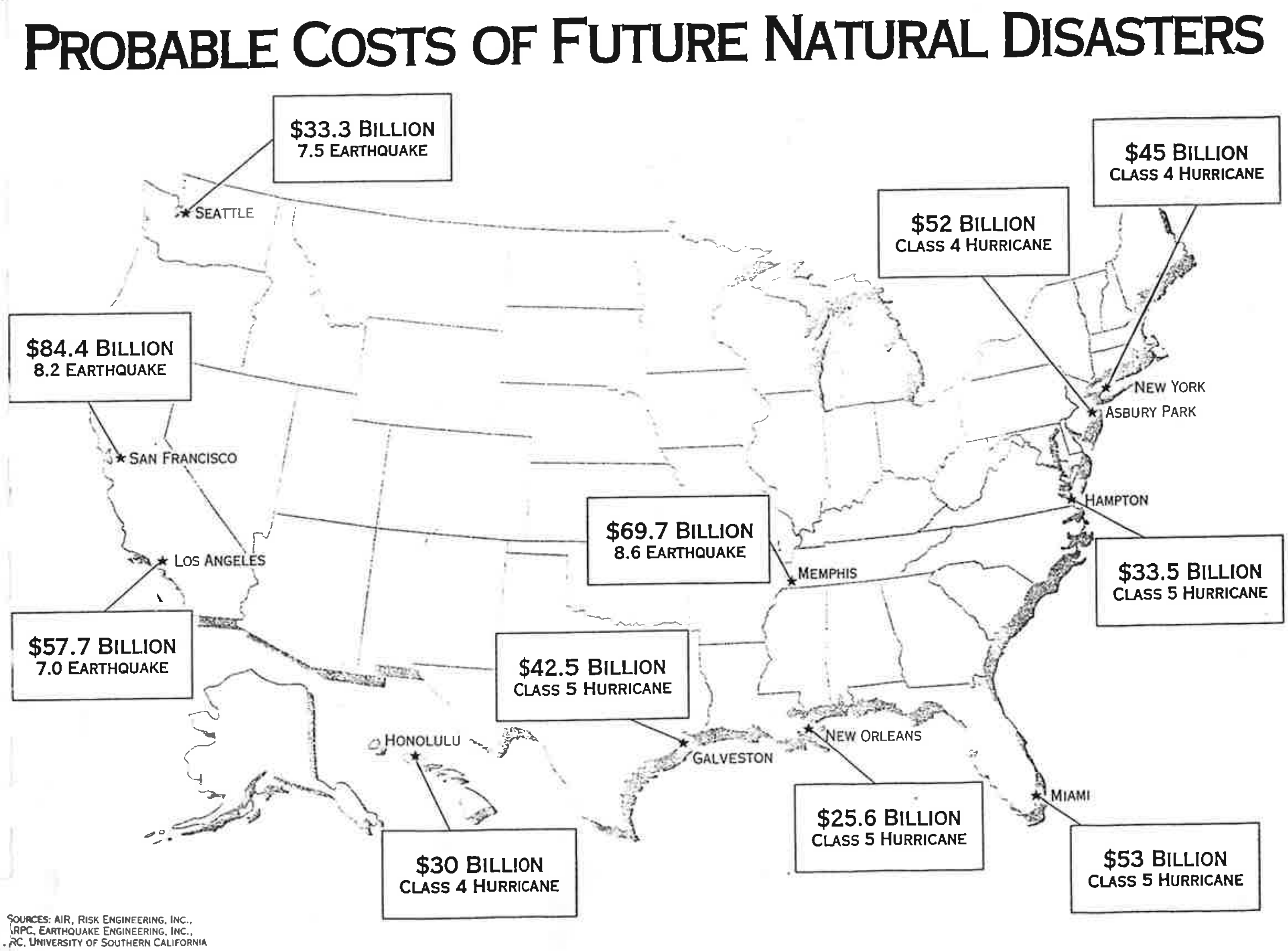
[16]Ibid.

[17]Natural Disaster Coalition, Fact Sheet.

[18]House of Representatives, Committee Report 103-848, op. cit.

[19]Ibid.

Figure 2-2 Probable Costs of Future Natural Disasters



SECTION 3.0
A HISTORY OF LEGISLATIVE ACTIVITY DURING THE 103RD CONGRESS

A number of bills were drafted during the 103rd Congress to address various aspects of natural disaster preparedness and response. In addition, a bipartisan Congressional Task Force on Natural Disasters issued a report shortly before Christmas 1994, and the Administration presented its comments on natural disaster legislation on January 5, 1995. These efforts are discussed in the sections that follow.

3.1 LEGISLATION IN THE 103RD CONGRESS

Five natural disaster-related bills were introduced in the 103rd Congress, four in the House of Representatives and one in the Senate. Three of these bills died without committee or subcommittee consideration; two were the subject of committee or subcommittee hearings, but only one, H.R. 2873, was reported out of committee. Figure 3-1 illustrates the history of these bills; they are discussed in more detail below.

- ***H.R. 935, the Earthquake, Volcanic Eruption, and Hurricane Hazards Act.*** Rep. Patsy Mink (D-HI) introduced the legislation in the House of Representatives on February 17, 1993. This act would have provided for a Federal program of insurance and reinsurance against catastrophic earthquake, volcanic eruption, and hurricane risk. The primary insurance coverage that would be provided as a result of the Act would apply to holders of Federally related mortgage loans only. After joint referral to the Committees on Banking, Finance, and Urban Affairs, and Science, Space and Technology, the bill died.

- ***H.R. 764, the Windstorm Hazard Reduction Plan Act.*** This bill was introduced in the House by Rep. Ron DeLugo (D-VI) on February 3, 1993, and would have required the Director of the Federal Emergency Management Agency (FEMA) to develop a plan and submit a report to Congress concerning establishment of a national windstorm insurance program. The legislation was jointly referred to the Committees on Public Works and Transportation and Banking, Finance and Urban Affairs. No hearings were held, and the bill died in committee.

- ***H.R. 1302, the Hurricane Hazard Reduction Act.*** Representative Clay Shaw (R-FL) introduced this bill in the House on March 10, 1993. This measure only addressed hurricane hazard reduction. It would have provided a national insurance and reinsurance program for this purpose. The legislation was referred to the Committee on Banking, Finance and Urban Affairs where it died.

Figure 3-1
History of Natural Disaster Legislation in the 103rd Congress

Legislation	Committee(s) of Jurisdiction		Status				
H.R. 935, The Earthquake, Volcanic . uption and Hurricane Hazards Act ,onsor: Rep. Patsy Mink (D-HI)	Referred jointly to House Banking, Finance and Urban Affairs, and Urban Affairs and Science, Space, and Technology Committees	→	Bill Died				
R. 764, The Windstorm Hazard :duction Plant Act Sponsor: Rep. Don DeLugo (D-VI)	Referred jointly to House Public Works and Transportation, and Banking, Finance, and Urban Affairs Committees	→	Bill Died				
...R. 1302, The Hurricane Hazard Reduction Act ˜ ponsor: Rep. Clay Shaw (R-FL)	Referred to House Banking, Finance, and Urban Affairs Committees	→	Bill Died				
...R. 2873, The Natural Disaster Protection Act ˜ onsor: Rep. Norman Mineta -CA)	Referred jointly to House Public Works and Transportation and Banking, Finance, and Urban Affairs Committees	→	Subcommittee Hearings	→	Full committee mark-up	→	Reported out of committee October 7, 1994 (bill not considered on House Floor)
1350, The Natural Disaster Protection Act Sponsor: Sen. Daniel Inouye -HI)	Referred to the Senate Commerce Committee	→	Committee Hearings	→	Bill Died		

- ***H.R. 2873, the Natural Disaster Protection Partnership Act.*** Norman Mineta (D-CA), Chairman of the House Public Works and Transportation Committee, introduced the bill. It was referred jointly to the Committees on Public Works and Transportation and Banking, Finance and Urban Affairs. One hundred fifty-nine Democratic and Republican House members cosponsored the legislation. These cosponsors are listed in Table 3-1. Hearings were held before the Subcommittee on Water Resources and the Environment on February 23, 1994. The bill was sent to the full committee on Public Works and Transportation. The committee substantially modified the legislation. The modified bill was reported out of committee on October 7, 1994, and is discussed in the section that follows. The bill did not reach the House floor before the 103rd Congress adjourned.

