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TESTIMONY OF

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U.S. HOUSE OF REPRESENTATIVES
COMMITTEE ON FINANCIAL SERVICES
SUBCOMMITTEE ON HOUSING AND INSURANCE

HEARING ON
"THE FACTORS INFLUENCING THE HIGH COST OF INSURANCE FOR CONSUMERS"

NOVEMBER 2, 2023

Chairman Davidson, Ranking Member Cleaver, and members of the Subcommittee on Housing and Insurance, thank you for the opportunity to testify during today's hearing on "The Factors Influencing the High Cost of Insurance for Consumers," and thank you for your interest in the U.S. property casualty (re)insurance industry.

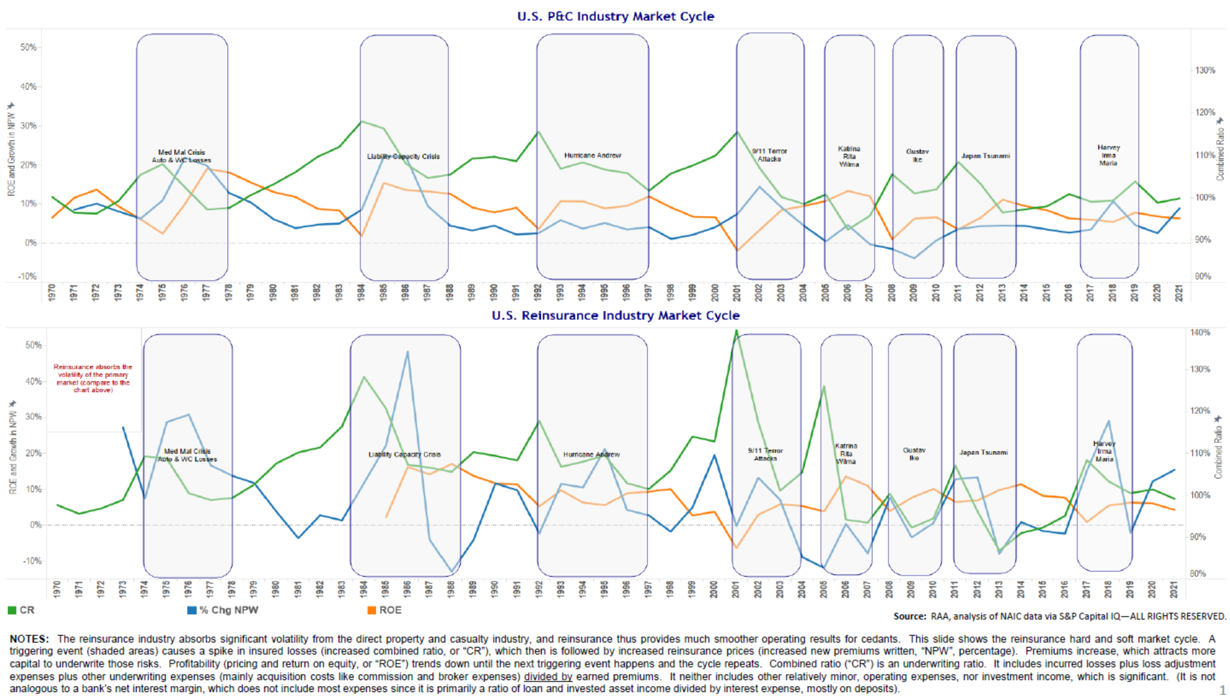
I am Frank Nutter, President of the Reinsurance Association of America (RAA). The RAA is the leading trade association of property and casualty reinsurers doing business in the United States. RAA membership is diverse, including reinsurance underwriters and intermediaries licensed in the U.S. and those that conduct business on a cross border basis. The RAA also has life reinsurance affiliates and insurance-linked securities (ILS) fund managers and market participants that are engaged in the assumption of property/casualty risks. The RAA represents its members before state, federal and international bodies.

The RAA appreciates the Committee facilitating a discussion on what is driving up costs in the U.S. property insurance market. My testimony will provide a brief overview of reinsurance, discuss factors that contribute to the cost of property insurance and reinsurance, and offer a few recommendations.

Reinsurance

Reinsurance is essentially insurance for insurance companies. It is a successful, critical, and efficient risk management tool used by private sector companies and government programs to provide a crucial safety net for low frequency, high severity natural and man-made events that result in extreme insured losses. Figure 1 includes two U.S. property and casualty industry graphs that demonstrate this by showing over 50 years of data, dating back to 1970. For example, the peaks in the U.S. Reinsurance Industry Market Cycle show that reinsurance absorbed the most significant insured event losses in the U.S. (See Appendix A for a larger version of Figure 1).

Figure 1.



Reinsurance helps the private sector companies and government programs improve capacity and financial performance, enhance financial security, and reduce financial volatility. Insurers rely on reinsurers to assume losses for a single event or, in many cases, for an accumulation of losses from hurricanes, earthquakes, winter storms, wildfires, or terrorist attacks. Some historic events illustrate this. Hurricanes Katrina, Rita and Wilma in 2005 caused over $92 billion in insured losses, and reinsurers bore around 28% of the losses from those events.[1] Reinsurers assumed 55% of $41 billion in insured losses from the terrorist events of September 11.[2] Superstorm Sandy caused $25 billion in insured losses with reinsurers taking 30% of those losses.[3]

Reinsurance also is the primary mechanism for spreading risk globally, thereby accessing a greater pool of capital to pay for inevitable catastrophic losses. Reinsurance is extensively used by the private markets to diversify risk and protect against future losses. Reinsurance is purchased for

[1] Holborn Corporation, "Holborn Perspectives, Looking Closer At…SuperStorm Sandy," December 12, 2012
[2] Holborn Corporation, "Holborn Perspectives, Looking Closer At…SuperStorm Sandy," December 12, 2012
[3] Holborn Corporation, "Holborn Perspectives, Looking Closer At…SuperStorm Sandy," December 12, 2012

essentially four reasons: (1) to limit liability on specific risks; (2) to stabilize loss experience; (3) to protect against catastrophes; and (4) to increase capacity. Depending on the purchaser's goals, different types of reinsurance contracts are available to bring about the desired result.

For federal programs, purchasing reinsurance can mitigate the financial impact of any large-scale future losses and help to prevent any future funding lags as it is pre-arranged financing for losses. Reinsurance also allows federal programs to gain financial flexibility and not be forced to rely on emergency federal funding in the event of defaults that could put programs in jeopardy. Reinsurance has been used by federal programs, including FEMA's National Flood Insurance Program (NFIP), the Export-Import Bank of the U.S. (EXIM), and the Government Sponsored Enterprises (GSEs), Fannie Mae and Freddie Mac. It also has been used by state programs, including the California Earthquake Authority, California Wildfire Fund, Florida Hurricane Catastrophe Fund, and Florida Citizens Property Insurance Corporation.

Consistent with the intent of Congress, reinsurers believe the private sector can and should voluntarily assume more Federal government risk and help manage exposure to losses. The use of private capital will protect consumers, taxpayers, and communities, while spreading risk throughout the globe to insurers and other capital providers who are willing to assume such risk. Risk transfer via reinsurance and the capital markets strengthens government programs and private sector insurers by giving them the financial flexibility to ensure they continue to remain viable in the long term. Reinsurers are poised to work with the Congress and the Administration to expand and maximize the Federal government's utilization of the private market to the extent the industry can write the risk.

