GENE TAYLOR
4TH DISTRICT, MISSISSIPPI

COMMITTEE ON ARMED SERVICES

CHAIRMAN
SUBCOMMITTEE ON SEAPOWER AND
EXPEDITIONARY FORCES

COMMITTEE ON TRANSPORTATION
AND INFRASTRUCTURE

http://www.house.gov/genetaylor

Congress of the United States
House of Representatives
Washington, DC 20515–2404

2269 RAYBURN HOUSE OFFICE BUILDING
WASHINGTON, DC 20515–2404
(202) 225–5772
FAX: (202) 225–7074

DISTRICT OFFICES:
2424 14TH STREET
GULFPORT, MS 39501
(228) 864–7670

701 MAIN STREET
SUITE 215
HATTIESBURG, MS 39401
(601) 582–3246

2900 GOVERNMENT STREET, SUITE B
OCEAN SPRINGS, MS 39564
(228) 872–7950

527 CENTRAL AVENUE
LAUREL, MS 39440
(601) 425–3905

Statement of

U.S. Representative Gene Taylor
Fourth District, Mississippi

Committee on Financial Services
Subcommittee on Housing and Community Opportunity

H.R. 920, the Multiple Peril Insurance Act

July 17, 2007

Thank you, Chairwoman Waters, for conducting this hearing on H.R. 920, the Multiple Peril Insurance Act.

I am personally grateful for all the time and effort that you have devoted to the Katrina recovery. You have conducted several subcommittee hearings on Katrina concerns here in Washington, but you also brought the Housing Subcommittee to Mississippi and Louisiana so that the Members could see the challenges for themselves.

Under Chairman Frank's leadership, the Financial Services Committee has translated the housing concerns into legislative solutions. We have another opportunity to continue that record by approving H.R. 920, the Multiple Peril Insurance Act, and H.R. 1682, the Flood Insurance Reform and Modernization Act.

H.R. 920 will create an option within the National Flood Insurance Program to cover both wind and flood risk in one policy. Property owners would be able to purchase insurance and know that it would cover their damages from a major hurricane.

Hurricane Katrina caused massive destruction where it made landfall in Southeast Louisiana and the Mississippi Gulf Coast. The worst destruction in Katrina, as in any major hurricane, was caused by the combination of the highest winds and the storm surge near the eye and in the right front quadrant of the hurricane. Most property owners had evacuated, as demanded by the government, so they were not there to witness and document the damage caused by the four or five hours of hurricane winds that preceded the storm surge.

Katrina's high winds caused damage in six states. Insurance companies paid claims in every county in Mississippi, in almost every parish in Louisiana, in most of Alabama, in South Florida and the Florida panhandle, and even in Georgia and Tennessee. Hundreds of thousands of insurance claims were paid in inland communities where there was no flooding. It is good that companies paid those wind damage claims without lawsuits, but it is irrelevant to the question of how they handled claims where homes were destroyed by the combination of wind and water.

Thousands of homeowners who had purchased all the insurance that was available to them – homeowners, windstorm, and flood coverage – were left with large uncovered losses because several insurance companies blamed all the damage on flooding.

Two weeks after Katrina, State Farm issued a *Wind/Water Claim Handling Protocol* that instructed its adjusters that "Where wind acts concurrently with flooding to cause damage to the insured property, coverage for the loss exists only under flood coverage, if available."

State Farm took the position that covered wind damage became uncovered flood damage once the water reached the property. From court testimony and depositions, we know that State Farm instructed its adjusters to pay the full federal flood claim immediately without conducting a detailed damage assessment. Adjusters have testified that State Farm trained them that the homeowner had the burden to prove that damage was caused by winds, despite the fact that case law and precedents in all state and federal courts place the

burden on the insurance company to prove that the damage is excluded in order to deny claims.

On September 7, 2005, one week after Katrina, hundreds of insurance representatives met in Atlanta with Louisiana Insurance Commissioner Robert Wooley and other government officials, including David Maurstad, Director of the National Flood Insurance Program. Some Members of the Financial Services Committee may recall that at a hearing in this room on February 28, 2007, Robert Hartwig assured Chairwoman Waters that insurance companies had not met to collaborate on how to handle claims from Katrina:

WATERS: Are you aware or do you know or is it common practice for insurance companies to talk with each other, and in particular in the case of Katrina and Rita, Were there conversations? Were there any meetings? Did people get together? Did they talk about how they were going to handle this?

HARTWIG: Absolutely not.

