

Hurricanes Katrina & Rita:

Impacts on the P/C Insurance & Reinsurance Industries

Insurance Information Institute

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Presentation Outline

- **P/C Financial Overview: A Position of Strength**
- **Industry Claims-Paying Resources**
- **Underwriting Performance pre-Katrina**
- **Catastrophe Loss Management:**
 - **Loss estimate overview**
 - **Hurricanes Katrina & Rita's place in history**
 - **Loss distribution (geographic & by line)**
 - **Impact on financial & underwriting performance**
 - **Influence of legal environment on Katrina claims**
- **National Flood Insurance Program Overview**
- **The Role of the Fed. Government & CAT Risk**
- **Managing Natural CATs in a Post-9/11 World**
- **Q & A**

P/C Financial Overview

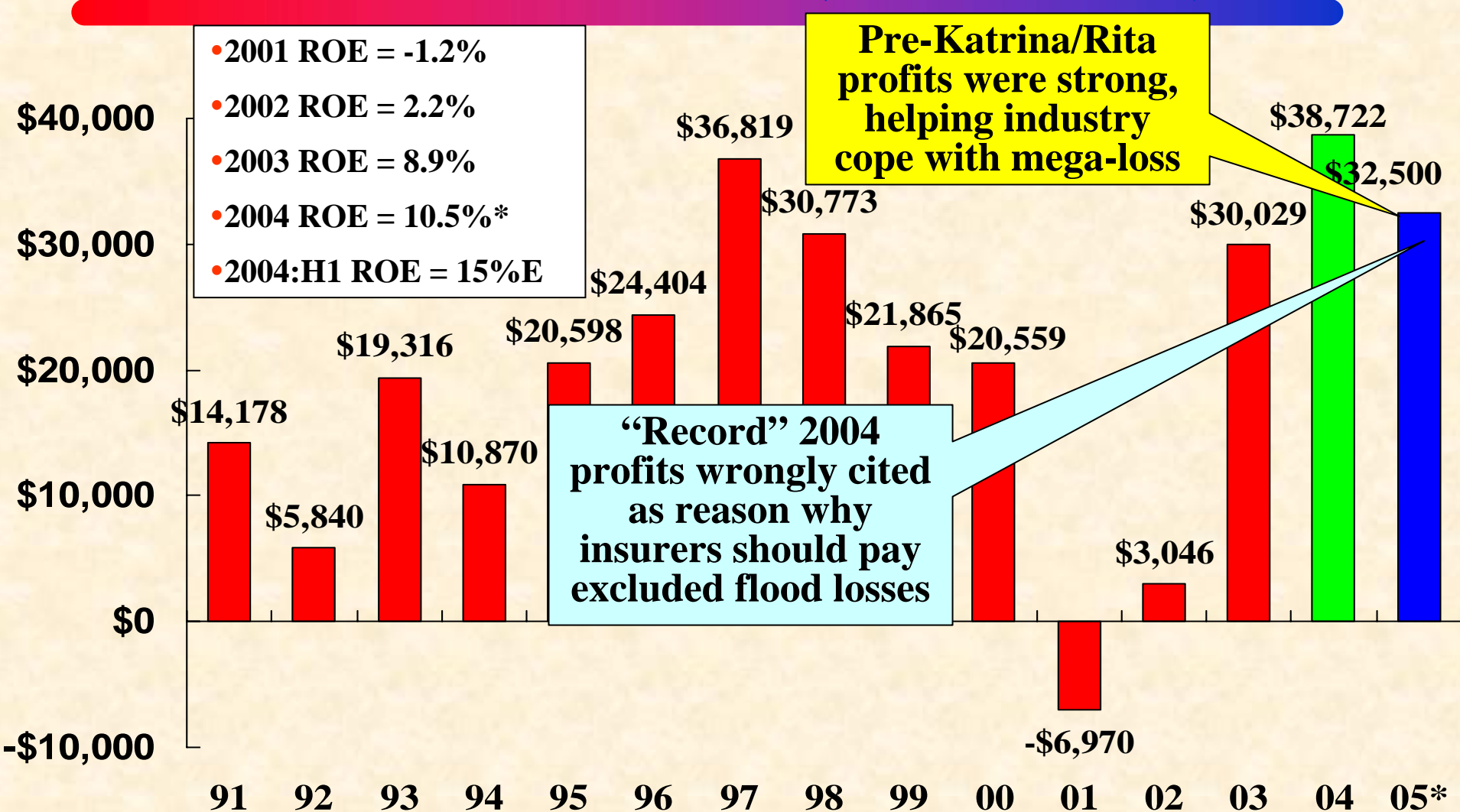
Strong Pre-Katrina

Results Help Industry

!!! *Meet the Challenge*



P/C Net Income After Taxes *1991-2005:H1 (\$ Millions)**



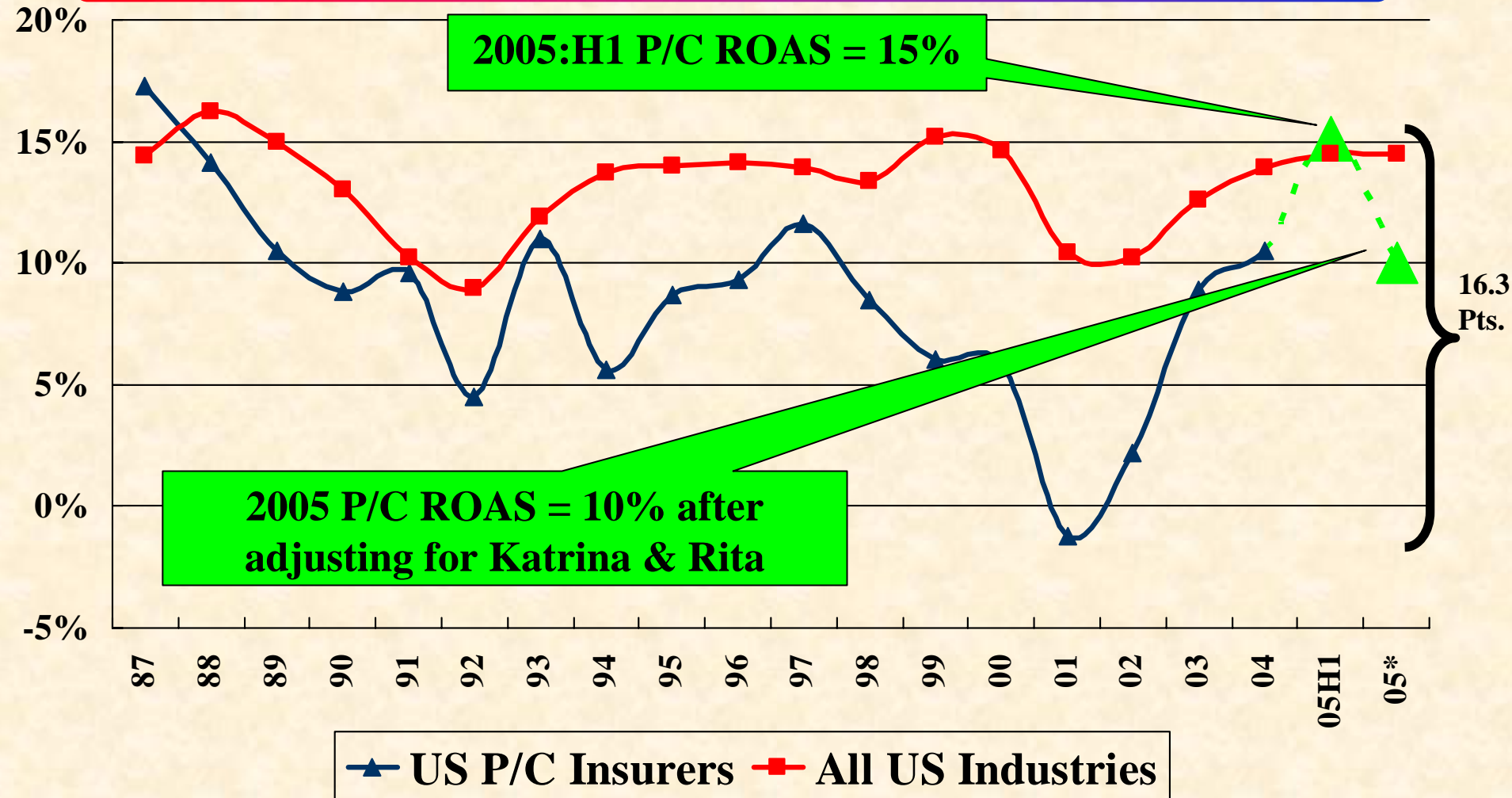
*ROE figures are GAAP; 2004 figure is return on average surplus. 2005 figure is estimate

Sources: A.M. Best, ISO, Insurance Information Institute.



ROE: P/C vs. All Industries

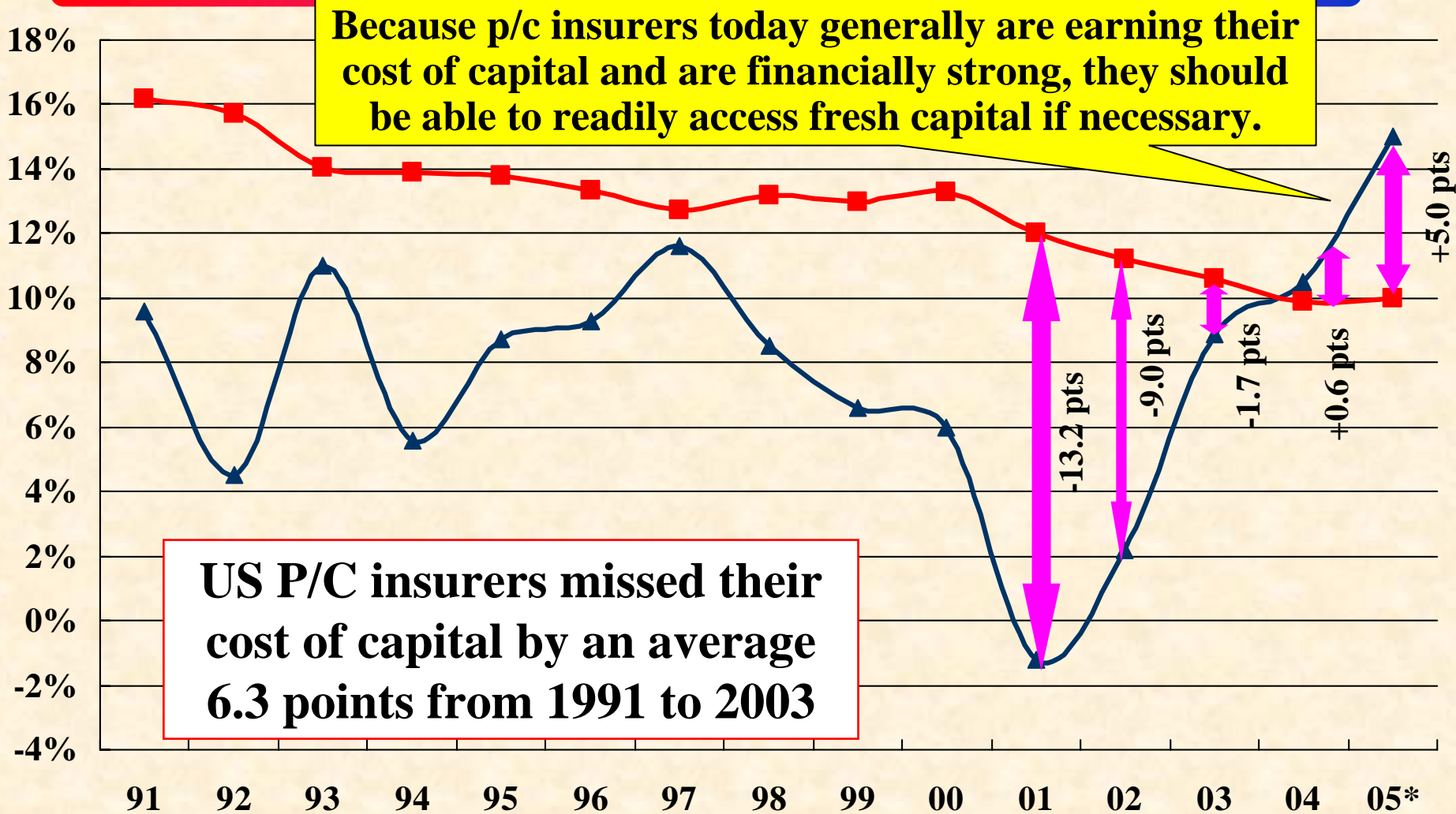
1987–2005F*



*GAAP ROEs except 2004/5 P/C figure = return on average surplus. 2005 figure is Ill full-year estimate.
Source: Insurance Information Institute; *Fortune* for all industry figures



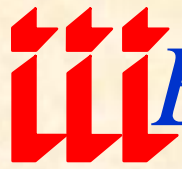
ROE vs. Equity Cost of Capital: US P/C Insurance: 1991 – 2005*



*First half 2005 estimate.

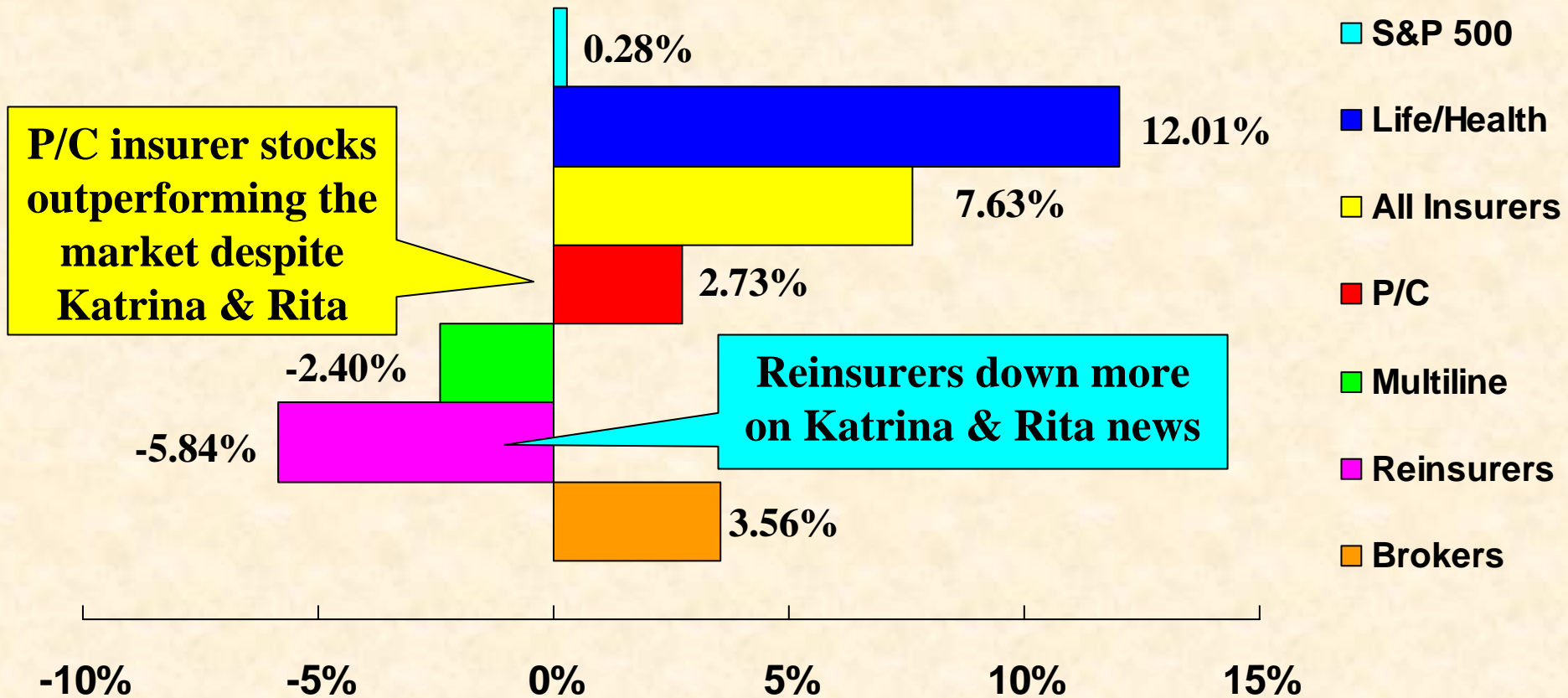
Source: The Geneva Association, Ins. Information Inst.

—▲— ROE —■— Cost of Capital



P/C Insurers Stocks Remain Up, Brokers Up Too, Reinsurers Down

Total Return 2005 YTD Through September 23, 2005

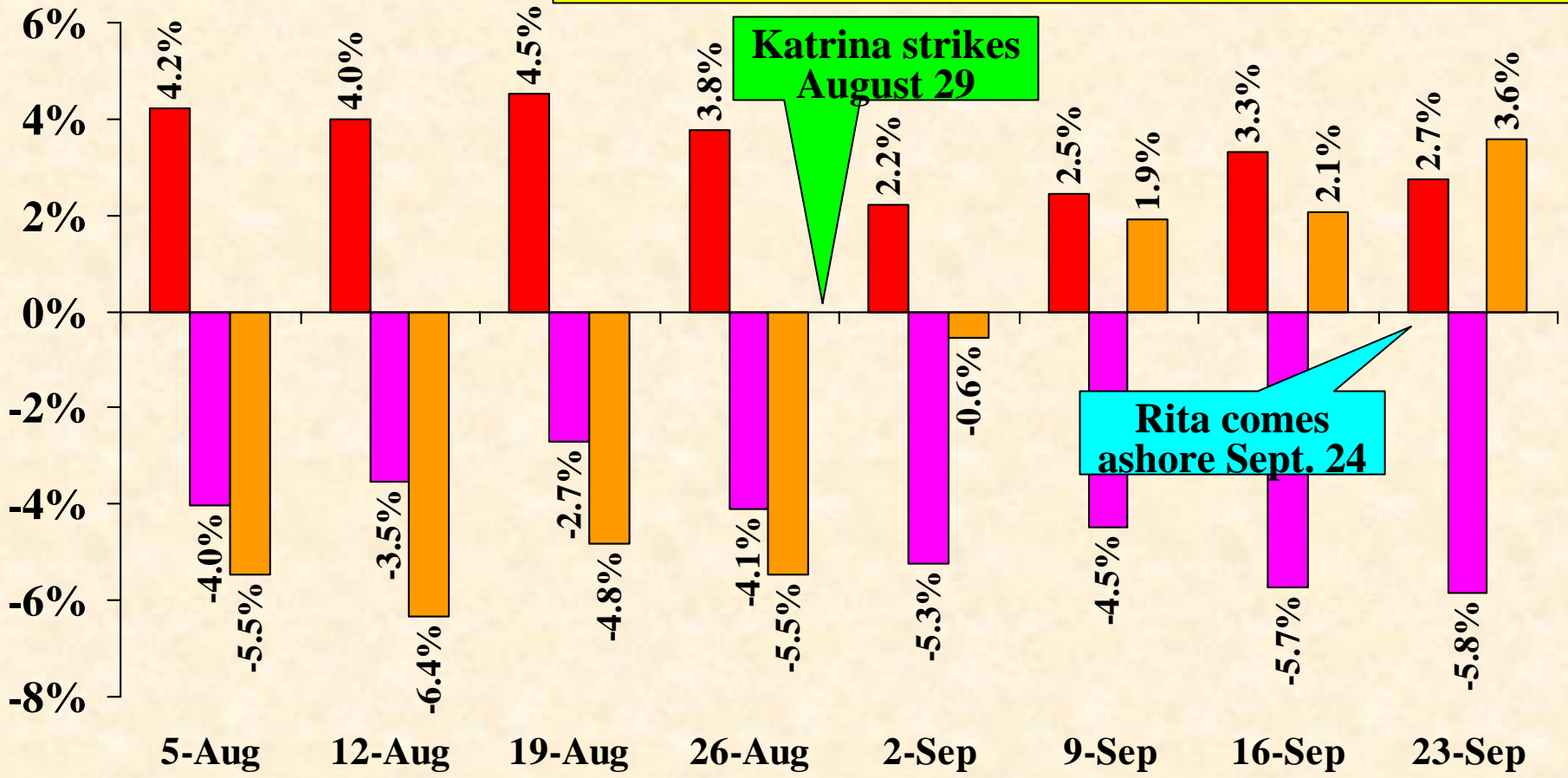


Change in YTD Stock Performance by Sector Pre- & Post-Katrina/Rita



■ P/C ■ Reinsurers ■ Brokers

P/C & reinsurer stocks hurt by Katrina & Rita, broker stocks rose on expectation of tighter conditions and demand for broker services



Katrina strikes August 29

Rita comes ashore Sept. 24

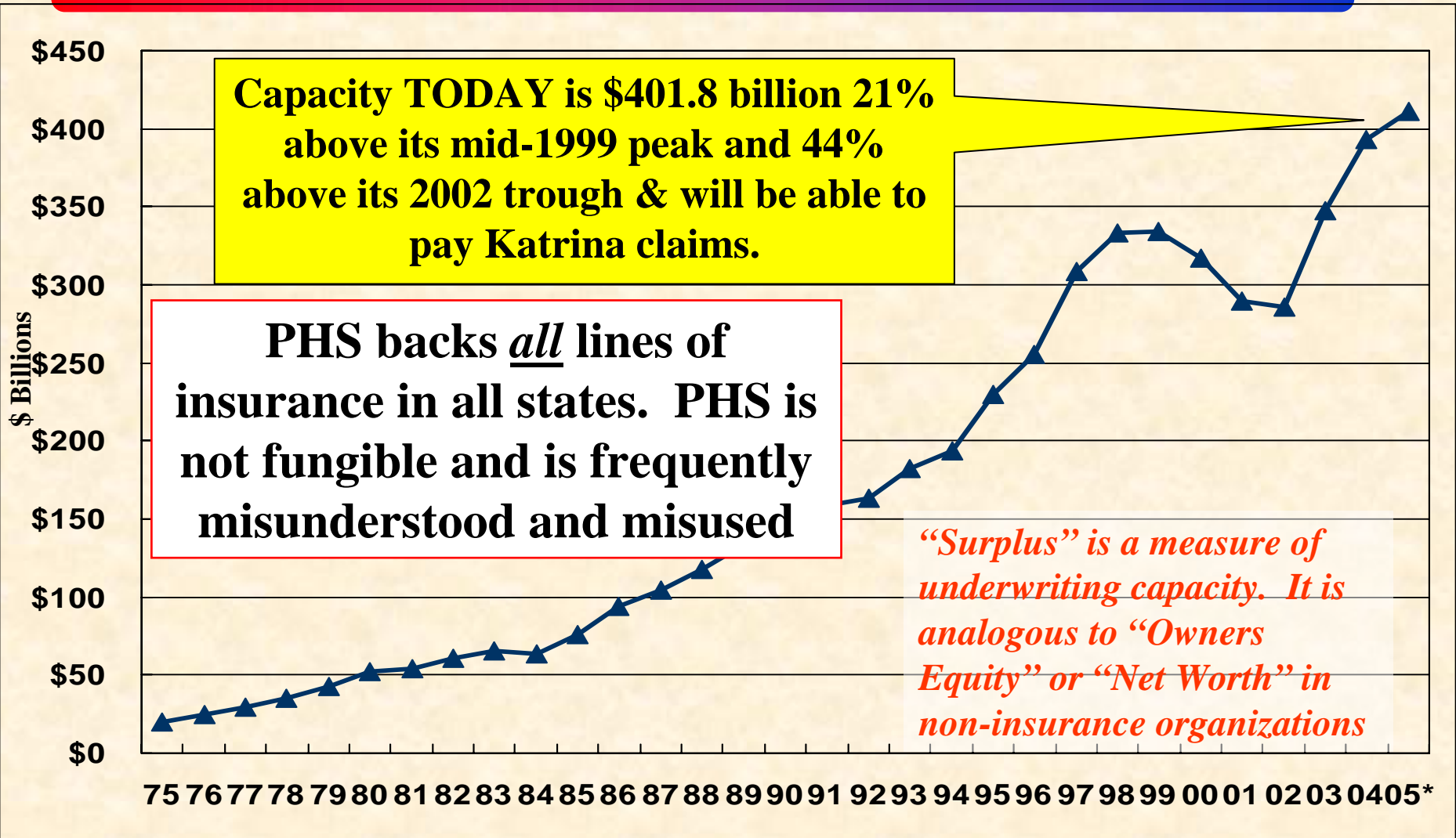
Source: SNL Securities; Insurance Information Institute

Insurer Claims Paying Resources



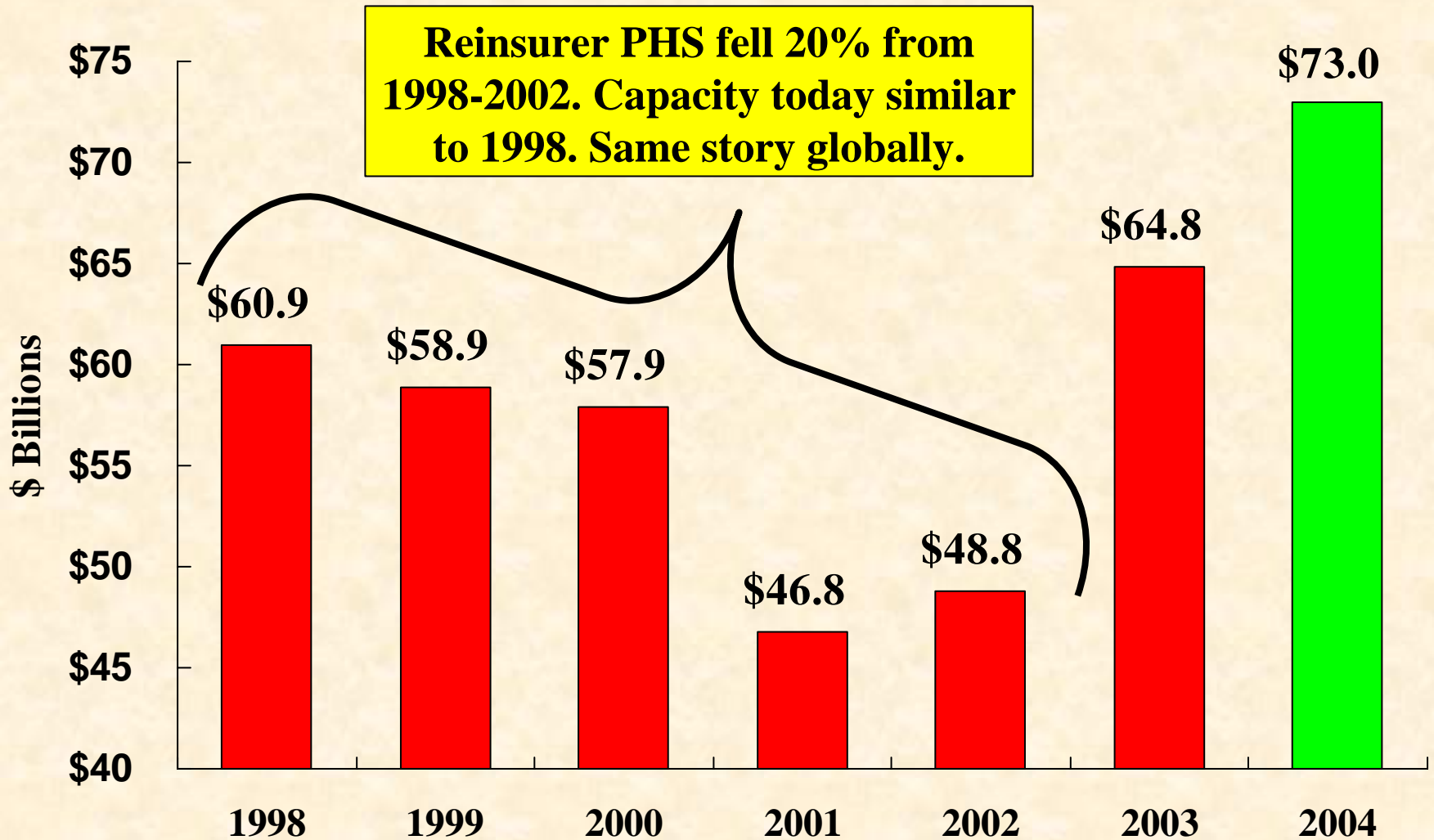


U.S. Policyholder Surplus: 1975-2005*





US Reinsurers: Change in Policyholder Surplus (\$ Billions)



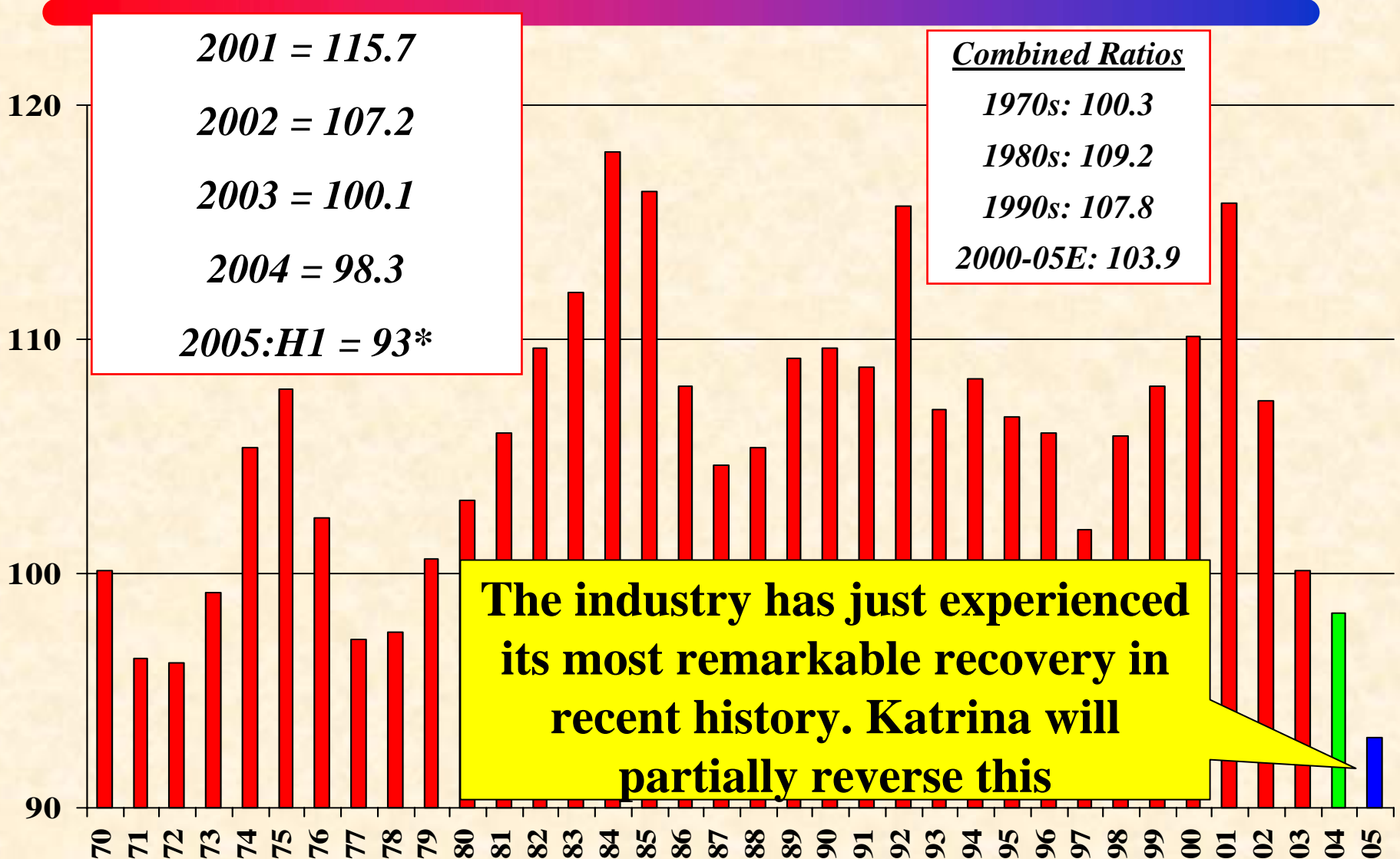
UNDERWRITING

*Strong Underwriting Results
Pre-Katrina Will Help
Industry Weather the Storm*





*P/C Industry Combined Ratio**



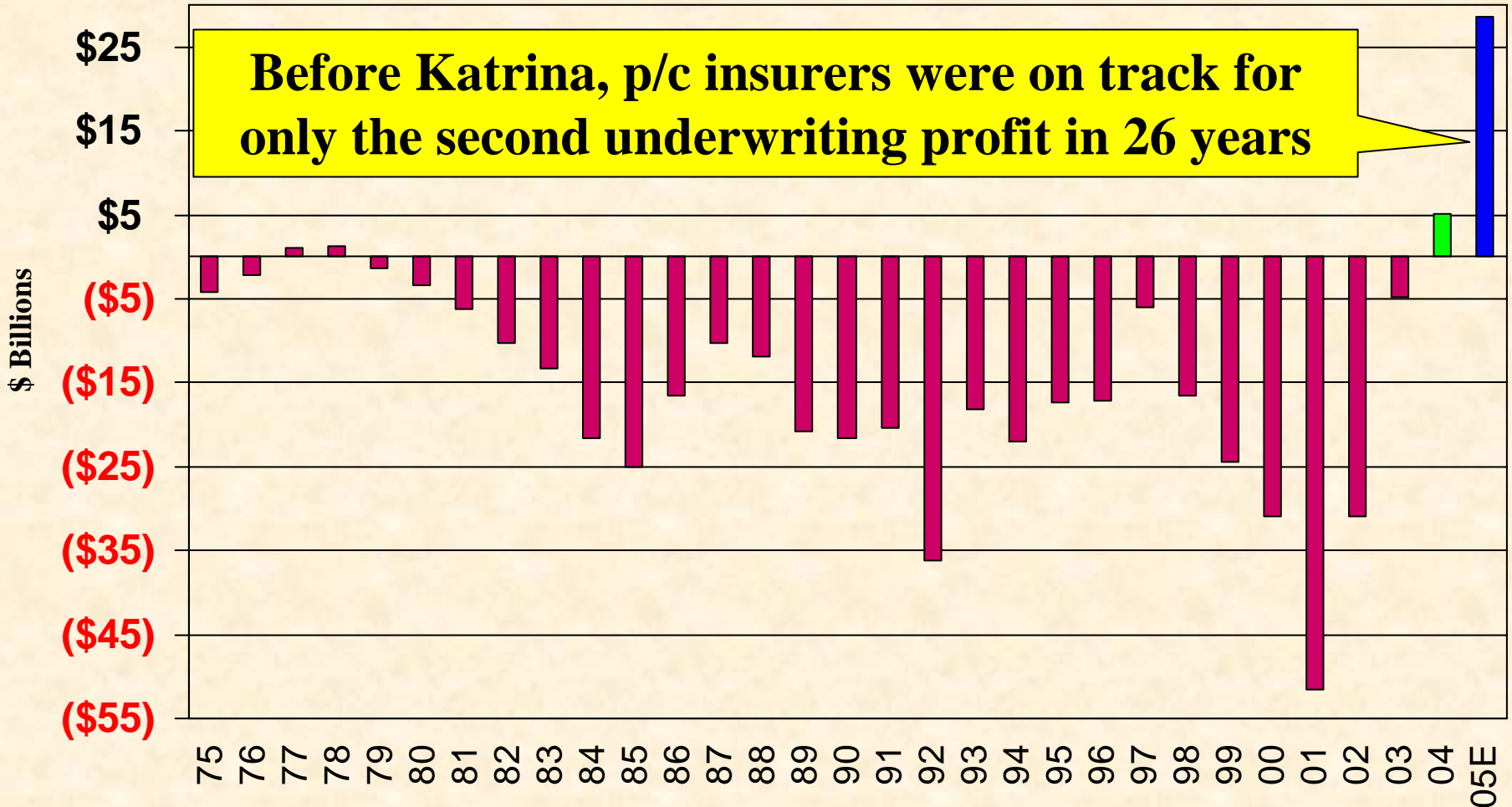
Sources: A.M. Best; ISO, III.