- ***S. 1350, the Natural Disaster Protection Act.*** Senator Daniel Inouye (D-HI), joined by Senators Stevens, Akaka, Dodd, Gorton, Murkowski and Simon, introduced the bill on August 4, 1993. The bill was read twice and referred to the Senate Commerce Committee. This bill was a companion bill to H.R. 2873. The Senate Commerce Committee held hearings on May 26, 1994, but no further action was taken by the Committee, and the bill died. There were 23 Democratic and Republican cosponsors of the legislation. The cosponsors are listed in Table 3-2.

3.2 The Bipartisan Congressional Task Force on Disasters

The bipartisan Congressional Task Force on Disasters was appointed by the leadership of the House of Representatives in February 1994, as a result of the Northridge earthquake that occurred in Southern California the month before. It was tasked with recommending improvements in the nation's disaster strategy and reducing the cost of disasters to the nation and the Federal taxpayer.

The membership of the Task Force included nine Republican and nine Democratic members of Congress from areas affected by recent disasters as well as members of Congressional committees involved in authorizing and funding disaster relief. The Co-chairmen were Representatives Richard J. Durbin (D-IL) and Bill Emerson (R-MO). Majority Leader Gephardt and Minority Leader Michel served as *ex officio* members. The members of the Task Force are listed in Table 3-3.

After extensive consultation with numerous organizations and experts on disaster management and policy, the Task Force released a report on December 14, 1994. The report presents and discusses the recommendations of the Task Force. These recommendations include many of the elements contained in H.R. 2873 and its companion bill, S. 1350, namely:

- Creation of a nationally-based all-hazard insurance program;
- Establishment of a private corporation to provide reinsurance; and
- Implementation of mitigation programs, including enforcement of building codes.

Table 3-1
Natural Disaster Protection Act (H.R. 2873) Co-Sponsors

Abercrombie (HI)	**Dunn (WA)**	~~Kopetski (OR)~~	Rahall (WV)
Andrews (NJ)	~~Edwards (CA)~~	~~Kreidler (EA)~~	~~**Ravenel (SC)**~~
~~Bacchus (FL)~~	**Emerson (MO)**	~~**Kyl (AZ)**~~ **Senate**	~~**Ridge (PA)**~~ **Governor**
Bachus (AL)	Engel (NY)	Lantos (CA)	**Ros-Lehtinen (FL)**
Baesler (KY)	Eshoo (CA)	Laughlin (TX)	~~**Santorum (PA)**~~ **Sen.**
Ballenger (NC)	**Ewing (IL)**	~~**Levy (NY)**~~	**Saxton (NJ)**
~~Barlow (KY)~~	Farr (CA)	**Lewis (CA)**	**Schiff (NM)**
~~Bilbray (NV)~~	Fazio (CA)	~~**Lewis (FL)**~~	**Shaw (FL)**
Bilirakis (FL)	**Fields (TX)**	Lipinski (IL)	**Shays (CT)**
Bliley (VA)	Filner (CA)	**Livingston (LA)**	~~Shepherd (UT)~~
Borski (PA)	~~**Fish (NY)**~~	~~Lloyd (TN)~~	**Solomon (NY)**
Boehlert (NY)	Foglietta (PA)	Martinez (CA)	**Spence (SC)**
Brown (CA)	Ford (TN)	~~**Matchley (RI)**~~	Stark (CA)
Brown (FL)	**Fowler (FL)**	Matsui (CA)	**Sterns (FL)**
Brown (OH)	Frank (MA)	**Manzullo (IL)**	Stenholm (TX)
Burton (IN)	Frost (TX)	**McCollum (FL)**	~~**Sundquist (TX)**~~ **Gov.**
Callahan (AL)	Furse (OR)	~~McCloskey (IN)~~	~~Swett (NH)~~
Calvert (CA)	**Gallegly (CA)**	**McDade (PA)**	~~Swift (WA)~~
Canady (FL)	Gibbons (FL)	McDermott (WA)	**Talent (MO)**
~~Cantwell (WA)~~	**Gillmor (OH)**	**McHugh (NY)**	Tanner (TN)
Clement (TN)	Gordon (TX)	**McKeon (CA)**	**Taylor (NC)**
Clinger (PA)	Green (TX)	~~**McMillan (NC)**~~	Thurman (FL)
Clyburn (SC)	Hall (TX)	Meek (FL)	Torres (CA)
Collins (GA)	**Hastert (IL)**	Mineta (CA)	Torricelli (NJ)
Condit (CA)	Hastings (FL)	**Mica (FL)**	Towns (NY)
~~Cooper (TN)~~	Hayes (LA)	**Miller (FL)**	Traficant (OH)
Costello (IL)	**Herger (CA)**	Minge (MN)	Tucker (CA)
Cramer (AL)	~~Hoagland (NE)~~	**Molinari (NY)**	Underwood (GA)
Crane (IL)	**Hobson (OH)**	**Moorhead (CA)**	~~Unsoeld (WA)~~
Crapo (ID)	**Horn (CA)**	**Myers (IN)**	Volkmer (MO)
~~Darden (GA)~~	**Hutchinson (AR)**	Neal (MA)	**Vucanovich (NV)**
Deal (GA)	~~Hutto (FL)~~	Oberstar (MN)	**Walsh (NY)**
DeFazio (OR)	~~**Inhofe (OK)**~~ **Senator**	Olver (MA)	Waxman (CA)
~~Derrick (SC)~~	~~Inslee (WA)~~	Pallone (NJ)	**Weldon (PA)**
Deutsch (FL)	Jefferson (LA)	Pastor (AZ)	Wise (WV)
Diaz-Balart (FL)	E. Johnson (TX)	**Paxon (NY)**	**Young (AK)**
Dicks (WA)	Johnston (FL)	Peterson (FL)	
Dickey (AR)	Kim (CA)	Peterson (MN)	
Dixon (CA)	Kleczka (WI)	**Porter (IL)**	
Doolittle (CA)	~~Klein (NJ)~~	**Quillen (TN)**	
Dreier (CA)	**Knollenberg (MI)**	**Quinn (NY)**	

Crossed-out names indicate members who were not relected to the 104th Congress.

TABLE 3-2
NATURAL DISASTER PROTECTION ACT (S. 1350) CO-SPONSORS

S. 1350

Inoye (HI)	Pryor (AR)
Stevens (AK)	Dorgan (ND)
Akaka (HI)	Reid (NV)
Murkowski (AK)	Johnston (LA)
Dodd (CT)	Bryan (NV)
Simon (IL)	Feinstein (CA)
Gorton (WA)	Jeffords (VT)
~~Mathews (TN)~~	Murray (WA)
Ford (KY)	Moynihan (NY)
Lott (MS)	Hutchison (TX)
Breaux (LA)	Kerrey (NE)
Cochran (MS)	

Crossed-out names indicate members who were not relected to the 104th Congress.

TABLE 3-3
MEMBERSHIP OF THE BIPARTISAN TASK FORCE ON NATURAL DISASTERS, 103RD CONGRESS

EX OFFICIO MEMBERS:

Richard Gephardt (D-MO), House Majority Leader
Robert Michel (R-IL), House Minority Leader

CO-CHAIRMEN:

Richard J. Durbin (D-IL)
Bill Emerson (R-MO)

MEMBERS:

Ken Calvert (R-CA)
Lincoln Diaz-Balart (R-FL)
Julian C. Dixon (D-CA)
Elizabeth Furse (D-OR)
Steny H. Hoyer (D-MD)
Joseph P. Kennedy II (D-MA)
Howard P. "Buck" McKeon (R-CA)
Norman Y. Mineta (D-CA)
David Minge (D-MN)
Jim Nussle (R-IA)
Ralph Regula (R-OH)
Joe Skeen (R-NM)
Neal Smith (D-IA)
Curt Weldon (R-PA)

SECTION 4.0
THE NATURAL DISASTER PROTECTION PARTNERSHIP ACT OF 1994 - A SECTION-BY-SECTION ANALYSIS

4.1 SECTION-BY-SECTION ANALYSIS

This section presents a section-by-section analysis of H.R. 2873, the Natural disaster Protection Partnership Act as marked up and reported out of the House Public Works and Transportation Committee October 7, 1994.[20] H.R. 2873 would amend existing legislation, the Robert T. Stafford Disaster Relief and Emergency Assistance Act to provide for an expanded Federal program of hazard mitigation, relief and insurance against the risk of catastrophic natural disasters, such as hurricanes, earthquakes and volcanic eruptions. It can be expected that H.R. 2873 and S. 1350 will be substantially modified during the 104th Congress. The discussion will focus primarily on sections that are of interest to the real estate industry, and analyze the expected impacts on realtors.

