



Property Casualty Insurers
Association of America

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**Testimony
Property Casualty Insurers Association of America (PCI)**

“Controlling the Rising Cost of Federal Responses to Disaster”

**The Subcommittee on Economic Development, Public Buildings,
and Emergency Management
House Transportation and Infrastructure Committee
United States House of Representatives
May 12, 2016**

The Property Casualty Insurers Association of America (PCI) is pleased to offer testimony on the rising cost of federal responses to disaster. PCI believes that the federal government can reduce the potential burdens on taxpayers by transferring risk to the private sector and by adopting enhanced risk mitigation measures. PCI represents nearly 1,000 member property casualty insurance companies comprising the broadest cross-section of insurers of any national trade association. PCI members write over \$195 billion in annual premium – approximately 35 percent of the nation’s property casualty insurance. PCI’s mission is to promote and protect the viability of a competitive private insurance market for the benefit of consumers and insurers.

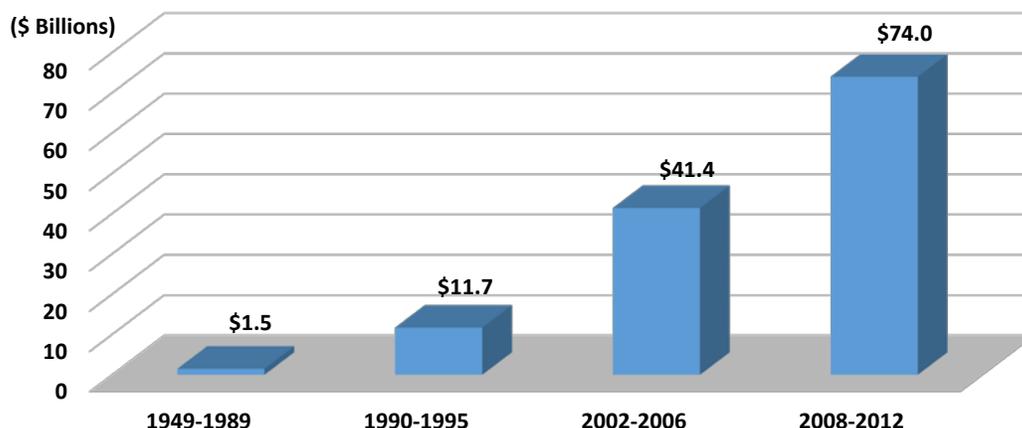
Background on the Cost of Natural Disasters

The number of disaster declarations has increased over time, as have the overall costs and insured losses associated with natural catastrophes. Based on data from the Federal Emergency Management Agency (FEMA), the average annual number of federal disaster declarations (which trigger federal assistance) has significantly increased over time, from 32 in the 1960s-70s, to 51 in the 1980s-90s, to more than 100 just since 2000.¹ From 1980 to 2013, there were 153 billion-dollar natural catastrophes in the U.S., costing an estimated \$1.1 trillion (in 2013 dollars) and increasing significantly over time in both number and costs.²

¹ PCI, based on Federal Emergency Management Agency, Disaster Declarations by Year, <https://www.fema.gov/disasters/grid/year> (including major hurricane and fire management assistance declarations). See also the Federal Insurance Office, “Report Providing an Assessment of the Current State of the Market for Natural Catastrophe Insurance in the United States”

² PCI *Natural Catastrophe Guidebook: 2014*. Note: there were no U.S. hurricanes in 2013-2015 meeting the industry’s definition of a catastrophe.

Average Annual U.S. Economic Hurricane-Related Losses
(in 2013 dollars)



Source: PCI, based on data from National Science Board and Aon Benfield

Increasing losses are partly a result of population growth and increasing population concentration in disaster-prone areas. According to 2010 Census data, nearly 40 percent of the U.S. population live in counties directly on the shoreline, with 23 of the 25 most densely populated U.S. counties along a coast and the average population density of the Coastal Shoreline Counties (excluding Alaska) more than six times greater than the density of corresponding inland counties.³ According to the Government Accountability Office, which reviewed various studies on storm intensity, U.S. hurricane losses (adjusted for inflation) are predicted to increase 14 to 47 percent by 2040.⁴