*2005 figure is III estimate.



Underwriting Gain (Loss)

*1975-2005E**



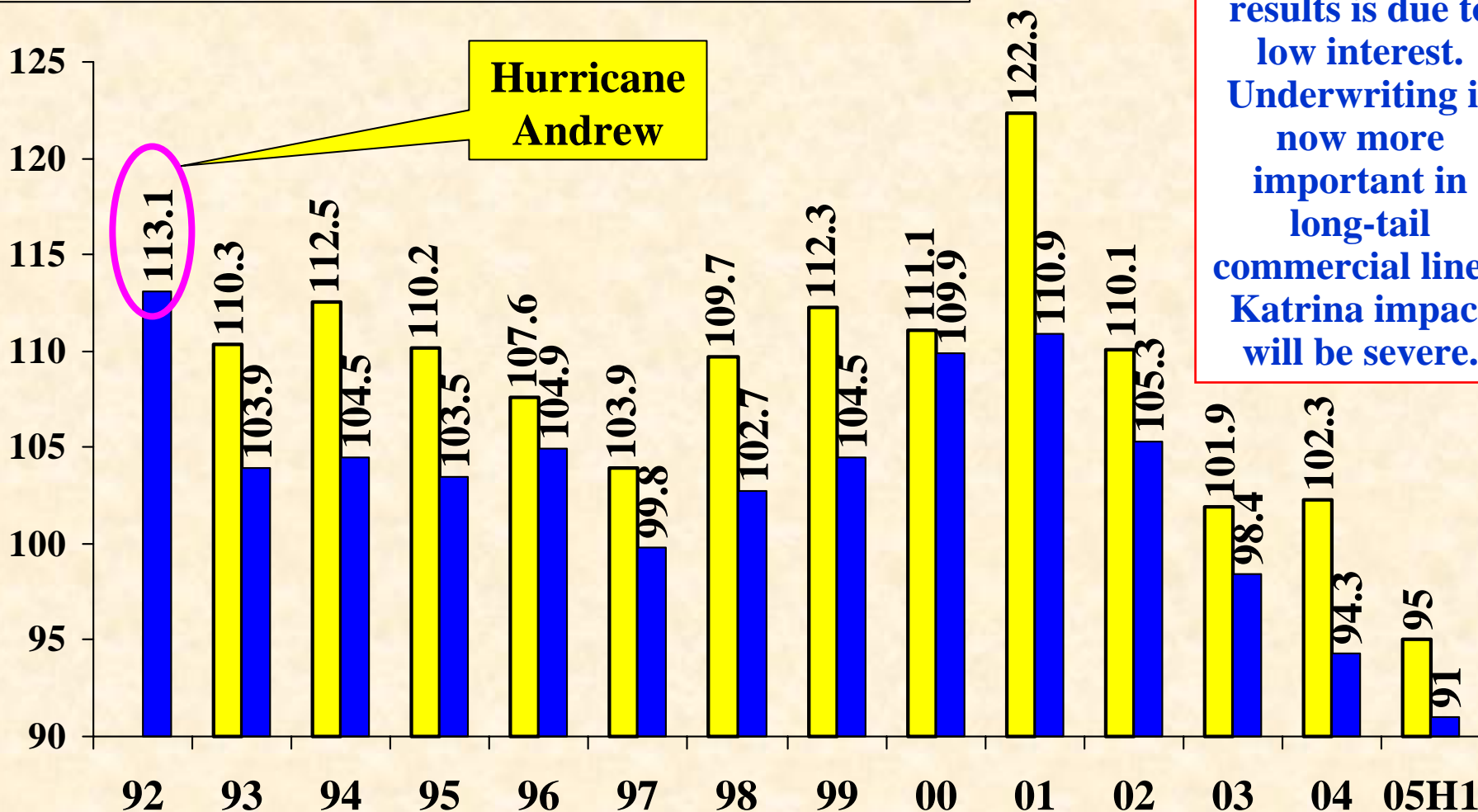
*2005 estimate is based on annualized actual 05Q1 underwriting profit of \$7.1 billion.

Source: A.M. Best, Insurance Information Institute



Commercial vs. Personal Lines Combined Ratios, 1993-2005:H1*

Commercial--Net Basis Personal--Net Basis



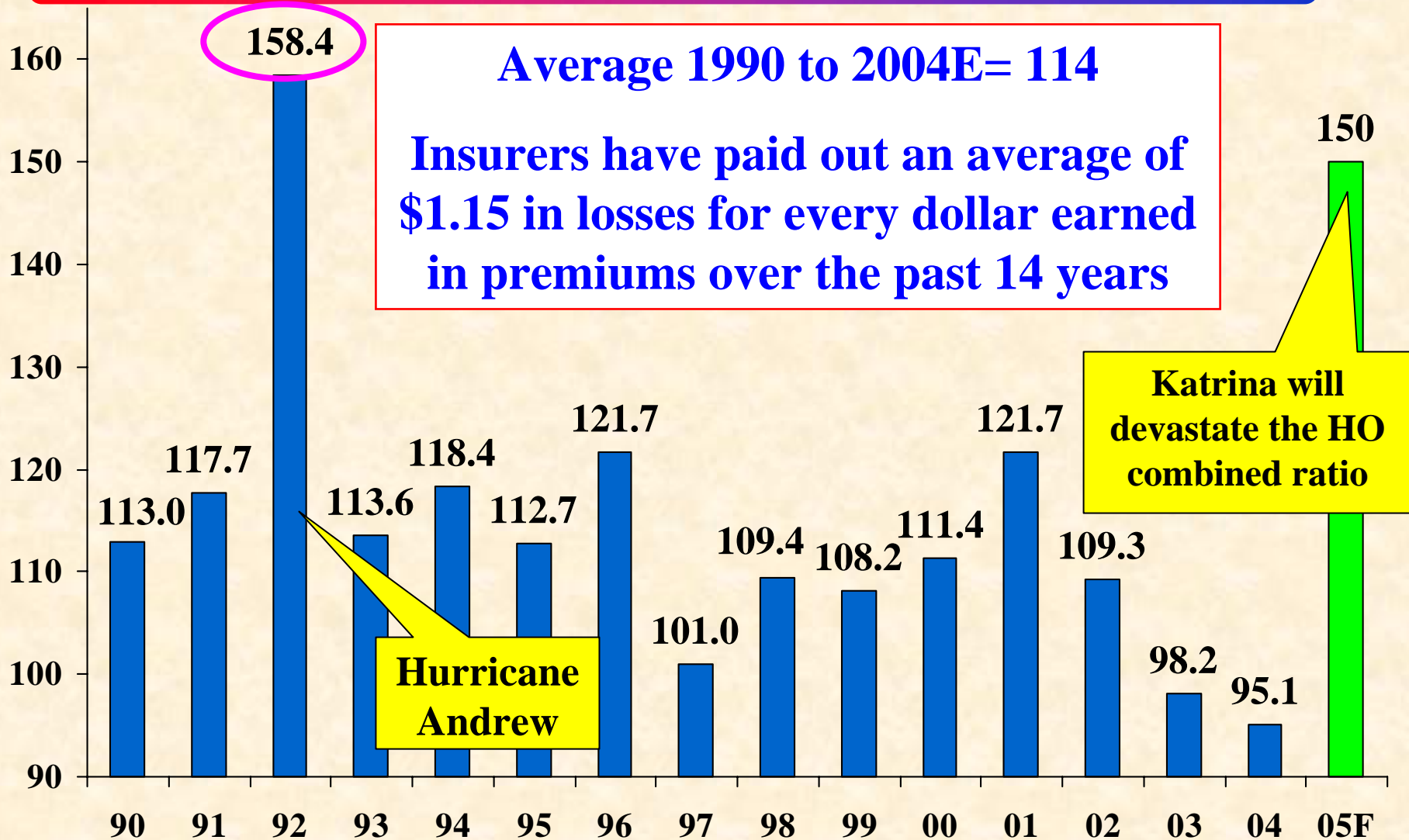
Compression of results is due to low interest. Underwriting is now more important in long-tail commercial lines. Katrina impact will be severe.

Source: A.M. Best; Insurance Information Institute

*III estimate for first half 2005.

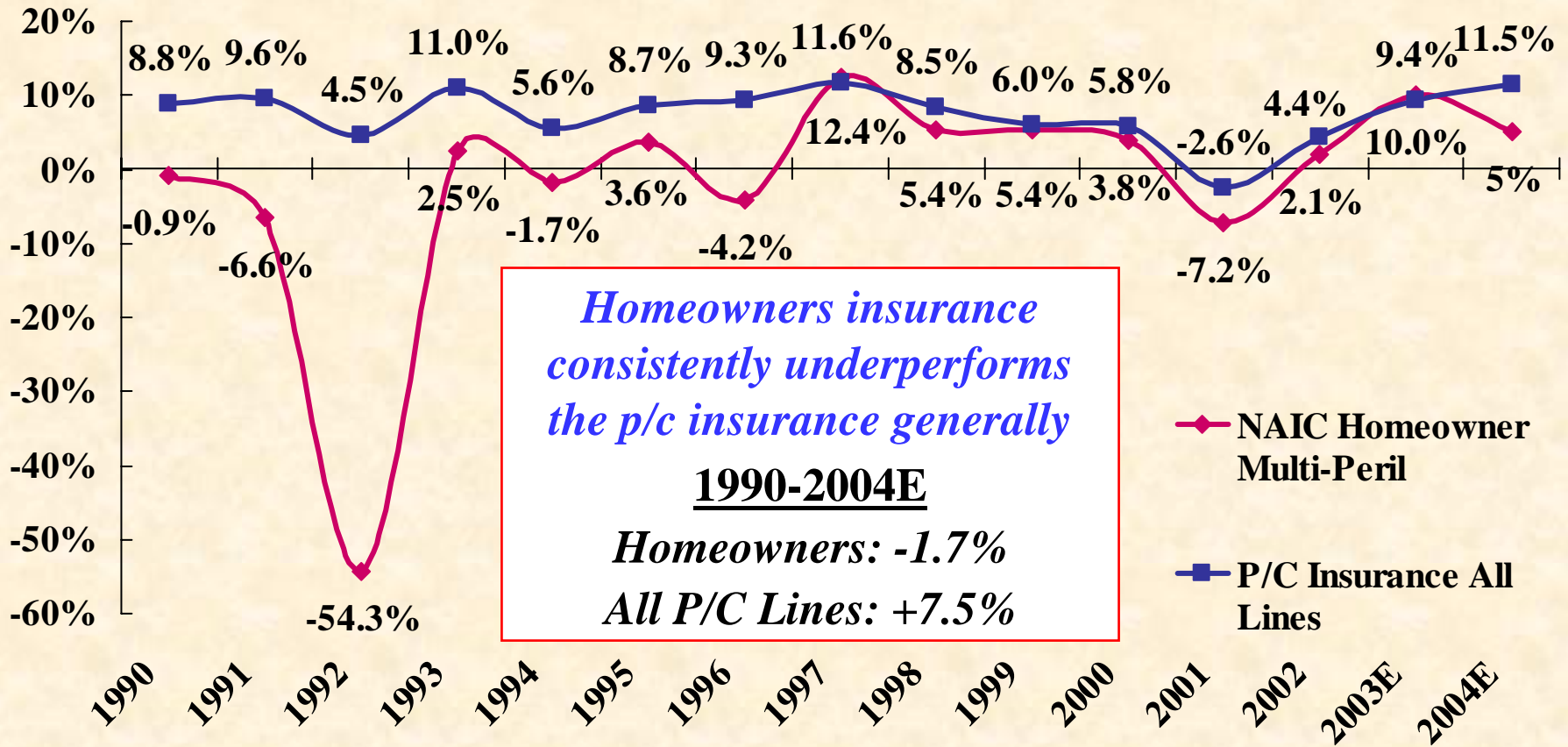


Homeowners Insurance Combined Ratio





Homeowners Insurance: Rates of Return on Net Worth vs. P/C Insurance All Lines



Source: NAIC, Insurance Information Institute

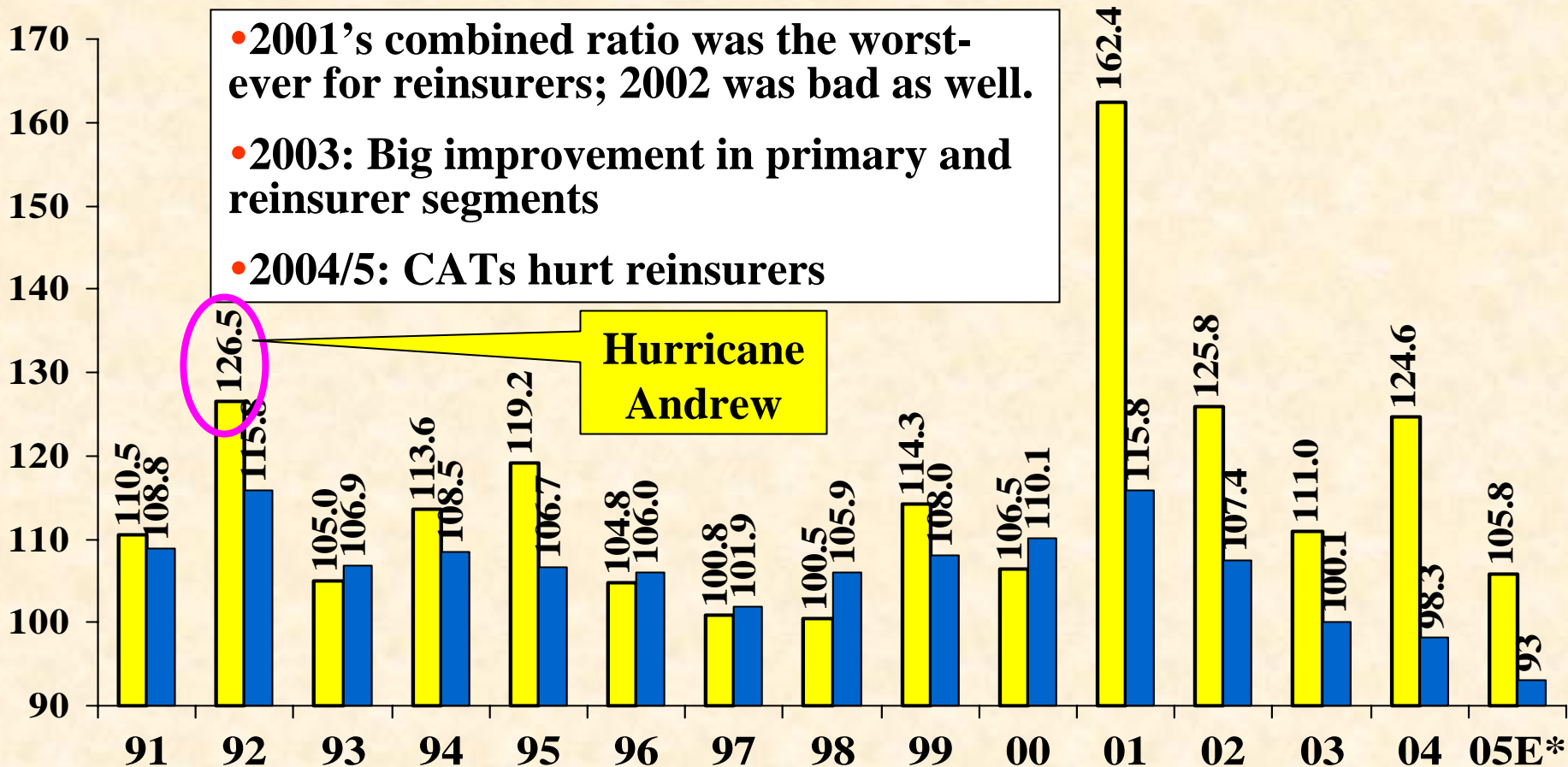
* Average is 1.22% if excluding 1992 (year of Hurricanes Andrew and Iniki).



Combined Ratio:

Reinsurance vs. P/C Industry

■ Reinsurance ■ All Lines Combined Ratio



* First half 2005 III estimate for all lines. RAA figure for 2005:H1

Source: A.M. Best, ISO, Reinsurance Association of America, Insurance Information Institute

UNDERWRITING AFFECTS FINANCIAL STRENGTH

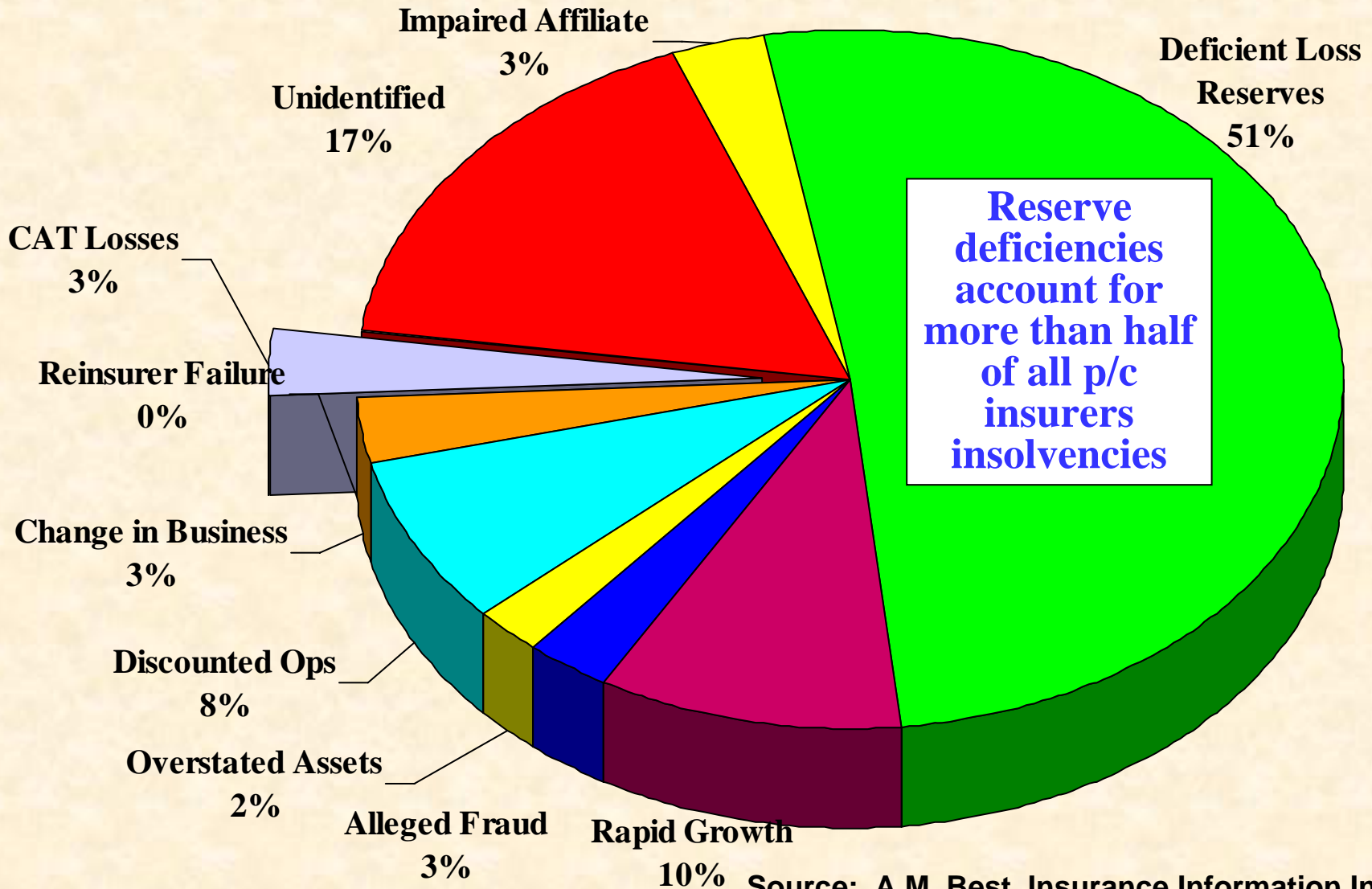
*Is There Cause
for Concern?*





Reason for P/C Insolvencies

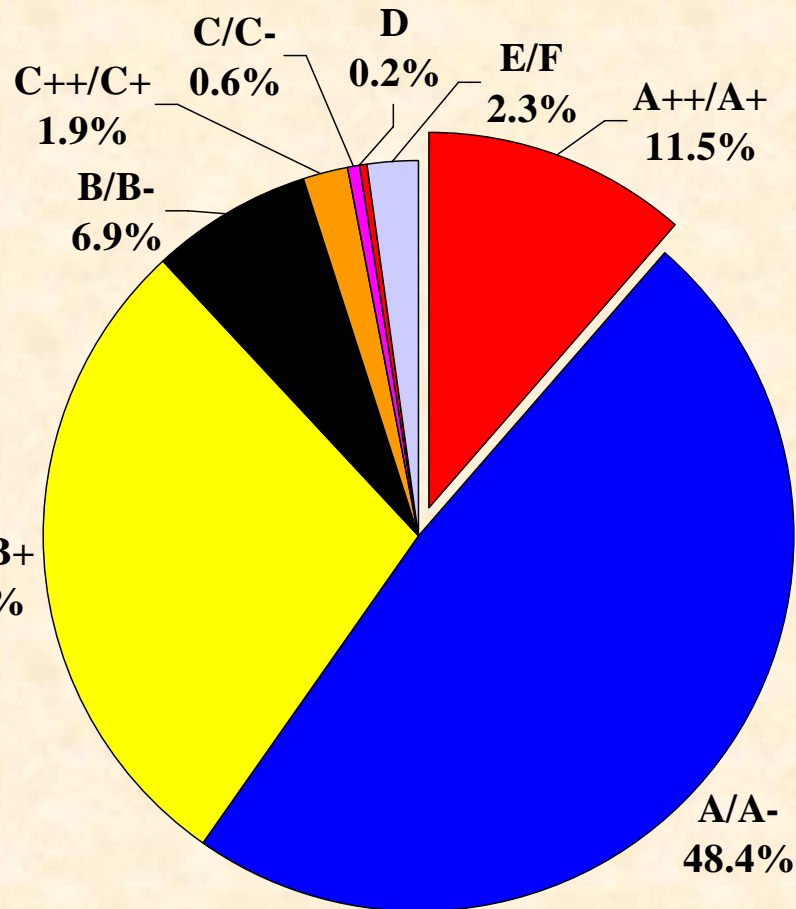
(218 Insolvencies, 1993-2002)



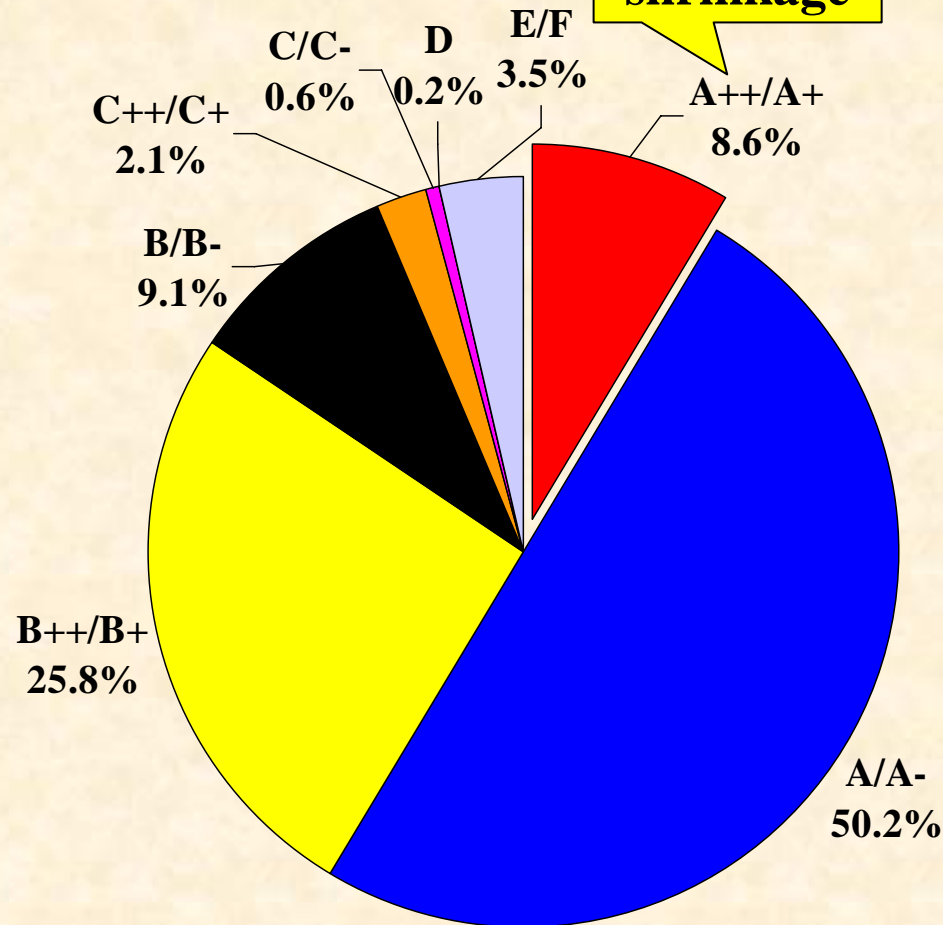


Historical Ratings Distribution, US P/C Insurers, 2000 vs. 2004

2000

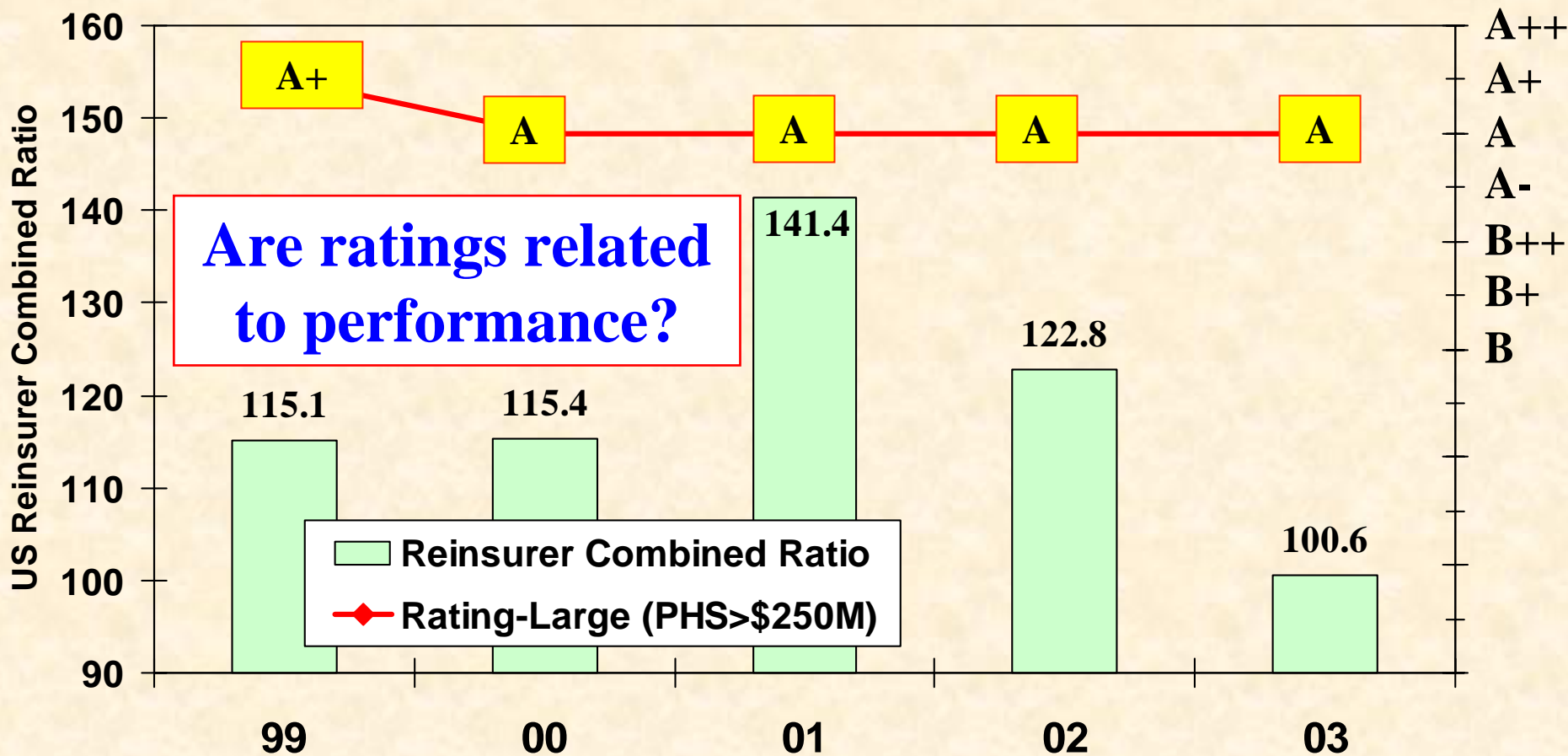


2004





US Reinsurer Combined Ratio vs. Median Rating, 1999-2003*



*Combined ratio is for all US reinsurers. Rating is for large reinsurers (policyholder surplus exceeding \$250 million). The median rating for small reinsurers (PHS<\$250M) was A- throughout the 1999-2003 period.