SECTION 1. SHORT TITLE.

SECTION 2. FINDINGS AND PURPOSES. This section of the reported bill would amend Section 101 of the Stafford Act to emphasize the following objectives: the promotion of hazard mitigation, such as stricter enforcement of building codes, improving first emergency response capabilities, establishing a funding mechanism for state emergency planning and mitigation activities, mandating disaster insurance for residential properties, and the provision of enhanced insurance coverage backed by a natural disaster protection fund.

SECTION 3. DEFINITIONS. This section of the reported bill amends Section 102 of the Stafford Act by modifying the definition of "Federal Agency" to include Freddie Mac and Fannie Mae. This section would also add 21 new definitions to the Stafford Act that define important terms used in the bill.

SECTION 4. AMENDMENTS TO THE STAFFORD ACT. This section of the reported bill adds three new titles at the end of the Stafford Act: Title VII entitled "Disaster Mitigation"; Title VIII titled "Mandatory Disaster Coverage"; and Title IX titled Natural Disaster Protection Fund".

[20]This section incorporates analysis included in House of Representatives Report 103-840, Part 1, dated October 7, 1994.

TITLE VII - DISASTER MITIGATION

SUBTITLE A. FEDERAL EMERGENCY MANAGEMENT AGENCY

SECTION 701. SUPPORT PROGRAMS. This section of the reported bill would require the Director of the FEMA to carry out natural disaster mitigation programs for the following purposes:

1) To undertake research to strengthen building codes and promote development of cost-effective building technologies and other related hazard mitigation measures;

2) To develop hazard mitigation technologies for states, local communities, and other persons, (e.g. building contractors) responsible for implementation and enforcement of hazard mitigation measures;

3) To undertake educational programs to enhance public awareness of the risks associated with natural disasters and ways to mitigate losses from such disasters.

SECTION 702. NEW FEDERAL BUILDING STANDARDS. This section of the reported bill would codify into statute, Executive Order 12699 (55 Fed. Reg. 835) which relates to the seismic safety of Federal and Federally assisted or regulated new building construction.

SECTION 703. STUDIES. This section of the reported bill directs the FEMA Director to conduct the following four studies:

- *Section 703(a). **Flood**.* FEMA would be required to study and report within 18 months means of increasing the purchase of flood insurance under the National Flood Insurance Program (NFIP), including the addition of the NFIP policy, or its content, to the standard residential property insurance contract.

  Discussion: The NFIP is a complex program that has been developed incrementally over a period of 27 years. If such integration occurs, it needs to be done carefully with the input of FEMA, floodplain managers, and others with expertise and experience in the area. In addition, expanding floodplain insurance may be potentially more controversial than expanding earthquake insurance. Environmental groups may claim that it will allow development in ecologically sensitive areas, such as wetlands and barrier islands that would otherwise not occur.

- *Section 703(b). **National Minimum Consensus Building Construction Standards**.* FEMA would be required to conduct a study with the National Academy of Sciences (NAS) to conduct a study of the advisability and feasibility of establishing national minimum consensus building construction standards addressing natural disaster mitigation issues through private sector standards development organizations. The study would be conducted by a NAS-appointed blue-ribbon panel of experts, including builders, realtors, insurers, representatives of organized labor, and building code officials from the model building code congresses. The study of national minimum consensus building construction standards would be limited to natural disaster issues, and the NAS would transmit a report to Congress which contains the results of the study within two years of enactment.

Discussion: The costs of mitigation could be substantial. According to numbers cited by FEMA during Congressional hearings, the average cost of upgrading for earthquakes was $8 to $10 per square foot for residences and $10 to $12 per square foot for commercial structures. For a 2000-square-foot house, that represents an investment of $16,000 to $20,000.[21] The price of new homes could also be increased significantly, potentially decreasing home sales.

- ***Section 703(c). Home Disaster Inspections***. FEMA would be required to have NAS conduct a study of the advisability and feasibility of establishing standards for the training and licensing of home inspectors, and using home disaster inspections as a means to promote hazard mitigation. The study would be performed by a panel of experts including builders, lending institutions, local community officials, representatives of organized labor, and representatives of homeowners. The NAS would transmit to Congress a report within two years of enactment which contains the results of the study.

Discussion: If such standards and inspections are implemented, they could also substantially increase the cost and complexity of real estate transactions, potentially discouraging home sales. In addition, the panel membership for the study does not include the real estate industry, as did the panel mentioned in 703(b).

SECTION 704(D). COMMERCIAL COVERAGE. FEMA and other relevant Federal agencies determined by FEMA would study the advisability and feasibility of expanding the coverage provided by the Natural Disaster Protection Corporation under Title VIII to include commercial losses and would report its recommendations to Congress within six months. Insurance industry representatives and other experts in loss estimation would participate in this study.

Discussion: This provision was not included in the original bill sent to the House Public Works and Transportation Committee. Its inclusion would be beneficial to the real estate industry, to the extent it would increase commercial coverage and sales of commercial properties.

---

[21] House hearings, op. cit., 30.

SECTION 704. EARTHQUAKE-PRONE STATES. This section would require FEMA, based on U.S. Geological Survey seismic data, to identify within six months of enactment which states are exposed to earthquake risk. These states will be classified as earthquake-prone for the purposes of the Act.

Discussion: The earthquake risk is not distributed evenly across states. For example, Cairo, Illinois is an area of high earthquake risk, while the risk of a significant earthquake in Chicago is remote. The same is true in Arizona; Yuma has a high earthquake risk, Phoenix and Tucson do not. Classification as an earthquake-prone state is critical because it will trigger certain requirements such as mandatory earthquake insurance for all Federally-related mortgages.

SUBTITLE B. STATE AND COMMUNITY PROGRAMS

SECTION 711. ADOPTION OF BUILDING AND SAFETY CODES. This section of the bill would require each state to either adopt a building code that meets or exceeds the mitigation portion of one of three model building codes or certify that local communities in the state are enforcing these codes. States with flood-prone communities as defined under NFIP would have to adopt and enforce flood minimum performance standards. These standards would apply to new and substantially modified residential and commercial construction.

Discussion: As stated previously, adoption and enforcement of building codes, especially in states without codes, could increase costs of new homes, and potentially reduce home sales. Also, state certification of building code enforcement by local communities may place an unreasonable burden on state governments. This also may be an unfunded mandate, since it does not appear that there are state funds for these activities. Also, there is the question of whether codes are necessary in states that are not prone to the types of disasters referenced in the legislation.

SECTION 712. DEVELOPMENT OF STATE MITIGATION PLANS. This section of the bill would require each state to develop a plan, or designate an existing plan, for improving the state's ability to reduce the hazard of natural disasters. At a minimum, the plan would include processes for 1) ensuring compliance with building codes; 2) improving emergency response; 3) training of first responders; 4) enforcing local land use and management ordinances; 5) addressing the impact of further development in high-risk areas on the environment; 6) ensuring all builders, plumbers, electricians, and building inspectors are licensed or certified; and 7) identifying critical facilities and public structures to be retrofitted within a fixed time period.

Discussion: Mitigation funds will probably be insufficient for these activities, thereby placing administrative burdens on state agencies.

SECTION 713. COMPLIANCE. This section of the bill would give states between two and five years to comply with the building codes and mitigation plan requirements of Sections 711 and

712. The compliance process would consist of a series of milestones the states must meet. This section would also require FEMA to promptly notify in writing, those states that fail to comply with the requirements. If corrective action is not taken within 180 days, the state would be subject to penalties outlined in Section 714 until the Director determines that the state has taken the necessary action. FEMA would issue guidelines defining what constitutes adequate compliance.

