

HOMEOWNERS' DEFENSE ACT OF 2010

JULY 13, 2010.—Committed to the Committee of the Whole House on the State of the Union and ordered to be printed

Mr. FRANK of Massachusetts, from the Committee on Financial Services, submitted the following

R E P O R T

together with

DISSENTING VIEWS

[To accompany H.R. 2555]

[Including cost estimate of the Congressional Budget Office]

The Committee on Financial Services, to whom was referred the bill (H.R. 2555) to ensure the availability and affordability of homeowners' insurance coverage for catastrophic events, having considered the same, report favorably thereon with an amendment and recommend that the bill as amended do pass.

CONTENTS

	Page
Amendment .....	2
Purpose and Summary .....	11
Background and Need for Legislation .....	12
Hearings .....	14
Committee Consideration .....	15
Committee Votes .....	15
Committee Oversight Findings .....	19
Performance Goals and Objectives .....	19
New Budget Authority, Entitlement Authority, and Tax Expenditures .....	20
Committee Cost Estimate .....	20
Congressional Budget Office Estimate .....	20
Federal Mandates Statement .....	27
Advisory Committee Statement .....	27
Constitutional Authority Statement .....	28
Applicability to Legislative Branch .....	28
Earmark Identification .....	28
Section-by-Section Analysis of the Legislation .....	28

## AMENDMENT

The amendment is as follows:  
Strike all after the enacting clause and insert the following:

**SECTION 1. SHORT TITLE; TABLE OF CONTENTS.**

(a) **SHORT TITLE.**—This Act may be cited as the “Homeowners’ Defense Act of 2010”.

(b) **TABLE OF CONTENTS.**—The table of contents for this Act is as follows:

Sec. 1. Short title; table of contents.  
Sec. 2. Findings and purposes.

## TITLE I—NATIONAL CATASTROPHE RISK CONSORTIUM

Sec. 101. Establishment; status; principal office; membership.  
Sec. 102. Functions.  
Sec. 103. Powers.  
Sec. 104. Nonprofit entity; conflicts of interest; audits.  
Sec. 105. Management.  
Sec. 106. Staff; experts and consultants.  
Sec. 107. Federal liability.  
Sec. 108. Authorization of appropriations.

## TITLE II—CATASTROPHE OBLIGATION GUARANTEES

Sec. 201. Purposes.  
Sec. 202. Establishment of debt guarantee program.  
Sec. 203. Effect of guarantee.  
Sec. 204. Full faith and credit.  
Sec. 205. Fees for guarantees; amount; collection.  
Sec. 206. Payment of losses.  
Sec. 207. Regulations.

## TITLE III—REINSURANCE COVERAGE FOR ELIGIBLE STATE PROGRAMS

Sec. 301. Program authority.  
Sec. 302. Contract principles.  
Sec. 303. Terms of reinsurance contracts.  
Sec. 304. Maximum Federal liability.  
Sec. 305. Federal Natural Catastrophe Reinsurance Fund.  
Sec. 306. Regulations.

## TITLE IV—MITIGATION GRANT PROGRAM

Sec. 401. Mitigation grant program.

## TITLE V—GENERAL PROVISIONS

Sec. 501. Eligible State programs.  
Sec. 502. Study and conditional coverage of commercial residential lines of insurance.  
Sec. 503. Study of risk-based pricing and State program rates.  
Sec. 504. Definitions.  
Sec. 505. Regulations.

**SEC. 2. FINDINGS AND PURPOSES.**

(a) **FINDINGS.**—The Congress finds that—

(1) the United States has a history of catastrophic natural disasters, including hurricanes, tornadoes, flood, fire, earthquakes, and volcanic eruptions;

(2) although catastrophic natural disasters occur infrequently, they will continue to occur and are predictable;

(3) such disasters generate large economic losses and a major component of those losses comes from damage and destruction to homes;

(4) for the majority of Americans, their investment in their home represents their single biggest asset and the protection of that investment is paramount to economic and social stability;

(5) the United States needs to take and support State actions to be better prepared for and better protected from catastrophes;

(6) as the risk of catastrophic losses grows, so do the risks that any premiums collected by private insurers for extending coverage will be insufficient to cover future catastrophes, and private insurers, in an effort to protect their shareholders and policyholders (in the case of mutually owned companies), have thus significantly raised premiums and curtailed insurance coverage in States exposed to major catastrophes;

(7) such effects on the insurance industry have been harmful to economic activity in States exposed to major catastrophes and have placed significant burdens on residents of such States;

(8) Hurricanes Katrina, Rita, and Wilma struck the United States in 2005, causing over \$200,000,000,000 in total economic losses, and insured losses to homeowners in excess of \$50,000,000,000;