During the last decade, the federal government has incurred more than \$357 billion in direct costs due to extreme weather and fire alone, including domestic disaster response and relief (\$205 billion), flood insurance (\$23 billion), crop insurance (\$67 billion), and wildland fire management (\$34 billion). During this same period, FEMA alone spent roughly \$90 billion for domestic disaster response and relief⁵ and has requested another \$17 billion for 2017.⁶

From 1980 to 2012, more than a third (34.2 percent) of natural catastrophes in the U.S. have been severe local storms; other frequent billion-dollar events have been tropical cyclones (22.6 percent), drought/heat waves (11.6 percent) and non-tropical floods (11.0 percent). In terms of losses (2013 dollars), tropical cyclones created almost half of the total property damage in the U.S. (46.5 percent). The remaining loss distribution is as follows: drought/heat waves (23.0 percent); severe local storms

³ *Climate Change Science Program's Coastal Sensitivity to Sea-Level Rise: A Focus on the Mid-Atlantic Region, 2009*, and NOAA, *National Coastal Population Report: Population Trends From 1970 to 2020*, 2013.

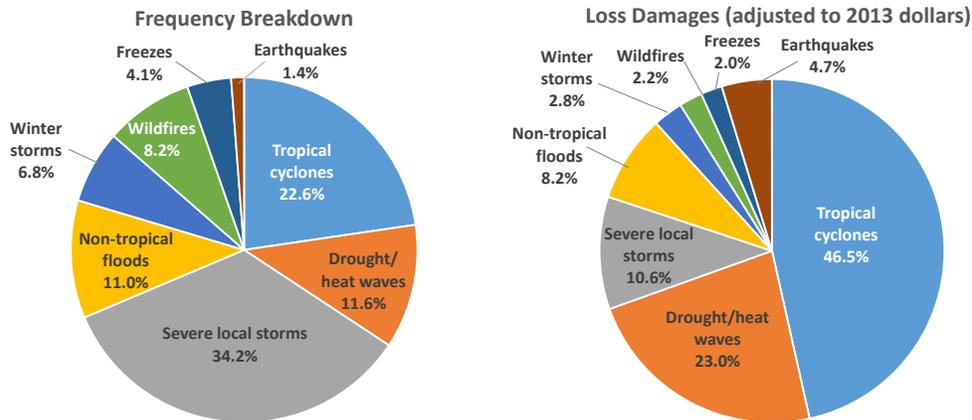
⁴ Office of Management and Budget, "Analytical Perspectives, Budget of the U.S. Government, Fiscal Year 2017" p. 362, <https://www.whitehouse.gov/sites/default/files/omb/budget/fy2017/assets/spec.pdf>

⁵ Office of Management and Budget, "Analytical Perspectives, Budget of the U.S. Government, Fiscal Year 2017" pp. 361-362, <https://www.whitehouse.gov/sites/default/files/omb/budget/fy2017/assets/spec.pdf>

⁶ Department of Homeland Security, "Budget in Brief, Fiscal Year 2017," p. 64, https://www.dhs.gov/sites/default/files/publications/FY2017_BIB-MASTER.pdf

(10.6 percent); non-tropical floods (8.2 percent); earthquakes (4.7 percent); winter storms (2.8 percent); wildfires (2.2 percent); and freezes (2.0 percent).⁷

Billion-Dollar Natural Catastrophic Events in the U.S.
1980-2012



Source: PCI, based on data from NOAA, Accuweather and San Francisco City Administrator

Insurance and Reinsurance Can Help Transfer Federal Risk

In the private sector, global insured losses from catastrophes have averaged \$62 billion over the last 10 years.⁸ In 2015, insurers paid \$28 billion in insured losses for 198 natural disaster events – the most ever recorded in one year-, including \$16.1 billion paid to consumers in the U.S. While global insured losses are very volatile, the long-term trend is clearly increasing at a significant pace. Global non-life (i.e., property casualty) reinsurance premiums in 2015 totaled about \$ 170 billion⁹, including \$60.6 billion in the U.S.¹⁰, with current global reinsurance capital of \$565 billion at near record levels. Alternative risk transfer markets are also rapidly growing and providing additional capital – particularly for natural disasters.