Source: A.M. Best: *Rating Downgrades Slowed but Outpaced Upgrades for Fourth Consecutive Year*, Special Report, November 8, 2004.



P/C Insurers Maintaining Rating of A+ or Better Rating for 50+ Years

P/C Company

1. AIU Insurance Co.
2. Alfa Mutual Ins. Co.
3. Amica Mutual Ins. Co.
4. Church Mutual Ins. Co.
5. Federal Insurance Co.
6. General Reinsurance Corp.
7. Great Northern Ins. Co.
8. Lititz Mutual Ins. Co.
9. Nationwide Mutual Fire Co.
10. Otsego Mutual Fire
11. Quincy Mutual Fire Ins. Co.
12. State Automobile Mutual Ins. Co.
13. State Farm Mutual Auto Ins. Co.
14. Vigilant Insurance Co.

Group Affiliation

1. American International Group
2. Alfa Insurance Group
3. Amica Mutual Group
4. None
5. Chubb Group of Ins Cos.
6. Berkshire Hathaway Ins. Group
7. Chubb Group of Ins Cos.
8. Lititz Mutual Group
9. Nationwide Mutual Group
10. None
11. Quincy Mutual Group
12. State Auto Ins. Group
13. State Farm Group
14. Chubb Group of Ins Cos.

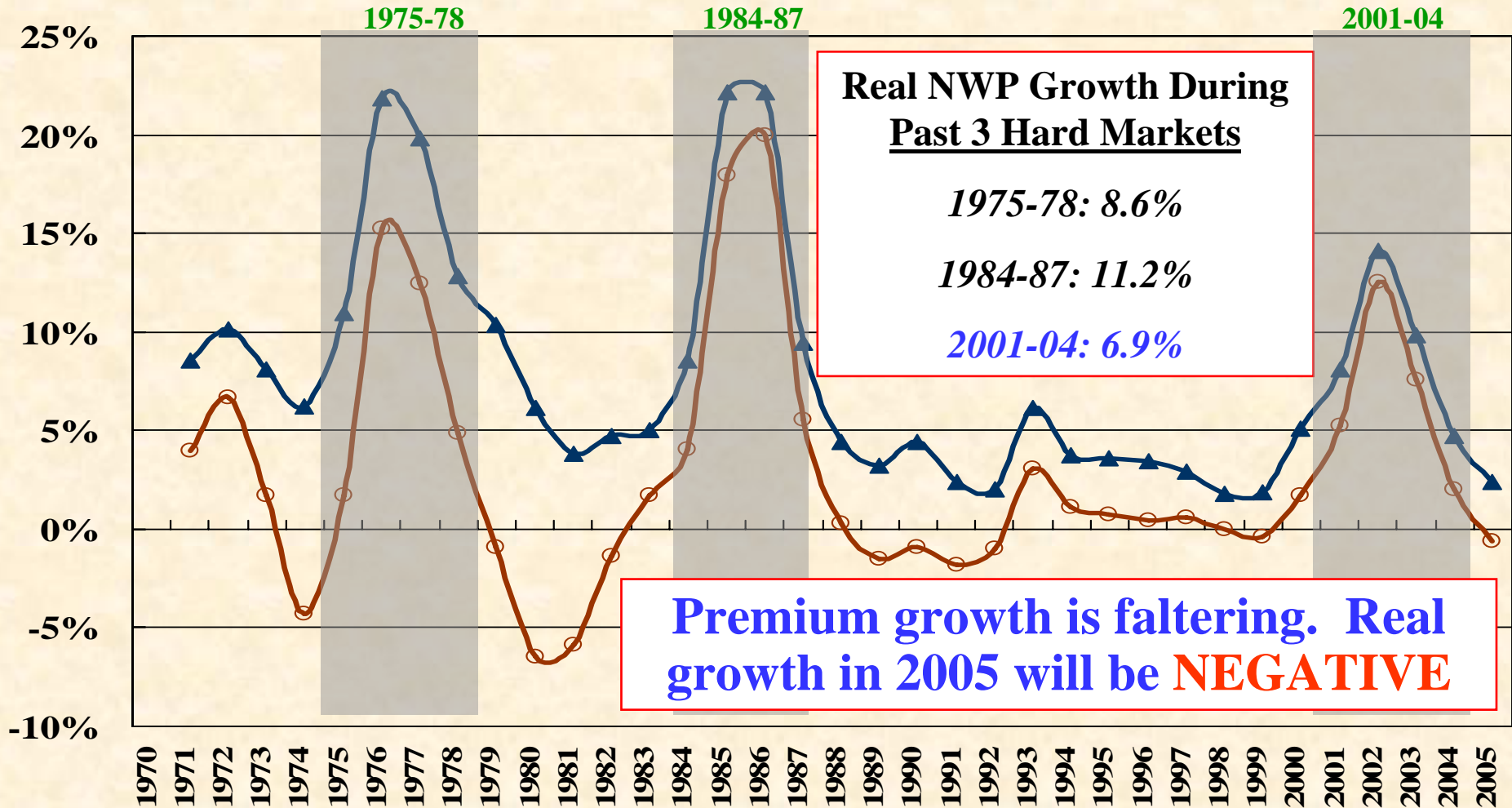
PRICING TRENDS

*Will Katrina & Rita
Harden Markets?*





Strength of Recent Hard Markets by NWP Growth*



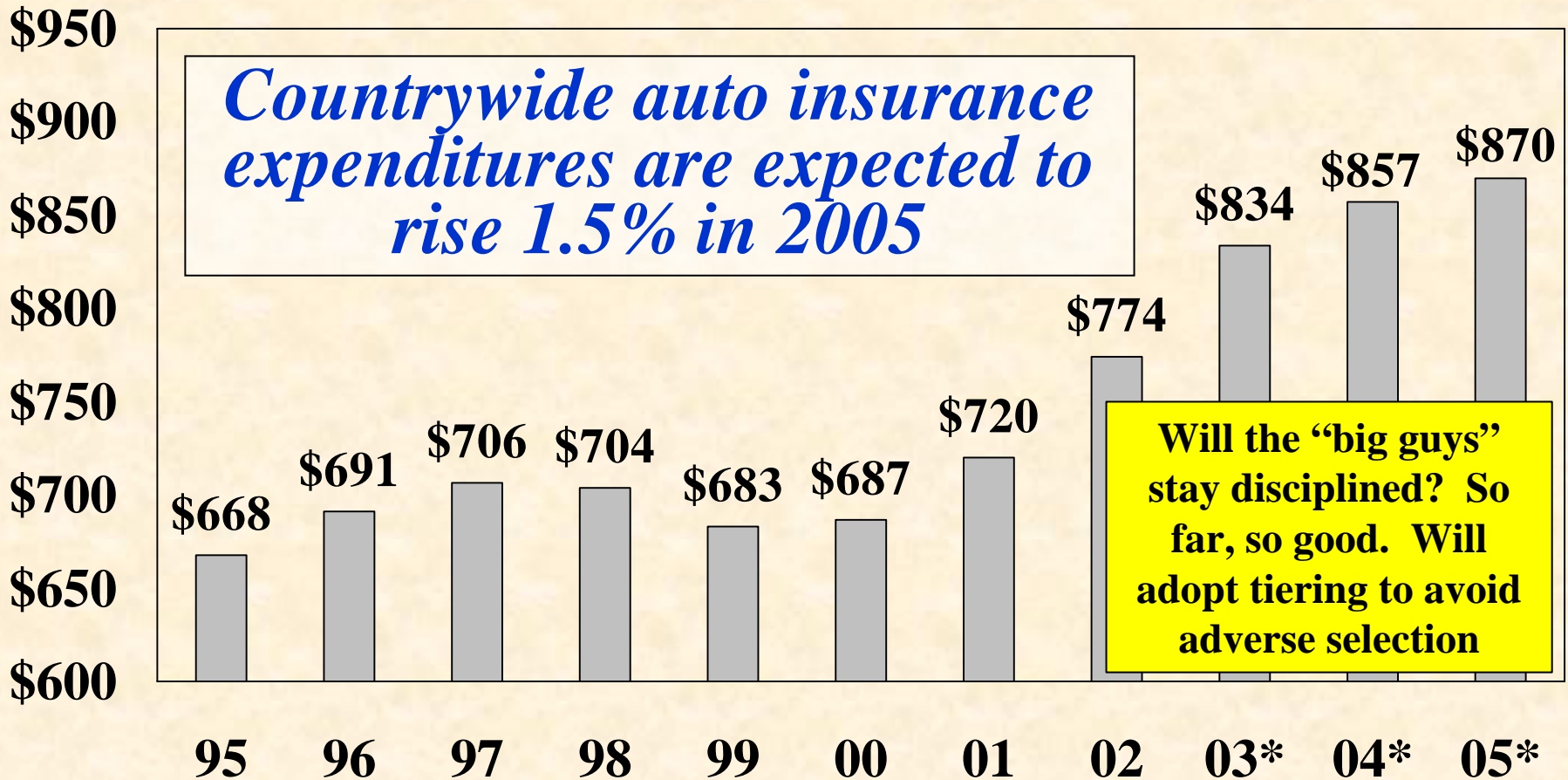
Note: Shaded areas denote hard market periods.

Source: A.M. Best, Insurance Information Institute

*2005 figure is III forecast based on 05Q1 result.



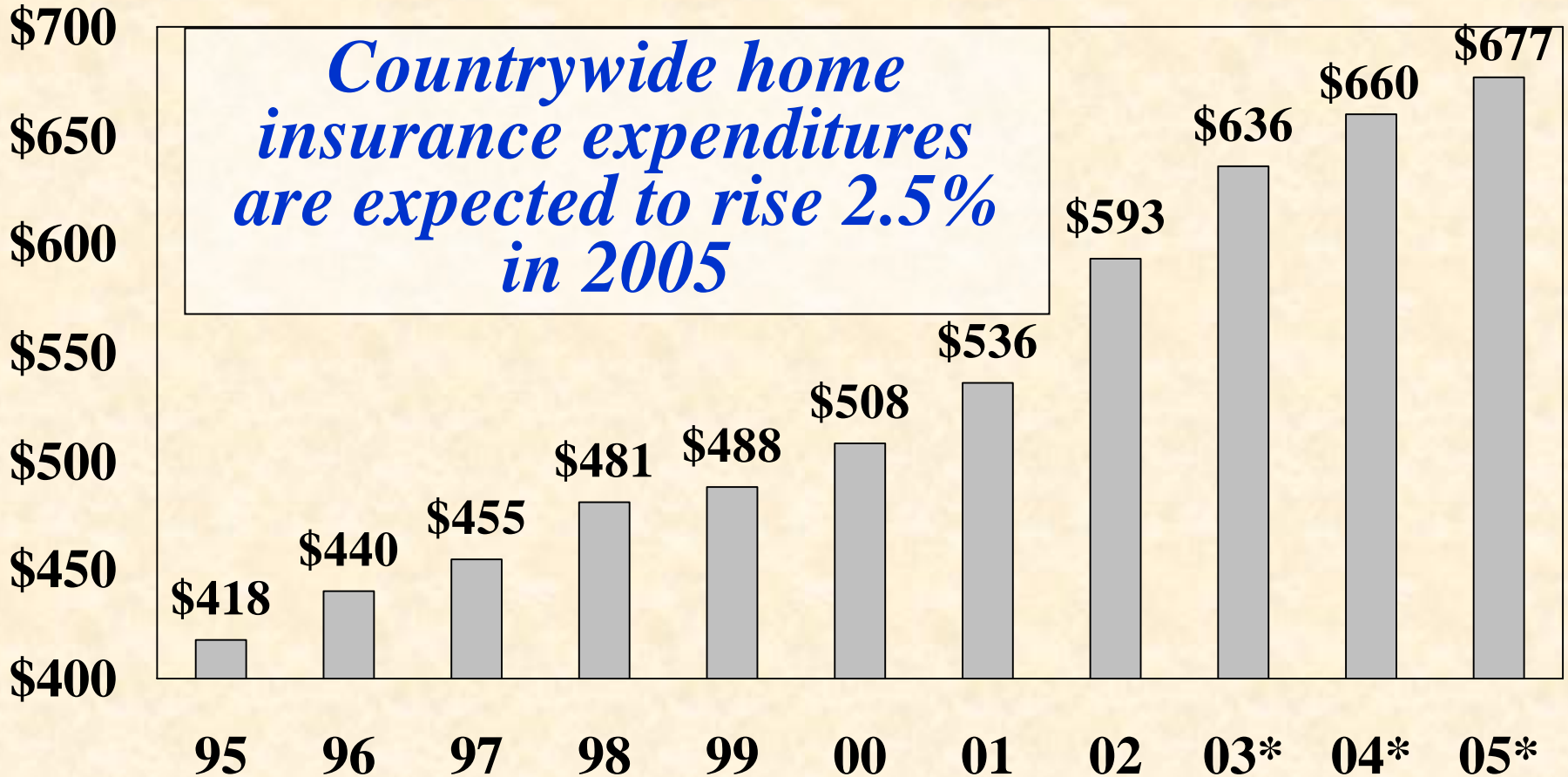
Average Expenditures on Auto Insurance



*Insurance Information Institute Estimates/Forecasts
Source: NAIC, Insurance Information Institute



Average Expenditures on Homeowners Insurance



*Insurance Information Institute Estimates/Forecasts

Source: NAIC, Insurance Information Institute



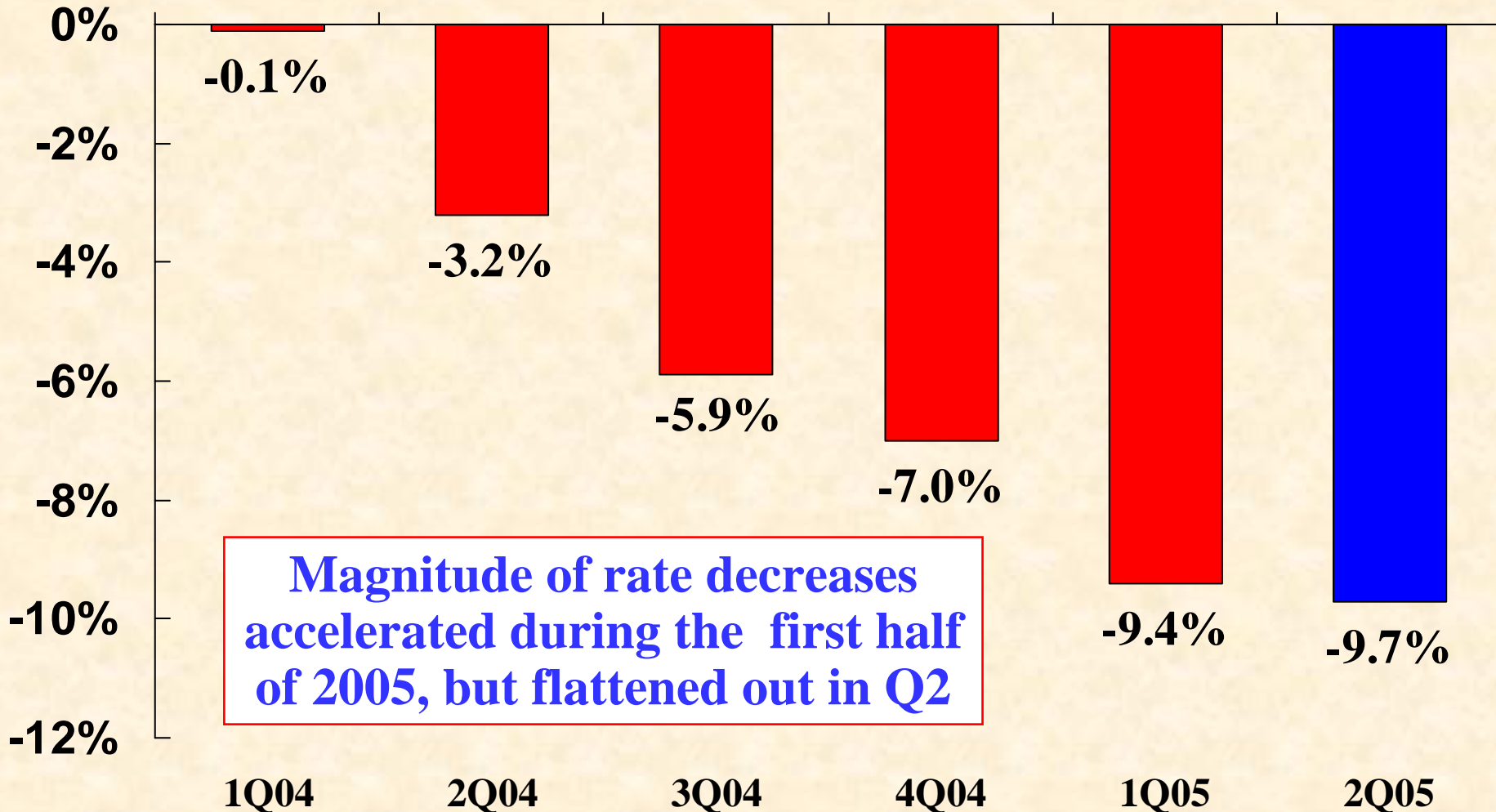
Commercial Premium Rate Changes Are Sharply Lower



Source: MarketScout.com

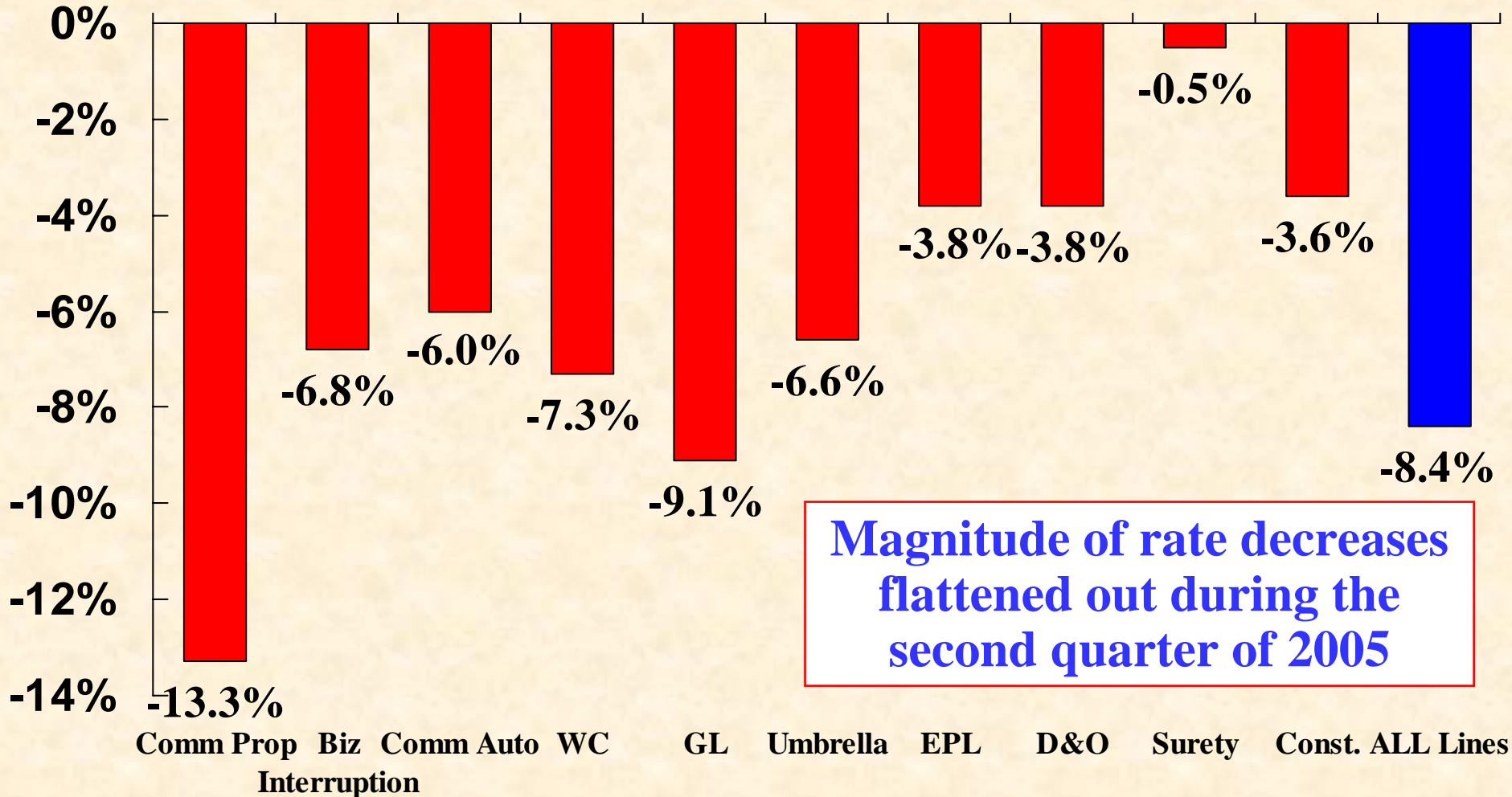


Average Rate Change, All Lines, (1Q:2004 – 2Q:2005)





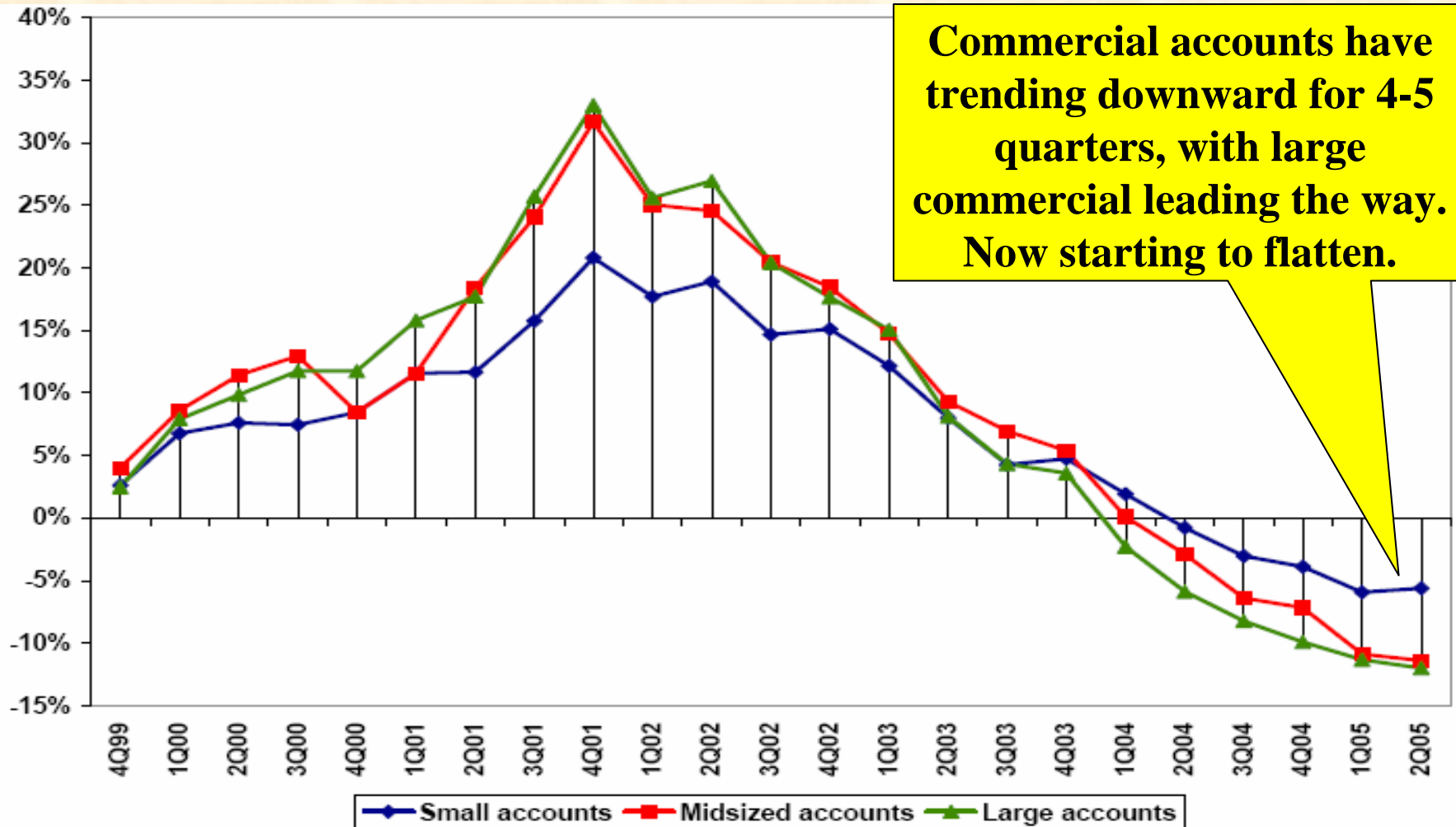
Rate Changes by Line, 2nd Qtr. 2005



Source: Council of Insurance Agents & Brokers; Insurance Information Institute



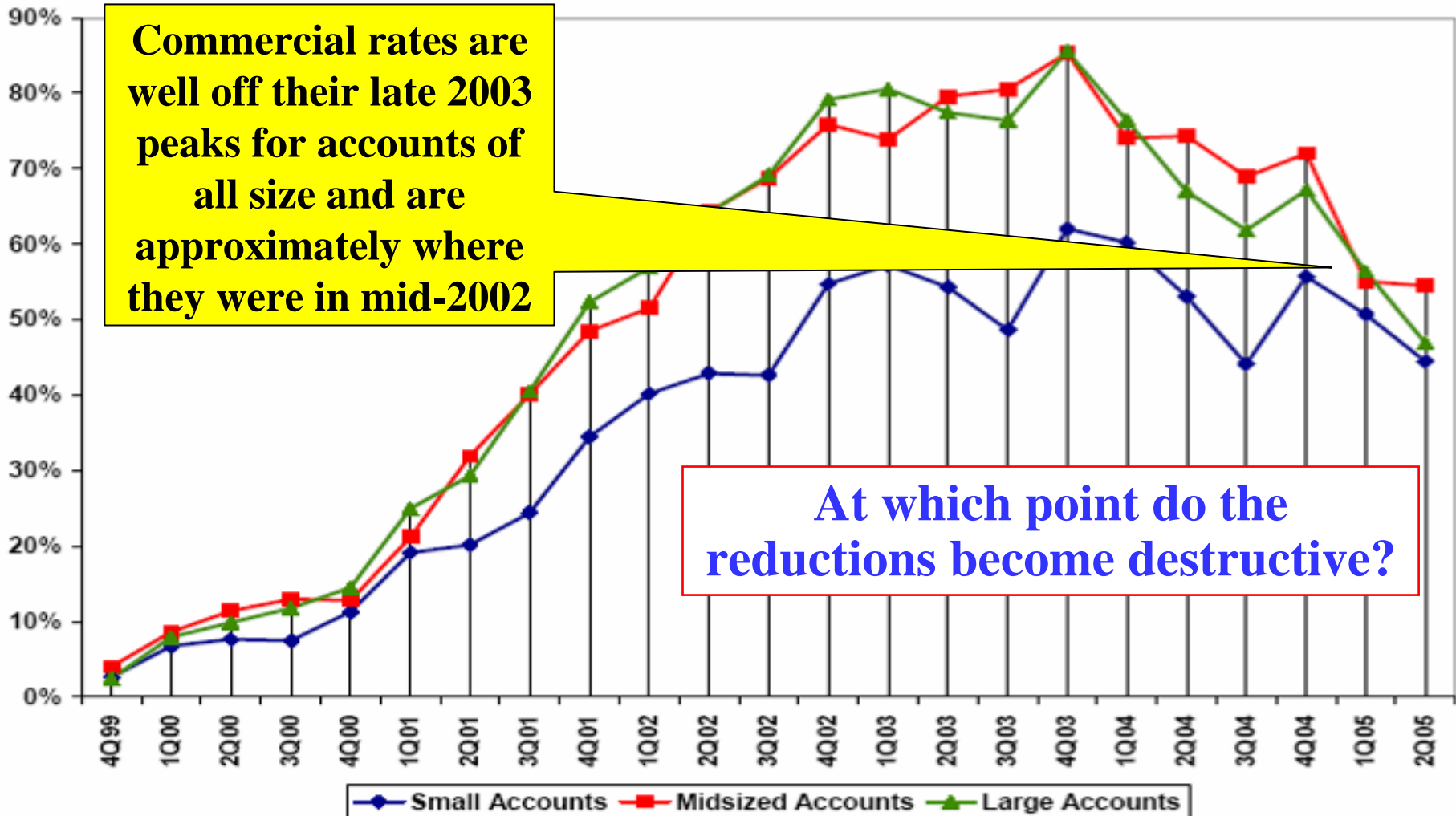
Average Commercial Rate Change by Account Size



Source: The Council of Insurance Agents & Brokers. Chart prepared by Lehman Brothers Equity Research.