Now we know that there was a meeting in Atlanta right after the storm. A recording of the meeting is on the website of the Louisiana Department of Insurance. In that recording, NFIP Director Maurstad says he already had several conference calls with the larger insurance companies about waiving the requirement for detailed flood adjustments. Maurstad suggested that FEMA might simply look at satellite photos, determine the areas where flooding occurred, and allow insurers to pay those claims without an investigation.

Maurstad did in fact implement that expedited claims procedure on September 21, 2005. The memo from David Maurstad to the Write Your Own insurance companies also includes the statement that "FEMA will not seek reimbursement from the company when a subsequent review identifies overpayments resulting from the company's proper use of the FEMA depth data and a reasonable method of developing square foot value in concluding claims."

In a recent article in the New Orleans *Times Picayune.* The American Insurance Association claimed credit for writing the expedited procedures.

> "We came up with the idea of doing it," said Eric Goldberg, assistant general counsel at the trade group. "We thought there ought to be some sort of policy in place that would enable the (insurance) companies to get money into the hands of consumers when it was absolutely clear that there was damage caused by flooding."[1]

The problem with that procedure is that the existence of flooding does not mean that all of the damage was caused by flooding. It also was absolutely clear that there was damage caused by hurricane winds, but AIA was not in a hurry to get the private insurance checks into the hands of consumers, only the checks from federal taxpayers.

Not only did insurance companies collaborate with one another about how to handle claims, but a lobbyist representing the industry claims credit for writing the government policy that enabled the companies to avoid their obligation to prove how much damage was caused by flooding. To make matters worse, the policy declared that FEMA would not make insurance companies repay federal taxpayers when it is later discovered that they overpaid flood claims using the expedited procedure.

At the September 7, 2005 meeting in Atlanta, Maurstad expressed regret that the NFIP policy limits would not be enough for many people to rebuild their homes. That statement implies that he already believed that the owners of many homes in the surge zone would receive no wind payments.

Under questioning from Ms. Waters at the February 28, 2007 hearing, Maurstad made it clear that he believes NFIP is obligated to pay for wind damage that occurs concurrently with flood damage.

WATERS: ... [A]s I understand it, you could have damage that had occurred by both, some by water, some by wind. Are you telling me you do the assessment, you have the information, you just pay the water, you don't pay the wind or you don't take any of that into consideration? If you have some coverage there, you pay everything?

MAURSTAD: If there is damage that's caused by both flood and wind we are obligated to pay for that damage.

---

[1] Rebecca Mowbray, "*Memo called blank check,*" Times Picayune, June 15, 2007

That means that as a matter of policy, NFIP has agreed to pay for some wind damage for which it has received no premiums. There is substantial evidence that NFIP overpaid and insurance companies underpaid in many cases.

A series of articles in the *Times Picayune* reported the following examples of wind claims shifted to taxpayers:

- Public adjusters who allege that NFIP paid for homes that had no flooding and for roof repairs to homes with minimal flooding;[2]

- Cases in which insurers estimated that identical building materials were more expensive when figuring the amount of the flood payment than when figuring the amount of the wind payment;[3]

- A case in which Allstate added contents that should have been in the upstairs wind claim to the ground floor flood claim that the homeowners had filed.[4]

In both Mississippi and Louisiana, engineering firms rewrote the observations and conclusions of on-site engineering assessments that had concluded that some damage was caused by winds. In many cases, the engineer who rewrote the report had never seen the property. Internal emails from one engineering firm document pressure from State Farm to rig its reports to blame all damage on flooding.

The Multiple Peril Insurance Act will protect homeowners from these tactics by ensuring that their hurricane losses will be covered without needing to hire lawyers, engineers, and public adjusters. The bill also will protect federal taxpayers by preventing insurance companies from shifting their liabilities to the National Flood Insurance Program.

---

[2] Mowbray, "Insurers bilked flood program, suit says, " Times Picayune, May 31, 2007
[3] Mowbray, "Same house. Same repairs. Same insurer. Why different prices?" Times Picayune, May 20, 2007
[4] Mowbray, "Inflated flood claim turns up at trial," Times Picayune, May 20, 2007.

H.R. 920 also will stabilize the insurance markets in coastal areas where insurance companies have stopped writing new policies. In every coastal state from Maine to Texas, insurers are dumping customers into state-sponsored wind pools or other insurers of last resort.

The multiple peril insurance program would enable insurance companies to return to coastal communities without taking on the catastrophic risk they are avoiding. Local insurance agents would sell private homeowners policies covering fire, theft, and liability. They would collect a commission for selling the federal multiple peril coverage, and they would sell private excess coverage above the policy limits of the federal program. Insurance companies should be eager to return to the market to sell homeowners policies without windstorm coverage and offer excess coverage with the equivalent of a $500,000 deductible.