Currently, the U.S. property-casualty insurance industry has \$687.2 billion in surplus,¹¹ with near record low-leveraging. While that surplus is the foundation for insurers’ current underwriting activities, there is long-term capacity to absorb more appropriately priced and underwritten risk. Most private businesses protect their interests through purchasing insurance and transferring risk to the U.S. and global (re)insurance markets. (Re)insurance not only reduces purchasers’ risk exposure, but it also sends appropriate price signals about the cost of risk, encourages risk mitigation and more accurately predicts catastrophe risk. The more insurance is purchased and risk transferred, the less the consequential burden to federal taxpayers when disasters occur. Government programs should encourage rather than displace the purchase of private insurance that can help transfer risk into the global capital markets.

⁷ PCI *Natural Catastrophe Guidebook: 2014*

⁸ Swiss Re, http://media.swissre.com/documents/sigma1_2016_en.pdf

⁹ Swiss Re, <http://reports.swissre.com/2015/financial-report/financial-year/market-environment/reinsurance-non-life.html>

¹⁰ Reinsurance Association of America, http://www.reinsurance.org/RAA/Industry_Data_Center/Quarterly_Underwriting_Results/Premium/Table_of_Quarterly_Underwriting_Results.html

¹¹ SNL Financial

In 2015, the National Railroad Passenger Corporation (“Amtrak”) for the first time obtained capital markets-based reinsurance for its wholly-owned captive insurer covering storm surge and wind from named storms and earthquake damage.¹² The catastrophe bond notes cover wind and earthquake events impacting the Northeast region of the U.S. for approximately three years. Gerald Sokol, the Chief Financial Officer (CFO) for Amtrak stated, “This is the first time Amtrak has used the capital markets to broaden our base of insurance coverage. The catastrophe bond market provides us with a means to diversify our sources of insurance in a cost effective manner.” Private market reinsurance can benefit the National Flood Insurance Program (NFIP) and other government programs by assuming some of the risk that would otherwise fall on U.S. taxpayers.

In light of the fact that government funding after a natural disaster is intended to provide not only immediate relief but long-term recovery, some may view the pace of federal spending to be slow.¹³ On the other hand, private insurers are able to respond very quickly to disasters in order to make their customers whole as soon as possible. Many insurers now have special catastrophe claims handling procedures to respond more quickly to disasters and provide more efficient claims services, using social media tools to transmit and receive information on emergency services and filing claims to injured victims more rapidly. Some insurers have teams solely dedicated to catastrophes with the intent of reaching disaster sites within 24 hours and providing uninterrupted service to assist customers and process claims shortly after a devastating event. They have sound disaster recovery plans (filed with state insurance departments) that address, among other items, whether claims will be handled locally or through a catastrophe claims office, whether adjusters will be brought in from other locations, how catastrophe claims information will be distributed, etc.

Mitigation is Crucial to Reducing Federal Risk

Strong building codes, responsible land use policies, disaster planning and response management, and incentives for mitigation are all important to minimizing the cost of natural disasters for both the federal government and private sector. Policies that emphasize responsible land use will reduce the frequency and severity of property damage following natural disasters such as hurricanes and wildfires. Several studies have suggested that strong building codes that are successfully implemented and enforced uniformly can significantly reduce losses suffered from natural disasters, reducing the subsequent need for federal aid. For example, according to a study conducted by the National Institute of Building Sciences’ Multihazard Mitigation Council (MMC) for FEMA, every dollar spent on hazard mitigation grants reduced post-disaster relief costs by \$3.65. In addition, the MMC found that every dollar spent on hazard mitigation provides \$4 in future benefits, including reduced property damage, business interruption, environmental damage, injuries, and costs of emergency response.¹⁴ The University of Pennsylvania’s Wharton School of Business cited a finding that cost savings related to a 100-year

¹² Guy Carpenter, “GC Securities Completes Catastrophe Bond PennUnion Re Ltd. Series 2015-1 Notes Ultimately Benefiting the National Railroad Passenger Corporation (“Amtrak”), Oct. 14, 2015, [http://www.guycarp.com/content/dam/guycarp/en/documents/PressRelease/2015/GC%20Securities_%20Completes%20Catasrophe%20Bond%20PennUnion%20Re%20Ltd.%20Series%202015-1%20Notes%20Ultimately%20benefitting%20the%20National%20Railroad%20Passenger%20Corporation%20\(Amtrak \).pdf](http://www.guycarp.com/content/dam/guycarp/en/documents/PressRelease/2015/GC%20Securities_%20Completes%20Catasrophe%20Bond%20PennUnion%20Re%20Ltd.%20Series%202015-1%20Notes%20Ultimately%20benefitting%20the%20National%20Railroad%20Passenger%20Corporation%20(Amtrak).pdf)