Reinsurance is not mandated for private sector insurers, the NFIP, EXIM, and the GSEs. It is voluntarily purchased by insurers and government programs. Insurers and government programs have options, including purchasing reinsurance, which is a form of rental capital, or they raise other forms of capital, such as equity or debt. Aon reported that, "Reinsurance remains an accretive source of capital for insurers when compared with debt and equity."[4] In general, when insurers or government programs choose to buy reinsurance, it is because it works for them as a more cost-effective way than the alternatives for them to manage their catastrophic risk.[5] On average, reinsurance capital is less than half the cost of equity capital.[6]

U.S. property and casualty reinsurers are regulated by the states, and non-U.S. property and casualty reinsurers doing business in the U.S. are regulated by other jurisdictions that are recognized as reciprocal jurisdictions by meeting criteria set forth in the 2017 U.S.-EU Covered Agreement and 2018 U.S.-UK Covered Agreement, both of which states have implemented, and the National Association of Insurance Commissioners (NAIC) Uniform Checklist for Reciprocal Jurisdiction Reinsurers.[7]

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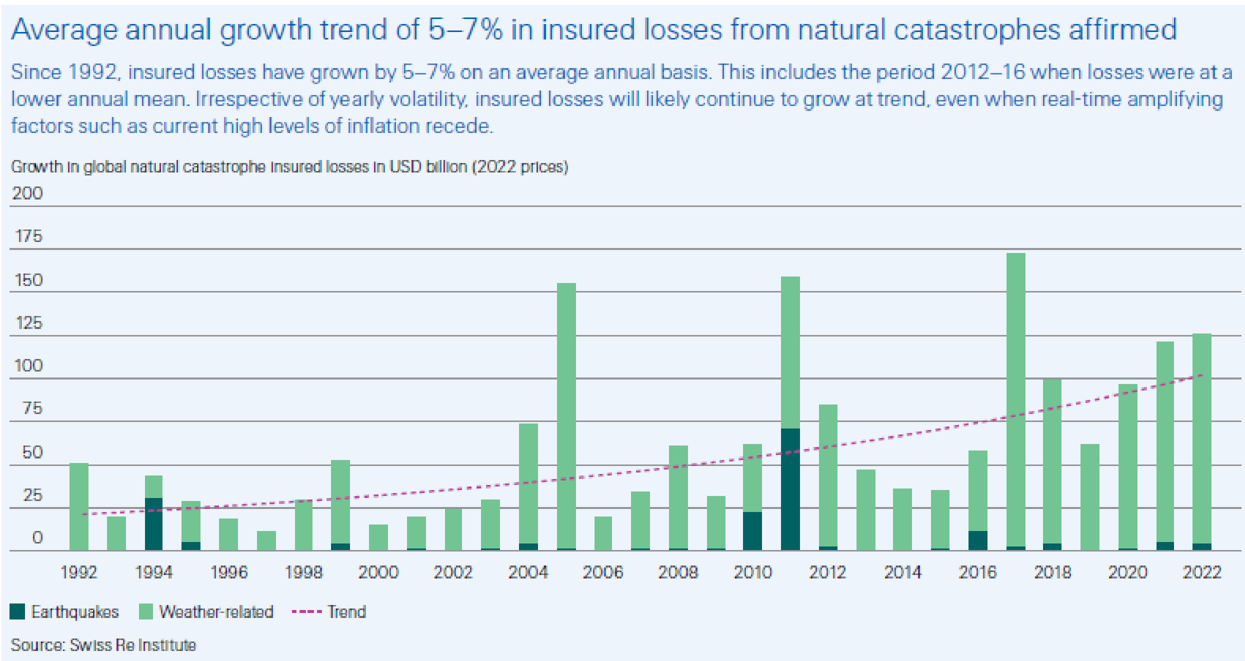
[4] https://www.aon.com/insights/reports/2023/reinsurance-market-dynamics
[5] https://www.reinsurance.org/Fundamentals/Fundamentals_of_Property_and_Casualty_Reinsurance/
[6] https://www.reinsurance.org/RAA/News/2023/RAA_Publishes_White_Paper_on_CA_Homeowners_Insurance_Market/
[7] https://home.treasury.gov/policy-issues/financial-markets-financial-institutions-and-fiscal-service/federal-insurance-office/covered-agreements/us-eu-covered-agreement; https://home.treasury.gov/policy-issues/financial-markets-financial-institutions-and-fiscal-service/federal-insurance-office/covered-agreements/us-uk-covered-agreement; and https://content.naic.org/cmte_e_reinsurance_certified_reciprocal_reinsurers.htm

Extreme Natural Disasters and Insured Losses

Extreme natural disasters have become more frequent and more severe. According to Aon, "2022 is anticipated to rank as the fifth costliest year on record for insurers." Direct economic losses resulting from natural disasters in 2022 are estimated at $313 billion"; and 75% of $132 billion of global insured losses were recorded in the U.S.[8] Two of the top ten events in 2022 were Hurricane Ian, resulting in approximately $52.5 billion in insured losses and the worst drought the U.S. has seen since 2012, which resulted in approximately $8 billion in insured losses.[9] The Swiss Re Institute reported (Figure 2), "Since 1992, insured losses have grown 5-7% on an average annual basis."[10]

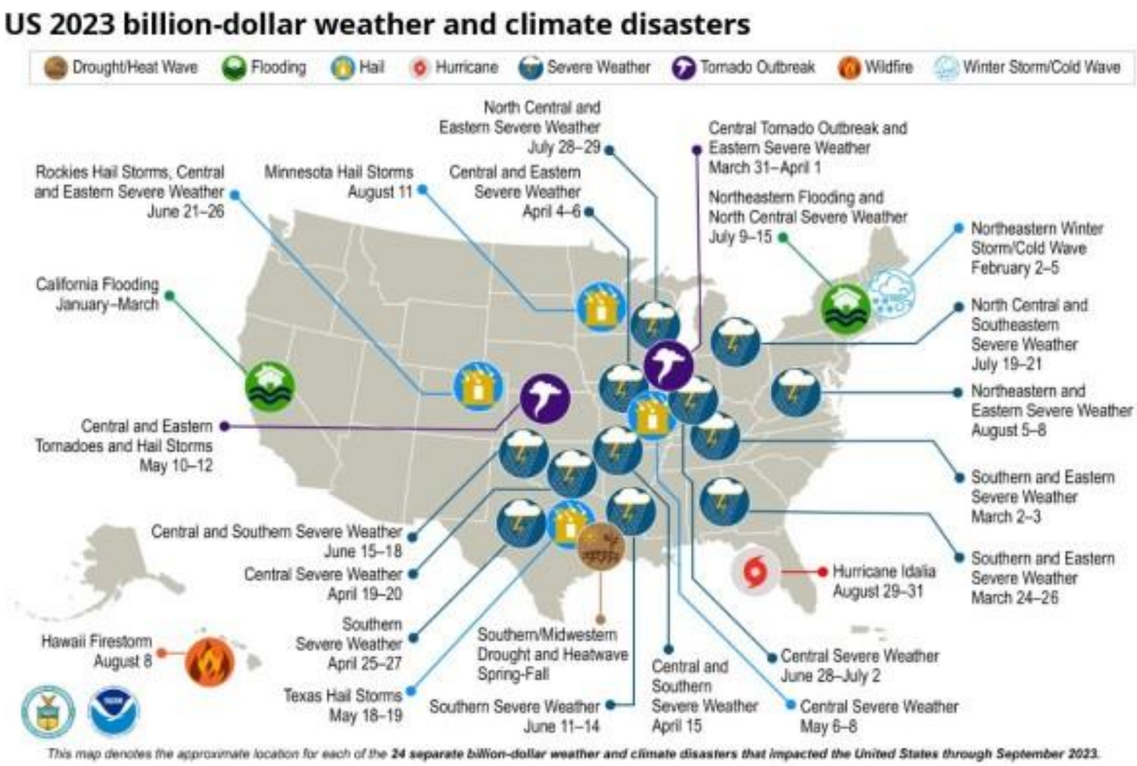
Figure 2.



