

CONGRESS SHOULD REJECT H.R. 2555, FOCUS ON MITIGATION

H.R. 2555, the Homeowners' Defense Act, is the latest attempt by Florida to make federal taxpayers pay for its flawed homeowners' insurance programs.

H.R. 2555, the Homeowners' Defense Act, introduced by Representative Klein on May 21, 2009, is a federal natural catastrophe bailout program principally designed to benefit hurricane-threatened Florida at the expense of all federal taxpayers. H.R. 2555 consists of three major components: (1) a federally facilitated consortium of states to pool their natural catastrophe risks, (2) federal reinsurance for state natural catastrophe funds and (3) federal guarantees of bonds issued by state funds. H.R. 2555 would cost taxpayers billions of dollars, result in incentives to build in unsafe or environmentally fragile areas and discourage the provision of insurance and reinsurance by the private sector.

Each of H.R. 2555's Major Provisions Is Flawed

Federally-Facilitated Consortium of States Unrealistic, Would Lead to U.S. Bailout. Nothing prevents states from pooling their natural catastrophe risks. There is no such pooling because only a few states actually would use the pooled funds, thus resulting in other states in the consortium asking their taxpayers to subsidize the few states' taxpayers. Louisiana and Texas, for example, have not chosen to pool their risks with those of Florida, which, over time, has suffered approximately 40% of all hurricane-related losses. The failure of the consortium to pay any amounts due inevitably would result in the federal government being asked to step in.

Federal Reinsurance for State Catastrophe Funds Unwise, Unnecessary. While currently each state buying reinsurance pays premiums based on its unique natural hazard exposures, federalization would force states with lower risks to subsidize a few states—principally Florida—with extensive natural catastrophe risks. In addition, since the private reinsurance and capital markets are robustly assuming catastrophe risk, federal reinsurance isn't necessary. Indeed, the private sector met its obligations arising from hurricanes Katrina, Rita, Wilma, Ike and Gustav. Further, the federal government has no expertise in underwriting natural catastrophe exposure, other than under the National Flood Insurance Program, which is more than \$20 billion in debt. Finally, the bill essentially exports failed state programs to federal taxpayers. Florida has two state entities that cannot meet their obligations and has no state income tax to fund its programs. More generally, federal subsidization of reinsurance for homeowners' insurance encourages development in unsafe or environmentally fragile areas.

Federal Guarantees of Debt for State Bonds Counterproductive, Narrowly Focused. Credit markets provide price discipline that gives private and public entities some confidence in the risk premium. Federal guarantees, by contrast, result in under-priced bond issuance and greater exposure. Since only government-controlled entities qualify under H.R. 2555, only Florida and California would be eligible. The bill asks taxpayers in states with low risks to subsidize those in states with high risks.

Mitigation: A Better Way

Congress should focus its natural catastrophe efforts on smart mitigation legislation that benefits homeowners—particularly those in the lower and middle classes—and makes their homes safer. Federal efforts to strengthen state-level mitigation programs at the state level will address the real needs of homeowners and better protect them.