¹³ Homeland Security, “DHS: Disasters and the Budgetary Impact on the Fed’s Response,” Oct. 8, 2013, <http://www.hstoday.us/channels/dhs/single-article-page/disasters-and-the-budgetary-impact-on-the-feds-response/aec39ef3c9464614389db8c81953c3dc.html>

¹⁴ National Institute of Building Sciences’ Multihazard Mitigation Council, “Natural Hazard Mitigation Saves: An Independent Study to Assess the Future Savings from Mitigation Activities,” pp. iii and 6, http://www.floods.org/PDF/MMC_Volume1_FindingsConclusionsRecommendations.pdf

hurricane range anywhere from 34 percent (in Texas) to 61 percent (in Florida) if appropriate mitigation steps are taken.¹⁵

PCI and many of our members support the Insurance Institute for Business and Home Safety (IBHS), which regularly tests residential and commercial construction materials for durability to wind, hail, and wildfire related property damage at their research facility in Richburg, South Carolina. The IBHS has noted that effective loss mitigation can save lives, encourage personal responsibility, enhance market-based solutions, promote long-term fiscal restraint, reduce public sector response and recovery costs, and create a more resilient society. An IBHS study on hail-loss found that homes with impact-resistant roofs had 40 percent fewer insurance claims and a 55 percent reduction in losses.¹⁶

Responsible land use policies are also important to mitigate natural disasters. For example, severe repetitive loss properties make up a small percentage of NFIP policies, yet result in a disproportionately high percentage of claims costs and federal subsidies. Government policymakers should carefully consider the moral hazards of subsidizing or providing continuing disaster assistance that encourages development or continued occupancy in environmentally sensitive and disaster-prone areas. Conversely, the NFIP helps reduce federal disaster assistance by requiring communities to adopt and enforce sound floodplain management regulation and ordinances before NFIP flood insurance is made available to those residents. PCI strongly encourages public education regarding the need for flood insurance and community participation in the NFIP, both of which help reduce federal disaster response costs.

Disaster planning and response management are also essential. Establishing critical communication lines between public and private sectors, developing response and continuity plans and gathering information prior to an event are the critical first steps towards successfully managing the response to a catastrophic situation. PCI has developed disaster tool kits for policymakers with suggestions for building those lines of communication, establishing Insurance Emergency Operations Centers, and disaster response and business continuity planning. A description of the tool kit can be found at:

http://www.pciaa.net/docs/default-source/default-document-library/pci_cat_action_toolkit.pdf?sfvrsn=2.

PCI supports a number of additional tools for policymakers to mitigate natural catastrophes including:

- requiring better adoption of and compliance with building codes;
- encouraging certification of building compliance with mitigation standards upon sale;
- providing federal assistance to qualifying state mitigation programs;
- making the purchase of insurance a prerequisite for certain federal disaster assistance;
- allowing tax deductions for approved retrofitting of property for mitigation;
- providing temporary state sales tax relief for building materials used to mitigate losses; create code-plus standards that exceed current building code requirements that consumers could voluntarily follow to receive potential benefits;
- providing enhanced educational materials and outreach on the cost-effectiveness of mitigation;
- making home inspections for mitigation compliance and retrofitting recommendations more available in disaster-prone areas; and
- encouraging responsible land use planning.

¹⁵ Kunreuther, Howard, The Wharton Business School, University of Pennsylvania, "Catastrophe Insurance Challenges for the U.S. and Asia"

¹⁶ IBHS Insurance Claim Hail Study, "Investigation into Insured Losses and Damages to Single-Family Homes Resulting from the April 5, 2003 North Texas Hailstorms," https://disastersafety.org/wp-content/uploads/Hail_Texas_ES.pdf

A more detailed discussion of these proposals can be found in PCI's Natural Catastrophe Guidebook available at <http://www.pciaa.net/industry-issues/catastrophic-risks>.

PCI appreciates the interest of the Subcommittee in addressing rising federal disaster response costs and looks forward to working constructively with members on potential solutions.