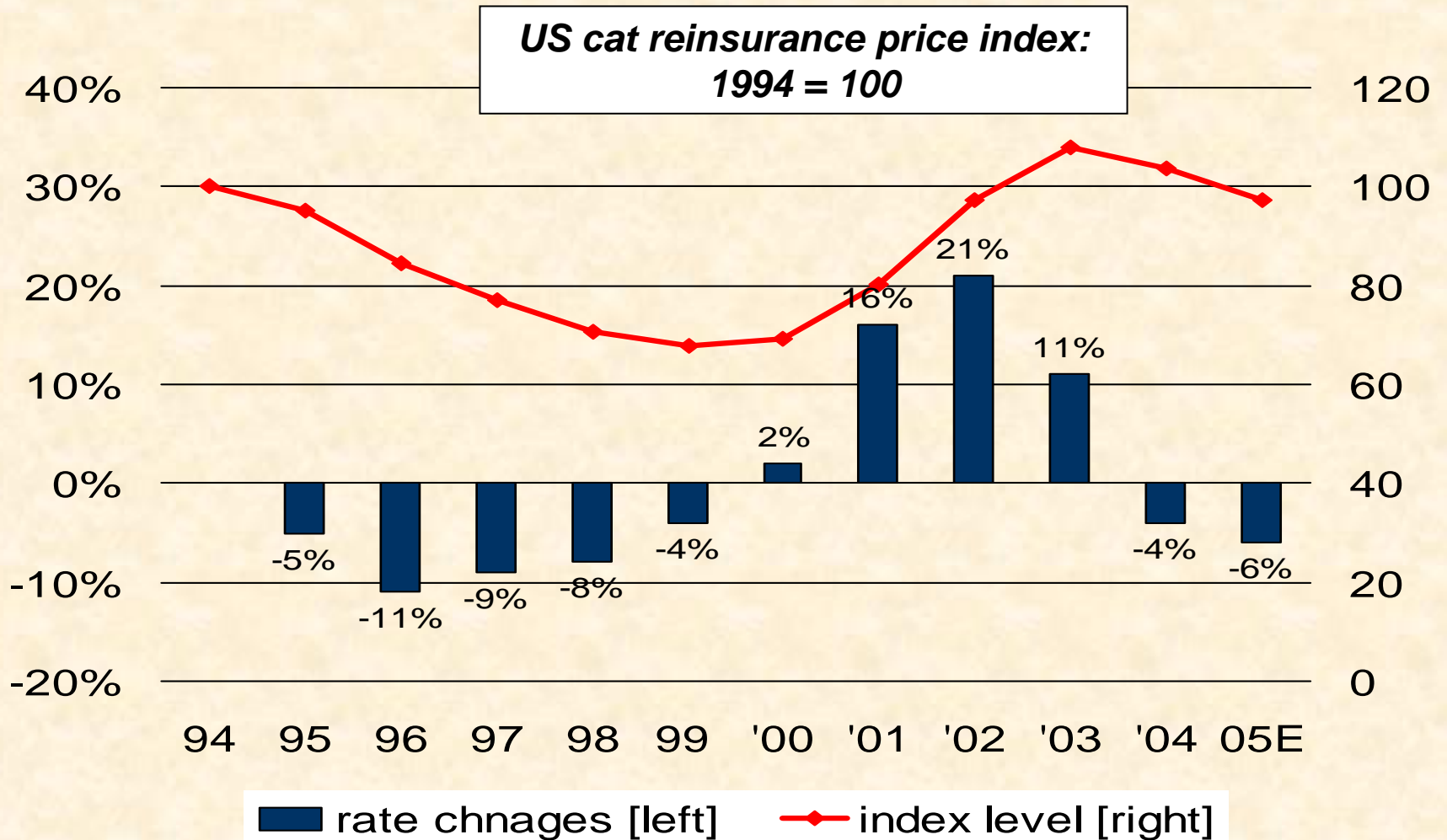


Cumulative Quarterly Rate Change by Account Size





Reinsurance Prices are Only at 1995 Levels, Despite Increased Risk



CATASTROPHE LOSS MANAGEMENT

Focus on Hurricanes

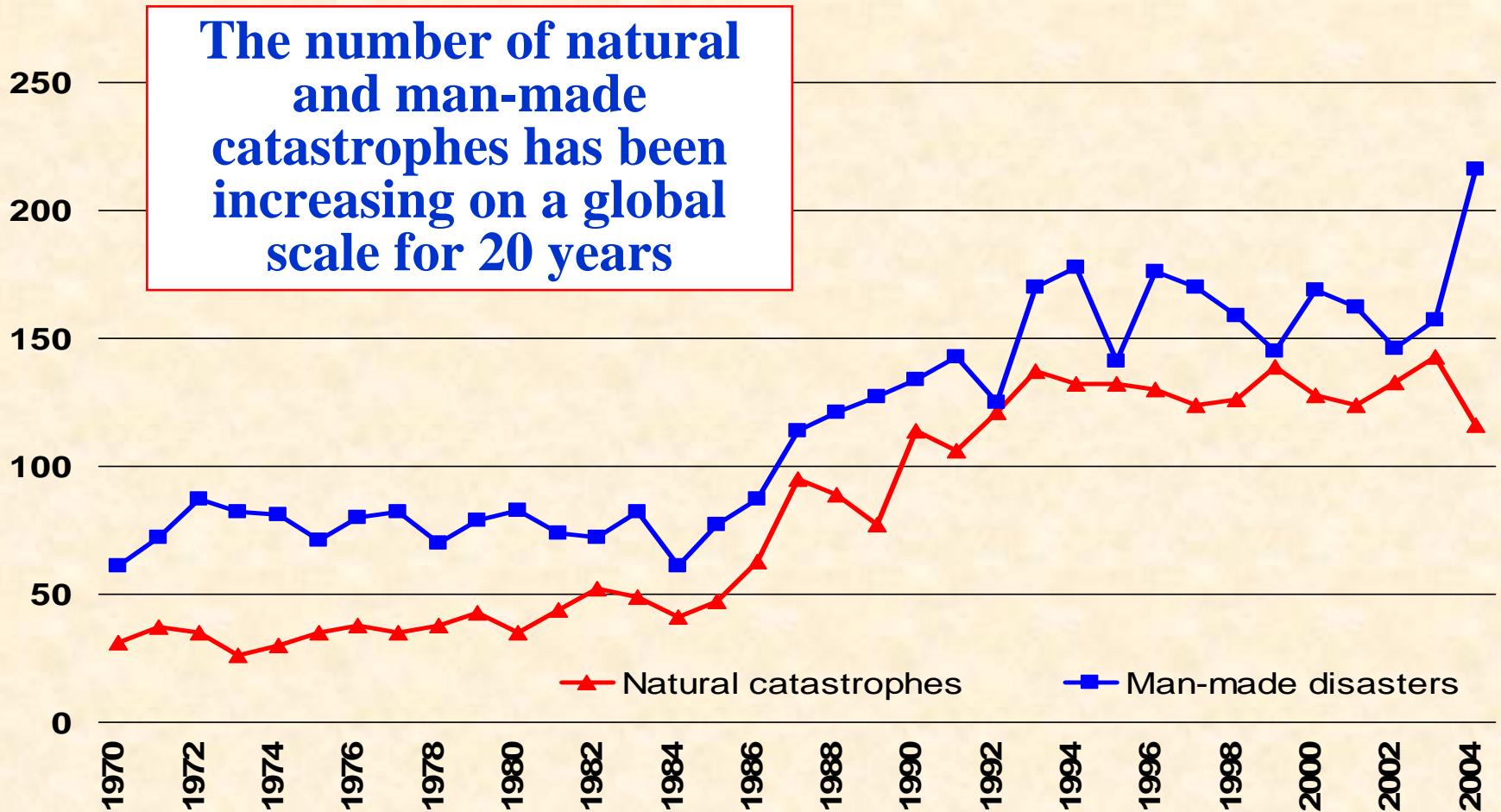


Katrina & Rita





Global Number of Catastrophic Events, 1970–2004

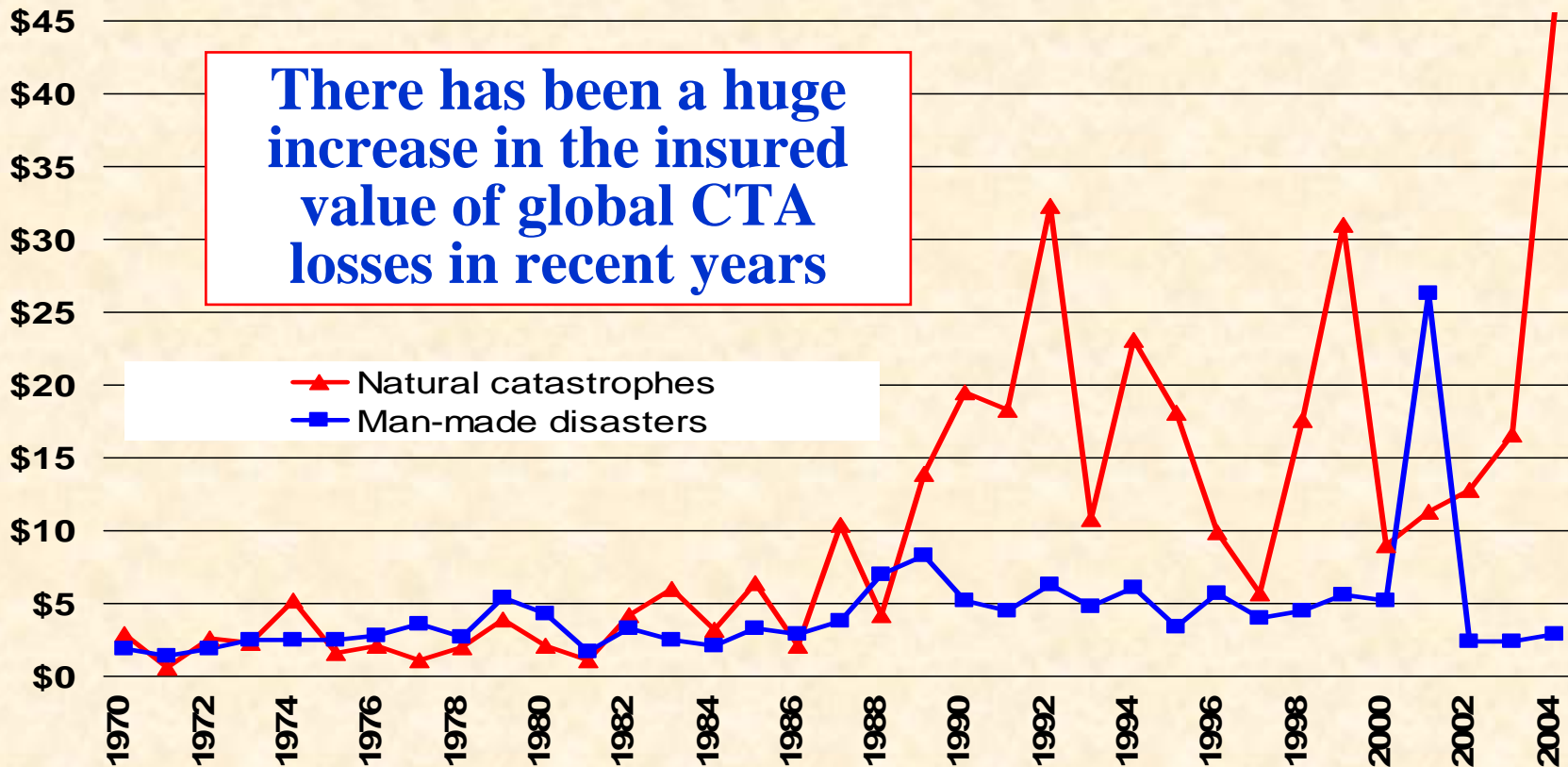




Global Insured CAT Losses, 1970–2004

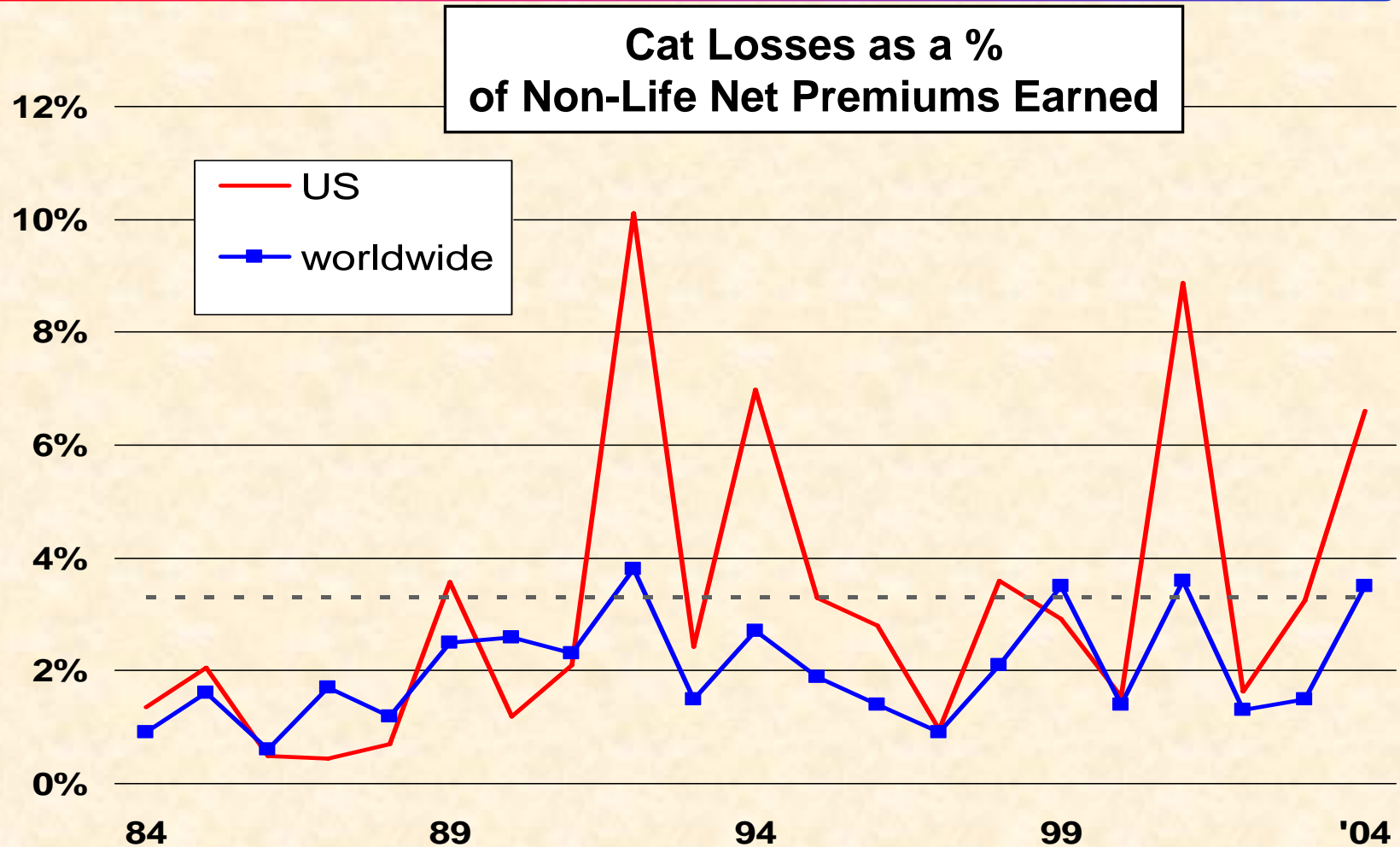
(Property and Business Interruption)

Billion USD, at 2004 prices



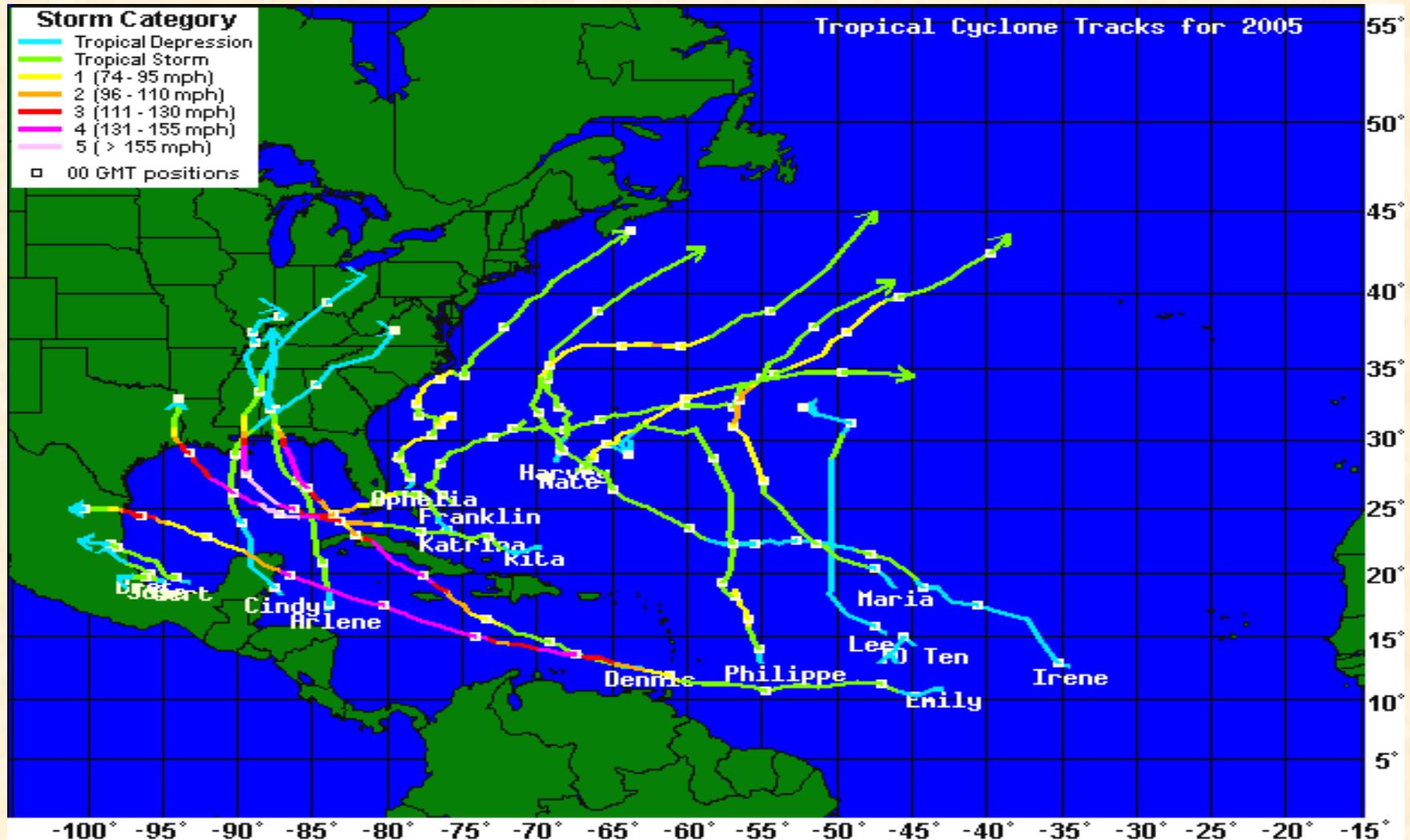


Insured Property Catastrophe Losses, 1983–2004





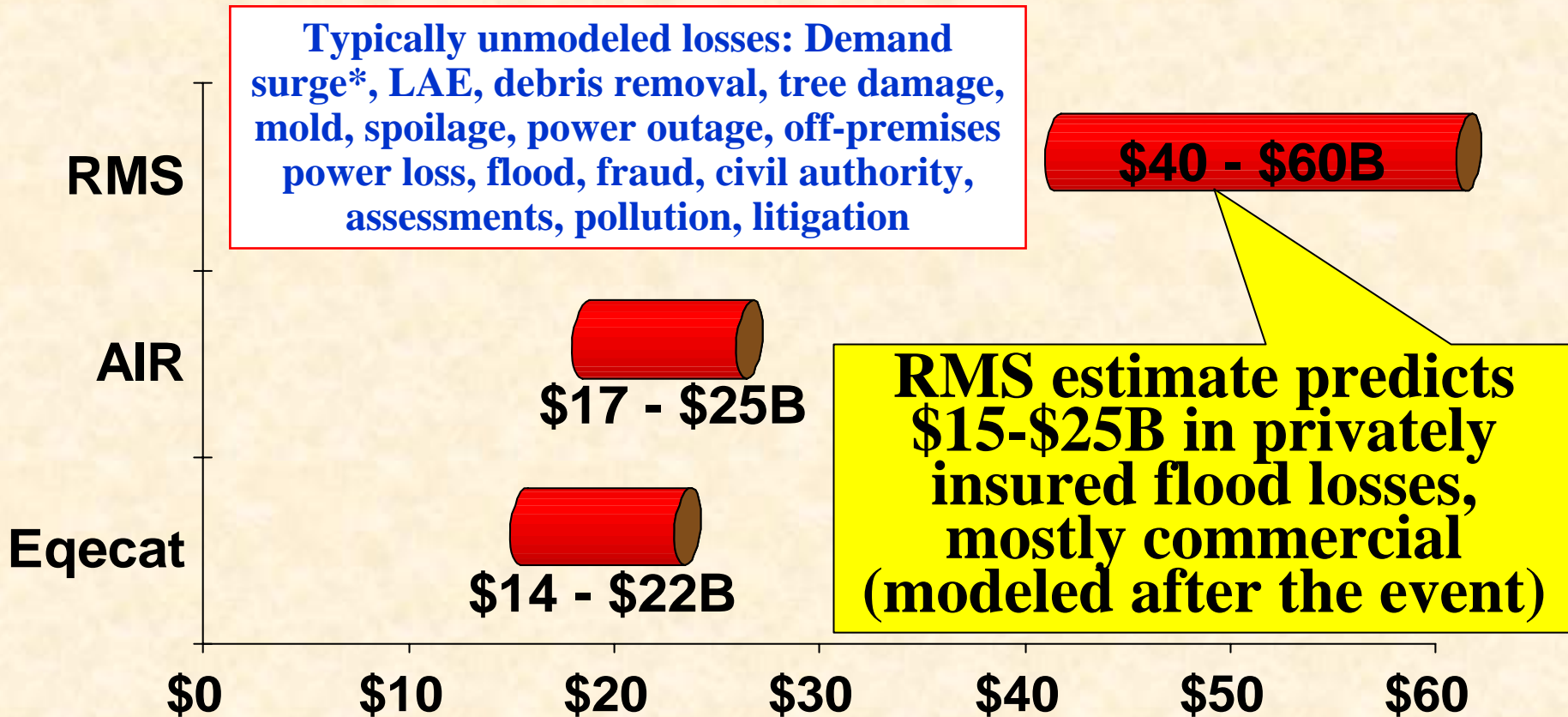
2005 Has Been a Busy, Destructive & Expensive Hurricane Season





Hurricane Katrina Insured Loss Estimates Still Vary Widely

(Billions of \$, As of September 11, 2005)



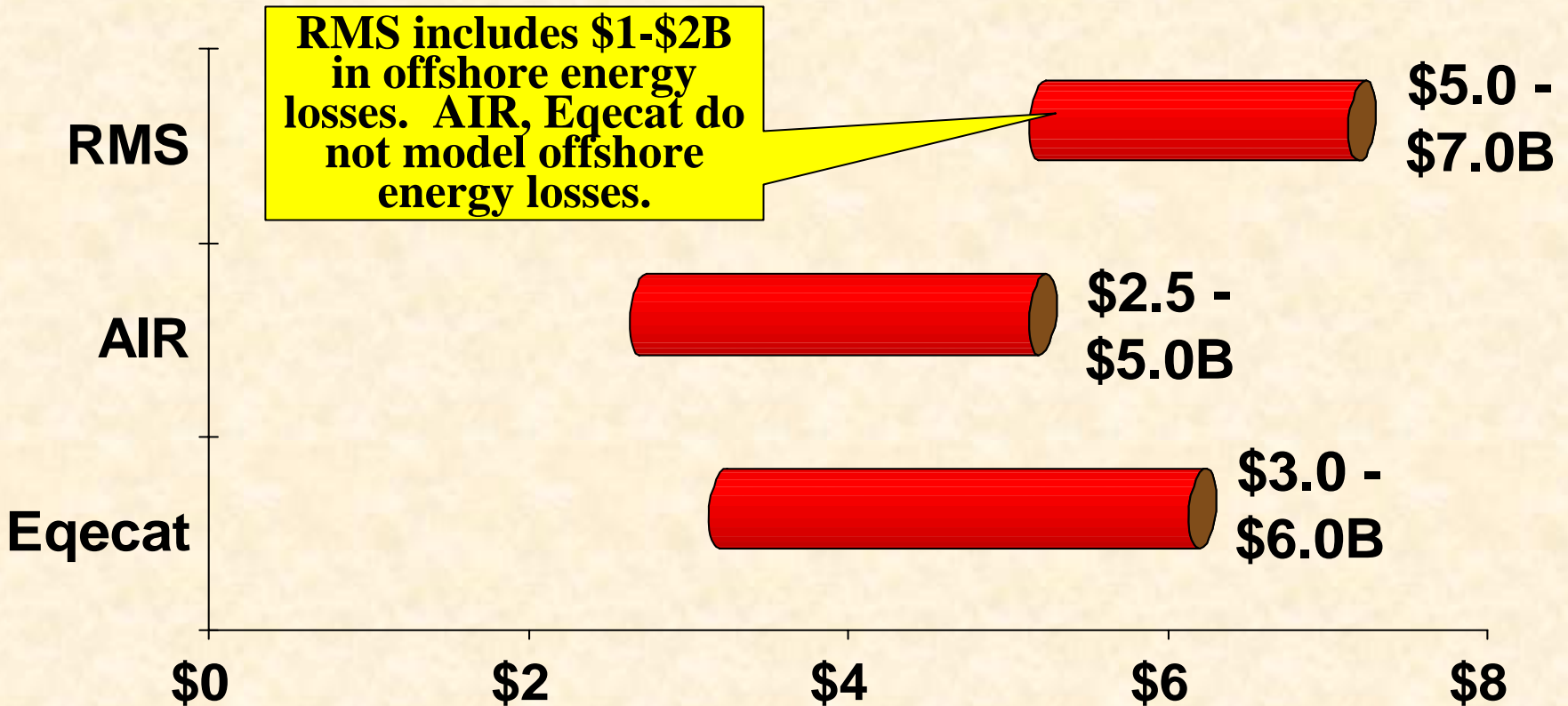
*Rising material costs, e.g., plywood rose 38% and framing lumber by 14% through Sept. 16, 2005.

Sources: RMS, AIR, Eqecat; Compiled by the Insurance Information Institute.



Hurricane Rita Losses: Much Smaller & Less Variable

(Billions of \$, As of September 26, 2005)





Breakdown of RMS \$40-\$60 Billion Loss Estimate

Type of Loss	Low	High
Windstorm & Surge	\$20	\$25
Flood, private (not incl. NFIP)*	\$15	\$25
Off Shore Energy, Marine	\$2	\$5
Misc., Possible Pollution	\$2	\$3
1 st Landfall (FL)	\$1	\$2
TOTAL	\$40	\$60

*Primarily commercial flood and associated business interruption losses.

Sources: RMS; Adapted from *Responding to Katrina*, Lane Financial LLC, Sept. 16, 2005.



Summary of Facts About Insured Losses Regarding Katrina

- **As of 9/28/05:**
 - 38 companies had announced pre-tax loss estimates
 - Announced loss total: \$14.5B to \$15.7B
 - This works out to about 43% of the mid-range insured loss estimate of \$35 billion
 - \$35B loss is 8.7% of US PHS; \$60B is 14.9%
- **Announced Company Loss Estimates:**
 - High: \$2.55 billion; Low: \$2 million
 - Upper loss est. % of 2Q:05 Equity: 0.2% to 46.1%
- **At least 20 companies put on watch for possible downgrades by various ratings agencies**
- **Many Lines Affected:**
 - Extreme events → loss correlations increase



Distribution of Announced Hurricane Katrina Losses (\$ Millions)

(As of September 28, 2005)



As of September 29, 38 companies had announced pre-tax losses totaling between \$14.5 and \$15.7 billion, about 43% of a mid-range industry loss estimate of \$35 billion

Note: If company gave range of estimates, upper end is used.

Sources: Morgan Stanley, Company Reports

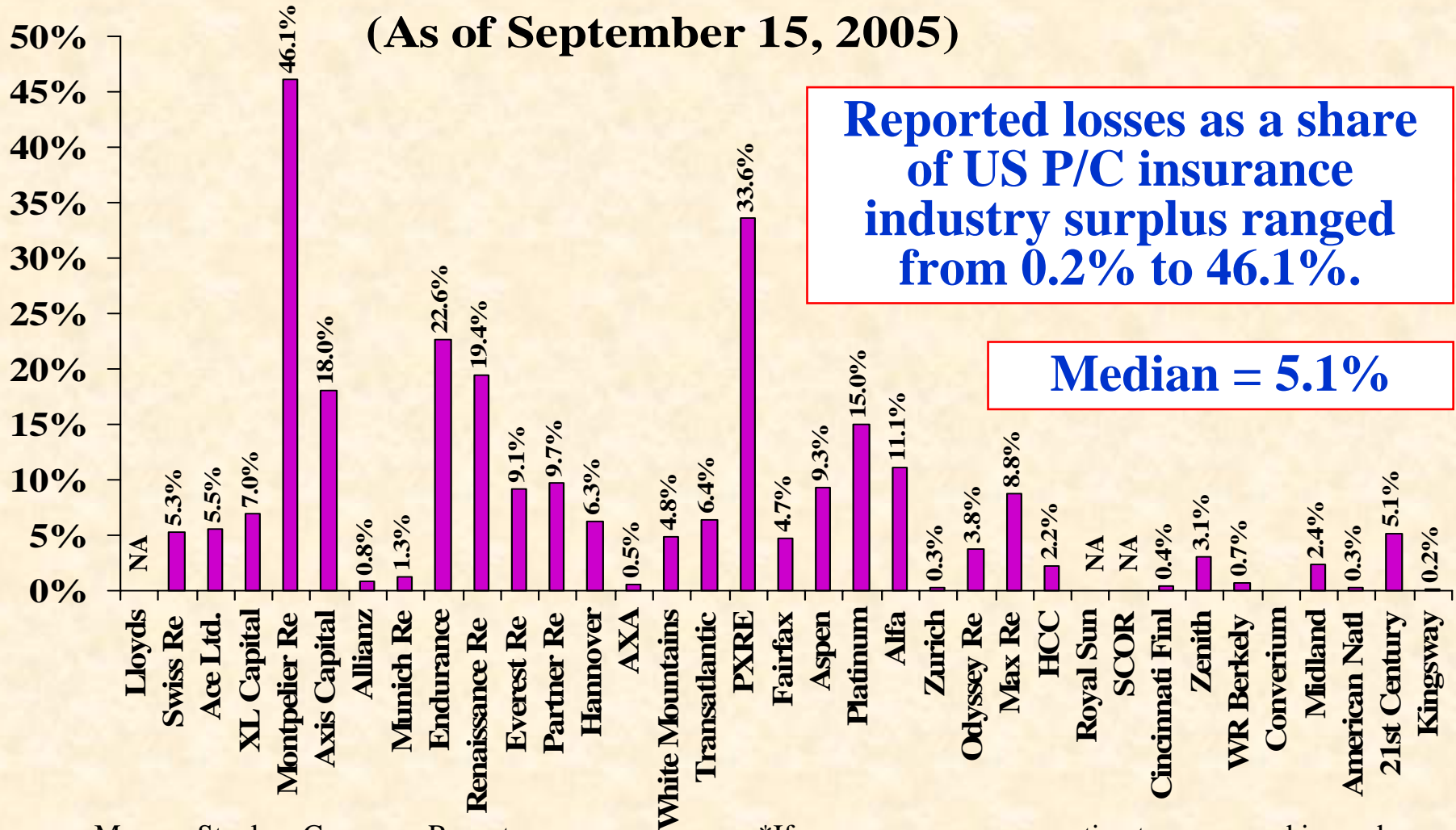
*After-tax figure. \$900 million after reinsurance recoverables.

**After-tax figure, net of reinsurance recoverables. Gross figure is \$2.5 billion.

***Pre-tax gross figure. After-tax net loss is \$78 million



Announced Hurricane Katrina Losses as % 2Q:05 Equity*

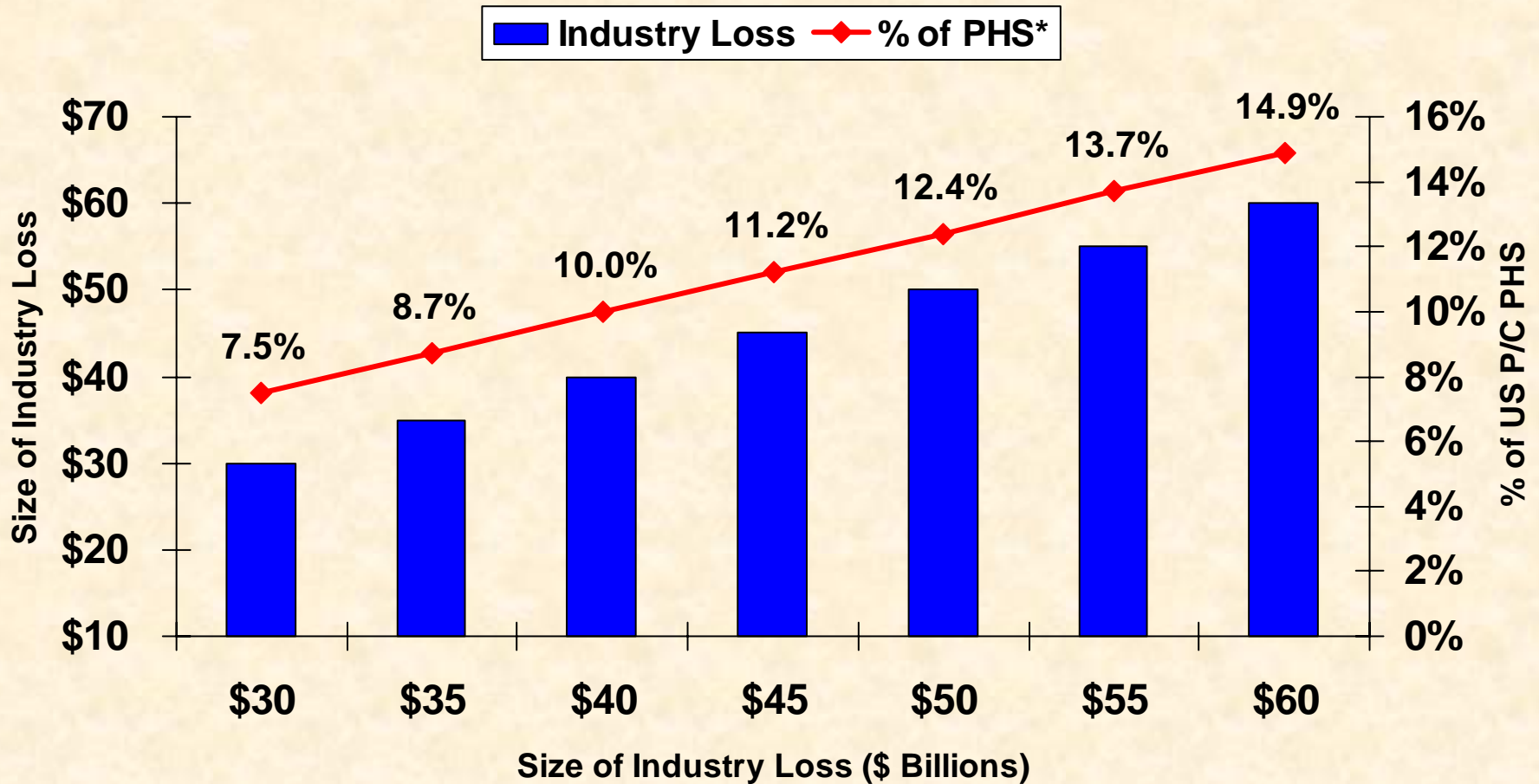


Sources: Morgan Stanley, Company Reports

*If company gave range estimate, upper end is used.