Section 714. Penalties. This section of the bill would impose two types of penalties on non-compliant states including 1) a reduction from 75% to 50% in the state's minimum cost share for Federal disaster aid; and 2) monies from the new Mitigation Account established under Section 715 would be cut off.

> **Discussion:** Complying communities within a non-complying state could be cut off from disaster aid. Also, monitoring compliance with the bill's provisions may not be easily accomplished, especially based on the amount of funding available.

Section 715. Mitigation Account. This section would allocate funds from the Mitigation Account established under Section 902 to the state annually, based on a pro rata formula of the premiums collected in the state. FEMA would issue regulations describing the pro rata formula. These funds could only be used for mitigation measures. FEMA would be authorized to audit state programs to ensure state programs are being spent on hazard mitigation activities. States would be required to transfer at least 25% of the money to local communities.

Subtitle C. Insurance Mitigation Incentives

Section 721. Insurance Pricing Incentives. This section of the bill would encourage each insurer who participates in the Natural Disaster Protection Fund described in Title IX to consider hazard mitigation measures when setting rates and deductibles for property insurance.

Subtitle D. Federal Lending Institutions

Section 731. Insurance Purchase Requirement. This section would require that no Federally related mortgage loan be made, increased, extended, or renewed that is secured for residential property located in an earthquake-prone state, unless such residential property is insured by an insurance policy which has coverage for earthquake and volcanic eruption perils.

> **Discussion:** This provision would include not only direct Federal loans, such as VA and FHA loans, but mortgages sold to Freddie Mac or Fannie Mae, and mortgages that are insured by the Federal Deposit Insurance Corporation (FDIC). Nonetheless, according to the U.S. General Accounting Office (GAO), this proposed mandatory purchase requirement would affect only

40% of all homeowners in the affected states.[22] If participation is not sufficiently broad so as to spread risks among a large number of individuals, disaster insurance will not be affordable without Federal subsidies.

SECTION 732. ESCROW INSURANCE PREMIUMS. This section of the bill would require that lending institutions which generally require escrowing, escrow earthquake and volcanic eruption insurance premiums for homeowners with Federally related mortgage loans.[23]

TITLE VIII - MANDATORY DISASTER COVERAGE

SUBTITLE A. ENHANCED INSURANCE PROTECTION

SECTION 801. EXTENSION OF RESIDENTIAL PROPERTY INSURANCE. This section of the bill would require all insurers participating in the Natural Disaster Protection Corporation described in Section 811 to provide earthquake and volcanic eruption coverage to all of their policyholders as part of their standard residential property insurance policy.

SECTION 802. CONDITIONS ON MANDATORY INSURANCE COVERAGE. This section would prevent the mandatory insurance provisions of Section 731 from going into effect until the following three conditions are satisfied: 1) the Natural Disaster Protection Corporation must be created; 2) the terms and conditions of the catastrophic insurance coverage issued under Subtitle B must fully satisfy the principles of Section 815; and 3) the premiums written by private insurers must represent at any given time, at least 51% of the private residential property insurance in the United States.

SECTION 803. NON-PARTICIPATING INSURERS. This section would require insurers not participating in the Natural Disaster Protection Corporation to notify their homeowner policyholders.

SECTION 804. FLOOD WARNING. This section of the bill would require that each homeowners policy state that flood peril is not covered unless the policy holder has a separate flood endorsement or flood insurance policy.

Discussion: The primary concern with this Title of the bill is whether participation in the program will be broad enough to make earthquake and volcanic eruption insurance affordable. If risk is not spread over a large enough number of people, premiums would be prohibitively costly. This already the case in California where earthquake insurance is available, but only

[22] U.S. General Accounting Office, "Comments on Changes to the Natural Disaster Protection Act". November 7, 1994, page 2. B-258682.

[23] Federally-related mortgage loans include direct government loans as well as loans guaranteed by the Federal Deposit Insurance Corporation (FDIC).

25% of homes are insured for earthquake damage. Earthquake insurance averages about $200 per year in addition to standard homeowners coverage (on average about $350 per year). The deductible can be 10% of the total coverage on a home, which for moderately priced homes in California can easily be in the $25,000 range. The Natural Disaster Coalition, however, has claimed that if the bill is enacted, these provisions will reduce the cost of earthquake insurance in California to about $60 per year.[24]

SUBTITLE B. NATURAL DISASTER PROTECTION CORPORATION

SECTION 811. CREATION. This section would establish a private Natural Disaster Protection Corporation. Private insurers and state insurance pools that meet minimum criteria and financial viability standards would be eligible to participate.

SECTION 812. STRUCTURE AND OPERATIONS. This section of the bill would require the Corporation to set and issue minimum guidelines for structure and operation within 12 months. The minimum guidelines would include standards for size, term of office, composition, bylaws, and powers of the Board of Directors, initial and ongoing capitalization provided by the entities participating in the Corporation, rate-setting, and hazard mitigation.

SECTION 813. COVERAGE. This section of the bill would authorize the Corporation to provide catastrophic coverage to participating private insurers and states for residential property losses only. The coverage would include losses caused by earthquakes, volcanic eruptions, tsunamis, and hurricanes, including losses from debris removal, additional living expenses, and ordinance and law coverage.

Discussion: Commercial losses would not be covered.

SECTION 814. PAYMENTS. This section of the bill would require participating private insurers and state pools to make annual payments to the Corporation for the coverage described in section 813. This section addresses the establishment of rates (Section 814(b)). This section includes the following provisions:

- Payments would have to be based on risk exposure using actuarial principles developed by the Corporation. The rates would be certified as actuarially sound by an independent ratemaking commission.
- Annual contributions from insurers and state pools would be placed in a reserve account and held in trust by the Corporation. This reserve account would be exempt from Federal and state taxation.

[24] House hearings, op. cit., p. 56.

- The Corporation would be required to pay 7.5% of the annual payments received from private insurers to the Mitigation Account established in Section 903(c).

- Section 814(e) would require that state insurance regulators, when reviewing and approving casualty insurance rates, consider and accept the rating structure of private insurers participating in the Corporation and the impact of their annual payment made to the Corporation.

  Discussion: It may be difficult to set affordable, actuarially sound rates and attain a high enough level of participation to effectively spread risk and significantly reduce the cost of multihazard insurance coverage. The U.S. General Accounting Office has raised this concern in reports and at Congressional hearings.[25] Despite advances in computer modeling techniques to determine risk exposures and potential losses, limitations remain. A recent example of these limitations is the earthquake that occurred in Northridge, California during January 1994. The earthquake occurred on a fault line that was unknown to the insurance industry, and it was a rare type of quake for which little information existed.

SECTION 815. TERMS AND CONDITIONS. This section of the reported bill would require the Corporation, in consultation with FEMA and other relevant Federal agencies determined by FEMA, to set the terms and conditions of catastrophic coverage, including levels of retained losses, for the coverage provided under section 813.

SECTION 816. FEDERAL LOANS. This section of the bill would require that direct loans from the Private Loss Account of the Natural Disaster Protection Fund described in Title IX be used to make up any shortfall the Corporation might suffer in paying claims to participating private insurers or state pools who purchased the coverage. The Corporation would repay all Federal loans from future premiums under the terms set forth in Section 904 and private insurers would be required to participate in the Corporation until all borrowed monies they receive are fully repayed. If the Corporation fails to pay mitigation funds to the Mitigation Account as provided in Section 814, it would become ineligible to receive Federal funds.

SECTION 817. INDEPENDENT RATE-MAKING COMMISSION. This section would establish an independent rate-making commission of five professional actuaries who would certify rates issued by the Corporation as actuarially sound.

Discussion: Although the commission may be able to independently set rates, setting actuarially sound rates may be difficult for the reasons stated under Section 816.

[25]U.S. General Accounting Office, November 7, 1994, op. cit., page 2.

SECTION 818. NO FEDERAL FUNDS. This section would prohibit Federal funding of any activity of the Corporation, except for providing Federal loans under Section 904.

SECTION 819. GAO AUDIT. This section would direct the GAO, after the Corporation has operated for one year, to conduct an audit of the Corporation and the Independent Rate-Making Commission to ensure that the activities of both are in compliance with the Act. Follow-up audits would be conducted every three years thereafter and the results submitted to Congress.