(9) the Federal Government has provided and will continue to provide resources to pay for losses from future catastrophes;

(10) when Federal assistance is provided to the States, accountability for Federal funds disbursed is paramount;

(11) the Government Accountability Office or other appropriate agencies must have the means in place to confirm that Federal funds for catastrophe relief have reached the appropriate victims and have contributed to the recovery effort as efficiently as possible so that taxpayer funds are not misspent and citizens are enabled to rebuild and resume productive activities as quickly as possible;

(12) States that are recipients of Federal funds must be responsible to account for and provide an efficient means for distribution of funds to homeowners to enable the rapid rebuilding of local economies after a catastrophic event without unduly burdening taxpayers who live in areas seldom affected by natural disasters;

(13) State insurance and reinsurance programs can provide a mechanism for States to exercise that responsibility if they appropriately underwrite and price risk, and if they pay claims quickly and within established contractual terms;

(14) making available Federal guarantees to enhance the capability of eligible State programs to issue debt will minimize the exposure of State and Federal taxpayers who otherwise may bear the consequences of underfunded programs or under-insured communities following catastrophic events, especially during today's historic market turmoil; and

(15) it is the proper role of the Federal Government to prepare for and protect its citizens from catastrophes and to facilitate consumer protection, victim assistance, and recovery, including financial recovery.

(b) **PURPOSES.**—The purposes of this Act are to establish a program to provide Federal support for State-sponsored insurance programs to help homeowners prepare for and recover from the damages caused by natural catastrophes, to encourage mitigation and prevention for such catastrophes, to promote the use of private market capital as a means to insure against such catastrophes, to expedite the payment of claims and better assist in the financial recovery from such catastrophes.

## **TITLE I—NATIONAL CATASTROPHE RISK CONSORTIUM**

### **SEC. 101. ESTABLISHMENT; STATUS; PRINCIPAL OFFICE; MEMBERSHIP.**

(a) **ESTABLISHMENT.**—There is established an entity to be known as the “National Catastrophe Risk Consortium” (in this title referred to as the “Consortium”).

(b) **STATUS.**—The Consortium is not a department, agency, or instrumentality of the United States Government.

(c) **PRINCIPAL OFFICE.**—The principal office and place of business of the Consortium shall be such location within the United States determined by the Board of Directors to be the most advantageous for carrying out the purpose and functions of the Consortium.

(d) **MEMBERSHIP.**—Any State that has established a reinsurance fund or has authorized the operation of a State residual insurance market entity, or State-sponsored provider of natural catastrophe insurance, shall be eligible to participate in the Consortium.

### **SEC. 102. FUNCTIONS.**

The Consortium shall—

(1) work with all States, particularly those participating in the Consortium, to gather and maintain an inventory of catastrophe risk obligations held by State reinsurance funds, State residual insurance market entities, and State-sponsored providers of natural catastrophe insurance;

(2) at the discretion of the affected members and on a conduit basis, issue securities and other financial instruments linked to the catastrophe risks insured or reinsured through members of the Consortium in the capital markets;

(3) coordinate reinsurance contracts between participating, qualified reinsurance funds and private parties;

(4) act as a centralized repository of State risk information that can be accessed by private-market participants seeking to participate in the transactions described in paragraphs (2) and (3) of this section;

(5) establish a catastrophe risk database to perform research and analysis that encourages standardization of the risk-linked securities market;

(6) perform any other functions, other than assuming risk or incurring debt, that are deemed necessary to aid in the transfer of catastrophe risk from participating States to private parties; and

(7) submit annual reports to Congress describing the activities of the Consortium for the preceding year, and the first such annual report shall include an assessment of the costs to States and regions associated with catastrophe risk and an analysis of the costs and benefits, for States not participating in the Consortium, of such nonparticipation.

**SEC. 103. POWERS.**

The Consortium—

(1) may make and perform such contracts and other agreements with any individual or other private or public entity however designated and wherever situated, as may be necessary for carrying out the functions of the Consortium; and

(2) shall have such other powers, other than the power to assume risk or incur debt, as may be necessary and incident to carrying out this Act.

**SEC. 104. NONPROFIT ENTITY; CONFLICTS OF INTEREST; AUDITS.**

(a) **NONPROFIT ENTITY.**—The Consortium shall be a nonprofit entity and no part of the net earnings of the Consortium shall inure to the benefit of any member, founder, contributor, or individual.

(b) **CONFLICTS OF INTEREST.**—No director, officer, or employee of the Consortium shall in any manner, directly or indirectly, participate in the deliberation upon or the determination of any question affecting his or her personal interests or the interests of any Consortium, partnership, or organization in which he or she is directly or indirectly interested.