*Insured Loss Estimates as a % US Policyholder Surplus**



*Policyholder surplus as of 3/31/05 of \$401.8 billion (ISO).

Source: Insurance Information Institute.

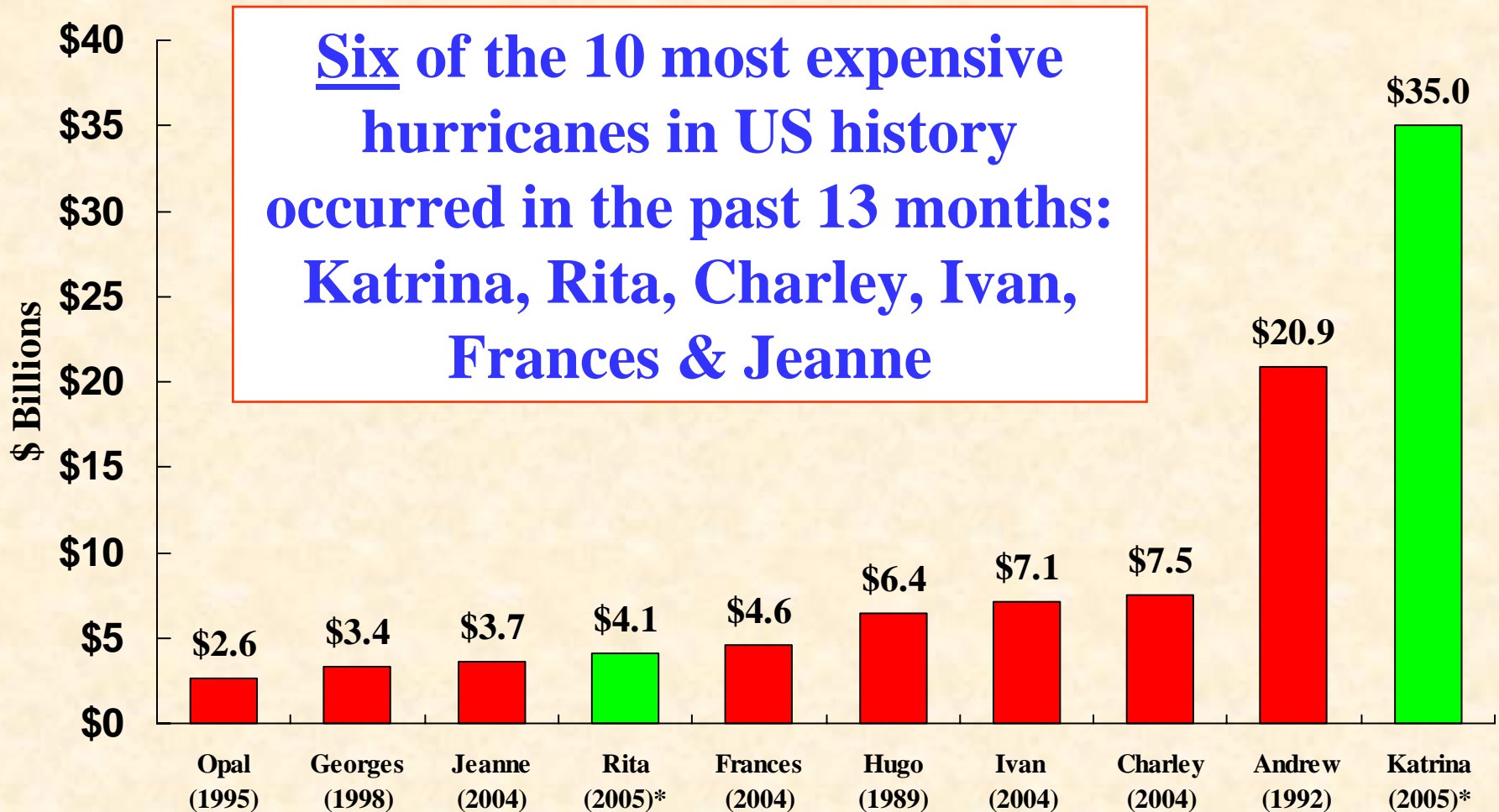
Hurricanes Katrina & Rita:

Their Place in History





Top 10 Most Costly Hurricanes in US History, (Insured Losses, \$2004)



*Estimates as of September 26, 2005 in 2005 dollars.

Sources: ISO/PCS; Insurance Information Institute.



Top 10 Insured Property Losses in US (\$2004)



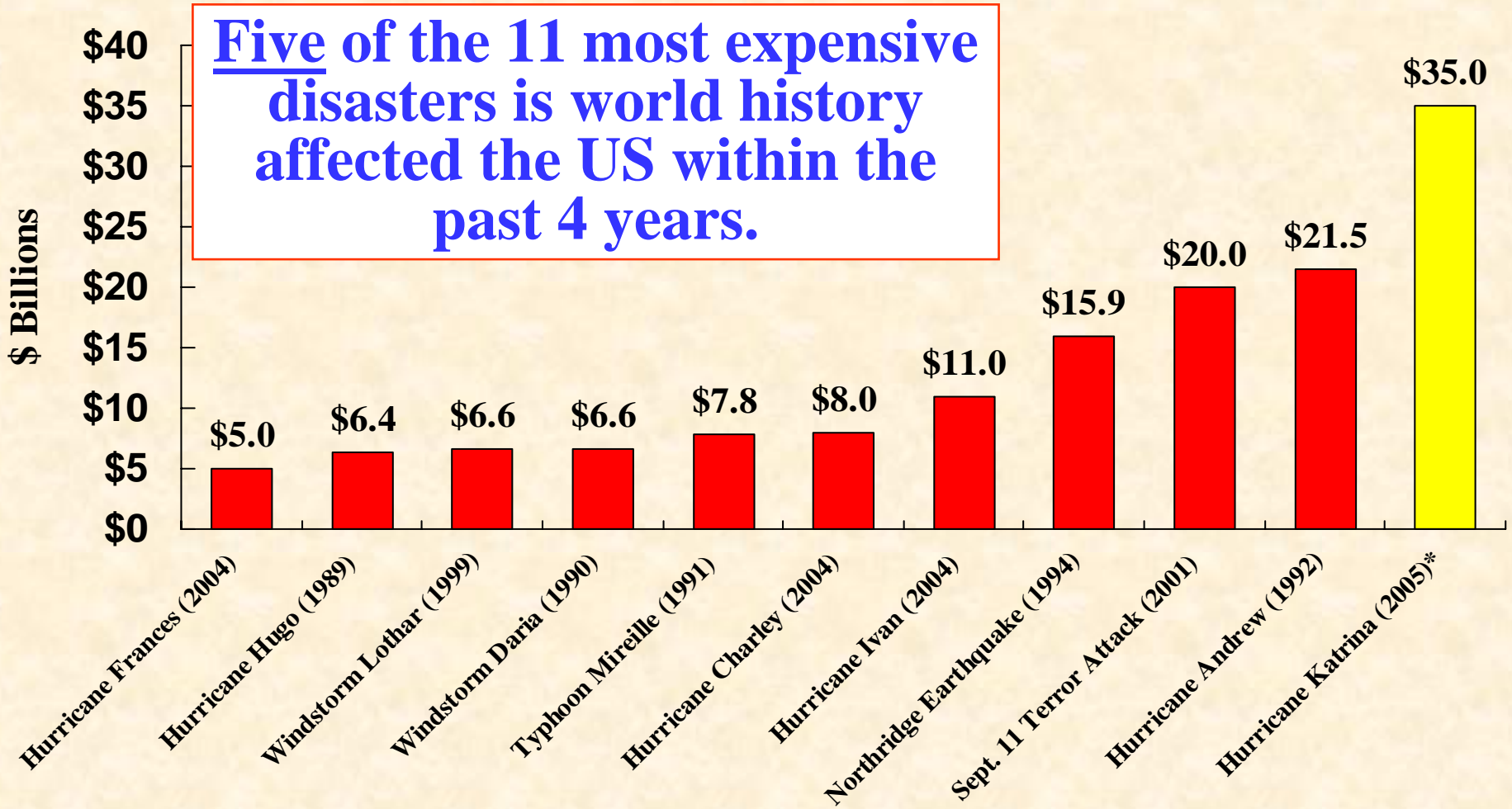
*Estimate, stated in 2005 dollars, as of 9/26/05.

Note: 9/11 loss figure is for property claims only. Total insured losses (\$2004) are approximately \$34B.

Sources: ISO/PCS; Insurance Information Institute.



Top 11 Insured Property Losses Worldwide, 1970-2005 (\$2004)*

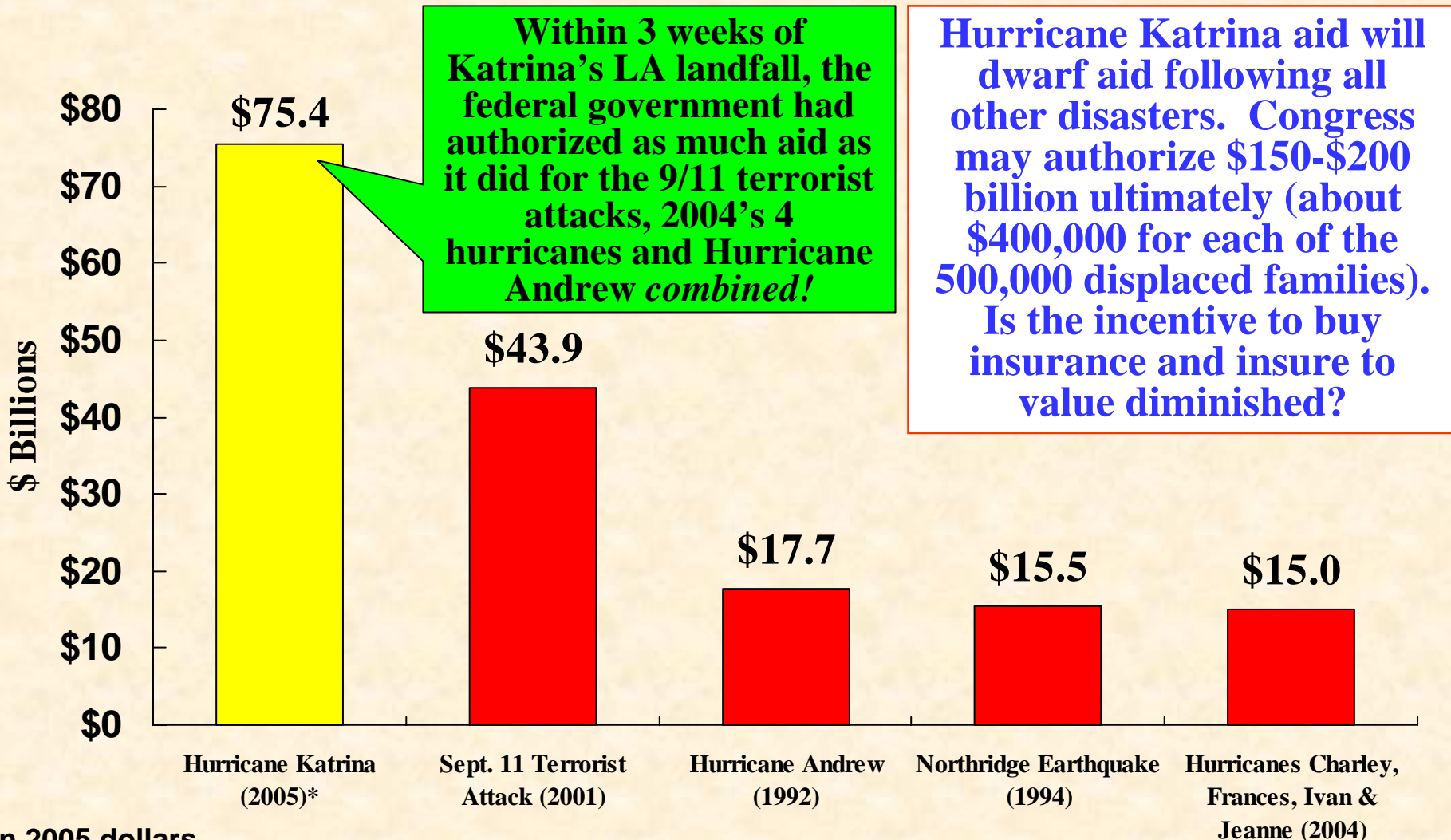


*All figures are for total losses across all locations, not just US. Katrina loss est. is preliminary and stated in 2005 dollars.

Sources: ISO/PCS; Swiss Re, "Natural Catastrophes and Man-Made Disasters in 2003," *Sigma*, no.1, 2004



Government Aid After Major Disasters (Billions)*



*In 2005 dollars.

Source: United States Senate Budget Committee as of 9/19/05; Insurance Information Institute.



Itemization of Federal Government Spending on Hurricane Relief

Legislation	5-Yr. Cost	Status
Emergency Spending Supplement #1, HR 3645	\$10.500	Public Law 109-61
Emergency Spending Supplement #2, HR 3673	\$51.8	Public Law 109-62
Flood Insurance Borrowing Authority	\$2.000	Passed House & Senate
Pell Grant Relief, H.R. 3169	\$0.002	Passed House & Senate
TANF Disaster Relief, H.R. 3672	\$0.294	Passed House & Senate
Katrina Short-Term Tax Relief Bill, H.R. 3768	\$6.500	Passed Senate
Sarbanes Housing Amend. To H.R. 2862	\$3.500	Passed Senate
Harkin Legal Services Amend. To H.R. 2862	\$0.008	Passed Senate
Snowe Small Business Amen. To H.R. 2862	\$0.595	Passed Senate
Baucus Economic Develop. Amend to H.R. 2862	\$0.210	Passed Senate
TOTAL	\$75.409	
Emergency Health Care Relief Act, S. 1716	\$5.0-\$7.0B	Introduced in Senate
Additional Flood Insurance Borrowing Authority	\$10.0-\$30.0B	N/A

Hurricane Katrina:

Loss Distribution

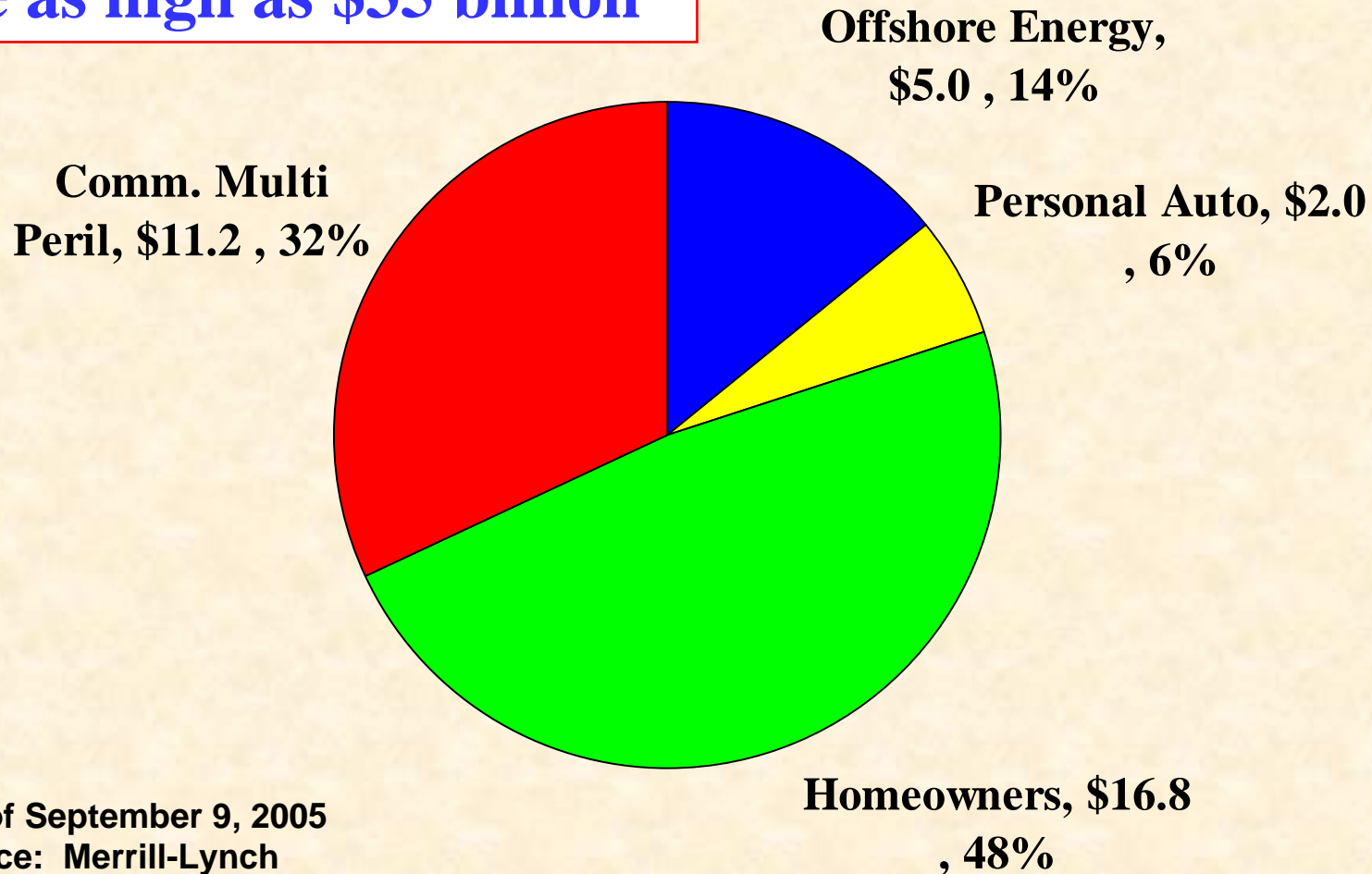




Hurricane Katrina Loss

*Distribution by Line (\$ Billions)**

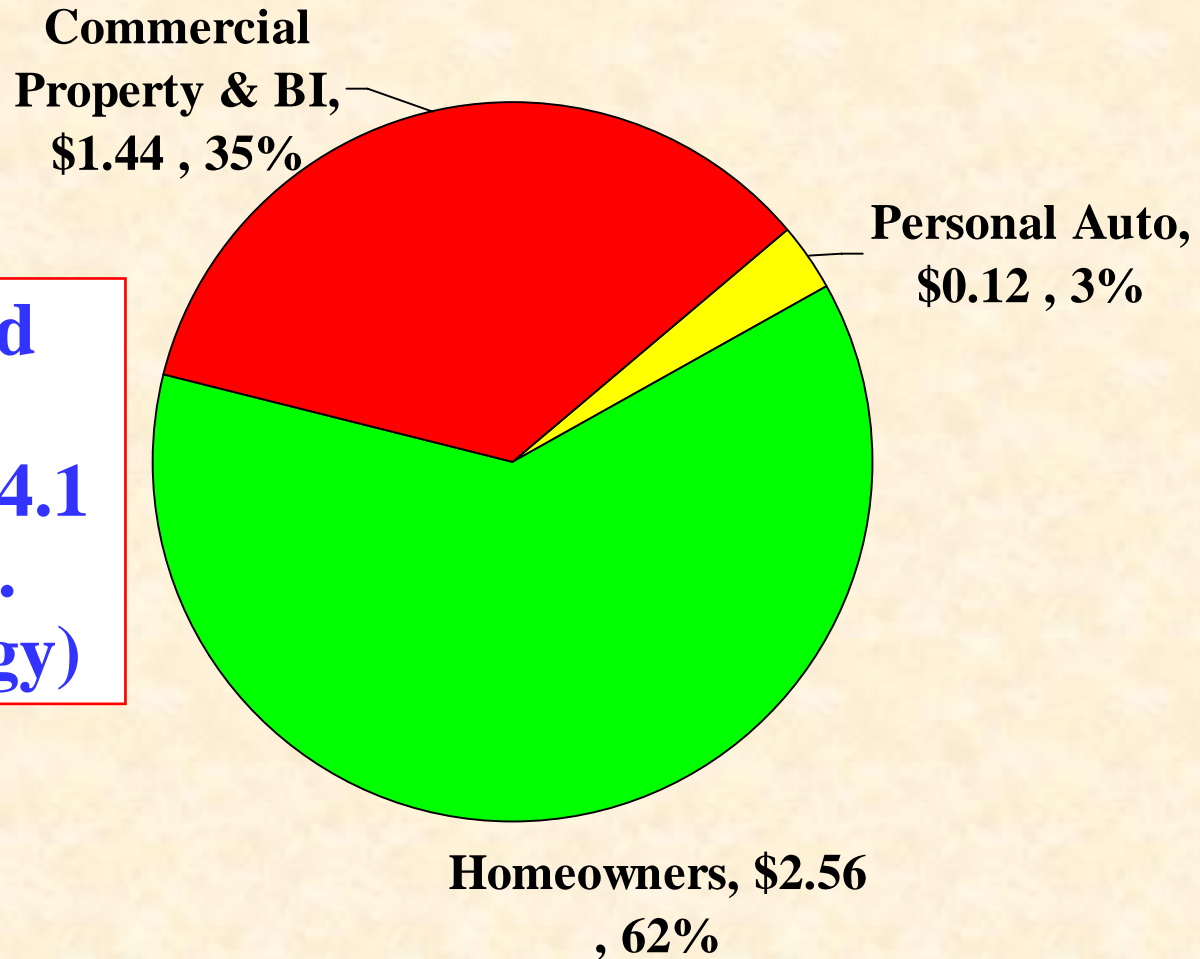
Total insured losses could be as high as \$35 billion



*As of September 9, 2005
Source: Merrill-Lynch



*Hurricane Rita Loss Distribution by Line (\$ Billions)**



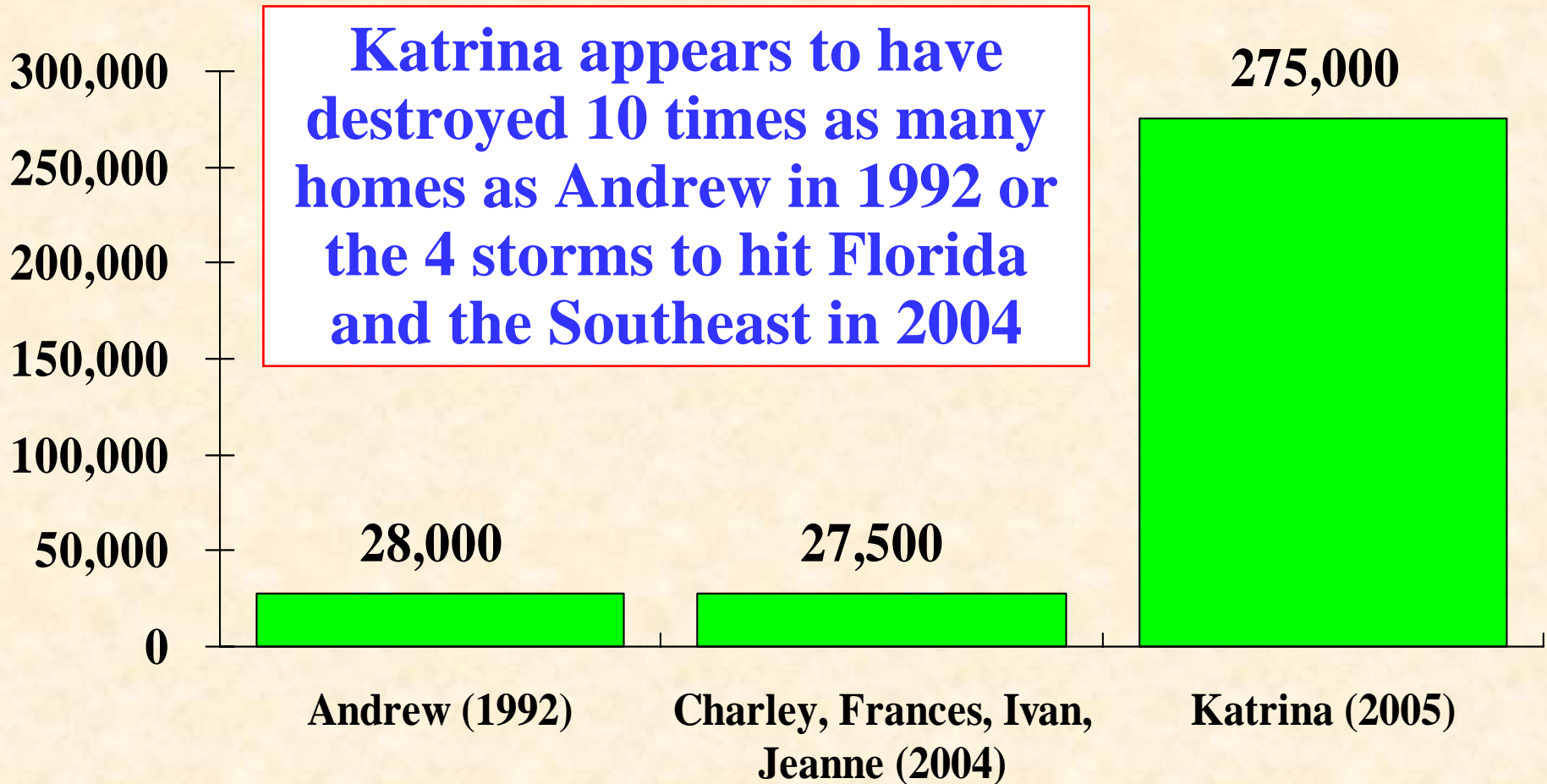
Total insured losses are estimated at \$4.1 billion (excl. offshore energy)

*As of September 26, 2005

Source: Insurance Information Institute



*Number of Homes Destroyed by Major Hurricanes**

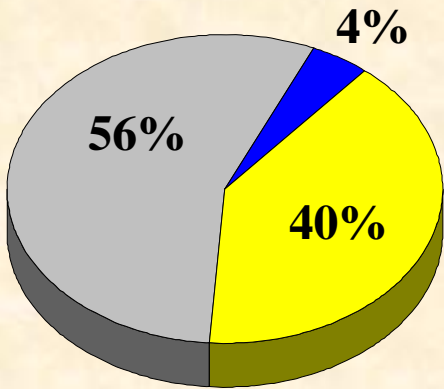


*Destruction is defined as a structure made uninhabitable or damaged beyond economic repair.
Source: National Association of Home Builders, National Red Cross (as of 9/15/05).

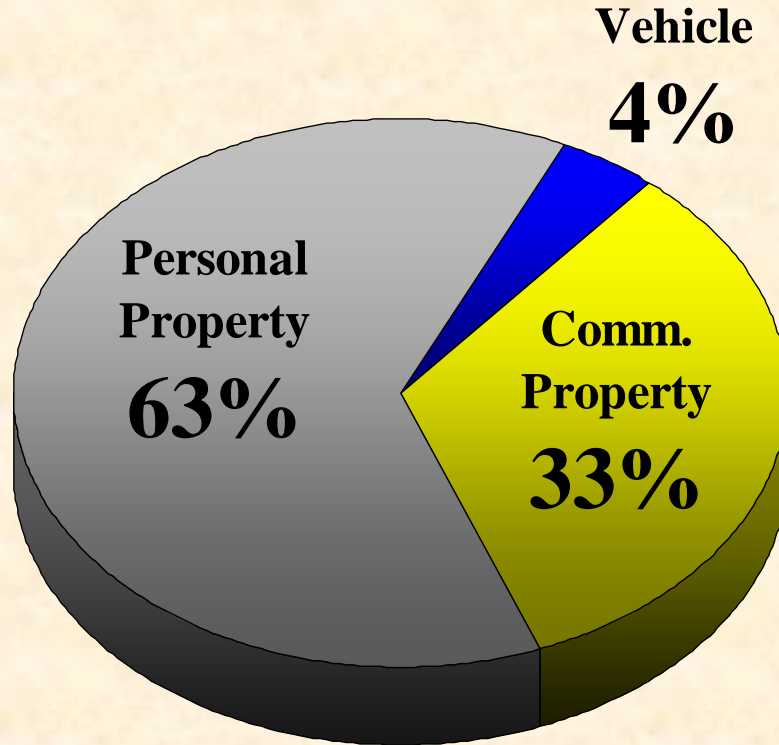


Personal Property Losses Accounted for Largest Share Damage from 2004 Hurricanes*

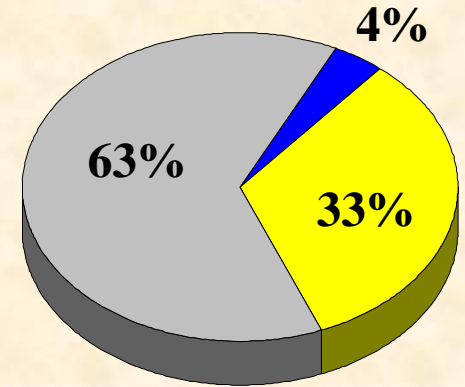
Charley



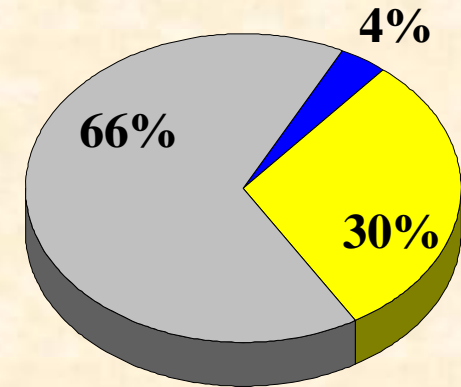
TOTAL



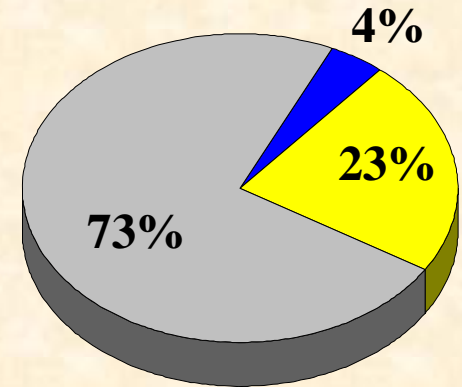
Ivan



Frances



Jeanne

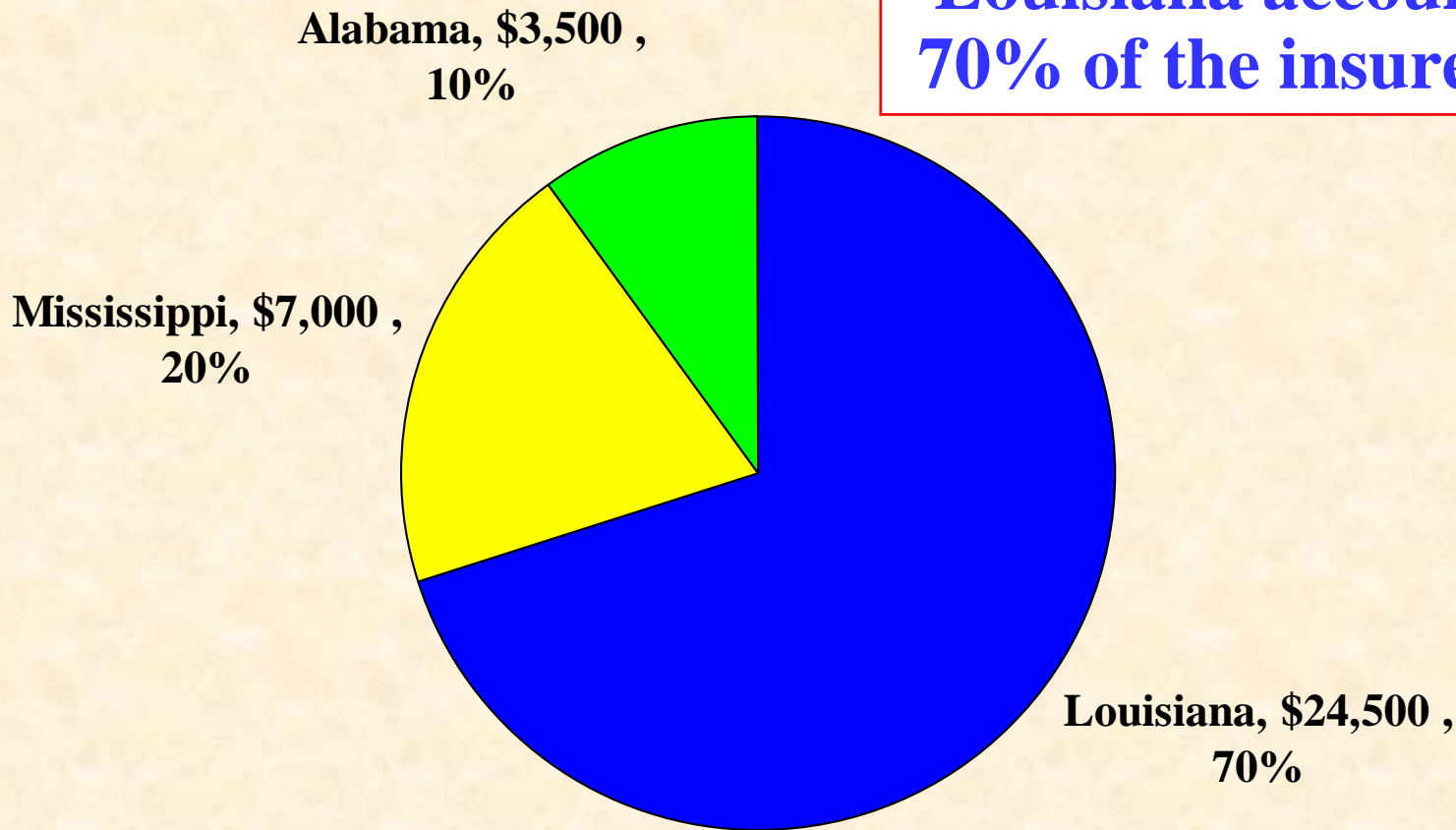


Source: ISO/PCS; Insurance Information Institute.