SECTION 820. PRIVATE CORPORATION. This section would clarify that the Corporation is a private entity with no governmental powers.

TITLE IX -- NATURAL DISASTER PROTECTION FUND

SECTION 901. ESTABLISHMENT. This section of the bill would establish within the Treasury Department, a trust fund to be known as Natural Disaster Protection Fund. FEMA would administer the fund and its separate accounts.

SECTION 902. ACCOUNTS. This section of the bill establishes three separate accounts in the fund: a Private Loss Account; a Public Loss Account; and a Mitigation Account. The Private Loss Account would provide loans to cover residential property losses for which the Corporation could not provide complete compensation. The Public Loss Account would cover losses to public structures and other critical facilities, and the Mitigation Account would be allocated to the states to fund hazard mitigation activities as described in Section 715.

SECTION 903. FINANCING. This section of the bill specifies the amounts and sources of funds that would be transferred and credited to the three separate accounts.

SECTION 904. OPERATION OF THE ACCOUNTS. This section of the bill specifies how the three accounts established in Section 902 would operate.

- ***Section 904(a). Private Loss Account.*** This account would make up any shortfalls suffered by the Corporation pursuant to Section 816 by providing direct loans to the Corporation. However, any borrowing by the Corporation would have to be repaid, with interest, within 15 years. Such borrowing would be limited to the Corporation's capacity to repay within the prescribed period, would have to be at zero cost to the government at the time the loans are made; and would be subject to such extent and in such amounts as are provided in advance in appropriations acts.

  Discussion: This has been and remains the most controversial part of the legislation. With memories of the S&L debacle still fresh, many expressed concern during Senate and House hearings that an open-ended entitlement program was being created. This section was substantially modified in committee. The limits on borrowing, e.g. borrowing limited to the Corporation's capacity to repay within the 15-year period, sets a cap not in terms of dollars but in principles on Federal financial liability. Nonetheless, the GAO has continued to express concern that the reinsurance triggers continue to be based on the amount of surplus held by the industry and private companies. As a result, the basis for determining when the fund would become liable for payment of disaster losses could still be subject to insurer manipulation which could result in substantial increases in the fund's liability.[26]

- ***Section 904(b). Public Loss Account.*** This account addresses losses to public infrastructure as a result of natural disasters. The account would provide grants for the repair and rebuilding of highways, and other critical facilities and damaged or destroyed by natural disasters. Funds would also be provided for pre-disaster retrofitting and other hazard mitigation activities. States not in compliance with the mitigation provisions of the bill would receive less Federal funding.

  Discussion: This section was modified as a result of comments made during hearings on H.R. 2873 by FEMA and others urging Federal funds for public infrastructure losses which are appropriated "before the fact" rather than is "after the fact" in emergency funding bills. Such public infrastructure losses account for large portions of Federal disaster aid for earthquake damage.

- ***Section 904(c). Mitigation Account.*** This account would provide funds to qualified states for hazard mitigation activities as described in Section 715.

4.2 ASSESSMENT OF THE POSITIVE AND NEGATIVE IMPACTS OF H.R. 2873 ON THE REAL ESTATE INDUSTRY

GOALS OF LEGISLATION ADDRESS THE PROBLEM OF INSURANCE AVAILABILITY

Homeowners insurance is a necessary component in securing a mortgage and in buying or selling a home. When insurance is not available, sales may be held up indefinitely and may not go through at all. The lack of affordable coverage has disrupted insurance markets in the Virgin Islands, Hawaii, Florida, California, and other scattered areas throughout the U.S.

One of the main goals of H.R. 2873 is to expand insurance coverage to address the current lack of affordable insurance in high risk areas. The programs put in place by the Mineta Bill and other proposals would address the availability and affordability of insurance against the risk of

[26]GAO, op. cit., page 7.

earthquake, hurricane, volcanic eruptions and catastrophic natural disasters. This is certainly an important positive aspect of this legislation.

First Major Concern: Viability of The Primary Insurance Program

The concerns, however, are in the details. The Mineta Bill would require earthquake and volcanic eruption insurance for all Federally-related mortgages. It would also require that rates be actuarially sound. The largest concern is whether the legislation could result in affordable insurance without subsidization of high risk areas by low risk areas. Currently, there is a major debate on this issue. The Natural Disaster Coalition claims that implementation of the mandatory insurance provision of the Mineta Bill would result in premium reductions of $65 for earthquake insurance in California, while in other states at lower risk, premiums would increase only $3 to $5 or not at all.[27]

The U.S. General Accounting Office (GAO), however, has questioned whether the Mineta Bill's requirements would result in participation sufficiently broad to ensure affordable coverage. There are two reasons for these concerns. First, according to FEMA officials, the proposed mandatory purchase requirement would affect only 40% of all homeowners in the affected states. Consequently, homeowners not affected by this requirement could still obtain earthquake-free insurance from nonparticipating insurers. Those most likely to do so would live in parts of the U.S. where earthquakes are possible, but the risks are low.[28] Second, because of difficulties in enforcing the mandatory purchase requirement, full compliance is questionable. GAO cites the example of the National Flood Insurance Program, which has a similar mandatory purchase requirement, but low participation (only 20% of homeowners living in flood plains have flood insurance).[29] GAO also questions whether actuarially sound rates can be developed for earthquake-prone areas as was discussed under Section 814(e) of the reported bill above.

GAO, the Congressional Research Service, and the Congressional Budget Office have recently completed a study of the economics of the Mineta Bill. This report is not public, but if released, it may provide more information on some of the cost impacts of this legislation.

Second Major Concern: Potential Impact of the Reinsurance Program on the Federal Deficit

The most controversial aspect of the proposed program has been the reinsurance program. The issue the Congress has struggled with is how to provide meaningful relief to private insurers in the case of a truly catastrophic natural disaster, without exposing the Federal government and taxpayers to a potentially enormous financial liability, or requiring Federal regulation of the insurance industry. This concern has been expressed by members of both

---

[27]House hearings, op. cit., page 56.

[28]GAO, op. cit., page 4.

[29]U.S. General Accounting Office, Response to the Congressional Task Force on Natural Disasters. August 31, 1994. B-258200.

parties in Congress, and is likely to gain additional support in the fiscally conservative 104th Congress. GAO, FEMA, and state and local officials have also raised this concern.

Failure to adequately address the issue of Federal liability could indirectly, but significantly affect the housing and real estate industry through limitations on future economic activity and increases in interest rates.

THIRD CONCERN: COSTS OF MITIGATION

There are several concerns regarding the mitigation provisions of the proposed legislation. The mitigation program would require states to adopt and enforce building codes that meet or exceed the mitigation portions of one of three model building codes. States would be required to enforce these codes. Non-compliance would be penalized by reductions in Federal disaster aid and funds from the hazard mitigation account established under the legislation. Specific concerns with the mitigation section of the bill include the following:

- Adoption and enforcement of building codes could substantially raise home prices, especially in areas where the risk of natural disasters is low. Although stricter codes may be necessary in some areas to reduce loss of life and property, such codes need to be cost-effective, i.e. the increased costs should be commensurate with the reduction in risk attained. Any measures that could increase costs, especially to first-time home buyers, who are most price sensitive, need to be carefully examined.

- Requirements for home disaster inspections would increase the complexity and cost of real estate transactions without producing significant benefits, especially in areas where disaster risk is not high.

- Enforcement of building codes is predominantly a local function. Requiring states to enforce or certify building codes could result in the development of bureaucracies in many states where none currently exist. In addition, this may constitute an unfunded mandate, since the bill only provides funds for hazard mitigation.

- Designation of earthquake-prone states may not be appropriate. Earthquake risk is not evenly distributed across states. Such designation may result in areas being subject to requirements that are not justified in terms of risk.

SECTION 5.0
PROPONENTS AND OPPONENTS

There is consensus inside and outside of Congress that the present system of preparing for and responding to natural disasters is flawed and that the situation will probably only get worse in the future. There is agreement that something needs to be done, and even critics support the goals of the current legislative initiatives.

Despite the fact that natural disaster legislation has enjoyed broad, bipartisan support in Congress, individual Congressmen and various groups have expressed concern with some provisions, notably the reinsurance provisions, and the potential liability that may be borne by the Federal government. This section will identify the key players or stakeholders in the debate and their positions on natural disaster protection legislation.