[8] https://www.aon.com/weather-climate-catastrophe/index.aspx?utm_source=media&utm_medium=org-digital&utm_campaign=0_ri_esg_ins_rin_global_r0&utm_content=engagement_climate-change_read-article
[9] https://www.aon.com/weather-climate-catastrophe/index.aspx?utm_source=media&utm_medium=org-digital&utm_campaign=0_ri_esg_ins_rin_global_r0&utm_content=engagement_climate-change_read-article
[10] https://www.swissre.com/institute/research/sigma-research/sigma-2023-01.html#:~:text=A%20prevailing%20economic%20storm%20in,at%20USD%2050%2D65%20billion.

According to the National Oceanic and Atmospheric Administration (NOAA) National Centers for Environmental Information (NCEI): "In 2023 (as of October 10), there have been 24 confirmed weather/climate disaster events with losses exceeding $1 billion each to affect the United States. These events included 1 drought event, 2 flooding events, 18 severe storm events, 1 tropical cyclone event, 1 wildfire event, and 1 winder storm event. Overall, these events resulted in the deaths of 373 people and had significant economic effects on the areas impacted. The 1980-2022 annual average is 8.1 events (CPI-adjusted); the annual average for the most recent 5 years (2018-2022) is 18.0 events (CPI adjusted)."[11] Figure 3, by NCEI, shows the approximate location of these 24 events that occurred in the U.S. through September 2023.[12]

Figure 3.



Source: National Centers for Environmental Information, NOAA

[11] https://www.ncei.noaa.gov/access/billions/
[12] https://www.ncei.noaa.gov/access/billions/

In July, Gallagher Re reported that for the first six months of 2023, "…insured loss was 18% higher than the decadal average (USD44B) and 39% above the 21st Century average (USD38B)." Gallagher also reported that 13 of the 17 events with insured losses over $1 billion were in the U.S. Figure 4 shows insured losses by peril for the first half of 2023 that that 69% of the losses were due to severe convective storms (SCS), which may produce thunder, hail, strong winds, brief tornadoes, and/or flooding.[13]

Figure 4.

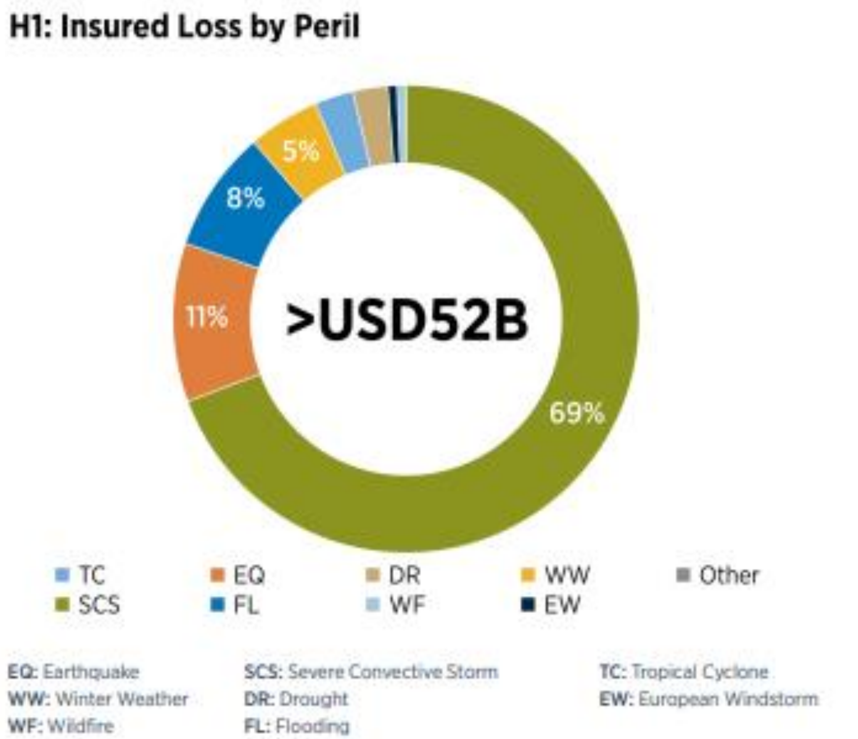
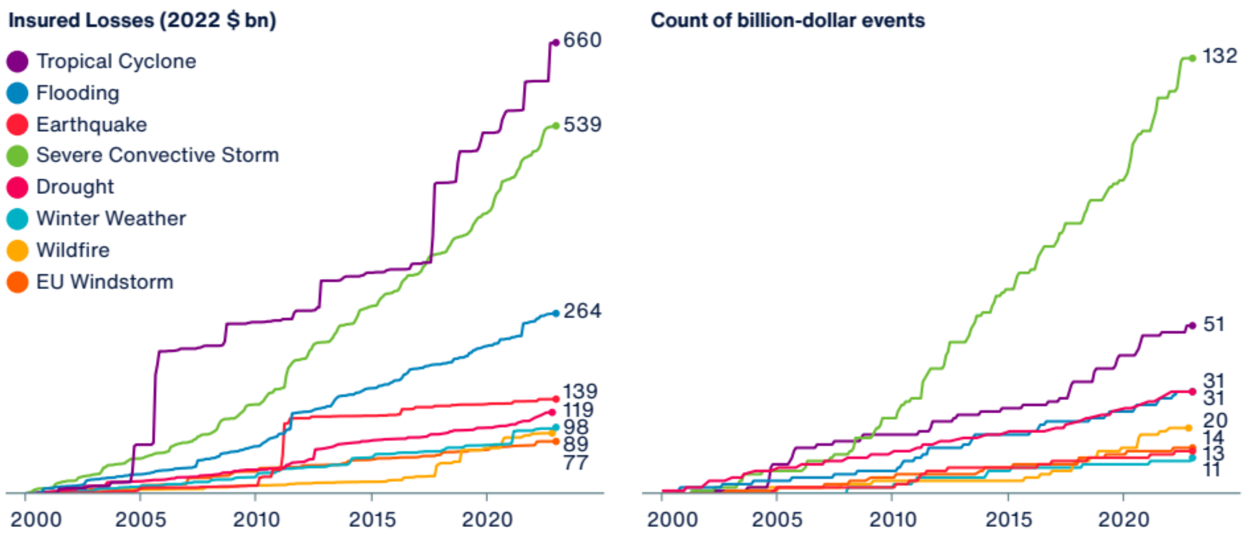


Figure 2: H1 global insured loss statistics. | Data and Graphic: Arthur J. Gallagher & Co.

[13] https://www.ajg.com/gallagherre/news-and-insights/2023/july/2023-natural-catastrophe-report/; https://www.nssl.noaa.gov/education/svrwx101/thunderstorms/types/

According to Aon, "When viewing insured losses on a cumulative basis since the start of the 21st century, Tropical Cyclone is the costliest global peril. Like Earthquake, it is largely driven by extreme loss years and single catastrophic events, as opposed to severe convective storms (SCS) -- losses, which are driven by an increasing frequency of events. Approximately 40 percent of cumulated losses from Tropical Cyclone were caused by only five Atlantic Hurricanes — Katrina, Ian, Irma, Ida and Sandy. On the other hand, the number of costly SCS events outpaced other perils by a large margin."[14] See Exhibit 11.