*Breakdowns based on FL losses, which accounted for 85% of losses for all affected states.



*Hurricane Katrina Loss Distribution by State (\$ Billions)**



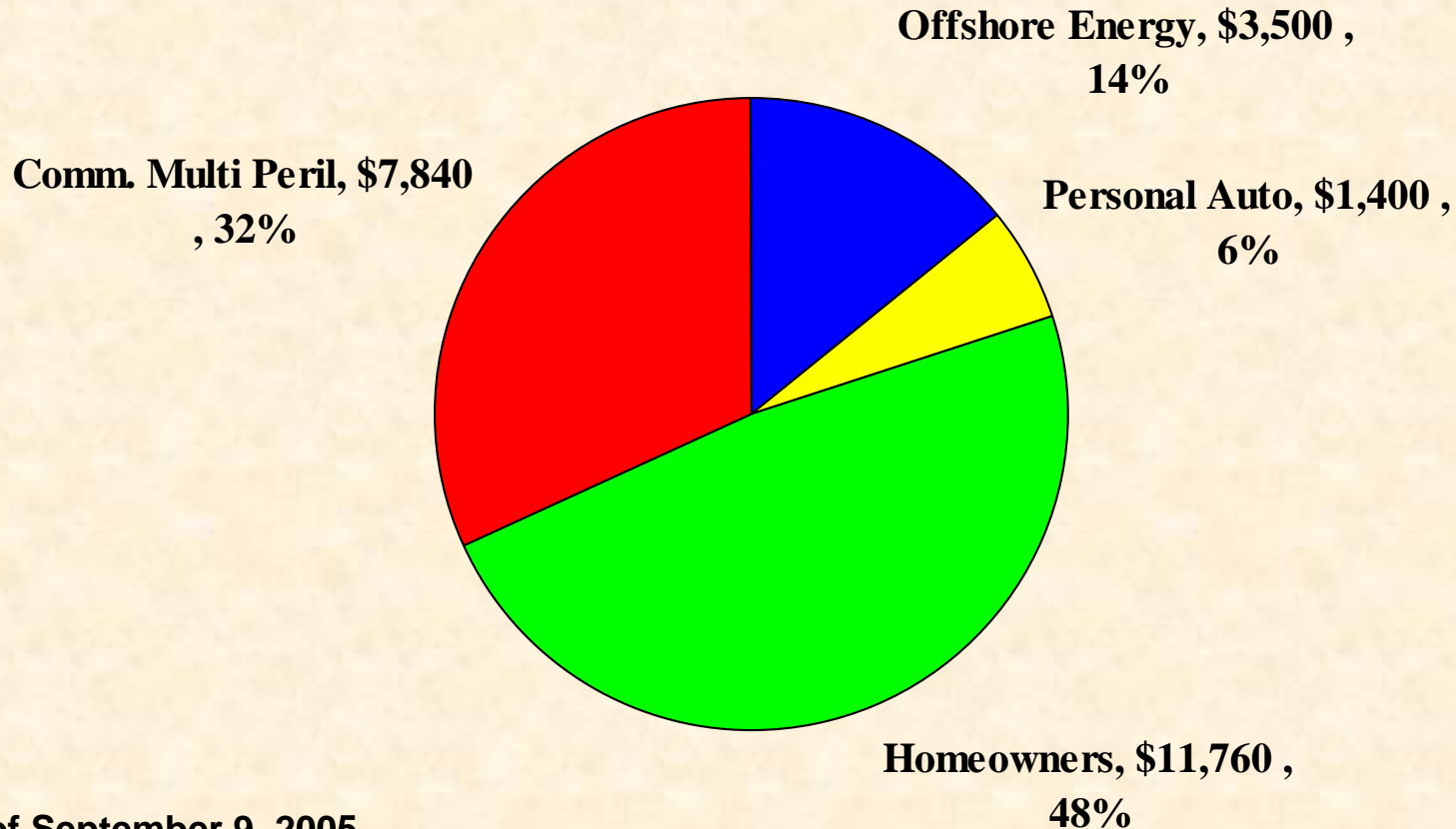
**Louisiana accounted for
70% of the insured losses**



Louisiana: Hurricane Katrina Loss

*Distribution by Line (\$000)**

Louisiana insured losses are estimated at \$24.5 billion

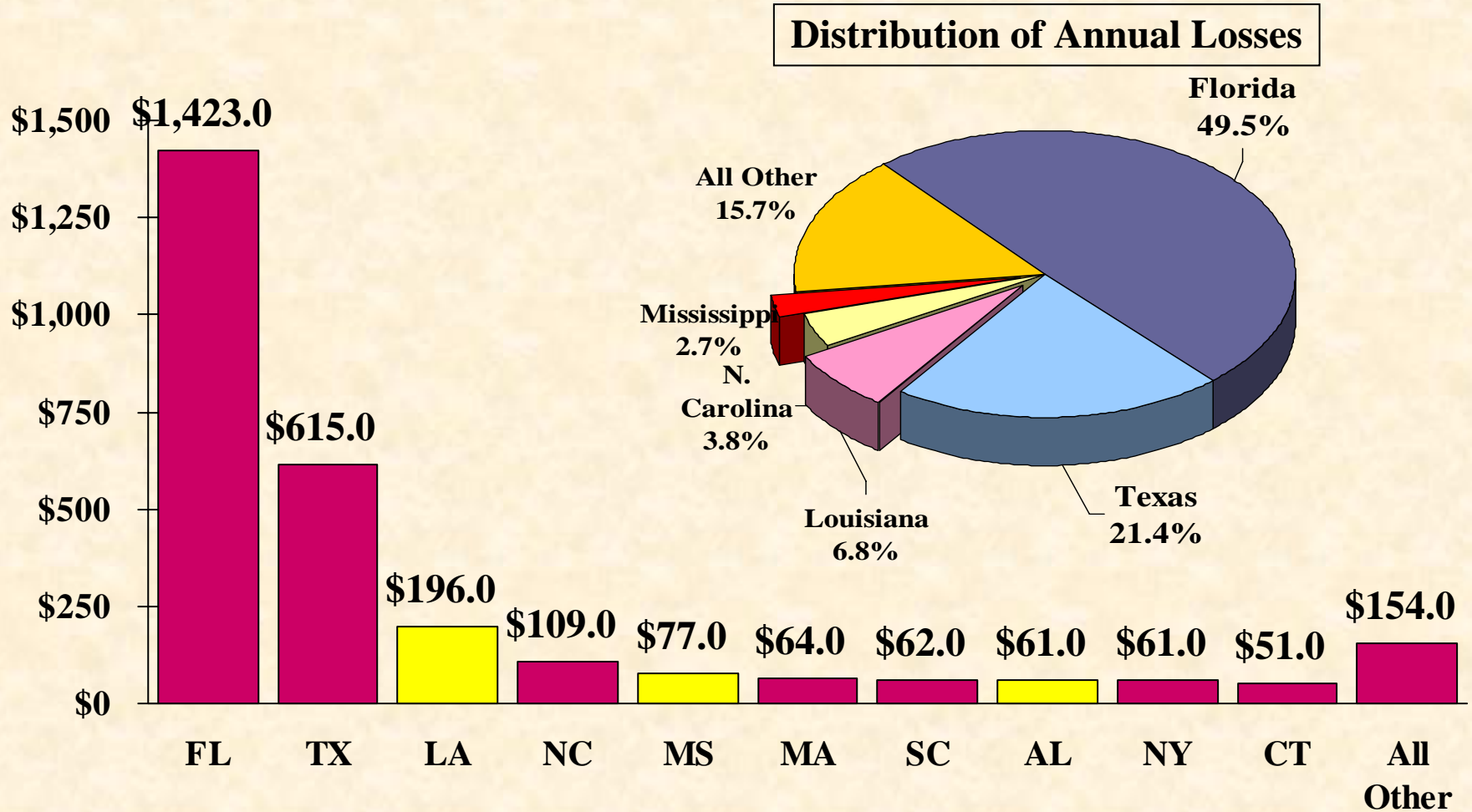


*As of September 9, 2005
Source: Merrill-Lynch



Average Annual Tropical Cyclone Insured Losses*

(Top 10 States, \$ Millions)

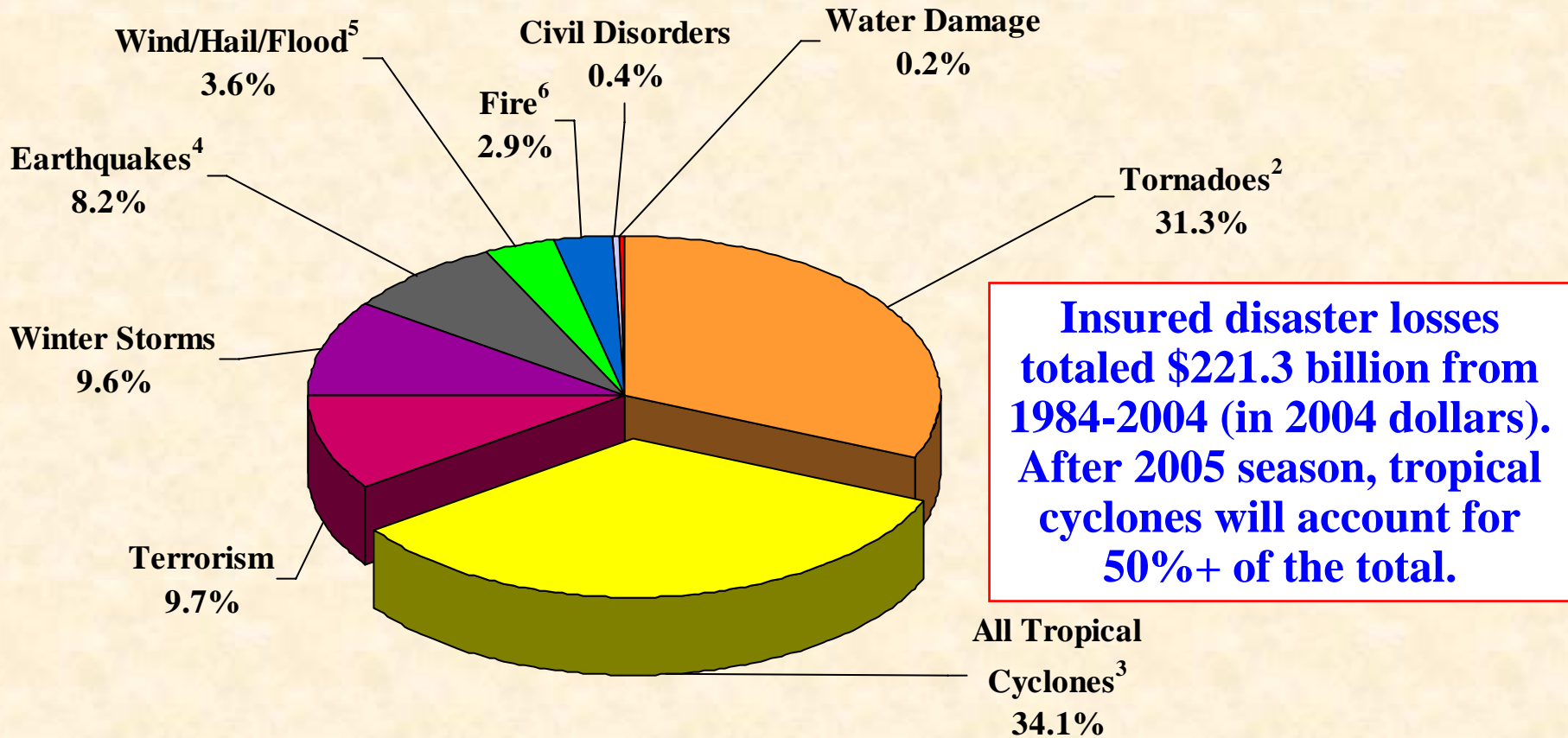


*Normalized losses adjusted for inflation, housing density, wealth and wind insurance coverage, based on historical data for 100-year period 1900-1999.

Source: Tillinghast-Towers Perrin



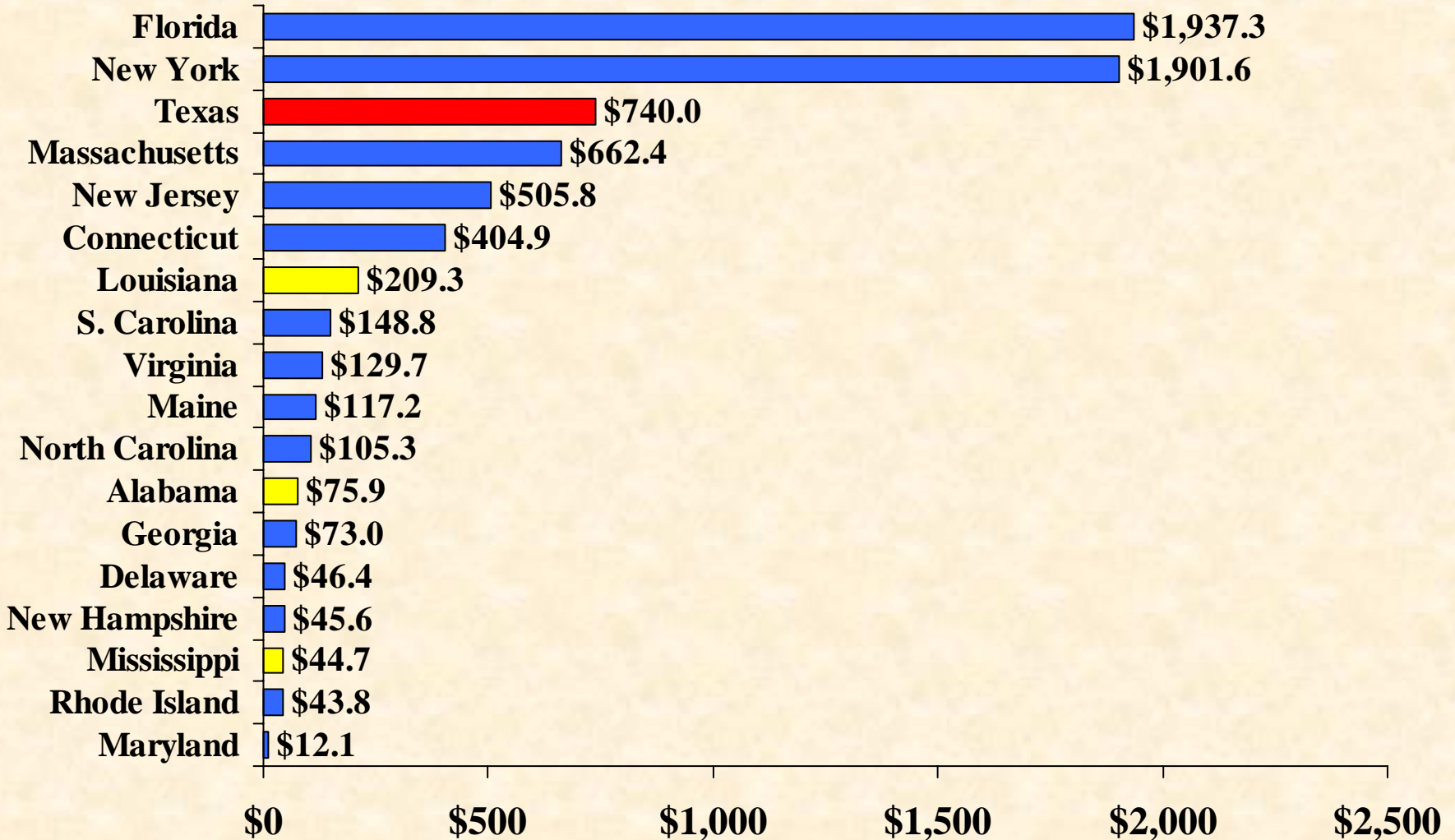
Inflation-Adjusted U.S. Insured Catastrophe Losses By Cause of Loss, 1984-2004E¹



¹ Catastrophes are all events causing direct insured losses to property of \$25 million or more in 2004 dollars. Catastrophe threshold changed from \$5 million to \$25 million beginning in 1997. Adjusted for inflation by the III.
² Excludes snow. ³ Includes hurricanes and tropical storms. ⁴ Includes other geologic events such as volcanic eruptions and other earth movement. ⁵ Does not include flood damage covered by the federally administered National Flood Insurance Program. ⁶ Includes wildland fires.

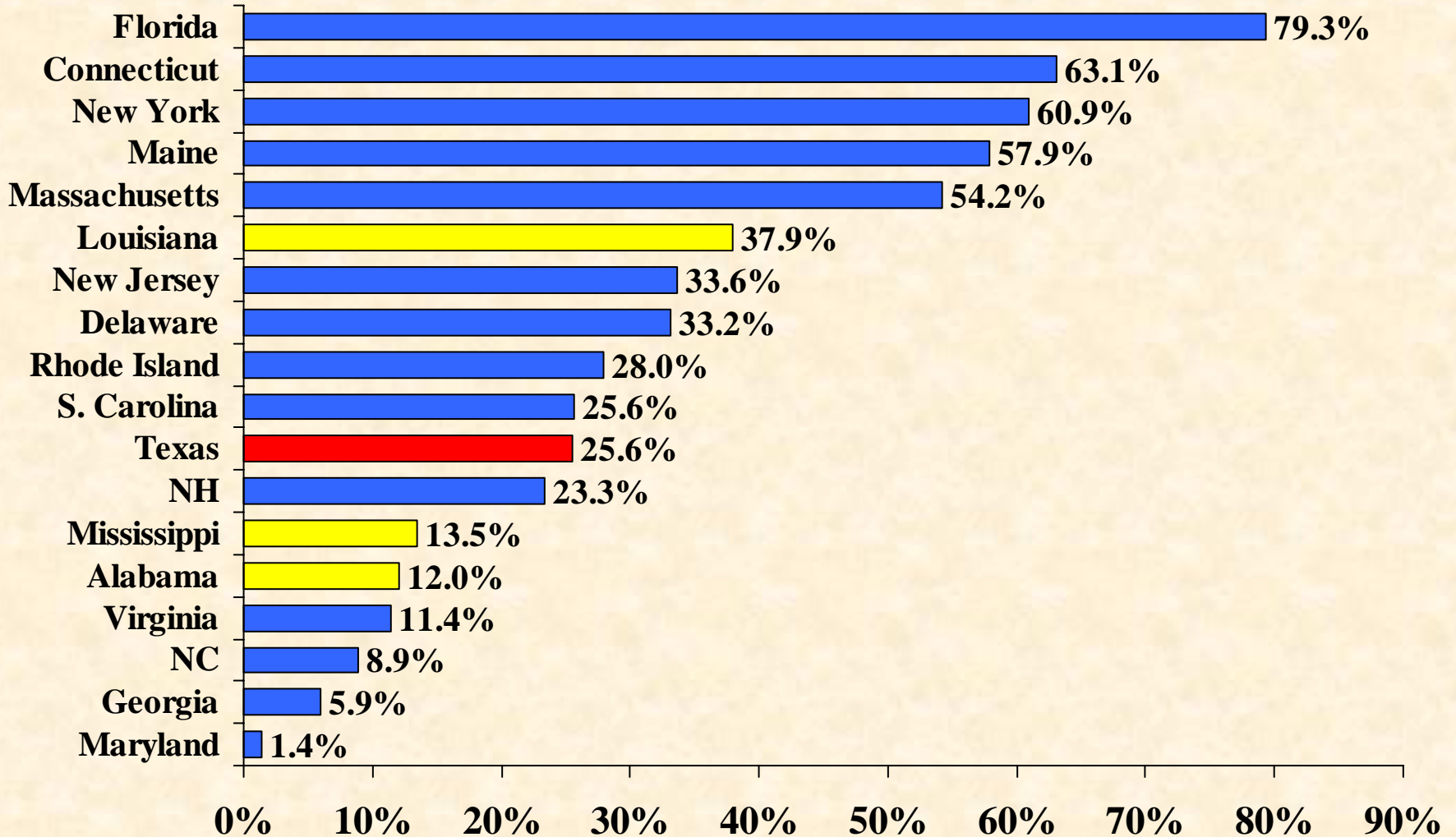


Total Value of Insured Coastal Exposure (2004, \$ Billions)





Insured Coastal Exposure as a % of Statewide Insured Exposure (2004, \$ Billions)



Source: AIR Worldwide

Hurricane Katrina:

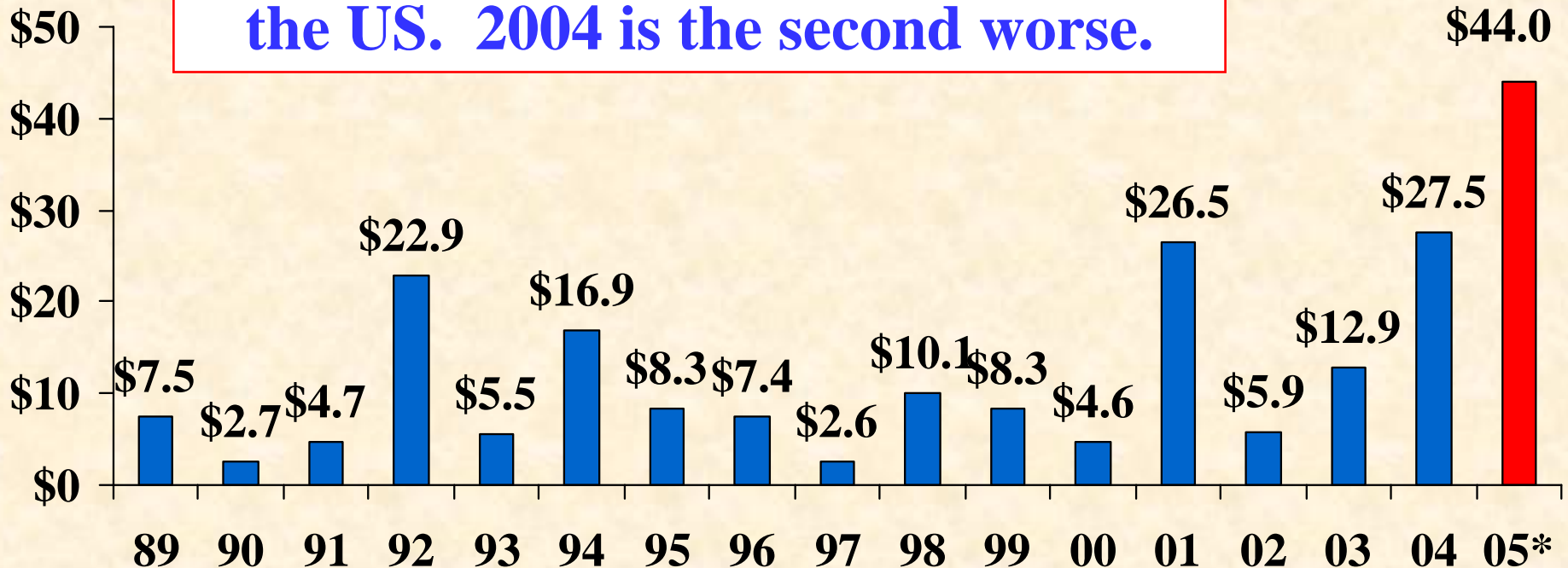
*Exacting a Toll on
Underwriting
Performance & Profits*





U.S. Insured Catastrophe Losses (\$ Billions)

2005 will be by far the worst year ever for insured catastrophe losses in the US. 2004 is the second worse.



*As of 6/30/05 plus \$920 in insured for Hurricane Dennis in July, \$35 billion (est.) for Hurricane Katrina in August, \$800 million (AIR est.) for Hurricane Ophelia in September and \$4.1B for Hurr. Rita.

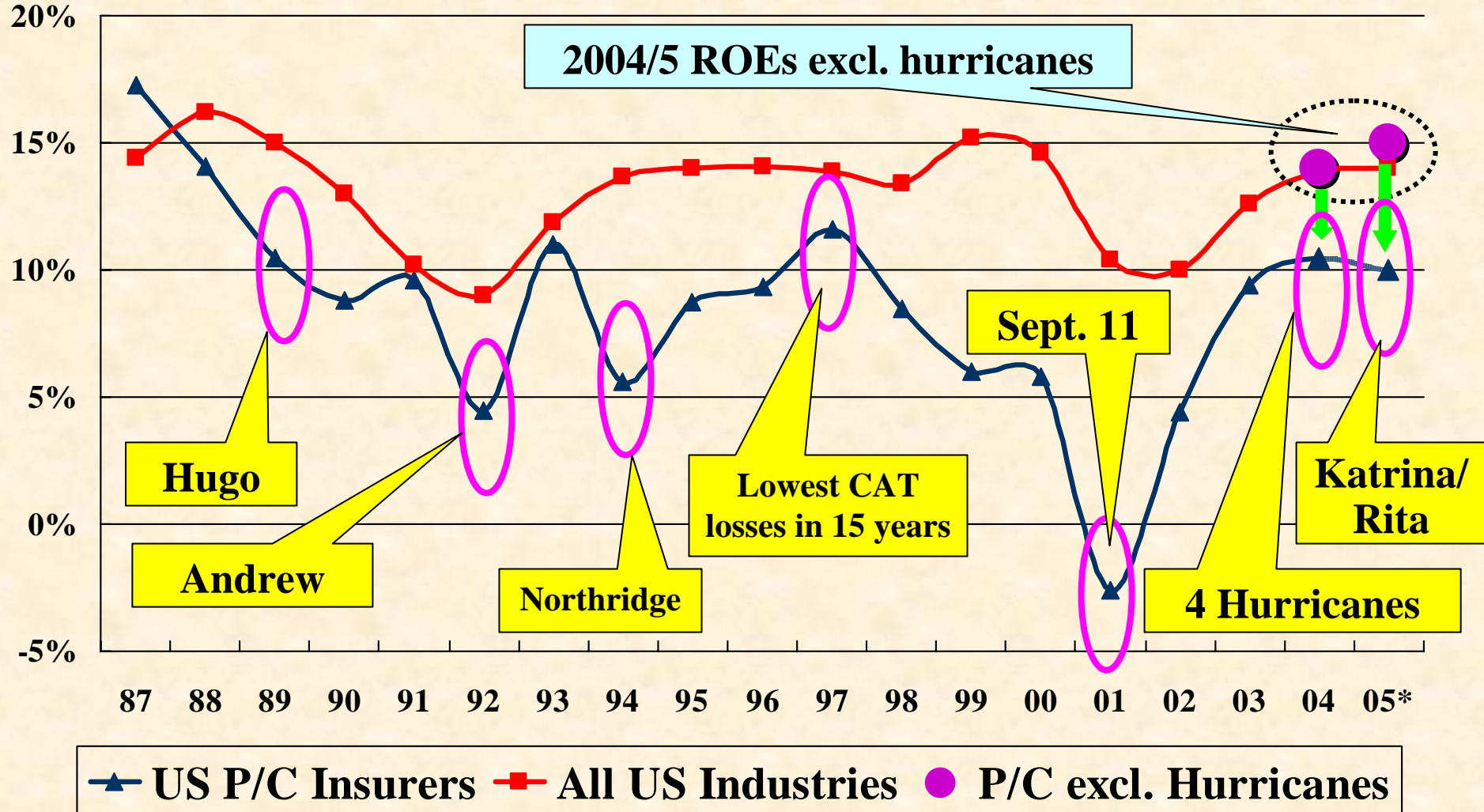
Note: 2001 figure includes \$20.3B for 9/11 losses reported through 12/31/01. Includes only business and personal property claims, business interruption and auto claims.

Source: Property Claims Service/ISO; Insurance Information Institute



ROE: P/C vs. All Industries

1987-2005E



*Legal Environment
Will Affect
Katrina's Outcome*





Business Leaders Ranking of Liability Systems for 2005

Best States

1. Delaware
2. Nebraska
3. North Dakota
4. Virginia
5. Iowa
6. Indiana
7. Minnesota
8. South Dakota
9. Wyoming
10. Idaho

New in 2005

ND, IN, SD, WY

Drop-Offs

ID, UT, NH, KS

Worst States

41. Hawaii
42. Florida
43. Arkansas
44. Texas
45. California
46. Illinois
- 47. Louisiana**
- 48. Alabama**
49. West Virginia
- 50. Mississippi**

Newly Notorious

HI, FL

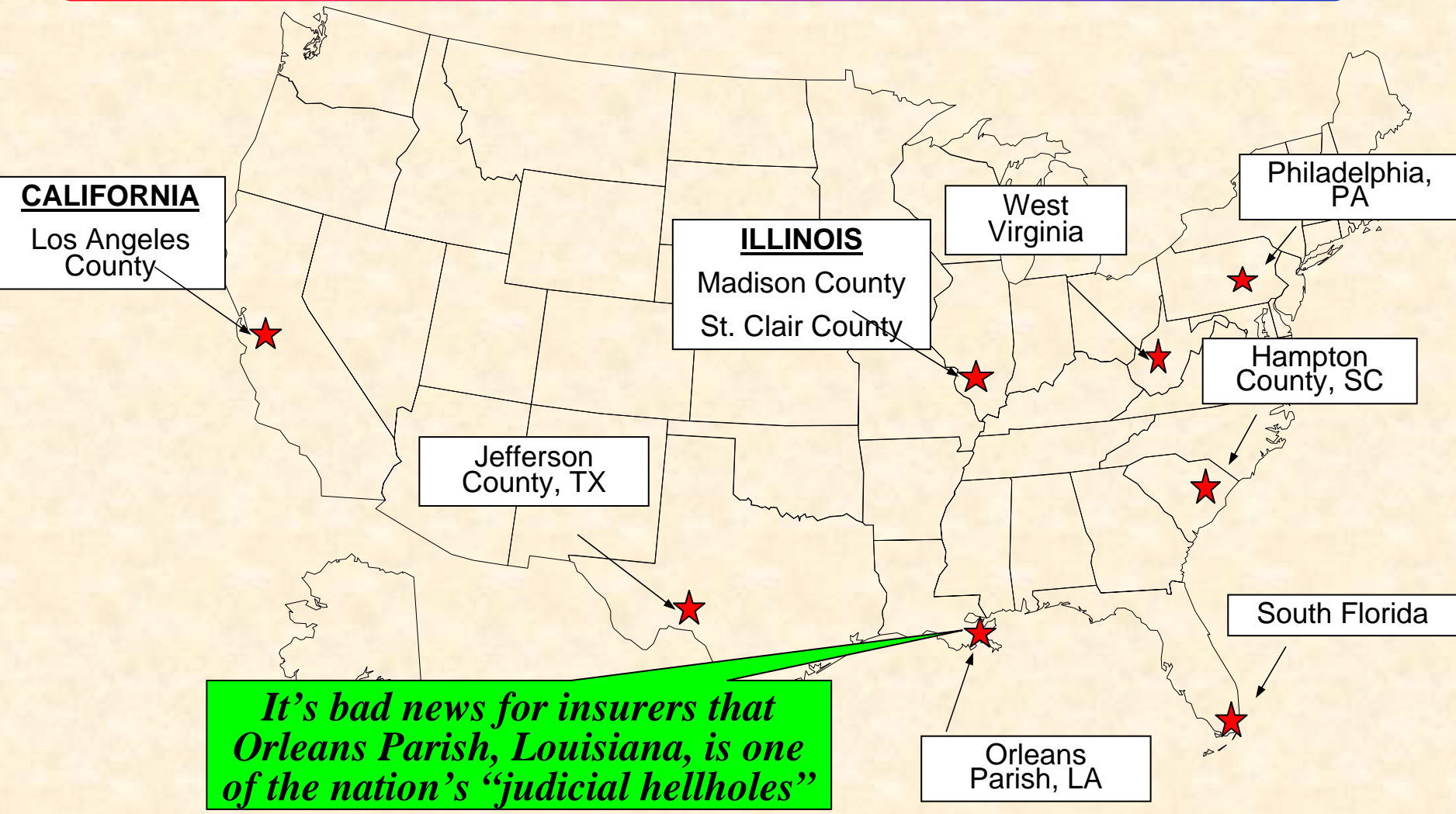
Rising Above

MO, MT

*LA, AL and MS's
liability systems are
ranked among the worst
in the country by the US
Chamber of Commerce*



The Nation's Judicial Hellholes





Types of Lawsuits Being Filed in the Wake of Hurricane Katrina

- **Insurance**

- Lawyers (e.g., Dicky Scruggs) and Mississippi Attorney General Jim Hood are suing insurers over whether homeowners policies should cover flood.