A. CONGRESS

Natural disaster protection legislation received significant bipartisan support in both the House of Representatives and the Senate during the 103rd Congress. H.R. 2378 attracted 88 democratic and 71 Republican co-sponsors in the House of Representatives; in the Senate, S. 1350, was co-sponsored by 23 Senators, 7 Republicans and 16 Democrats. The co-sponsors for these two bills are listed in Tables 3-1 and 3-2. The bipartisan task force on Disasters is comprised of nine Democratic and nine Republican members; those members are listed in Table 3-3.

Two of the key proponents of natural disaster legislation in the Senate are Senator Inouye (D-HI) and Senator Stevens (R-AK). Senator Inouye chaired the hearings on S. 1350 which occurred on May 26, 1994. The other Senators from each state, Akaka (D-HI) and Murkowski (R-AK) are also co-sponsors of H.R. 2378. Both states are at high risk for earthquakes, tsunamis and volcanic eruptions. Hawaii is a low risk area for hurricanes, but two devastating hurricanes nonetheless hit the islands in the 1980s. Senator Lott (D-MS), who represents a state that experienced one of the strongest hurricanes recorded this century, is also a strong sponsor of the legislation.

Senator Hollings (D-SC) was the chairman of the Senate Commerce Committee during the 103rd Congress. During the May 1994 hearings, he stated his support for improvements in natural disaster mitigation, preparedness and response. The new committee chairman, Senator Pressler (R-SD), however, is from a state that does not experience the types of natural disasters that the bill addresses. Although he has stated support for legislation that would reduce the cost of emergency relief to the American taxpayer, he questioned whether the primary insurance program proposed would result in subsidization of high risk states by low risk states such as

South Dakota. He also voiced a desire that the hearings address the kind of "special needs", i.e. tornados, floods, and fires, of lower risk states.[30]

While supporting the goals of the S. 1350, Senator Kerry (D-MA) expressed concern over the reinsurance provisions of the bill during the committee hearings. He expressed the fear that if private insurance companies were to go bankrupt, the taxpayers would end up bailing them out. The Senator also related his experience with the National Flood Insurance Program, as evidence of the difficulty of setting actuarially sound rates.[31]

The strongest proponent of the legislation in the House of Representatives during the last Congress was Norman Mineta (D-CA), Chairman of the House Public Works and Transportation Committee, and also a member of the Congressional Task Force on Disasters. He chaired Committee hearings on the disaster legislation in May of 1994, and produced a committee substitute to H.R. 2873 that was reported out of committee in October of 1994. Congressmen Bill Emerson (R-MO) and Richard Durbin (D-IL) were co-chairmen of the Bipartisan Task Force on Disasters.

In addition to the bill's co-sponsors, a number of members voiced support of the bill during committee hearings. These members include Congressman Boehlert (R-NY); Ron DeLugo (D-VI); William Zeliff, Jr. (R-NH); Nick J. Rahall III (D-WV); James Hayes (D-LA); Stephen Horn (R-CA); Robert Borski (D-PA); Glenn Poshard (D-IL); Pete Geren (D-TX); Tim Valentine (D-NC); and Douglas Applegate (D-OH). Although no members opposed the legislation during the hearings, several members asked for clarification regarding certain provisions. For example, Thomas Ewing (R-IL) raised a concern that the cost of stricter building codes should be commensurate to the risks faced. He stated that by trying to make everybody meet standards we might "make housing and building so expensive that we may protect some things but cause more problems..."[32] Pete Geren questioned how much the cost of earthquake insurance premiums might be reduced by mandatory purchase requirements.[33] Karen Shepherd (D-UT) questioned whether commercial real estate would be covered.[34]

Congressman Bud Shuster, (R-PA), who is the new chairman of the House Public Works and Transportation Committee, stated in the additional views of the committee report on H.R. 2378 that the mark-up committee bill was significantly improved, and that he looked "forward to

[30]U.S. Senate, Hearings on S. 1350, the Natural Disaster Protection Act, before the Committee on Commerce, Science and Transportation. May 26, 1994, page 93.

[31]Ibid., pp. 2-5.

[32]House hearings, op. cit., page 53.

[33]Ibid., pp. 55-57.

[34]Ibid., page 62.

working with Chairman Mineta during the next Congress in furtherance of this goal."[35] However, he urged a fuller review of the reinsurance provisions of the bill, "before committing the full faith and credit of the United States." [36] He also said the committee needs to understand the impact on Federal revenues from certain provisions and the cost of mandates such as 1) mandatory earthquake insurance purchase requirements, 2) state and local government enforcement of building codes, potentially leading to higher construction costs, 3) licensing of plumbers, builders, and electricians, and 4) studies that may lead to requirements for home disaster inspections.

In a dissenting view to the Task Force report, Congressman Joseph P. Kennedy II (D-MA), expressed support for the overall efforts of the Task Force, but could not support the multi-hazard insurance and reinsurance programs. While supporting the mitigation recommendations of the Task Force, he remained concerned that the impact on the Federal budget of the other programs was unclear, and could expose "Federal taxpayers to contingent liability of unknown, and perhaps massive, amounts." [37]

CONGRESSIONAL AGENCIES

Three Congressional agencies, the Congressional Research Service, the General Accounting Office, and the Congressional Budget Office have devoted considerable effort to the study of natural disaster legislation (see References). The sections below detail briefly the viewpoints stated by those agencies.

THE U.S. GENERAL ACCOUNTING OFFICE (GAO). GAO has been the most vocal in expressing viewpoints before Congress on the various legislative proposals. Thomas J. McCool, Associate Director, General Government Division, testified before the Senate Commerce Committee on May 26, 1994. In this testimony, and in published studies (e.g. "Federal Disaster Insurance: Goals are Good, But Insurance Programs Would Expose the Federal Government to Large Potential Losses"), GAO has been critical of S. 1350. While applauding the mitigation aspects of the legislation, GAO has raised serious doubts about the multihazard insurance and reinsurance provisions of the legislation. GAO's greatest concerns are over the reinsurance provisions, and most specifically, the extent of the Federal government's liability in backing up catastrophic losses. Other concerns include: 1) difficulty in setting actuarially sound rates; 2) the possibility of "cherry-picking" by insurers by providing incentives for private insurers to insure the safest risks and pass on the least insurable risks to the Federally-insured program.

[35]U.S. House of Representatives, Report 103-848, Part 1 on the Natural Disaster Protection Partnership Act. October 7, 1994, p. 59.

[36]Ibid.

[37]U.S. House of Representatives, "Report of the Bipartisan Task Force on Natural Disasters". December 14, 1994, page 23.

The reinsurance program was also criticized on the grounds that it would require the Federal government to provide reinsurance to companies engaged in risky or poorly managed activities; and might allow insurers to tap the reinsurance fund before suffering losses substantial enough to justify assumption of risk by taxpayers.

The bill was substantially modified to respond to these criticisms. In a November 7, 1994 report to Senator Inouye, GAO commented on these changes. While the changes "may enhance aspects of these insurance programs", GAO continued to "have concerns regarding both programs."[38] The major concerns were:

- Difficulty in setting affordable actuarially sound rates for national disaster insurance, despite recent advances by the insurance industry in computer modeling techniques;
- Difficulty in obtaining a high level of participation in the program to effectively spread risks and significantly reduce the cost of multihazard coverage;
- Basing the triggers for Federal reinsurance payments to private insurers and reinsurers on the amount of surplus held by the industry and individual companies, and still exposing the taxpayer to potential significant liability;
- FEMA's lack of authority to deny Federal excess reinsurance coverage to eligible companies, regardless of the companies' condition, business practices, or any other factor; and
- The questionable inclusion of certain types of losses that would qualify for reimbursement.

CONGRESSIONAL RESEARCH SERVICE. The Congressional Research Service (CRS) has authored several papers on natural disaster insurance (see "Natural Hazard Risk and Insurance: The Policy Issues", July 5, 1994) and specifically analyzed S. 1350. CRS did not take a position on the legislation, but rather explained the bill's provisions, and presented proponents' arguments for and critics' arguments against the legislation.