Exhibit 11: Cumulative Global Insured Losses by Peril



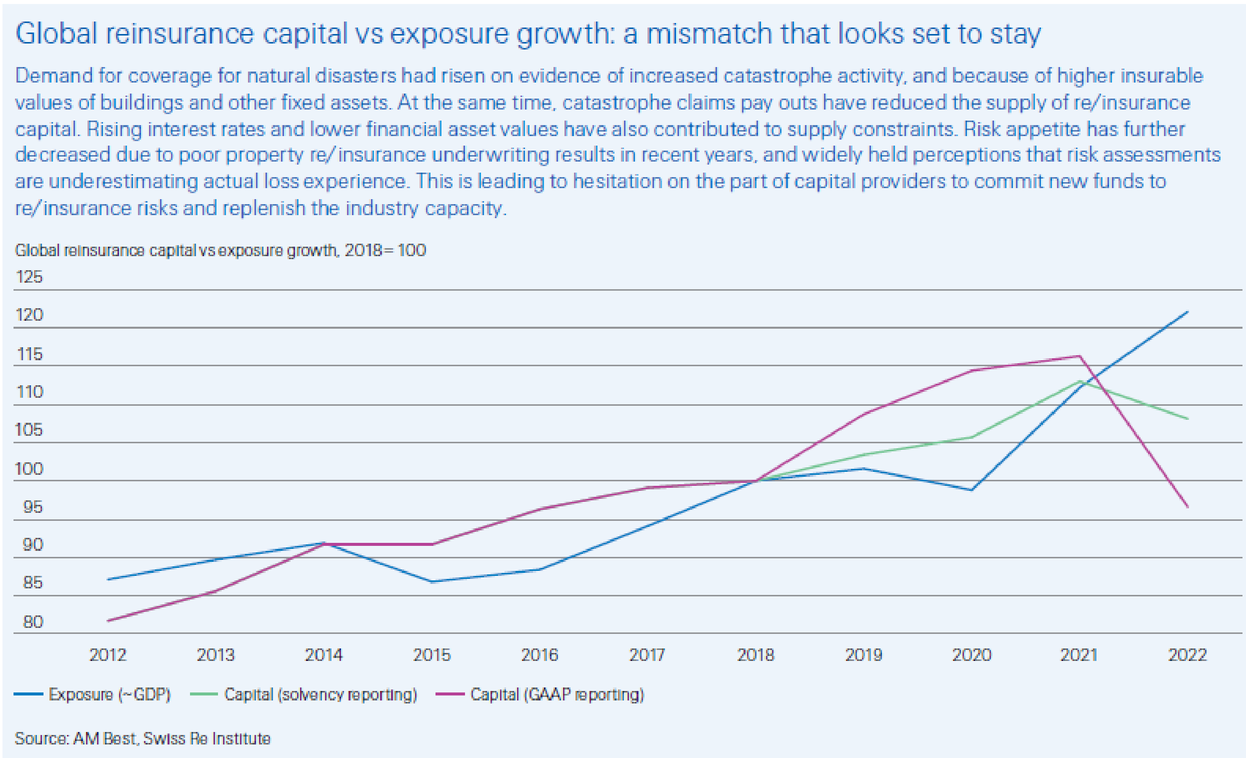
Data: Catastrophe Insight, Aon

[14] https://www.aon.com/weather-climate-catastrophe/index.aspx

Reinsurance Capital

With record-breaking losses, reinsurance exposures have outpaced capital (Figure 5), and insurers have spent more in claims payments and expenses than they collected in premiums.[15]

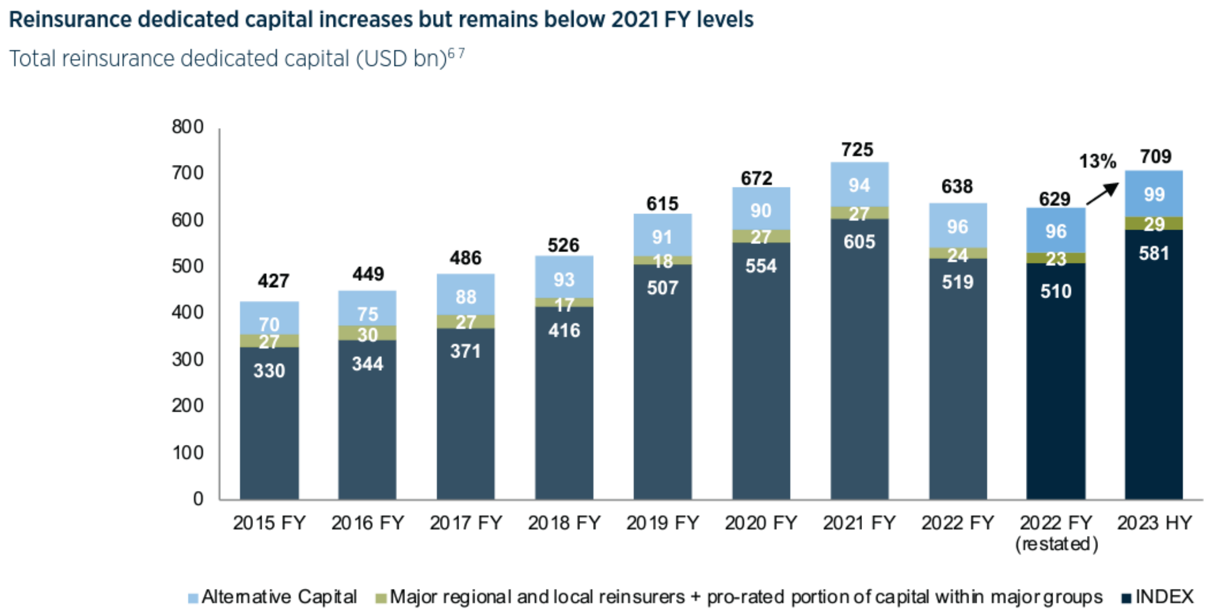
Figure 5.



[15] https://www.swissre.com/institute/research/sigma-research/sigma-2023-01.html#:~:text=Global%20economic%20losses%20from%20natural,from%20natural%20catastrophes%20are%20standard.; and https://www.spglobal.com/marketintelligence/en/news-insights/research/us-pc-insurance-market-report-profitability-to-remain-elusive-in-2023#:~:text=%E2%9E%A4%20The%20S%26P%20Global%20Market,even%20point%20for%20underwriting%20profitability.

However, according to Fitch Ratings "…reinsurers [are] still offer[ing] ample cover against the most severe events…". Gallagher Re's half year 2023 report estimated that reinsurance dedicated capital (Figure 6) rebounded to $709 billion, a "…robust increase in [reinsurers'] capital base…" primarily due to "…unrealized investment appreciation...".[16] In September, Fitch Ratings projected that the reinsurance sector would "…maintain very strong capital in 2024…".[17]

Figure 6.



The reinsurance industry also has continued to support the National Flood Insurance Program. There are 18 reinsurance companies participating in the NFIP Reinsurance program in 2023.[18] In the first year of the program, the benefit of the reinsurance program was evident when FEMA recovered $1.042 billion from 25 reinsurers to help pay the cost of NFIP losses and claims resulting from Hurricane Harvey (2017). This 2017 coverage, which also improved NFIP's financial viability and protected taxpayers, cost $150 million, and the program successfully renewed the subsequent year.

Loss Costs

Several factors contribute to the cost of insurance and reinsurance.