Thank you again for holding this hearing to consider the Multiple Peril Insurance Act. I look forward to working with the committee to address the insurance crisis facing the residents of coastal communities.

Frequently Asked Questions about the Multiple Peril Insurance Act

Rep. Gene Taylor, 4th District of Mississippi

How would the new multiple peril coverage fit into the insurance market?

The new multiple peril insurance program will be available only in communities that participate in the National Flood Insurance Program (NFIP), comply with its flood plain management obligations, and agree to adopt and enforce the windstorm building code obligations that will be created by the bill. Windstorm coverage will be available only as part of the multiple peril package with flood coverage. While any local government theoretically could opt into the program, only coastal communities that face both flood and wind risk have an incentive to do so.

Private insurers have stopped offering windstorm coverage in coastal hurricane-risk areas, but have not abandoned inland markets. Disputes about the cause of hurricane damage arise in coastal areas subject to both the highest hurricane winds and the storm surge. Although many inland communities may face both flood and wind risk, there is no dispute that river or creek flooding is a flood and a tornado and hail damage are caused by windstorms. Those communities have no reason to disrupt their current markets where federal flood coverage and private windstorm coverage are available separately.

Another reason that an unintended expansion of the program is unlikely is that almost all multiple peril policies will be sold by private insurance agents. The multiple peril insurance bill does not create a sales force of federal insurance agents. In coastal areas, local agents whose companies have stopped covering wind risk will sell homeowners policies covering fire, theft, and liability, and earn commissions for the selling the federal policy as they do now with NFIP coverage. Once the multiple peril program is in place, a private market should develop for excess coverage above the policy limits of the multiple peril coverage. Some parts of coastal communities are far enough inland to have little or no flood risk, yet may not have access to private windstorm coverage. State-sponsored wind pools probably will continue to serve those homeowners.

If the program is for coastal areas, why should taxpayers from other regions support the bill?

When a natural disaster causes massive destruction, the property losses either are covered by insurance, absorbed by the property owners themselves, or compensated by taxpayers through direct assistance, tax deductions, and other programs. Federal programs also pay increased costs to compensate for the effects of an economic decline caused by a delayed recovery from a disaster. Taxpayers all across America will benefit when more hurricane damage is covered by insurance premiums rather than by federal disaster assistance.

Private insurers paid $17.5 billion in homeowners insurance claims from Hurricane Katrina, and $20 billion in business and commercial claims. NFIP estimates that it will pay approximately $19.5 billion in Katrina flood claims and adjustment expenses.

The federal government has allocated more than $30 billion for direct housing assistance, including $16.7 in Community Development Block Grants for housing repairs, $7.5 billion for FEMA trailers and mobile homes, and $6 billion for FEMA rental assistance and home repair grants. The Small Business Administration has approved $10 billion in disaster assistance loans to home and business owners. Congress also approved $8 billion in Katrina tax relief, with much of it targeted to deductions for property losses and tax incentives for rebuilding.

Where the private insurance industry has been unwilling or unable to offer insurance for certain risks, the federal government has stepped in to create insurance programs to try to manage risks and collect premiums. Every state participates in the National Flood Insurance Program. The federal government also provides multiple peril crop insurance to protect farmers from disaster losses that private insurers will not cover.

Multiple peril insurance will ensure that homeowners will be able to buy insurance and know that their hurricane damage will be covered. Many Mississippi and Louisiana homeowners built their homes to high standards and bought all the insurance that was available to them - homeowners, windstorm, and flood insurance – yet were left with large uncovered losses because the insurers blamed all the damage on flooding. The maximum NFIP policy is $250,000 for a residential structure. H.R. 920 will permit homeowners to purchase up to $500,000 in multiple peril coverage at risk-based rates.

How would the multiple peril program set actuarially sound premiums?

H.R. 920, the Multiple Peril Insurance Act, does not micromanage the program, but anticipates that NFIP would establish windstorm risks and set premiums in precisely the same manner as insurance companies and state-sponsored wind pools and FAIR plans. NFIP would contract for risk models and loss data in order to estimate potential losses in specific geographic locations. From that community risk profile, premiums for specific properties would be set using existing industry products that adjust for location, construction methods, foundation, wall, and roof types, and other building characteristics.