CONGRESSIONAL BUDGET OFFICE. The Congressional Budget Office (CBO) has not yet published an analysis of natural disaster insurance. However, a study conducted jointly with GAO and CRS for Congressman Mineta examine H.R. 2873 as reported out of committee. That results of that study have not yet been made publicly available.

FEDERAL AGENCIES

Although the Clinton Administration commissioned an Interagency Task Force on Natural Disasters, the views of the Task Force are not yet known, since the report has

[38]GAO, November 7, 1994, op. cit., page 1.

not yet been completed. The FEMA and the National Oceanic and Atmospheric Administration, however, have been active in the Congressional debate.

Federal Emergency Management Agency. Representatives of FEMA testified at both the Senate and House hearings.[39] Although in favor of the legislation's goals of broader, affordable insurance coverage and increased mitigation, and one of the key agencies represented on the Administration Task Force on Natural Disasters, FEMA nonetheless raised numerous questions concerning different provisions of the legislation. Some of the key concerns presented in FEMA testimony relate to the following:

- The efficacy of the mitigation provisions, specifically the absence of mechanisms to enforce the compliance of states or localities with mitigation measures, and no provision for mitigation programs for public structures;
- The extent to which the primary insurance program would effectively spread risk and reduce the need for Federal disaster assistance;
- The potential for the reinsurance program to become an open-ended obligation of the Federal Government to companies whose solvency and practices are regulated by the states.

The National Oceanic and Atmospheric Administration. Representatives of the National Weather Service of the National Oceanic and Atmospheric Administration (NOAA) also testified at both congressional hearings.[40] The testimony focused on the probability that more destructive hurricanes are likely to hit the U.S. mainland during the next decade, with corresponding increases in the likelihood in catastrophic property damage. NOAA also urged development of better disaster warning systems, restriction of development in certain high risk areas, and improved evacuation procedures and mitigation plans to reduce damages.

Industry and Trade Associations

The insurance industry has been and continues to be, one of the major proponents of natural disaster insurance. Although individual companies and insurance trade organizations such as the American Insurance Association and the Independent Insurance Agents of America have lobbied for natural disaster legislation, the effort has been led by a lobbying organization made up of predominantly insurance industry affiliated groups called the Natural Disaster Coalition. This effort began in 1986 as a lobbying effort called the Earthquake Project, with the goal of establishing a national reinsurance fund backed by the Federal government. After the recent string of natural disasters in the late 1980s and early 1990s, it expanded to incorporate the support of other non-insurance industry groups and to cover other natural disasters.

---

[39] Senate and House hearings, op. cit.

[40] Ibid.

The Homebuilders. The National Homebuilders Association (NHA) has not yet taken an official position on natural disaster insurance. However, it can be reasonably expected that the housing industry will object to some of the mitigation provisions of the legislation, especially those pertaining to stricter enforcement of codes, licensing of homebuilders, tying disaster assistance to compliance with building codes, and possible requirements for natural disaster mitigation as part of home inspections.

The American Institute of Architects. During the Senate and House hearings, the American Institute of Architects (AIA) voiced concern about the mitigation provisions of the legislation, and strongly endorsed the legislation with changes.[41] Some of the suggested changes are definitional, while others concern guidelines for compliance verification, requirements to update building codes, the licensing of architects and building inspectors, technology transfer of hazard mitigation technology, provisions for historic structures, and requirements for the retrofitting of existing buildings and public structures.

Consumers Union. The Consumers Union supports the legislation, but recommends changes to several provisions. The major concern is that H.R. 2873 "erects too wide a safety net under the insurance industry without holding the industry accountable for loss prevention and protection and ensuring the goals of disaster assistance are met."[42] Other concerns are 1) lack of protection for older housing stock in the mitigation program; 2) the omission of commercial properties; and 3) objections to the incorporation of flood insurance within the program. The group recommends that Federal regulation of the insurance industry should be the quid pro quo for the insurance and reinsurance programs.

Homeowners Association. The United Homeowners Association "feels strongly that the quick passage of the Natural Disaster Partnership Act is necessary for the protection of homeowners as disaster victims and as taxpayers."[43] No changes to the legislation were suggested.

The National Taxpayers Union. The National Taxpayers Union is one of the few organizations to strongly oppose the legislation. The major concern is that the insurance and reinsurance programs would subsidize insurance companies and put taxpayers at "great risk." Also, the group claims that people living in low risk areas would subsidize those living in high risk areas, and that the program would promote development in disaster prone or ecologically sensitive areas since insurance availability is guaranteed, thereby increasing the risk of injuries, fatalities, property damage and ecological disruption.[44] Also, the legislation is criticized for failing to account for damage to public infrastructure. The group also recommended a cost-benefit analysis of the proposed program of Federal primary insurance and reinsurance to

---

[41]House and Senate Hearings, op. cit.

[42]House hearings, op. cit., pp. 66-68.

[43]Ibid., page 213.

[44]Senate hearings, op. cit., pp. 103-104.

determine its impact on the Federal budget, as well as other studies on the relationship between Federal tax policy and insurance company reserves, and the role of mitigation and other policy in reducing losses.

PLUMBING-HEATING-COOLING CONTRACTORS. Two associations, the National Association of Plumbing-Heating-Cooling Contractors (NAPHCC), and the International Association of Plumbing and Mechanical Officials (IAPMO) spoke during Congressional hearings to recommend that the legislation recognize their respective plumbing codes in the legislation. The NAPHCC sponsors the National Standard Plumbing code and the IAPMO sponsors the Uniform Plumbing Code. They were otherwise in favor of the legislation.

STATE & LOCAL OFFICIALS

A number of state and local officials have testified before Congress on natural disaster legislation. The officials and organizations have included the Director of the South Carolina Division of Emergency Preparedness, the Association of State Floodplain Managers, the Director of the Office of Emergency Services for the City of San Jose, California; the Lieutenant Governor of the U.S. Virgin Islands; a member of the Florida House of Representatives responsible for setting up that state's emergency catastrophe fund; the Commissioner of the Texas Department of Insurance; the Director of the Missouri Emergency Management Agency; the Director of the Governor's Office of Emergency Services for the State of California; and the Maryland State Floodplain Manager.

All these individuals and organizations recognize the need for a natural disaster policy to replace the ad hoc disaster response that has occurred to date. They support the legislation, but some have concerns with certain provisions of existing legislation. For example, the Director of Missouri's Emergency Management Agency urged the inclusion of flood insurance in the primary insurance program. The Maryland State Floodplain Manager questioned the enforceability of mitigation provisions, the effect on the economy of a Federal reinsurance fund, the impact on Federal tax revenues of some provisions, and the potential for unlimited Federal liability. Other concerns included whether the cost of mitigation would drive up the cost of housing, the extent to which an insurance availability crisis actually exists, whether subsidization of high risk states by low risk states would occur, the effect of the program on disaster aid, effectiveness of mitigation provisions, and recommendations for study of the items above.[45]

[45] Senate and House hearings, op. cit.

SECTION 6.0
LEGISLATIVE OUTLOOK

According to House and Senate Committee staff, although there is bipartisan support in Congress for addressing the overall issue of natural disaster insurance, mitigation, and preparedness, action will not occur until at least late in the spring, if not later. It is also likely that the legislation will be substantially modified, especially the reinsurance provisions.

Broad bipartisan support continues to exist for addressing the problems of insurance availability and affordability in disaster-prone areas, reducing disaster losses and Federal disaster aid, and ensuring the ability of the insurance industry to pay after a catastrophic disaster. Areas subject to catastrophic natural disasters include some of the most populous regions of the United States and include both Republican and Democratic and conservative and liberal constituencies. Also, there is recognition that these problems won't go away, and that, in fact, they are likely to get worse. This bipartisan support is evidenced by the 159 bipartisan cosponsors of H.R. 2873 in the House and the 23 Republican and Democratic cosponsors of S. 1350.

Despite this sense of urgency, efforts to implement the Republicans' "Contract with America" and the debate surrounding that effort, may dominate the first year of the 104th Congress. Cutting taxes, cutting spending, reforming welfare and other major issues will preoccupy the legislative as well as the executive branch of government. Of course, legislation must be reintroduced in both Houses, since this is a new Congress. That legislation will probably not be considered at least until late spring at the earliest.