According to the Insurance Information Institute, "Much of the increase can be attributed to supply-chain issues and labor shortages driving up the cost of home repairs and replacement.[19]

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[16] https://www.ajg.com/gallagherre/news-and-insights/2023/september/1h-2023-reinsurance-market-report/
[17] https://www.fitchratings.com/research/insurance/global-reinsurers-pull-back-from-natural-catastrophe-cover-24-08-2023; and https://www.fitchratings.com/research/insurance/global-reinsurance-sector-outlook-revised-to-improving-07-09-2023
[18] https://www.fema.gov/flood-insurance/work-with-nfip/reinsurance
[19] https://www.iii.org/sites/default/files/docs/pdf/state_of_the_risk_homeowners_02032022.pdf

Social inflation is also a factor that contributes to the cost of insurance and reinsurance.[20] For example, a proclamation issued by the Governor of Florida in 2022 stated that "…according to the Office of Insurance Regulation, Florida accounted for 79% of the nation's homeowners insurance lawsuits over claims filed while making up only 9% of the nation's homeowners insurance claims."[21]

Increasingly, more and more people in the U.S. are living near the water and the woods, aesthetically pleasing places to live but also much more dangerous, high-cost areas. According to the Insurance Information Institute, "In the United States much of rising loss trend is due to people moving into risk-prone areas. More people, homes, businesses and infrastructure means more costly damage when extreme weather events occur."[22] In September, this was verified by Verisk: "The growth in exposure values, driven primarily by continued construction in high-hazard areas, and rising replacement costs – largely due to inflation – are the most significant factors responsible for increasing catastrophe losses. The other significant factor is the impact of climate change, which is often cited as the primary reason for the increase in losses. But, while this plays a role, year-over-year growth of exposure and rising replacement values have a far greater short-term impact."[23]

The Insurance Information Institute also published a map (Figure 7) by Aon demonstrating that: "…the number of housing units in the United States has increased most dramatically since 1940 in many areas that are most vulnerable to weather and climate-related damage. Red and purple represent the greatest increases, and these colors disproportionately cluster around hurricane- and flood-prone areas in Florida and Texas, as well as parts of California, Nevada and Washington that are at an elevated risk of wildfire or drought — and, consequently, mudslides and flash floods."[24]

Figure 7.

[20] https://content.naic.org/cipr-topics/social-inflation#:~:text=Issue%3A%20Social%20inflation%20is%20a,monetary%20relief%20for%20their%20injuries.
[21] https://www.flgov.com/2022/04/26/calling-on-the-legislature-to-hold-a-special-session-regarding-property-insurance/
[22] https://www.iii.org/white-paper/flood-beyond-risk-transfer-042921
[23] https://www.verisk.com/newsroom/insurance-industry-faces-average-annual-natural-catastrophe-losses-of-$133b-a-new-high-according-to-verisk-report/
[24] https://www.iii.org/white-paper/flood-beyond-risk-transfer-042921

Uninsured Losses and Subsidized Insurance

In addition to property owners and the insurance industry, the Federal government pays for uninsured losses that result from extreme natural disaster events. In June 2023 Taxpayers for Common Sense reported:[25]

- "Presidential major disaster declarations, which trigger funding of emergency and recovery efforts led primarily by the Federal Emergency Management Agency (FEMA), tripled from 200 in the 1960s to 600 in the first decade of this century. Taxpayers spent more than $120 billion responding to 2017 disasters."

- "To put the high costs of federal disaster spending into perspective, 2017 spending exceeded the annual discretionary budget of every federal agency except the Pentagon that year. A federal agency funded at an amount equal to the 2017 disaster spending would have received more funding than the combined fiscal year appropriations for the Departments of Commerce, Energy, Interior, Labor, Transportation, Treasury, as well as the Environmental Protection Agency and the U.S. Army Corps Engineers."

Ultimately, it is U.S. taxpayers and property owners paying for uninsured losses through emergency government assistance, amounts which are less than compared to claims payments. Federal disaster assistance is provided only when there is a federally declared disaster and typically results in a fraction of what insurance assistance can provide. For example, according to FEMA, the average, annual flood insurance premium was $700 (about $58 per month) in 2019, and the average claim payout was $53,000.[26] Meanwhile, in 2019, federal disaster assistance was capped at $34,900 with an average annual payment of $6,246.[27]

Fully relying on the Federal government for insurance or disaster assistance supported by taxpayers is not a long-term solution. When the Federal government doesn't have sufficient funds to pay for the cost of extreme events, it borrows them. NFIP provides a good example. FEMA's most recent NFIP financial statement, the Program is $20.5 billion in debt.[28] According to the U.S. Government Accountability Office's most recent study on the NFIP: "NFIP was created with competing policy goals—keeping flood insurance affordable and the program fiscally solvent. A historical focus on affordability has led to premiums that do not fully reflect flood risk, insufficient revenue to pay claims, and, ultimately, $36.5 billion in borrowing from Treasury since 2005."[29] Congress cancelled $16 billion of the program's debt in 2017, and NFIP has paid $5.71 billion in interest to the U.S. Department of the Treasury, which also is paying interest on U.S. borrowing to the tune of $659 billion for the federal fiscal year that ended in September, according to a Treasury report issued on Friday. [30]

Congress and FEMA should be commended for taking steps in recent years to address the fundamental flaws in the NFIP and toward removing inequitable and unjustifiable rate subsidies.

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[25] https://www.taxpayer.net/climate/paying-the-price/
[26] https://www.fema.gov/data-visualization/historical-flood-risk-and-costs
[27] https://www.federalregister.gov/documents/2018/10/22/2018-22884/notice-of-maximum-amount-of-assistance-under-the-individuals-and-households-program; FEMA communication with RAA, 4/16/2021
[28] https://www.fema.gov/flood-insurance/work-with-nfip/watermark-financial-statements
[29] https://www.gao.gov/products/gao-23-105977
[30] https://www.fema.gov/flood-insurance/work-with-nfip/watermark-financial-statements; and https://www.washingtonpost.com/business/2023/10/20/interest-debt-payment-treasury/

As a result, the NFIP is today on a path toward a stronger financial framework and resiliency to pay claims without additional borrowing from taxpayers. The RAA urges Congress to avoid retreating from this progress and strongly encourages Congress to fully examine reforms that will improve the program to the benefit of those with homes, businesses, and communities facing flood risk and taxpayers alike. (Please refer to the RAA's testimony before the House Financial Services Subcommittee on Housing, Community Development, and Insurance for its May 25, 2022, hearing on "Reauthorization and Reform of the National Flood Insurance Program" for the RAA's views on flood reform.[31])

Unlike the NFIP, insurers and reinsurers are required by states to have adequate capital to pay for losses, including catastrophic losses. The industry raises capital through premiums paid by consumers -- policyholders and cedents (insurers that purchase reinsurance) -- and investment returns insurers and reinsurers made with those premiums. The investors in turn expect some return on their investment. Consumers expect to be paid if a claim is filed and covered in a (re)insurance agreement. If insurance investors and consumers are not paid for their investment in and purchase of (re)insurance respectively, they will invest their money elsewhere or purchase (re)insurance from another company. Ultimately, insurers and reinsurers investing consumer premiums, allows premiums to stay lower than they would be otherwise, helps the (re)insurer remain solvent after claims are paid, and provides investors with a return on their investment.

Recommendations

What should Congress do about increasing costs of insurance, reinsurance, and federal emergency disaster expenditures?

