

Date:	November 7, 2015
To:	NAR Insurance Committee
From:	Henry Kammandel, Chair, Disaster Informal Work Group
Subject:	Natural Disaster Legislation Report and Recommendations

Charge: To evaluate natural disaster legislation, identify any gaps in NAR policy and report back to the Insurance Committee.

The Work Group recommends that the Committee:

1. **In the near term, keep the focus on reauthorizing the National Flood Insurance Program (NFIP).**
Reauthorization is critical to tens of thousands of property sales that occur each month.
2. **Continue a longer term discussion on natural disaster legislation.** This issue is more complex and multifaceted than it first appears. More in-depth research, analysis and discussions are necessary than is possible in the current time frame. Nevertheless, the Work Group made significant headway by meeting with a number of experts and identifying major issues for the Committee to delve into:
 - a. *“A line of credit” or “all-perils” insurance?* Previous bills have relied on states or the private market to provide insurance coverage. Typically, all the federal government offers is some temporary backstop funding for qualifying state insurance programs in some large events.
 - b. *How many states would qualify under these bills?* Under these proposals, each state must first create its own “all perils” insurance program and charge actuarially sound rates. It is unclear how many states would have the resources or capacity to do this.
 - c. *Property Insurance Mandate?* Without a requirement to participate, many property owners will opt out of insurance until the highest risks remain. This phenomenon known as “adverse selection” has led to high premium rates and low participation. For instance, current take-up rates for California earthquake insurance is ~10%. Flood insurance, especially in areas where it is not required, is lower. Whether NAR would support requiring all property owners to buy disaster insurance is a question that must also be considered.
 - d. *Would these bills work for floods?* None of the experts who spoke with the group seemed to think so. Previous bill authors have excluded flooding because it brings its own unique set of challenges and constituencies which unnecessarily complicates program design.

NAR policy: No policy recommendations at this time; a work group would need to be re-established next year in order to spend more time and gather additional information to support policy development.

Key Findings:

- Insurance coverage for natural disasters is often very expensive and few property owners will opt to pay or be able to afford the full-risk premium needed.
- It is unclear how a federal backstop would change this, unless a) property owners are mandated to purchase insurance for those risks not now covered or b) are subsidized by taxpayers and other policyholders.
- A backstop may smooth out the “peaks and valleys” but it doesn’t reduce natural disaster losses.
- Federal reinsurance however would be less expensive than turning to the private market that will demand a risk premium and has historically charged 2-6 times the expected loss.

Natural Disaster Legislative Approaches

Federal Terrorism Risk Insurance Program (Current Law)

- Provides federal funding only for major attacks and after insurers pay initial layer of losses
- Requires the private market to “make available” coverage up to a limit
- Federal government doesn’t charge an upfront premium to insurers but recoups some funding through an assessment on commercial policy holders after a payout

Natural Disaster Backstop Legislation (HR 1101, 113th Congress)

- Provides a federal reinsurance fund and short-term loans only to qualifying states
- To qualify, the state:
 - Must create its own “all perils” insurance program *except floods*
 - Must charge actuarially sound rates and may not cross subsidize
- Charges upfront premiums to pre-pay the fund and provides for 100% loan repayment
- Provides mitigation grants for property owners to build stronger

Windstorm Amendment to National Flood Insurance Program (HR 1264, 111th Congress)

- Provides a “multi perils” insurance policy
- Requires purchase of insurance for federal related mortgages in high risk areas
- Charges full-risk premiums for most properties; one in five is explicitly subsidized
- Borrows from taxpayers in above average loss years when claims exceed premiums

Disaster Insurance Speakers & Experts:

- **Lloyd Dixon (RAND)** has extensively published on NFIP and the Terrorism Risk Insurance Program.
- **Ed Collins (Allstate)** co-wrote Federal Natural Disaster Backstop Legislation as part of the Protecting America Coalition.
- **Frank Nutter (Reinsurance Association of America)** as a leader of the Smarter Safer Coalition, opposed backstop legislation because he believes there is enough capacity in the private market.
- **Staff experts led by Michael Newman (Federal Insurance Office, U.S. Department of Treasury)**
 - Manages the Terrorism Risk Insurance Program
 - Reports to Congress on state insurance programs

Conference calls: Sept. 23; Oct. 15, 22; and Nov. 5, 2015

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