(c) **AUDITS.**—

(1) **ANNUAL AUDIT.**—The financial statements of the Consortium shall be audited annually in accordance with generally accepted auditing standards by independent certified public accountants.

(2) **REPORTS.**—The report of each annual audit pursuant to paragraph (1) shall be included in the annual report submitted in accordance with section 102(7).

(d) **PROHIBITION ON ELECTION AND LOBBYING ACTIVITIES.**—

(1) **FEDERAL.**—The Consortium may not—

(A) make any contribution to a candidate for election for Federal office or to a political committee;

(B) employ or retain—

(i) a registered lobbyist under the Lobbying Disclosure Act of 1995 (2 U.S.C. 1601 et seq.); or

(ii) an organization that employs one or more lobbyists and is registered under section 4(a)(2) of such Act (2 U.S.C. 1603(a)(2)); or

(C) provide any thing of value, other than educational materials or information, to any elected official of the Federal Government.

For purposes of this paragraph, the terms “contribution”, “candidate”, “Federal office”, and “political committee” have the meanings given such terms in section 301 of the Federal Election Campaign Act of 1971 (2 U.S.C. 431).

(2) **CONSORTIUM.**—The Consortium may not—

(A) make any contribution to a candidate for election for any State or local office or to any committee, club, association, or other group that receives contributions or makes expenditures for the purpose of influencing any such election;

(B) employ or retain any person who engages in influencing legislating (as such term is defined in section 4911(d) of the Internal Revenue Code of 1986 (26 U.S.C. 4911(d))) of any State or local legislative body; or

(C) provide any thing of value, other than educational materials or information, to any elected official of any State or local government.

**SEC. 105. MANAGEMENT.**

(a) **BOARD OF DIRECTORS; MEMBERSHIP; DESIGNATION OF CHAIRPERSON.**—

(1) **BOARD OF DIRECTORS.**—The management of the Consortium shall be vested in a board of directors (referred to in this title as the “Board”) composed of not less than 3 members.

(2) **CHAIRPERSON.**—The Secretary of the Treasury, or the designee of the Secretary, shall serve as the chairperson of the Board.

(3) **MEMBERSHIP.**—The members of the Board shall include—

(A) the Secretary of Homeland Security and the Secretary of Commerce, or the designees of such Secretaries, respectively, but only during such times as there are fewer than two States participating in the Consortium; and

- (B) a member from each State participating in the Consortium, who shall be appointed by such State.
- (b) **BYLAWS.**—The Board may prescribe, amend, and repeal such bylaws as may be necessary for carrying out the functions of the Consortium.
- (c) **COMPENSATION, ACTUAL, NECESSARY, AND TRANSPORTATION EXPENSES.**—
- (1) **NON-FEDERAL EMPLOYEES.**—A member of the Board who is not otherwise employed by the Federal Government shall be entitled to receive the daily equivalent of the annual rate of basic pay payable for level IV of the Executive Schedule under section 5315 of title 5, United States Code, as in effect from time to time, for each day (including travel time) during which such member is engaged in the actual performance of duties of the Consortium.
- (2) **FEDERAL EMPLOYEES.**—A member of the Board who is an officer or employee of the Federal Government shall serve without additional pay (or benefits in the nature of compensation) for service as a member of the Consortium.
- (3) **TRAVEL EXPENSES.**—Members of the Consortium shall be entitled to receive travel expenses, including per diem in lieu of subsistence, equivalent to those set forth in subchapter I of chapter 57 of title 5, United States Code.
- (d) **QUORUM.**—A majority of the Board shall constitute a quorum.
- (e) **EXECUTIVE DIRECTOR.**—The Board shall appoint an executive director of the Consortium on such terms as the Board may determine.

**SEC. 106. STAFF; EXPERTS AND CONSULTANTS.**

- (a) **STAFF.**—
- (1) **APPOINTMENT.**—The Board of the Consortium may appoint and terminate such other staff as are necessary to enable the Consortium to perform its duties.
- (2) **COMPENSATION.**—The Board of the Consortium may fix the compensation of the executive director and other staff.
- (b) **EXPERTS AND CONSULTANTS.**—The Board shall procure the services of experts and consultants as the Board considers appropriate.

**SEC. 107. FEDERAL LIABILITY.**

The Federal Government and the Consortium shall not bear any liabilities arising from the actions of the Consortium. Participating States shall retain all catastrophe risk until the completion of a transaction described in paragraphs (2) and (3) of section 102.

**SEC. 108. AUTHORIZATION OF APPROPRIATIONS.**

There are authorized to be appropriated to carry out this title \$20,000,000 for each of fiscal years 2010 through 2014.