The bill requires that premiums for multiple peril coverage be based on risks as determined by accepted actuarial principles. The premiums also must include administrative expenses and other operating costs. The bill instructs NFIP to establish regulations detailing the terms and conditions of the program, including risks, premiums, eligibility, and coverage. The bill also instructs NFIP to conduct studies and investigations, enter into contracts and agreements as needed, and coordinate with state and local governments.

How would the new windstorm coverage avoid the financial problems of the existing flood insurance program?

The bill requires the new coverage to be priced at actuarially sound rates. The flood program has intentional subsidies for properties that were grandfathered in because they were built before the flood maps were implemented. The new windstorm coverage does not include any subsidies. Furthermore, it is much easier to determine accurate windstorm risk than to compile accurate flood risk maps for several reasons:

- Thousands of insurance companies and most states offer windstorm coverage, so detailed loss data and risk models are available;
- Wind risk data does not have to be plotted on an ever-changing topographical map;
- Flood risk is much more sensitive than wind risk to changes in land use and development;
- Flood risk in many communities is contingent on levees, dams, pumps, sewer systems, and stormwater infrastructure.

H.R. 1682, the Flood Insurance Reform and Modernization Act, would address some of the problems plaguing the flood insurance program. It would accelerate the Map Modernization program, and study ways to improve and expedite more accurate flood mapping. The bill also would phase out the subsidies for some properties.

It should be pointed out that at least $7 billion in NFIP payments (and many billions more in federal relief funds) would have been saved if the New Orleans levee system had functioned to its design requirements. In Mississippi, the flood maps badly underestimated the storm surge risks. If the Mississippi Coast maps had been accurate, properties would have been built to higher elevations and wave-load standards or would have been subject to higher premiums.

Why should the federal government get involved when the states already have wind pools and FAIR plans?

One federal wind and flood pool can spread coastal risk much more efficiently than dozens of isolated state risk pools. The federal multiple peril insurance pool has several economic advantages that avoid the precarious fiscal condition of state risk pools. A federal pool can spread the risk geographically so that even if one or two states are hit hard in a year, the pool as a whole would be stable.

ISO, the insurance industry's own analyst, explains the economic advantage of a geographically dispersed pool rather than a pool concentrated in one location:

> An insurer with policies spread over many areas has a relatively high chance of suffering hurricane losses in any given year. Wherever a hurricane comes ashore, it's likely to hit some of the properties on which the insurer has written policies. But, in any one year, the insurer faces a

> relatively low likelihood of suffering losses on a substantial proportion of its geographically dispersed policies.
>
> An insurer with policies concentrated in one geographic area has a relatively low chance of experiencing any hurricane losses at all in a given year. The chance of a hurricane hitting any one place is low. But if a storm *does* strike the area where the insurer has concentrated exposures, the insurer faces a higher chance of suffering losses on a substantial proportion of its book of business than does an insurer with more geographically dispersed exposures.[5]

Mississippi has three counties on the Gulf of Mexico and 79 inland counties. Alabama has two counties on the Gulf. South Carolina and Georgia each have only six counties on the Atlantic. State by state wind pools or FAIR plans are not economically or politically capable of spreading their risk or of building up sufficient reserves to handle the claims from major hurricanes.

Insurance companies are dumping more and more policies into state-sponsored insurers of last resort, forcing those plans to go out and buy more and more reinsurance. Last year, the Mississippi wind pool paid $44 million for $350 million in reinsurance. Since Katrina, the risk in the Mississippi wind pool has risen from $1.6 billion to $6 billion. The state has used $80 million in federal CDBG funds to subsidize the wind pool for two years so that premiums doubled rather than quadrupling. Those federal tax dollars passed through the state and the wind pool to pay reinsurance premiums.

Other state-sponsored insurers of last resort are in a similar dilemma – increasing premiums to pay increasing reinsurance costs without building up their reserves. The Texas wind pool recently agreed to pay $170 million for $1 billion in reinsurance. Last year, the Massachusetts FAIR Plan bought reinsurance for the first time, paying $38.4 million for $455 million in coverage. The insurers of last resort in Texas, Massachusetts, and every coastal state between them have had to take on more and more risk.

The federal government would not have to pay for overpriced reinsurance as the state plans and private insurers have been forced to do. The federal government does not have the timing risk that insurers and state plans face. The multiple peril plan would not have to immediately build up the enough reserves or buy enough reinsurance to pay for a 100-year event. The plan would charge actuarially sound premiums based on annual loss estimates and administrative expenses. If a year has above average losses, the program would need to borrow from the Treasury, but would be able to repay the loan with future premiums.

---

[5] *Managing Catastrophe Risk,* ISO Properties, 1996.