I. The Federal government should allow each state to manage its own insurance regulatory and legal environment, as each state has unique insurance market challenges. For example, functioning, competitive insurance markets benefit consumers and allow insurers to charge risk-adequate rates to cover losses, so California is moving toward reforms to achieve that.[32] In 2022 and 2023, to reduce social inflation-related loss costs, Florida took significant action to curb litigation abuses and restore balance in the legal system while retaining consumer access to courts. As a result of Florida's reforms, new insurance companies have entered the Florida market in 2023.[33]

   Also, each state faces different perils, and in recent years, record-breaking events. Florida and other Gulf and East Coast states have experienced extreme hurricanes. California and other western states have experienced extreme wildfires. Midwest states have experienced severe convective storms (SCS), which may produce thunder, hail, strong winds, brief tornadoes, and/or flooding.[34]

   We have distributed to each member of the Subcommittee, for their congressional district, data from the Federal Emergency Management Agency's National Risk Index,

[31] https://financialservices.house.gov/calendar/eventsingle.aspx?EventID=408331
[32] https://www.reinsurance.org/RAA/News/2023/RAA_Publishes_White_Paper_on_CA_Homeowners_Insurance_Market/
[33] https://www.insurancejournal.com/news/southeast/2023/08/15/735429.htm
[34] https://www.insurancejournal.com/news/national/2023/04/27/718083.htm; https://www.ajg.com/gallagherre/news-and-insights/2023/july/2023-natural-catastrophe-report/; and https://www.nssl.noaa.gov/education/svrwx101/thunderstorms/types/

which depicts the perils in their congressional district. In short, no congressional district's peril data looks the same.

II. Congress should reform federal programs to provide incentives for people to live in more resilient homes and communities. Investing in pre-disaster mitigation can reduce the impact of future disasters on lives, property, and the economy. The National Institute of Building Sciences 2019 "Natural Hazard Mitigation Saves" report, funded by the U.S. Department of Housing and Urban Development, describes that federal disaster mitigation has saved $6 for every $1 invested since 1995.[35] Other mitigation-related activities, such as updating building codes to ensure resilient structures, and investments can save between $4 and $11 for every $1 spent. Federal agencies in charge of housing programs, transportation and other infrastructure, and forests and waterways, for example, should incentivize property owners and communities to improve resilience against the perils they face. A few examples include encouraging and providing funds for: stronger building codes and enforcement; better land use that promotes nature-based solutions to protect communities; and building fortified homes using standards like those developed by the Insurance Institute for Business & Home Safety.

III. In December 2022, President Biden signed into law the RAA-initiated Community Disaster Resilience Zones Act. It requires the Federal Emergency Management Agency to use a data driven approach to identify and prioritize the most in need and most at-risk communities in the U.S. facing natural hazard risks, directing public sector funds and private-sector resources to these communities to improve resilience. The CDRZ Act was supported by over 30 national organizations (See Appendix B). Last month, FEMA designated the first CDRZ communities to receive hazards assistance for resilience.[36] Congress should use this structure to improve resilience in communities across the U.S. Related to the data used for CDRZ Act implementation and for other purposes, Congress should fund the National Oceanic and Atmospheric Administration (NOAA) and National Aeronautics and Space Administration (NASA) for improved weather and climate risk assessment.

IV. In addition to increasing funding for pre-disaster mitigation grants for FEMA programs, such as the Building Resilient Infrastructure and Communities (BRIC), and other agency programs, Congress should establish more cost-effective ways to improve U.S. resilience instead of only appropriating limited federal funding. For example, based on the CDRZ act passed in December 2022, Congress should enact tax legislation that would incentivize the private sector to invest in resilience obligations issued by Federal, state and local governments. These financing vehicles would leverage federal spending with private capital to fund pre-disaster mitigation projects that reduce risk, improve resilience, and create insurable communities. And Congress should enact other common-sense legislation, including the "Disaster Mitigation and Tax Parity Act" to exempt state and local mitigation grants from federal taxation; and the

[35] https://www.nibs.org/projects/natural-hazard-mitigation-saves-2019-report

[36] https://www.fema.gov/press-release/20230906/fema-designates-first-communities-receive-targeted-assistance-hazards#:~:text=FEMA%20Designates%20First%20Communities%20to%20Receive%20Targeted%20Assistance%20for%20Hazards%20Resilience,-English&text=WASHINGTON%20%E2%80%93%20Today%2C%20FEMA%20is%20announcing,worsened%20by%20the%20climate%20crisis.

"Strengthening Homes and Eliminating Liabilities Through Encouraging Readiness (SHELTER) Act" to provide a disaster mitigation tax credit of 25% of qualifying mitigation expenses of up to $2,500 for individuals and $5,000 for businesses.[37]

V. Given the likelihood of future, significant, and costly natural disasters throughout the U.S. and uninsured residential costs, it is important to have a coordinated effort focusing on closing the insurance protection gap. That effort should include traditional insurance and risk transfer as well as innovative risk transfer mechanisms for communities. The National Association of Insurance Commissioners cited a statistic that "Only 1% of properties outside of flood zones have flood insurance, yet half of U.S. floods occur in these areas." A 2018 report by AIR Worldwide (now Verisk), warned that the next big earthquake to impact California, likely by 2044, could result in $170 billion in total damage and almost half would be residential-related loss, $37 billion of which would be uninsured.[38] The Federal Advisory Committee on Insurance (FACI) "Subcommittee on Addressing the Protection Gap through Public-Private Partnerships and Other Mechanisms" issued recommendations to achieve the goal of closing the flood insurance program gap.[39]

What should Congress <u>not</u> do?

Congress should not create a new federal property (re)insurance program to displace the insurance industry or states' regulatory role. Like the NFIP historically, such a federal program would likely subsidize premiums so they do not reflect property risk and expected loss, which can mask the true risk of a property, encourage ownership of property in hazard-prone locations, discourage property builders and owners from building properties that are resilient against natural hazards, and discourage pre-disaster mitigation of properties. A federal (re)insurance program would increase the cross subsidy from low or no risk persons and taxpayers to those living in high-risk areas. The classic "robbing Peter to pay Paul" analogy applies. Insurance subsidies or artificially low rates also have facilitated the development of environmentally sensitive coastal areas, including those at high risk to losses caused by natural disasters. Finally, like private sector insurers and reinsurers, unless government-chartered insurance programs have sufficient capital, they can become insolvent, just like the NFIP. Appendix C includes a letter by the SmarterSafer Coalition that opposes a federal reinsurance program and outlines concerns expressed by environmental groups, taxpayer advocates, insurance interests, housing organizations, and mitigation advocates.[40]

<u>Conclusion</u>

The RAA looks forward to continuing to work with you to address the very real, dangerous, and costly challenges caused by extreme natural disaster events that are increasingly impacting consumers, taxpayers, communities, and our industry and others. We must work together to increase the resiliency of our country. Thank you for your consideration of our views.