Another reason action may not occur quickly is because of the complexity of the programs that have been proposed, and the time it will take to address concerns and carefully craft any legislation. With Republican control of the House and the Senate, it is likely that the legislation introduced in the 103rd Congress will be substantially modified. There will be a tendency to limit government involvement in the any proposed program as well as government financial liability, and to rely on the private sector, as much as possible to solve the problem with limited Federal intervention. The Clinton Administration may also tend to move in this direction. This is the trend that was evidenced during a presentation of preliminary findings January 5, 1994, by the Administration Task Force on Natural Disasters. The issue receiving closest scrutiny in this Congress will be how to limit the liability of the Federal government in a reinsurance program and prevent potential insurer manipulation while providing meaningful relief to private insurers in the event of catastrophic losses. This is the issue that generated the broadest concern in the last Congress, and with a fiscally conservative Congress, these concerns will certainly be enhanced.

Other concerns will continue to be debated. These include developing catastrophic insurance rates that reflect actual risks, preventing subsidization of high risk areas by low risk areas, ensuring sufficient participation to make rates affordable, encouraging compliance with mitigation efforts, and determining whether or not to include flood insurance in any program.

These are all complex concerns that should and will receive considerable attention when debate resumes on natural disaster legislation. Despite the urgency of the problem, the potential impacts on the economy and the well-being of society dictate the any program must be carefully crafted and debated.

SECTION 7.0
CONCLUSIONS & RECOMMENDATIONS

Current legislative proposals, such as H.R. 2873, should be supported in principle, since they do attempt to address the problem of insurance availability and affordability. However, certain provisions of these proposals are potentially negative or unclear as to their impact on the real estate industry. Any legislation should be carefully crafted and debated. The National Flood Insurance Program is less sweeping than the natural disaster protection programs proposed during the 103rd Congress, yet it took 27 years to develop, and has only met with limited success. The current program is complex and can have profound impacts on the Federal deficit and the economy. Despite the urgency of the problem, the following concerns need to addressed in any final legislation to ensure the viability of a national program of natural disaster mitigation, primary insurance and reinsurance:

1) Development of a primary insurance program that promotes participation that is sufficiently broad to ensure affordable insurance coverage. This is a complex task, but many in and out of Congress share this goal.

2) Limits on Federal financial liability in any reinsurance program developed. However, the program still needs to offer adequate reinsurance to private industry in the case of a catastrophic disaster. This will be the most hotly debated natural disaster legislative issue in the 104th Congress. A fiscally conservative Congress and Clinton Administration will both be concerned about this issue.

3) Locally adopted and enforced building codes that are cost-effective, i.e. the reduction in risk to life and property is commensurate with increased costs.

4) Minimization of potential requirements that increase the cost and complexity of real estate inspections such as home disaster inspections.

5) Development of premiums that are actuarially sound and don't result in the subsidization of high risk areas by low risk areas.

In addition to addressing these concerns, more information is needed on the costs of certain mandates, such as the enforcement of building codes, or mandatory insurance coverage. It is expected that information on this and other economic issues will be provided by the joint CBO-CRS-GAO study of the Mineta Bill that has recently been conducted but not yet released.

APPENDIX A

REFERENCES

APPENDIX A

REFERENCES

U.S. General Accounting Office, "Flood Insurance:Financial Resources May not be Sufficient to Meet Future Expected Losses," March 1994, GAO/RECD-94-80.

Thomas J. McCool, Associate Director, Financial Institutions and Market Issues, Comments to The Honorable Daniel K. Inouye, U.S. Senate, November 7, 1994, B-258682.

"Flood Insurance: Statistics on the National Flood Insurance Program," April 1988, GAO/RCED-88-155FS.

"Flood Insurance: Private Companies' Participation in the Write Your Own Program," May 1987, GAO/RCED-87-108.

"Federal Disaster Insurance: Goals are Good, But Insurance Programs Would Expose the Federal Government to Large Potential Losses," May 26, 1994, GAO/GGD-94-153.

"Flood Insurance: Information on the Mandatory Purchase Requirement," July 27, 1992, GAO/T-RCED-92-86.

Correspondence with the Congressional Task Force on Disasters, August 31, 1994, B-258200.

"The Effect of Premium Increases on Achieving the National Flood Insurance Program's Objectives," February 28, 1983, GAO/RCED-83-107.

Takayama, Linda Chu, Insurance Commissioner for the State of Hawaii, Letter to Mr. Robert J. Hunter, National Insurance Consumer Organization, March 19, 1993.

Rawle O. King, "Insurance Markets After Hurricane Andrew," Congressional Research Service, April 21, 1993.

"Natural Hazard Risk and Insurance: The Policy Issues," Congressional Research Service, July, 1994.

"Summary and analysis of proposal to establish a Federal natural disaster insurance program against hurricanes, earthquakes and volcanic eruptions (S. 1350)," Congressional Research Service, June 28, 1994.

Daily News, Editorials and Letters, "Another Aftershock," July 5, 1994.

Journal of Commerce, "California Quake Loss Estimate Raised," August 5, 1994.

The New York Times, "Historic Hurricane Could Catch Northeast With Its Guard Down," August 23, 1994.

The Wall Street Journal, "Demands on Insurers Herald Financial Disaster," August 23, 1994.

Congress of the United States, House of Representatives, "Report of the Bipartisan Task Force on Disasters," December 14, 1994.

Subcommittee on Water Resources and Environment of the Committee on Public Works and Transportation, Hearings on H.R. 2873 to Amend the Robert T. Stafford Disaster Relief and Emergency Assistance Act," February 23, 1994.

Report on the Natural Disaster Protection Partnership Act of 1994, October 7, 1994, Rept. 103-848, Part 1.

United States Senate, Committee on Commerce, Science, and Transportation, Hearings on S. 1350, The Natural Disaster Protection Act, May 26, 1994.

Natural Disaster Coalition, Fact Sheets.

CQ Researcher, "Disaster Response: Does the Country Need a New Strategy?," October 15, 1993, Volume 3, No. 38.

The Task Force recommendations differ, however, in several aspects. First, the Task Force report is more of a "laundry list" or a set of guidelines rather than an integrated legislative proposal, such as H.R. 2873. For example, it does not explain in the recommendations how a nationally-based all-hazard insurance program would be set up, or how insurance would be made comprehensive and affordable. Second, the scope of the recommendations is broader than the final H.R. 2873 Bill. The recommendations cover not only insurance, reinsurance, and mitigation, but also disaster response and recovery. Some, but not all, of the items in the recommendations not included in H.R. 2873 are:

- A tax deduction for hazard insurance premiums;
- Flexibility in hazard insurance deductibles;
- Low interest loans to local governments for purchase of disaster equipment;
- A "rainy day" disaster trust fund to pay for preparedness and response efforts;
- A tax deduction for retrofitting structures;
- Consideration of the manner in which Forest Service and other agencies respond to fires in wildland areas that include residences and other property;
- Simplification of the requirements for declaring a disaster;
- FEMA authorization to provide some permanent housing after disasters;
- Elimination of the 10% floor for casualty losses; and
- Creation of a new Federal loan for repairs to condominiums and apartment buildings.

3.3 INTERAGENCY TASK FORCE ON NATURAL DISASTERS

President Clinton established an Interagency Task Force on Natural Disasters during 1994 to analyze the public policy questions raised by natural disaster legislation. The intent was to develop recommendations that would become part of an Administration-sponsored bill in Congress. Task force members include FEMA, the Office of Management and Budget (OMB), the Office of Science and Technology Policy (OSTP), the National Economic Council (NEC), the Department of Housing and Urban Development (HUD), the Department of the Treasury, the Department of Transportation (DOT) and the Department of Commerce.

Although the task force report, which was originally due in July of 1994, was still not available in January 1995, the task force held a briefing to present some of its tentative conclusions on January 5. The purpose of the meeting was to gain some preliminary feedback from the industry and trade association representative who attended the meeting. Since the findings were only preliminary and subject to change, they will not be discussed in detail here. However, the program presented in the findings emphasized reduced Federal involvement and a greater reliance on the private market than was emphasized in the Congressional proposals. A key element of the findings proposal is a reinsurance program that caps in total dollars the amount of reinsurance contracts available to insurers, and sets a $25 billion "trigger" for issuance of these contracts based on industry losses in one catastrophic event.