- **Oil Spills**

- Lawyers have sued the energy industry over ruptured oil tanks and pipelines that have fouled Louisiana neighborhoods.

- **Fishing Grounds**

- At least 2 cases filed on behalf of LA's fishermen over damage to estuaries, bays and oyster beds caused by the oil spills.

- **Wetlands**

- One suit filed against the oil & gas industry for its alleged role in the disappearance of wetlands that protected Louisiana from storm surges.



Legal Theories Being Floating by Trial Bar to Get Insurers to Pay Excluded Flood Losses

- **Valued Policy Law**

- Idea is that if property is a total loss the insurer cannot dispute the value of the property and must pay limits. Insurers will argue that flood is an excluded peril and VPL doesn't apply. Insurers lost Mierzwa case in FL, but FL provided a legislative "fix" for that wayward court decision. Could result in policyholders with flood coverage receiving 200% of limits. Applies only to insureds with flood cover. VPL for fire only in MS, none in AL.

- **Wind → Efficient Proximate Cause of Surge**

- Says that because surge was driven by wind and because wind is a covered cause of loss, it is the efficient proximate cause of the flood and should therefore should be triggered.
- Also alleges storm surge is not specifically excluded by name

- **Barge Breach Levee**

- A barge crashed into one levee, causing it to rupture. Theory is that this is a covered cause of loss because it's not excluded (even though damage produced a flood).



Relevant Homeowners Insurance Policy Language Governing Water Damage

- **Wind and Hail Coverage (*a named peril*)**
- **Flood Exclusion**
- **FEMA/NFIP Flood Definition**
- **Fungus & Mold Exclusion**
- **Earth Movement Exclusion**



Wind Coverage in HO Policy: Limits and Boundaries of Coverage

- **Wind and Hail Coverage (Named Peril)**
 - **Windstorm or Hail**
 - “We do not pay for loss to the interior of a building or to personal property inside, caused by rain, snow, sleet, sand or dust *unless the wind or hail first damages the roof or walls and the wind forces rain, snow, sleet, sand or dust through the opening.*”



Typical Flood Exclusion in Homeowners Insurance Policy

Flood Exclusion

- **Water Damage, meaning any loss caused by, resulting from, contributed to or aggravated by:**
 1. *flood, surface water, waves, tidal water or overflow of any body of water, or spray from any of these, whether or not driven by wind.*
 2. Water or water-borne material which backs up through sewers or drains, or which overflows or is discharged from a sump pump, sump pump well or other system that is designed to remove subsurface water which is drained from the foundation area; or
 3. Water or water-borne material below the surface of the ground, including water which exerts pressure on, or flows, seeps or leaks through any part of a building, sidewalk, foundation, driveway, swimming pool or other structure or water that causes earth movement.

This exclusion applies whether or not the water damage is caused by or results from human or animal forces or any act of nature.



Facts About the Flood Exclusion

- **Has existed in policies for decades**
- **Flood Exclusion is effectively absolute—excluding water under all circumstances**
- **It is the reason for the existence of FEMA's NFIP program since it was established in 1968**
- **Approved by regulators in all 50 states**



NFIP Flood Definition: Covers Exactly What HO Policies Don't

• "A general and temporary condition of partial or complete inundation of two or more acres of normally dry land area or of two or more properties (at least one of which is the policyholder's property) from:

- *Overflow of inland or tidal waters; or*
- *Unusual and rapid accumulation or runoff of surface waters from any source; or*
- *Mudflow; or*
- *Collapse or subsidence of land along the shore of a lake or similar body of water as a result of erosion or undermining caused by waves or currents of water exceeding anticipated cyclical levels that result in a flood as defined above."*



Typical Fungus & Mold Exclusion in Homeowners Insurance Policy

- **Fungus and Mold Exclusion**
 - *“We do not cover loss or damage, no matter how caused, to the property which results directly or indirectly from fungus and mold. There is no coverage for loss which, in whole or in part, arises out of, is aggravated by, contributed to by acts or omissions of persons, or results from fungus and mold. This exclusion applies regardless of whether fungus and mold arises from any other cause of loss, including but not limited to a loss involving water, water damage or discharge, which may be otherwise covered by this policy, except as granted [by exception].”*



Relevant Homeowners Insurance Policy Language Governing Water Damage

- **Earth Movement Exclusion**

- Applies to any loss caused by, resulting from, contributed to or aggravated by events that include, but are not limited to:
 1. Earthquake and earthquake aftershocks;
 2. Volcanic eruption and volcanic effusion;
 3. Sinkhole;
 4. Subsidence;
 5. ***Mudslide including landslide, mudflow, debris flow, avalanche or sediment;***
 6. ***Erosion*** or excavation collapse;
 7. The sinking, rising, shifting, expanding, bulging, cracking, settling or contracting of the earth, soil or land; and
 8. Volcanic explosion and lava flow except [by exception]

This exclusion applies whether or not the earth movement is combined with water or caused by or results from human or animal forces ***or any act of nature.***



Consequences of Mississippi AG's Actions

- **Sept. 15 suit by MS AG Hood constitutes and attempt to retroactively rewrite all HO insurance contracts in MS. *“Contract certainty” extinguished.***
- **Suit amounts to little more than an attempt to expropriate shareholder assets (and the equity of mostly non-MS policyholders of mutual insurers)**
- **The risk is fundamentally political, cannot be modeled or priced**
- **Insurers will necessarily be motivated to protect shareholder equity (and claims paying resources generally). Reinsurers will exert pressure too.**
- ***Also continues dangerous trend of AG assertion of authority over state insurance regulators***



Consequences if Coverage Rulings Went Against Insurers

- **Creates dangerous precedent of contract abrogation**
- **Effectively renders flood exclusion *null and void* & usurps authority of state insurance regulator**
- **Creates enormous financial liability for explicitly excluded peril for which *no premium was collected***
- **HO insurance rates *countrywide* become instantaneously inadequate**
 - **Would provoke largest homeowners insurance rate in history on a national basis**
- **Insurers would likely pull back from many markets because of lack of contract certainty**
- **Renders NFIP program useless**
- **Unfair to NFIP policyholders and other insureds**



MS AG and Scruggs Suits Not Supported by Governor, Regulator

• **Recent Quotes:**

- *“It’s crucial that people who enter contracts keep their contracts. And that’s what an insurance policy is, a contract....For those people [who didn’t buy flood coverage] we are working very hard that if they don’t have insurance or don’t have coverage, that we can up with a way to help them financially.”*
 - Mississippi Governor Haley Barbour, *WSJ*, 9/19/05, p.C9.

- *“The insurance industry can take care of so many, the flood insurance program can take care of so many...but there are still others out there that do not fit under either of these.”*
 - Mississippi Insurance Commissioner George Dale, *WSJ*, 9/19/05, p.C9.

- *For the government to make payments to people who didn’t buy flood insurance “undermines the purpose of an insurance scheme...If the government becomes the insurer of last resort, even when people don’t get insurance, then people won’t buy any insurance.”*
 - White House Budget Director Joshua Bolten as quoted in the *WSJ*, 9/26/05, p.A2.



Status of Litigation Against Insurers on Flood vs. Wind Issue

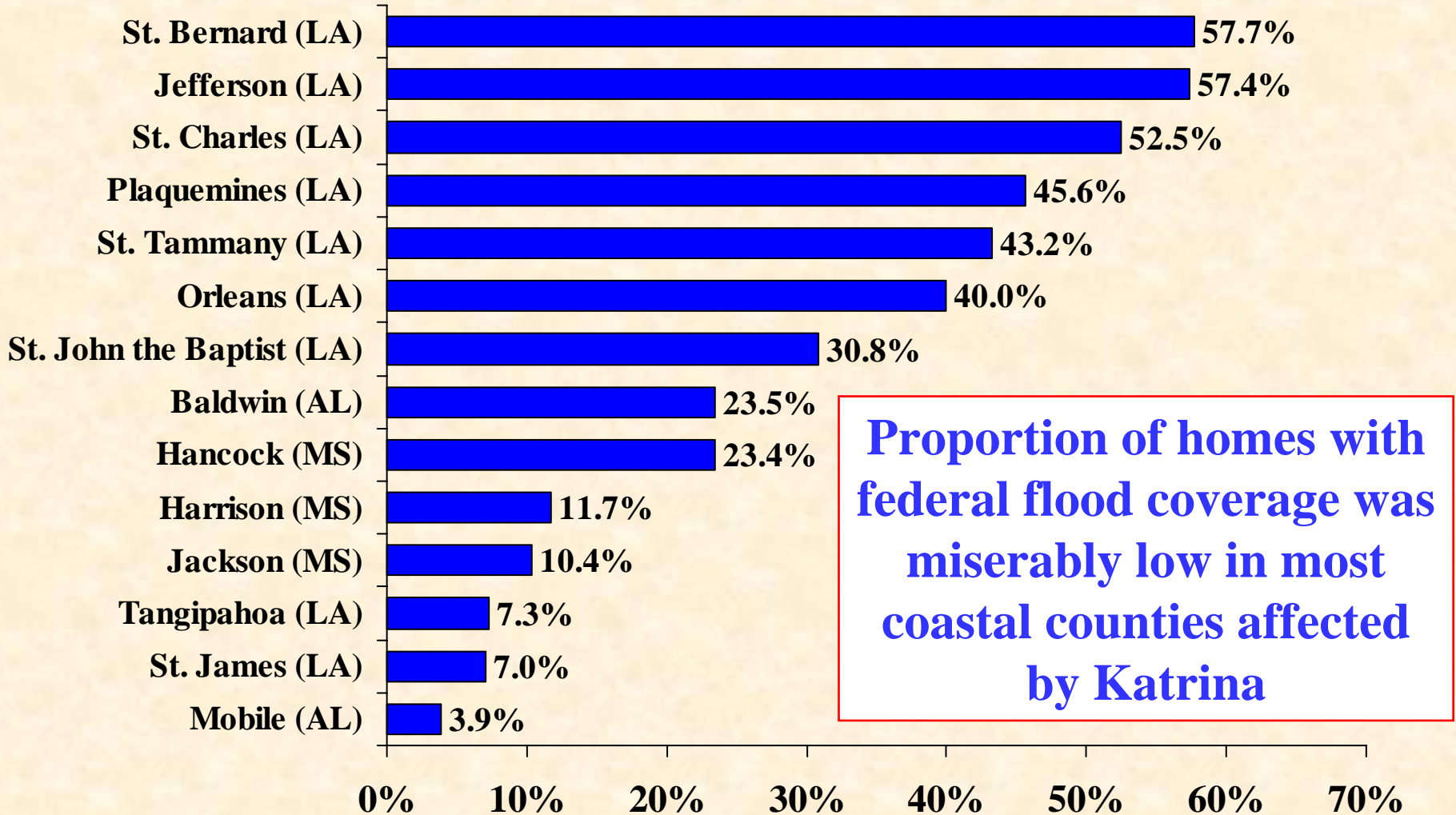
- **MS Atty. General Hood:**
 - Called actions of insurers “unconscionable.” Filed an unsuccessful order for immediate injunctive relief against 5 insurers seeking to stop them from drawing wind/water distinction. Suit was remanded to a federal court because it makes reference to NFIP. Will likely die there soon.
- **Scruggs Case:**
 - Stated that will he bring suits against insurers in MS week of 9/19/05.
 - Because of recent tort reform changes in MS, Scruggs can’t bring a class action, has to try cases individually.
 - Says he will take “drastically” reduced contingency fee
 - Failure of AG suit should kill Scruggs’ case.
 - FYI: Scruggs’ Pascagoula home was heavily damaged. He had flood coverage.
- **Louisiana Suit**
 - Suit is like MS. LA Supreme Court looking at it as contract law case
 - Likely to be resolved soon in insurers favor

FEMA's National Flood Insurance Program



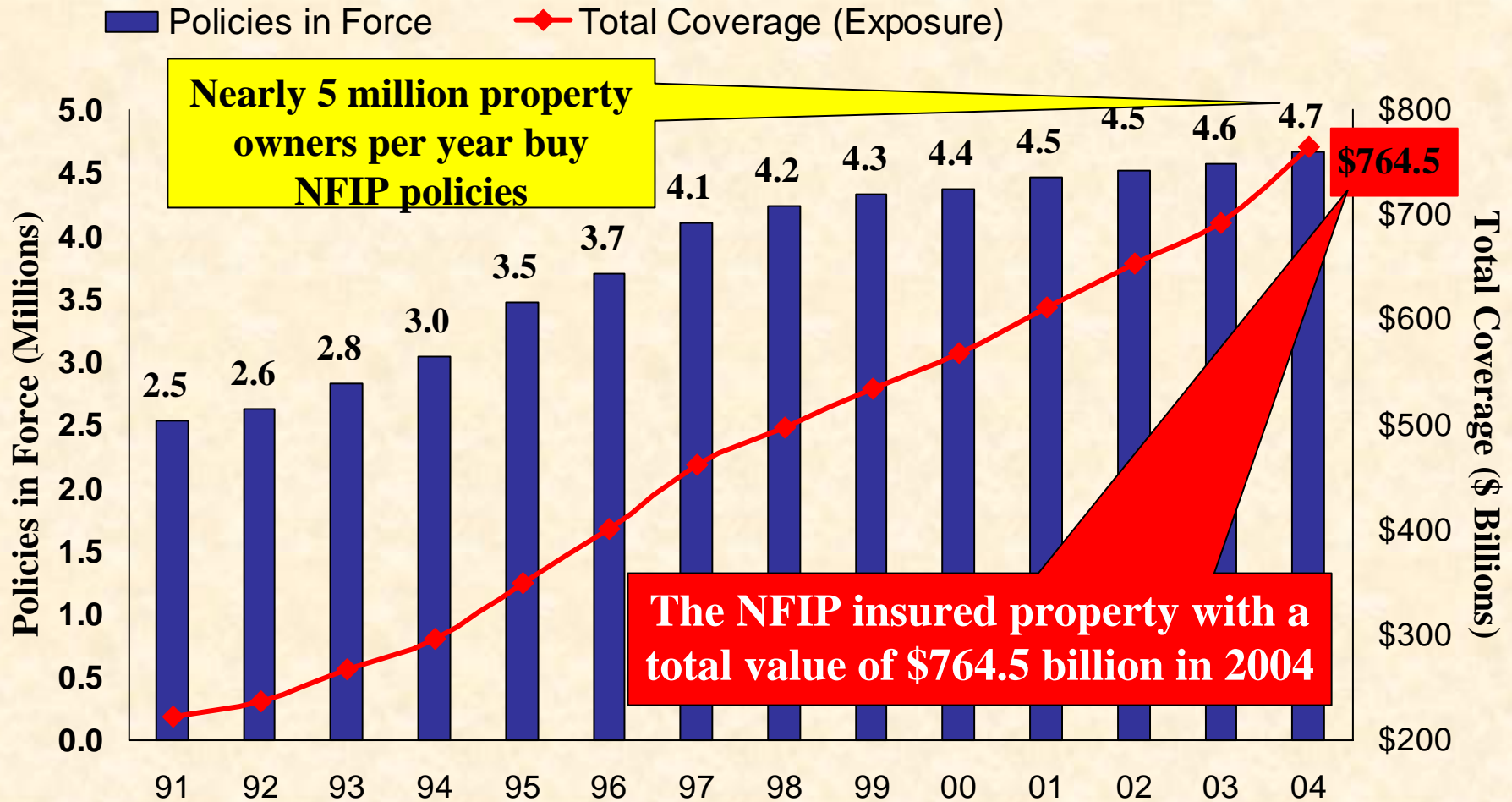


Percentage of Homes With Flood Insurance Policies: Coastal Counties Affected by Katrina





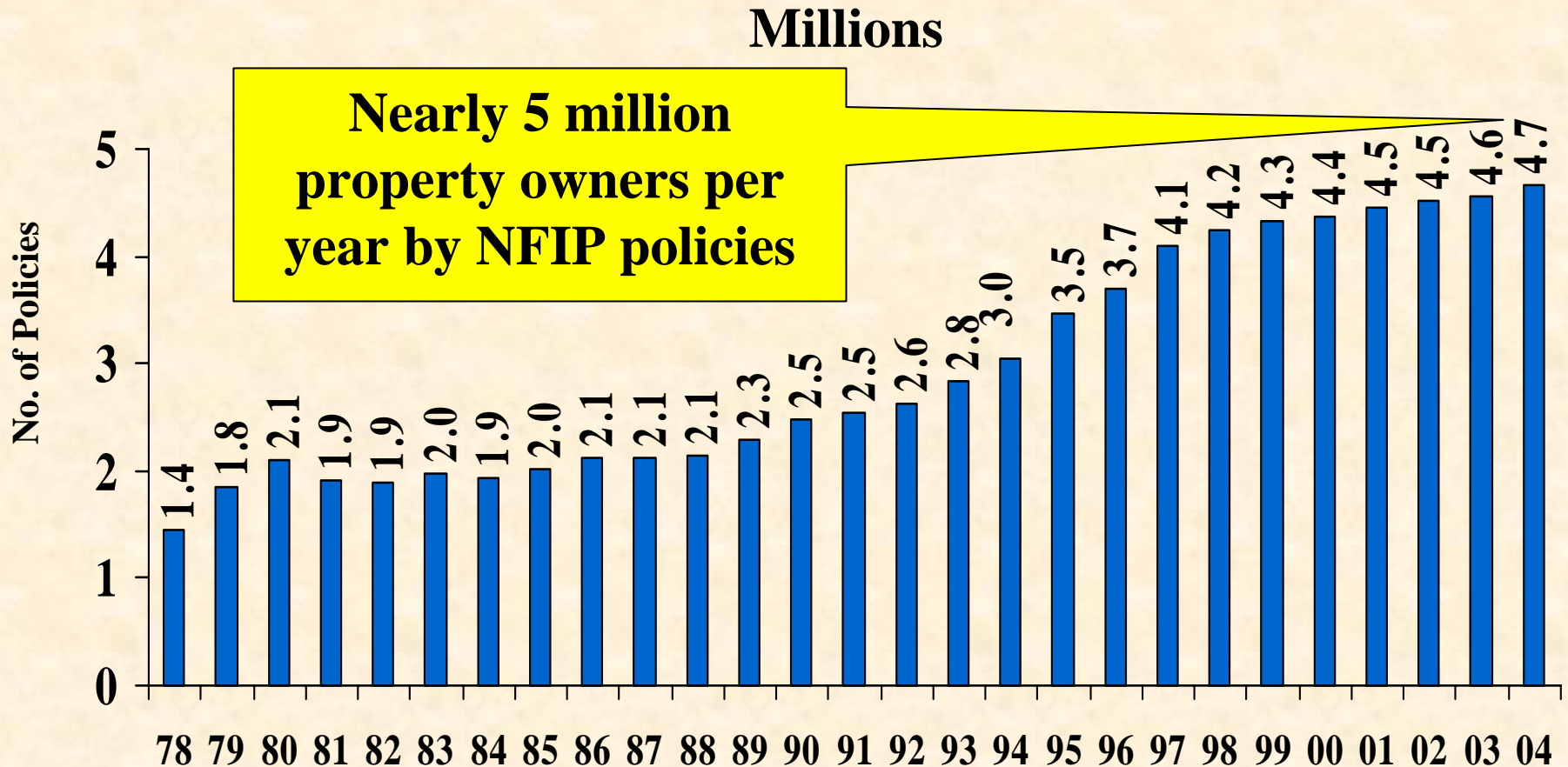
NFIP: Policies in Force and Total Coverage (Exposure)



Sources: FEMA, National Flood Insurance Program (NFIP)



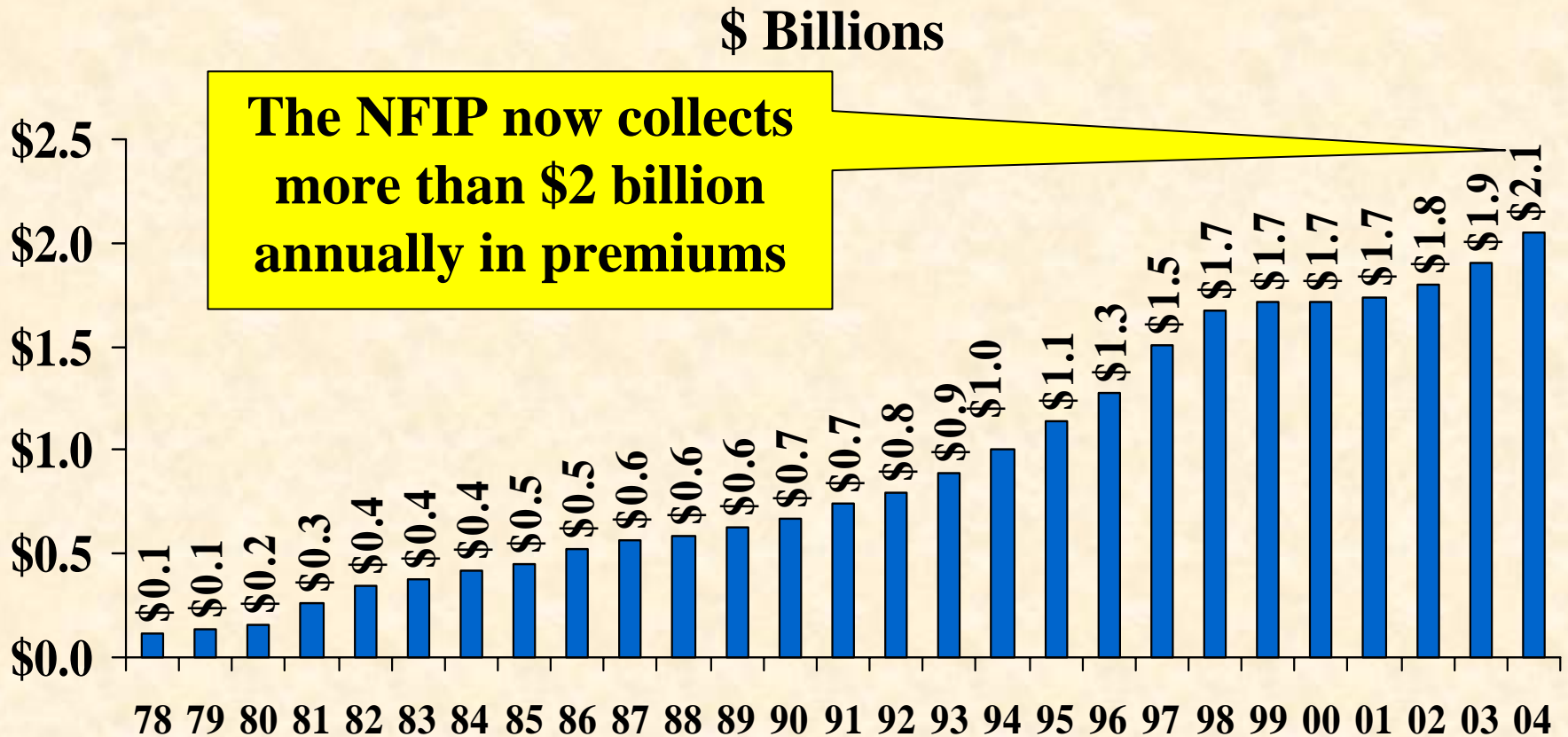
NFIP: Total Policies in Force by Calendar Year 1978-2004



Source: FEMA, National Flood Insurance Program (NFIP)

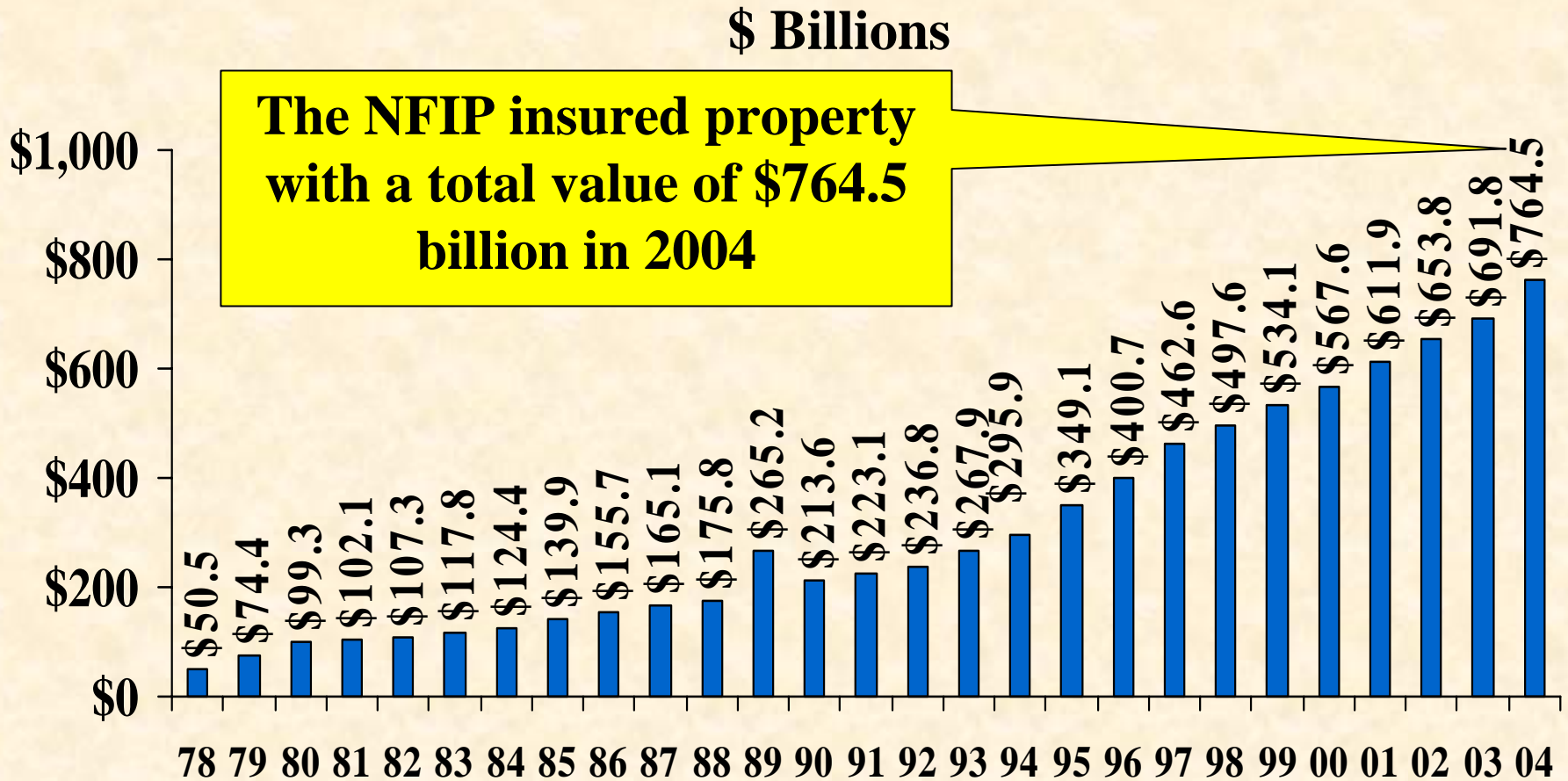


NFIP: Total Premium by Calendar Year 1978-2004





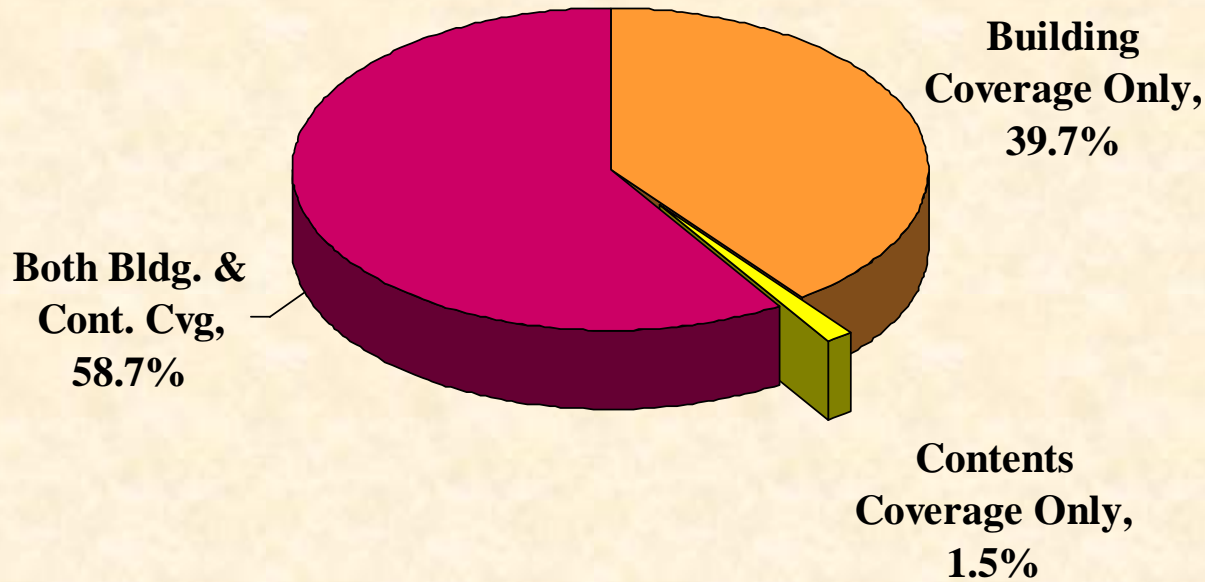
NFIP: Total Coverage by Calendar Year 1978-2004



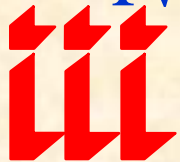
Source: FEMA, National Flood Insurance Program (NFIP)