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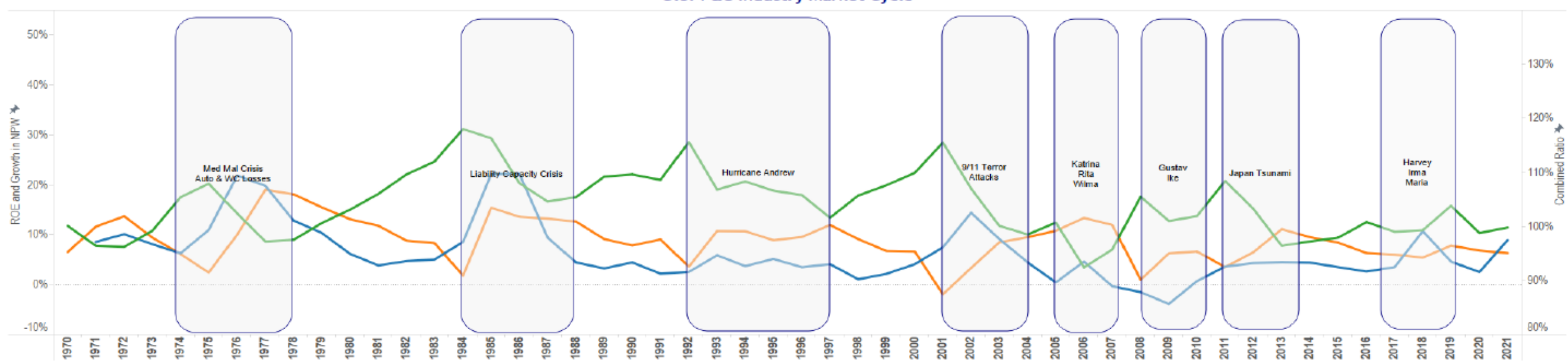
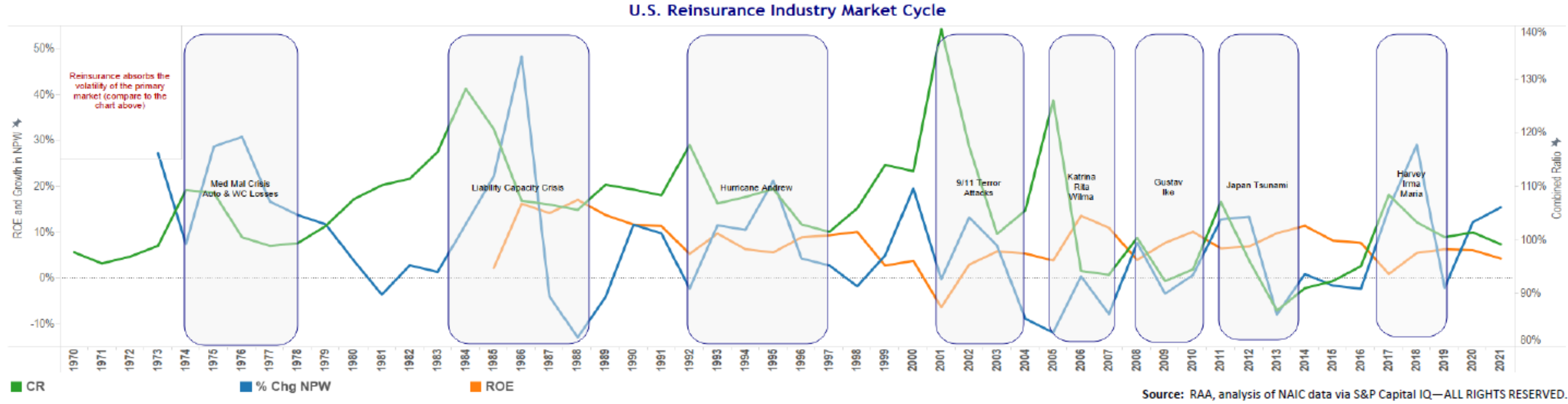
[37] https://www.congress.gov/bill/118th-congress/house-bill/4070; https://www.congress.gov/bill/118th-congress/house-bill/4305
[38] https://www.air-worldwide.com/Publications/Infographics/Who-Will-Pay-for-the-Next-Great-California-Earthquake-/
[39] https://home.treasury.gov/system/files/311/December2019FACI_ProtectionGapPresentation.pdf; https://home.treasury.gov/system/files/311/December2019FACI_ProtectionGapProposedRecs.pdf; and https://www.air-worldwide.com/Publications/Infographics/Who-Will-Pay-for-the-Next-Great-California-Earthquake-/
[40] https://www.smartersafer.org/2023/09/13/smartersafer-coalition-raises-concerns-about-federal-reinsurance-program-to-senate-banking-committee-leaders/

APPENDIX A

U.S. P&C Industry Market Cycle



U.S. Reinsurance Industry Market Cycle



Source: RAA, analysis of NAIC data via S&P Capital IQ—ALL RIGHTS RESERVED.

NOTES: The reinsurance industry absorbs significant volatility from the direct property and casualty industry, and reinsurance thus provides much smoother operating results for cedants. This slide shows the reinsurance hard and soft market cycle. A triggering event (shaded areas) causes a spike in insured losses (increased combined ratio, or "CR"), which then is followed by increased reinsurance prices (increased new premiums written, "NPW", percentage). Premiums increase, which attracts more capital to underwrite those risks. Profitability (pricing and return on equity, or "ROE") trends down until the next triggering event happens and the cycle repeats. Combined ratio ("CR") is an underwriting ratio. It includes incurred losses plus loss adjustment expenses plus other underwriting expenses (mainly acquisition costs like commission and broker expenses) divided by earned premiums. It neither includes other relatively minor, operating expenses, nor investment income, which is significant. (It is not analogous to a bank's net interest margin, which does not include most expenses since it is primarily a ratio of loan and invested asset income divided by interest expense, mostly on deposits).

1

APPENDIX B

December 5, 2022

The Honorable Peter DeFazio
Chairman
Committee on Transportation
and Infrastructure
U.S. House of Representatives
2165 Rayburn House Office Building
Washington, DC 20515

The Honorable Sam Graves
Ranking Member
Committee on Transportation
and Infrastructure
U.S. House of Representatives
2164 Rayburn House Office Building
Washington, DC 20515

Dear Chairman DeFazio and Ranking Member Graves:

We, the undersigned organizations, write to express support for S. 3875, the Community Disaster Resilience Zones (CDRZ) Act of 2022, which the Senate passed by unanimous consent and is nearly identical to the bill (H.R. 7242) your committee passed. Collectively, our organizations represent a wide variety of constituencies, including business, conservation, emergency managers, housing, infrastructure, local government, public safety, science, and taxpayer organizations. We commend the CDRZ Act bill sponsors, Representatives Sharice Davids and Garret Graves and Senators Gary Peters and Rob Portman, for their bipartisan, bicameral leadership and thank them for introducing the CDRZ Act bills. This legislation is a critical, foundational step toward prioritizing and directing a whole-of-nation focus on the most vulnerable communities facing the risk of potentially life-threatening and economically devastating climate and natural disaster events.

The CDRZ Act would amend the Stafford Act to establish a statutory structure to identify and designate CDRZ communities that are the most in need and most at risk to natural hazards, such as hurricanes, flooding, earthquakes, and wildfires, to increase public and private sector investments in housing, infrastructure, and community-wide resilience. Building smart, modern, resilient infrastructure, including nature-based infrastructure, has long been among our top priorities. We support the CDRZ Act, which would:

- Amend the Stafford Act by adding a requirement that FEMA maintain and update products and tools that define natural hazard risk across the U.S. and use that dataset to identify and designate CDRZ communities that are the most in need and most at risk to natural hazards;

- Authorize the President to provide CDRZ-designated communities with assistance and funding for pre-disaster mitigation planning and projects to increase resilience against the identified hazards; and

- Help prioritize and attract additional public and private sector funding (including public-private partnerships) for resilience projects in or primarily benefitting CDRZ-designated communities.

Thank you for your leadership. We look forward to continuing to work with you and Congress to ensure our communities most threatened by climate and natural disaster risk and most economically vulnerable have the support, resources, and opportunities they need to improve their resilience.

Sincerely,

US Resiliency Council (USRC)
U.S. Chamber of Commerce
Taxpayers for Common Sense (TCS)
SmarterSafer Coalition
SBP
Resilience Innovation Hub
Reinsurance Association of America (RAA)
R Street Institute
National Wildlife Federation (NWF)
National Special Districts Coalition (NSDC)
National Institute of Building Sciences (NIBS)
National Housing Conference (NHC)
National Emergency Management Association (NEMA)
National Association of Mutual Insurance Companies (NAMIC)
National Association of Counties (NACo)
Interstate Council on Water Policy (ICWP)
International Code Council (ICC)
International Association of Emergency Managers (IAEM)
Insurance Institute for Business & Home Safety (IBHS)
Ecological Restoration Business Association (ERBA)
The Council of Insurance Agents & Brokers (CIAB)
Central United States Earthquake Consortium (CUSEC)
Center for Climate and Energy Solutions (C2ES)
BuildStrong Coalition
Big City Emergency Managers (BCEM)
American Society of Landscape Architects (ASLA)
American Society of Civil Engineers (ASCE)
American Property Casualty Insurance Association (APCIA)
American Planning Association (APA)
American Institute of Architects (AIA)
American Council of Engineering Companies (ACEC)
After the Fire: Recover. Rebuild. Reimagine. (ATF3R)

cc: The Honorable Sharice Davids
The Honorable Garret Graves

APPENDIX C

SMARTERSAFER.ORG
Americans for Smart Natural Catastrophe Policy

September 13, 2023

The Honorable Sherrod Brown
Chair
Senate Banking Committee
503 Hart SOB
Washington, D.C. 20515

The Honorable Tim Scott
Ranking Member
Senate Banking Committee
104 Hart SOB
Washington, D.C. 20515

Dear Chair Brown and Ranking Member Scott:

SmarterSafer is a national coalition made up of a diverse chorus of voices who champion a united front for environmentally responsible and fiscally sound approaches to natural catastrophe mitigation and the promotion of public safety. SmarterSafer wishes to comment on the Senate Banking Committee's recent hearing focused on property and casualty insurance markets and policyholders.

We wholeheartedly champion the idea of public/private partnerships and private market participation as means to effectively manage the risks associated with natural disasters while ensuring the financial stability of communities and protecting the environment. Private reinsurance plays a crucial role in this equation. It offers an additional layer of financial support that can be instrumental in helping communities recover from catastrophic events without resorting to overwhelming public funds. As such, we are concerned by any conversation that would displace a vibrant private market with a federal reinsurance program for natural disaster risks, which we believe can have detrimental consequences. Our opposition to the establishment of any such reinsurance backstop revolves around what we view are inherent risks with such a concept.

Firstly, a federal reinsurance program can unintentionally incentivize risky behavior by obscuring the true cost of risk, which private reinsurance reflects. A federal reinsurance program ignores the underlying issues of overbuilding in high-risk areas, inflation, forward looking climate change impacts on severity and frequency of extreme weather and can encourage new development in environmentally sensitive and high-risk areas, putting both the environment and the safety of our communities at risk.

Secondly, establishing a federal reinsurance program would come with significant federal cost (billions) paid for by all taxpayers. A federal reinsurance program also does nothing to address the uninsured that rely on limited federal disaster assistance in the aftermath of natural disasters.

Displacing private insurance and reinsurance with a federal reinsurance program will supersede state-based insurance regulation, providing dual regulation, by adding the federal government as a regulator of property insurance markets across the country and encouraging additional, state-government programs to assume property risk.

SmarterSafer has strong concerns that efforts to establish a federal reinsurance program for natural disaster risks fail to effectively address the challenges posed by such disasters and could incentivize risky behavior, as noted, in addition to shifting financial burdens from the private sector to federal taxpayers, and ultimately hinder the pursuit of more responsible solutions.

We are strong advocates for means-tested assistance in addressing affordability concerns. Moreover, we firmly believe that the ultimate solution lies in reducing risk through proactive mitigation efforts, improving building codes and enforcement, and discouraging construction in hazard-exposed and environmentally sensitive areas. By emphasizing the importance of risk reduction and responsible land use planning, we can not only minimize the need for subsidies and a federal reinsurance program but also promote long-term sustainability and fiscal responsibility.

Furthermore, it is crucial to encourage states to transition to private insurance systems based on risk-based rates, an approach that aligns with the principles of risk-based insurance. This transition ensures that sufficient premiums are collected to cover claims without relying on additional federal taxpayer dollars. In areas where there are affordability concerns, we are strong advocates for means-tested financial assistance, that does not "mask" risk-based rates as they provide important signals of increasing risk.

While the global reinsurance markets have faced certain profitability challenges in recent years, they remain highly solvent. Global reinsurers have had to manage the cover they provide against catastrophic property insurance risks after several years of large catastrophe losses, particularly as prices have failed to keep pace with weather-related losses. Insurers and reinsurers are only able to attract additional investment capital if they are able to offer investors an adequate rate of return. The historically elevated catastrophe and claims activity since 2017 has created doubts on the part of re/insurers and investors, which slowed the capital supply response. However, reinsurers are still offering ample cover for severe catastrophes.[1] While global reinsurance capital in 2022 contracted by $87 billion, by the first quarter of 2023, global reinsurer capital increased by five percent ($30 billion) to $605 billion.[2] Additionally, by the end of the first half of this year, reinsurance capital grew 13% to $709 billion (close to the $725 billion peak in 2021).

The challenges facing reinsurers reflect the challenges facing the larger society. Losses from natural catastrophes, inflation and other factors are increasing exponentially for everyone, including reinsurers, and thus require long-term solutions to reduce future losses. SmarterSafer stands ready to collaborate with you and the Senate Banking Committee to explore alternative, more responsible solutions to the pressing issues surrounding natural disaster policy. We urge the Committee to consider our positions as we collectively work to protect both taxpayers, communities, and the environment.

Thank you for the opportunity to comment. We look forward to future discussions on this important issue.

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[1] https://www.fitchratings.com/research/insurance/global-reinsurers-pull-back-from-natural-catastrophe-cover-24-08-2023

[2] https://www.aon.com/getmedia/5bd28313-9c37-461c-b665-69a910bf0a6a/20230628-midyear-rmd.pdf

SMARTERSAFER.ORG
Americans for Smart Natural Catastrophe Policy

Sincerely,

The SmarterSafer Coalition

MEMBERS

Environmental Organizations

American Rivers
Center for Climate and Energy Solutions (C2ES)
ConservAmerica
Defenders of Wildlife
National Wildlife Federation
Natural Resources Defense Council (NRDC)
The Nature Conservancy
Surfrider Foundation

Consumer and Taxpayer Advocates

Coalition to Reduce Spending
National Taxpayers Union
R Street Institute
Taxpayers for Common Sense
Taxpayers Protection Alliance

Insurer and Reinsurer Interests

American Property Casualty Insurance Association (APCIA)
Association of Bermuda Insurers and Reinsurers (ABIR)
Chubb
Liberty Mutual Group
National Association of Mutual Insurance Companies (NAMIC)
National Flood Association
Reinsurance Association of America
Swiss Re
USAA

Mitigation Interests

Natural Hazard Mitigation Association

Housing

Habitat for Humanity
National Housing Conference
National Leased Housing Association

ALLIED ORGANIZATIONS

Allianz of America
American Conservation Coalition
American Consumer Institute
Center for Clean Air Policy
CoreLogic

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Friends of the Earth
Institute for Liberty
Zurich North Amercica