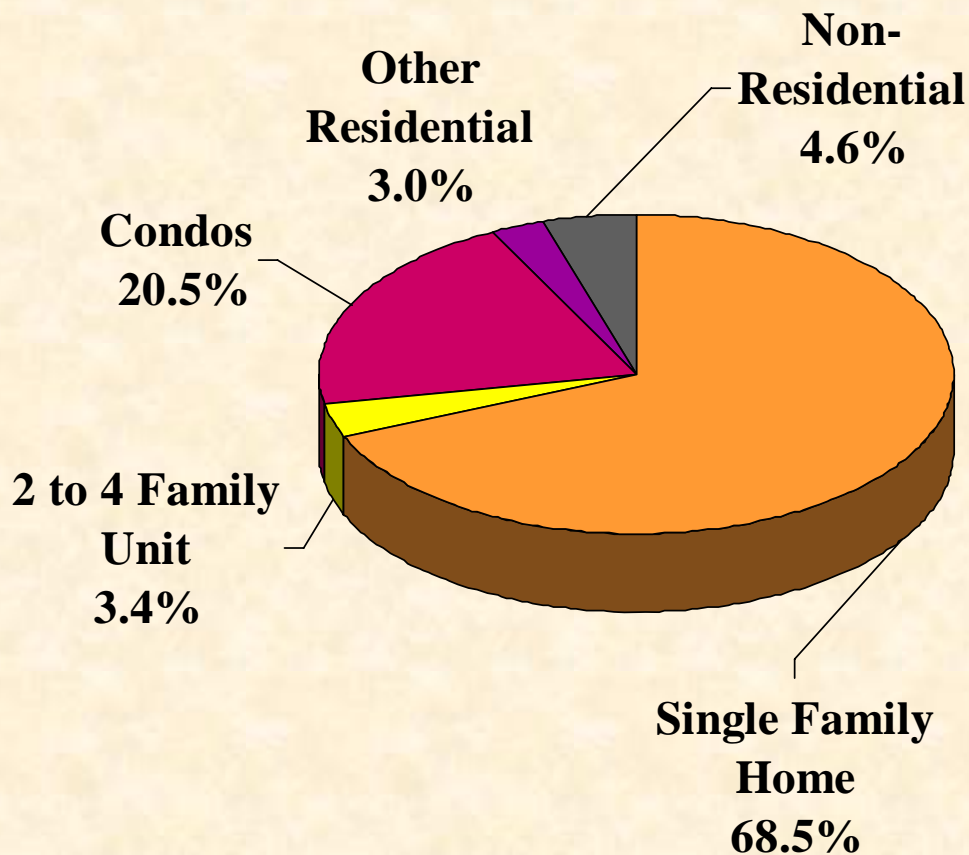
NFIP: Policies in Force By Coverage Type (As of July 31, 2005)



Coverage Type	Policies in Force
Building Coverage Only	1,845,481
Contents Coverage Only	72,008
Both Bldg & Cont Cvg	2,729,267
All Policies	4,646,756



NFIP: Policies in Force By Occupancy Type (As of July 31, 2005)

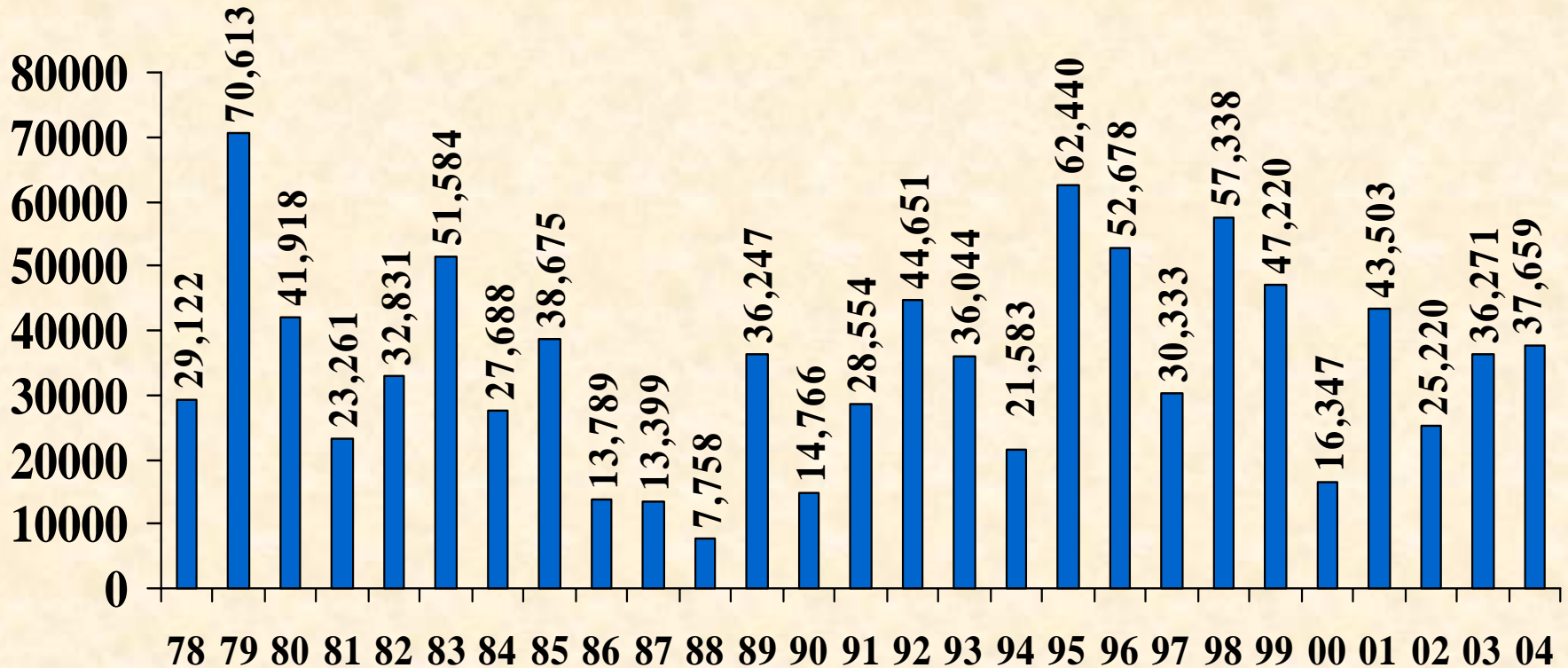


Occupancy Type	Policies in Force
Single Family Home	3,184,010
2 to 4 Family Unit	158,124
Condominiums	951,240
Other Residential	138,583
Non-Residential	214,799
Unknown Occupancy	--
All Policies	4,646,756



NFIP: No. of Losses Paid by Calendar Year 1978-2004

No. of Losses



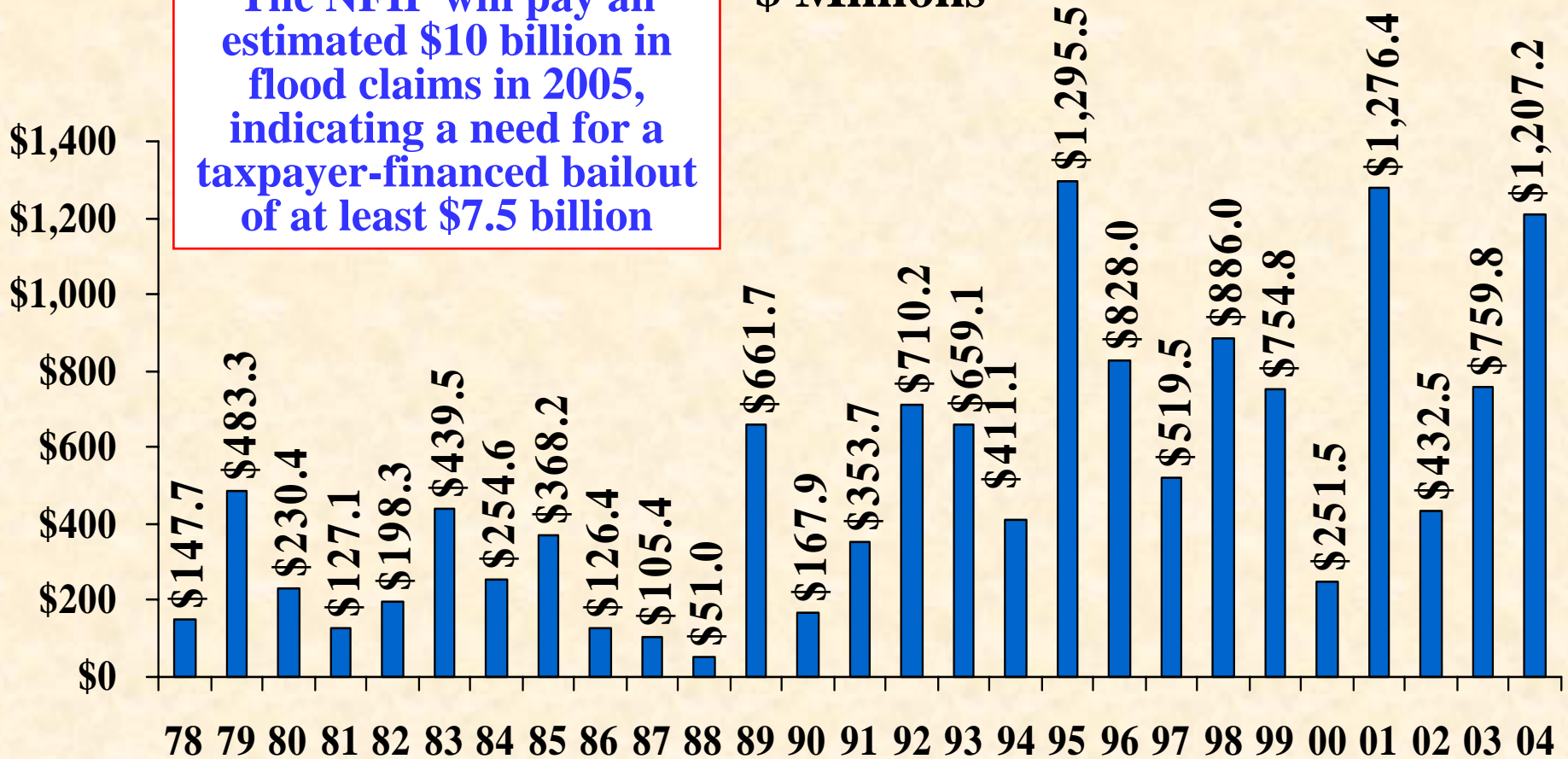
Source: FEMA, National Flood Insurance Program (NFIP)



NFIP: Loss Dollars Paid by Calendar Year 1978-2004

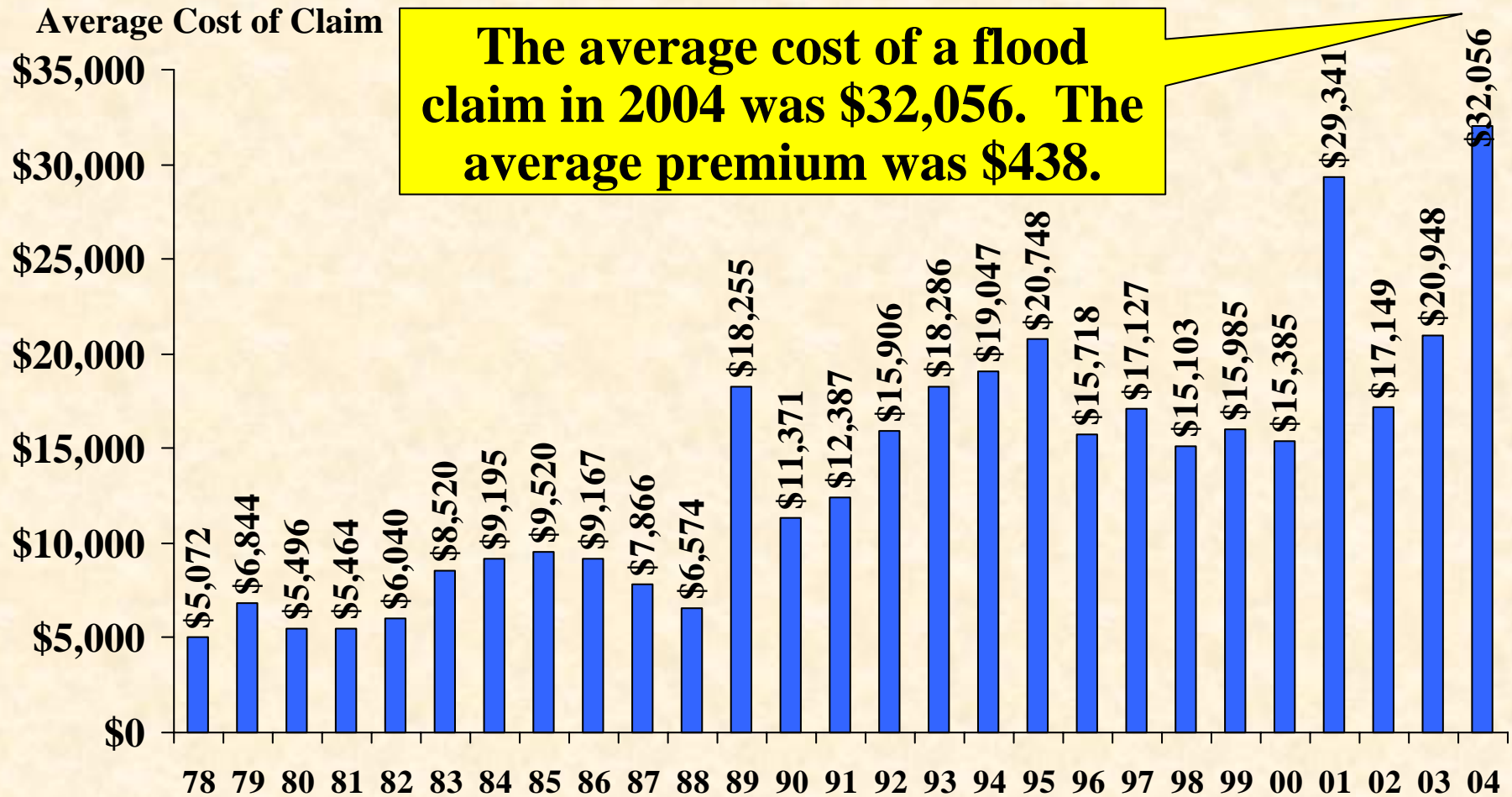
The NFIP will pay an estimated \$10 billion in flood claims in 2005, indicating a need for a taxpayer-financed bailout of at least \$7.5 billion

\$ Millions





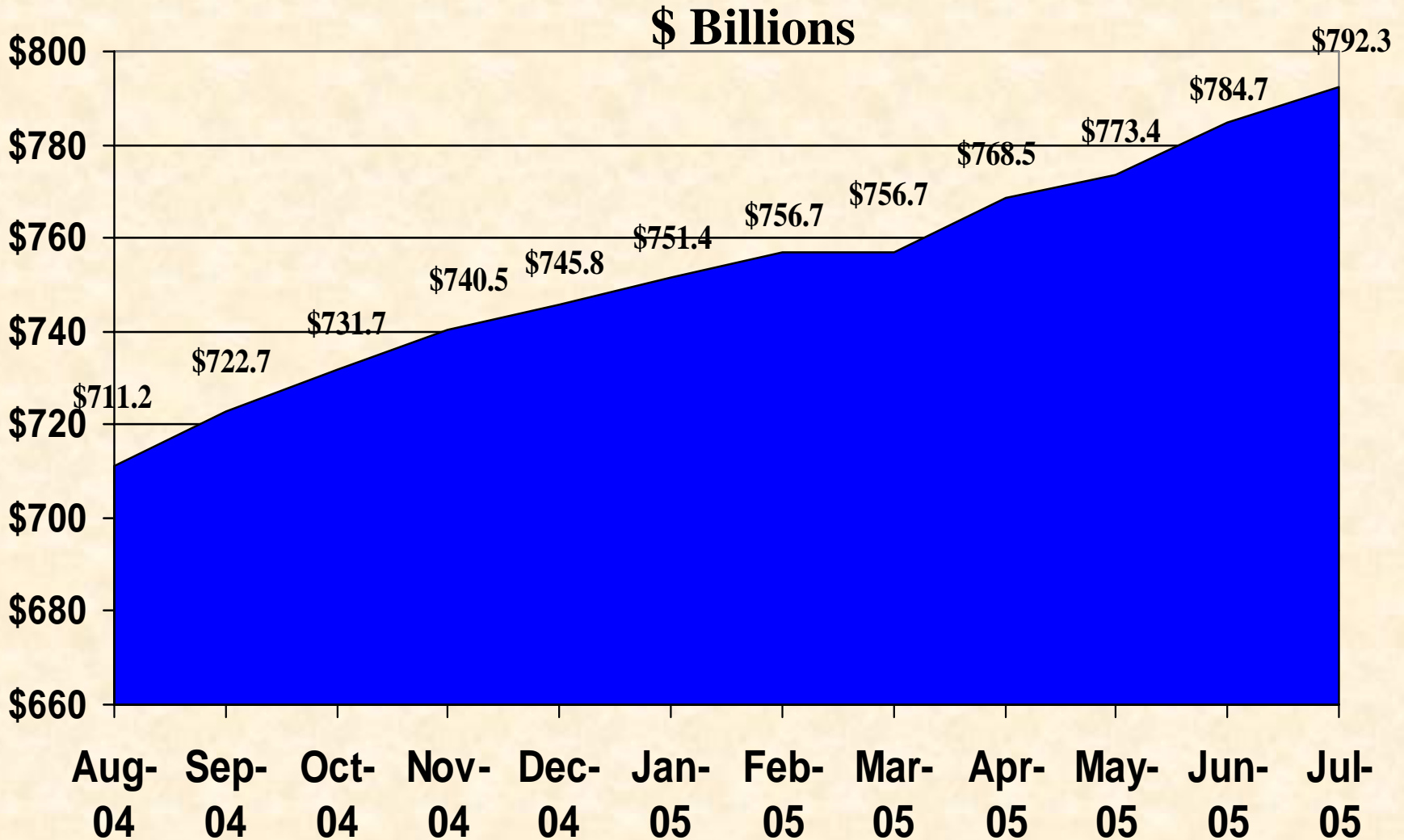
NFIP: Average Cost of Claim By Calendar Year 1978-2004



Source: FEMA, National Flood Insurance Program (NFIP)



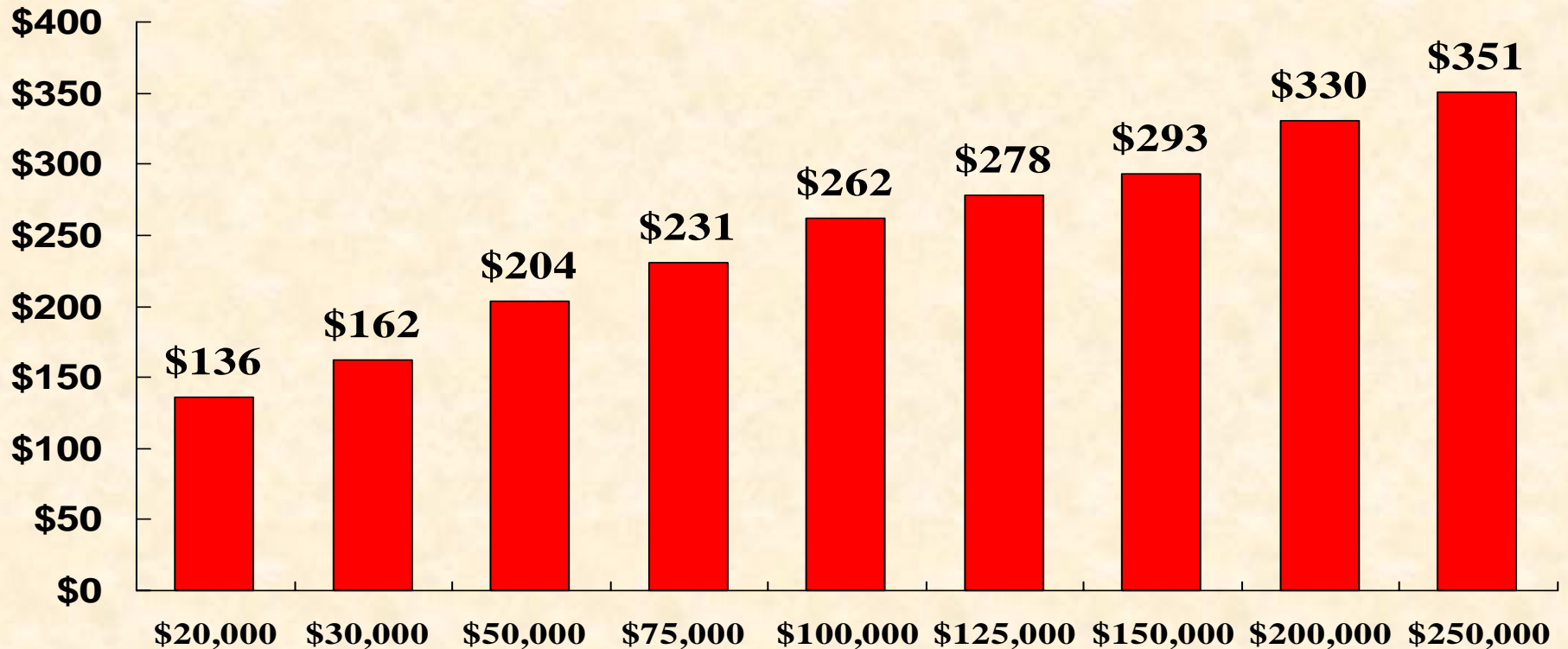
NFIP: Insurance In Force By Month (As of July 31, 2005)



Source: FEMA, National Flood Insurance Program (NFIP)

*Average Premium Preferred Risk Policy** *For Buildings with Basement Under NFIP*

Average Premium



Building deductible: \$500. Contents deductible: \$500. Deductibles applied separately.

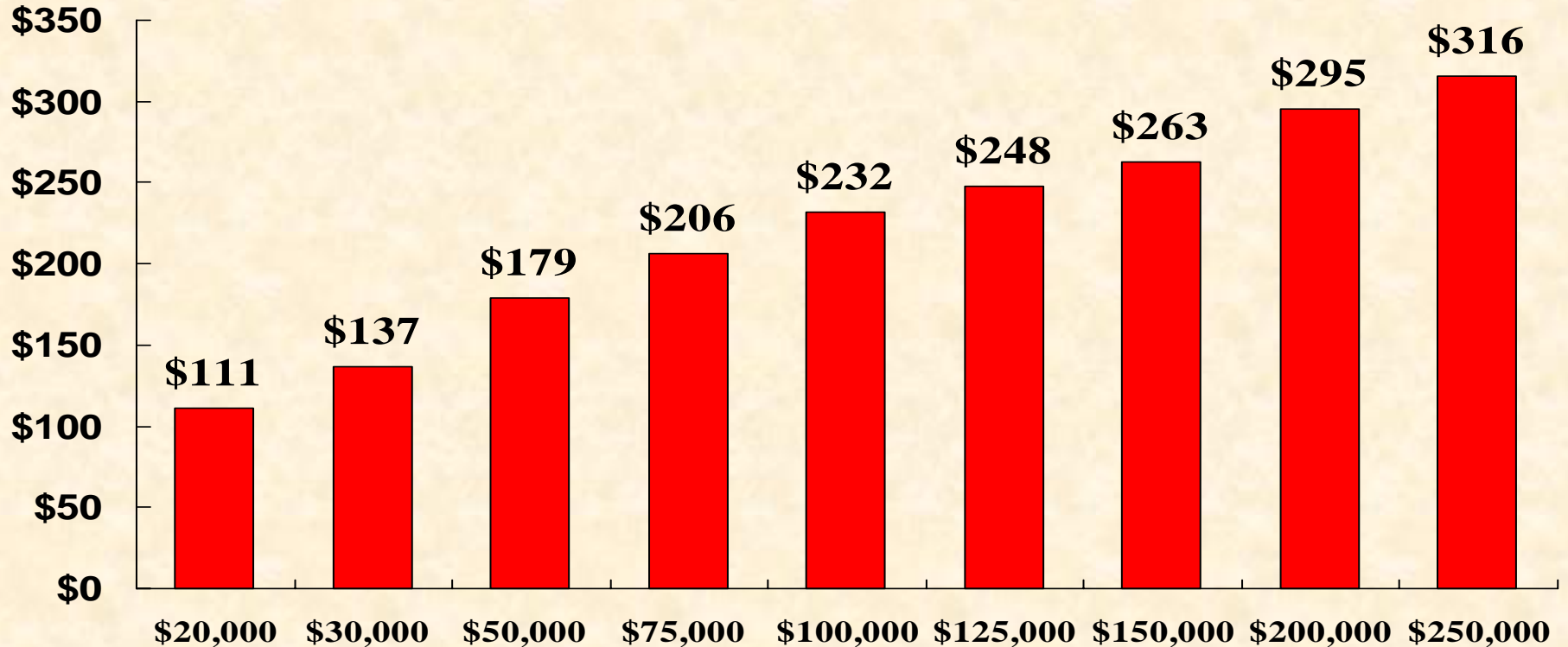
***Under the NFIP a low-cost Preferred Risk Policy is available to homeowners located in low- to moderate-risk areas.**

Sources: FEMA, National Flood Insurance Program (NFIP)



*Average Premium Preferred Risk Policy** *For Buildings without Basement* *Under NFIP*

Average Premium



Building deductible: \$500. Contents deductible: \$500. Deductibles applied separately.

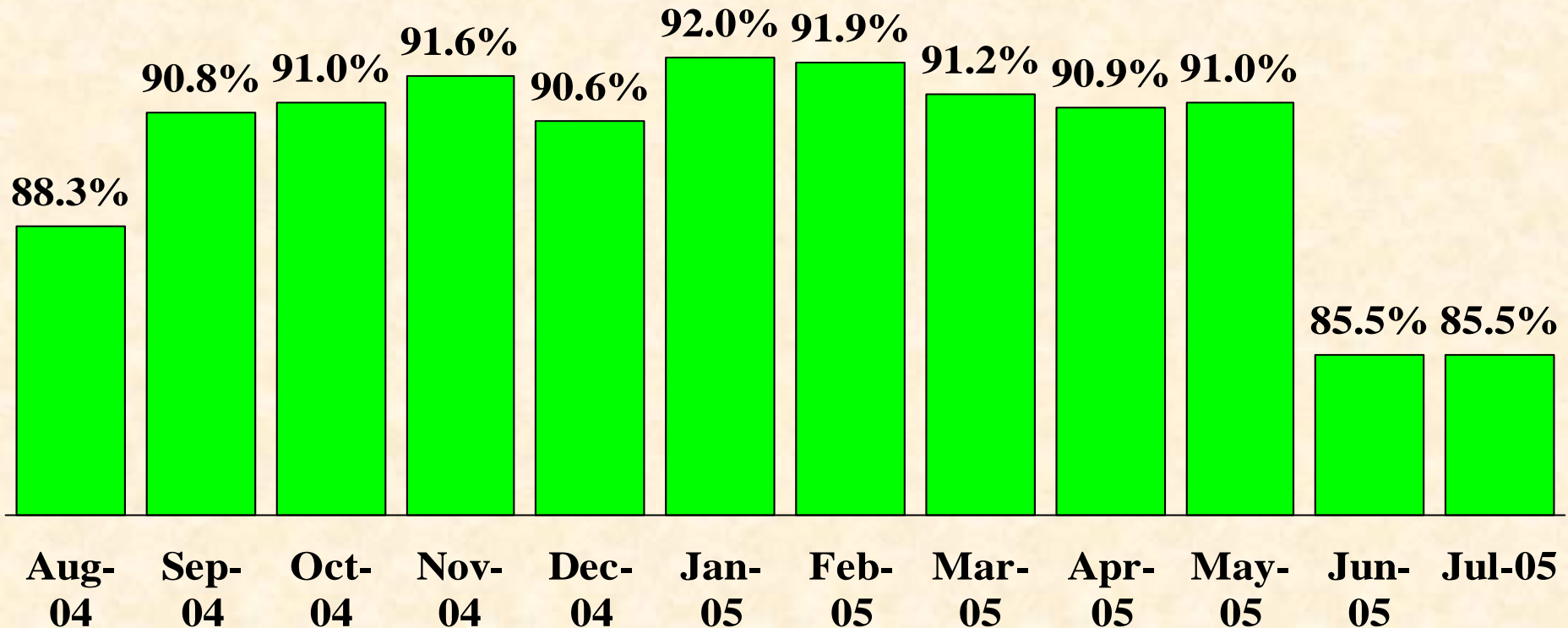
***Under the NFIP a low-cost Preferred Risk Policy is available to homeowners located in low- to moderate-risk areas.**

Sources: FEMA, National Flood Insurance Program (NFIP)



Policy Retention Rates, As Of July 31, 2005

Retention rates in the NFIP are poor, with 10-15% of policyholders allowing policies to lapse annually.





Total Claim Payments by State (Top 10) Jan 1, 1978 - Dec. 2004



*What Role Should the
Federal Government
Play in Insuring
Against Natural
Disaster Risks?*





Pros/Cons of Federal CAT

(Re) Insurance Facility

Rationale **FOR** Federal Involvement

- Insurance was not meant to handle mega-catastrophes
- Such risks are fundamentally uninsurable
- Federal government already heavily involved in insuring against weather-related mega-catastrophes (e.g., flood, crop)
- Insurers are not allowed to charge risk appropriate rates (including rising reinsurance costs)
- Price/availability of private reinsurance is volatile

Rationale **AGAINST** Federal Involvement

- Crowds-out pvt. insurance/reinsurance markets; stifles innovation
- Relationship between price and risk assumed is diminished since fed insurance programs are seldom actuarially sound
- Increases federal involvement and regulatory authority in p/c insurance (*not a negative for some market participants*)
- Cost to US Treasury (esp. taxpayers in less disaster prone states)
- Diminishes incentives for mitigation, tougher building codes and wiser land use policies if Fed rate are politically influenced



Options for a Federal Role in the Financing of Natural Disaster Risk

- 1. National Natural Disaster Pool**
- 2. Regional Natural Disaster Pool(s)**
- 3. Federal Reinsurance Program**
- 4. Tax-Favored Pre-Event Reserving**



National Natural Disaster Pool

KEY ELEMENTS

- **Share of property premiums (homeowners, commercial property) premiums collected would be ceded to pool and used to finance mega-catastrophes**
- **Funds would earn investment income tax-free to speed accumulation and keep prices modest**
- **Risk is diversified geographically and by peril (e.g., wind vs. quake)**
- **Federal government would provide a backstop to the pool as:**
 - **Reinsurance purchased by pool from the government**
 - **Line of credit offset by assessing authority**

KEY CHALLENGES

- **Is participation by insureds mandatory or optional?**
- **If optional, significant adverse selection problem**
- **Determination of “actuarially sound” rates**
- **Keeping rates free of political influence and manipulation**
- **Maintaining significant role for private reinsurers and ART**
- **Formula for assessing shortfalls in pool (including taxpayer share)**
- **Attracting support of states not prone to mega-catastrophes**
- **Appeasing deficit hawks, advocates of small government**



Regional Natural Disaster Pool(s)

KEY ELEMENTS

- **Share of property premiums in certain states (homeowners, commercial property) premiums collected would be ceded to pool and used to finance mega-catastrophes in participating states**
- **Funds would earn investment income tax-free to speed accumulation**
- **Federal government would provide a backstop to the pool as:**
 - **Reinsurance purchased by pool from the government**
 - **Line of credit offset by assessing authority**

KEY CHALLENGES

- **Is participation by insureds mandatory or optional?**
- **If optional, significant adverse selection problem**
- **Determination of “actuarially sound” rates**
- **Maintaining role for private reinsurance**
- **Keeping rates free of political influence and manipulation**
- **Formula for assessing shortfalls in pool (including taxpayer share)**
- **Attracting support of states not prone to mega-catastrophes**
- **Appeasing deficit hawks, advocates of small government**



Federal Reinsurance Program

KEY ELEMENTS

- Insurers purchase CAT reinsurance from federal government

KEY CHALLENGES

- Determination of “actuarially sound” rates
- Maintaining significant role for private reinsurers
- Maintaining significant role for ART and risk securitization
- Keeping rates free of political influence and manipulation
- Appeasing advocates of small government
- Keeping natural disaster risk programs separate and distinct from terrorism risk



Tax-Preferred Treatment of

Pre-Event Catastrophe Reserving

- **KEY ELEMENTS**

- Insurers would be allowed to deduct from their taxable income amounts set aside in reserve for natural disaster risks *in advance of the occurrence of the actual event*
- Presently, US tax law does not allow for such treatment
 - Most other countries already permit pre-event reserving

- **KEY CHALLENGES**

- Determination of appropriate reserve levels
- Overcoming criticism of impact on US Treasury receipts
 - Note that impact on Treasury is limited to time value of tax receipts



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