## **TITLE II—CATASTROPHE OBLIGATION GUARANTEES**

**SEC. 201. PURPOSES.**

The purposes of this title are to establish a program—

- (1) to promote the availability of private capital to provide liquidity and capacity to State catastrophe insurance programs; and
- (2) to expedite the payment of claims under State catastrophe insurance programs and better assist the financial recovery from significant natural catastrophes by authorizing the Secretary of the Treasury to guarantee debt for such purposes.

**SEC. 202. ESTABLISHMENT OF DEBT GUARANTEE PROGRAM.**

(a) **AUTHORITY OF SECRETARY.**—The Secretary of the Treasury is authorized and shall have the powers and authorities necessary to guarantee, and to enter into commitments to guarantee, holders of debt against loss of principal or interest, or both, on any such debt issued by eligible State programs for purposes of this title, provided that the total principal amount of debt obligations guaranteed by the Secretary—

- (1) for eligible State programs that cover earthquake peril shall not exceed \$3,500,000,000; and
- (2) for eligible State programs that cover all other perils shall not exceed \$17,000,000,000.

(b) **CONDITIONS FOR GUARANTEE ELIGIBILITY.**—A debt guarantee under this section may be made only if the Secretary has issued a commitment to guarantee to an eligible State program. The commitment to guarantee shall be for a period of 3 years and may be extended by the Secretary for a period of 1 year on each annual anniversary of the issuance of the commitment to guarantee. The commitment to

guarantee and each extension of such commitment may be issued by the Secretary only if the following requirements are satisfied:

(1) The eligible State program submits to the Secretary a report setting forth, in such form and including such information as the Secretary shall require, how the eligible State program plans to repay the debt.

(2) Based upon the eligible State program's report submitted pursuant to paragraph (1), the Secretary determines there is reasonable assurance that the eligible State program can meet its repayment obligation under the debt.

(3) The eligible State program enters into an agreement with the Secretary, as the Secretary shall require, that the eligible State program will not use Federal funds of any kind or from any Federal source (including any disaster or other financial assistance, loan proceeds, and any other assistance or subsidy) to repay the debt.

(4) The commitment to guarantee shall specify the fees for debt guarantee coverage.

(5) The maximum term of the debt that shall be specified in a commitment issued under this section may not exceed 30 years.

(6) The Secretary determines that the eligible State program does not cover losses arising from floods to properties located in areas having special flood hazards (as such term is defined for purposes of the National Flood Insurance Act of 1968 and the Flood Disaster Protection Act of 1973).

(c) **MANDATORY ASSISTANCE FOR ELIGIBLE STATE PROGRAMS.**—The Secretary shall upon the request of an eligible State program and pursuant to a commitment to guarantee issued under subsection (b), provide a guarantee under subsection (d) for such eligible State program in the amount requested by such eligible State program, subject to the limitation under subsection (d)(2).

(d) **CATASTROPHIC DEBT GUARANTEE.**—A debt guarantee under this subsection for an eligible State program shall be subject to the following requirements:

(1) **PRECONDITIONS.**—The eligible State program shows to the satisfaction of the Secretary that insured losses in the State to the eligible State program arising from the event or events covered by the commitment to guarantee are likely to exceed the eligible State program's available cash resources, as calculated on the date of the event.

(2) **AMOUNT.**—The aggregate principal amount of the debt guaranteed following an event or events referred to in paragraph (1) may not exceed the amount by which the insured losses expected to be sustained by the State program as a result of such event or events exceed 80 percent of the qualifying assets of the eligible State program as stated in the most recent quarterly financial statement filed with the domiciliary regulator of the program prior to the event or events, except that, for eligible State programs that are not required to file such quarterly financial statements, the aggregate principal amount of the debt guaranteed may not exceed the amount by which insured losses sustained by the State program as a result of such event or events exceed 80 percent of the unrestricted net assets as stated in the annual financial statement for the program's fiscal year ending immediately prior to the event or events.

(3) **USE OF FUNDS.**—Amounts of debt guaranteed under this section shall be used only to pay the costs of issuing debt and to pay the insured losses and loss adjustment expenses incurred by an eligible State program. Such amounts shall not be used for any other purpose.

(e) **FUNDING.**—There are authorized to be appropriated such sums as may be necessary to carry out this section.

**SEC. 203. EFFECT OF GUARANTEE.**

The issuance of any guarantee by the Secretary under this title shall be conclusive evidence that—

- (1) the guarantee has been properly obtained;
- (2) the underlying debt qualified for such guarantee; and
- (3) the guarantee is valid, legal, and enforceable.

**SEC. 204. FULL FAITH AND CREDIT.**

The full faith and credit of the United States is pledged to the payment of all guarantees issued under this title with respect to principal and interest.

**SEC. 205. FEES FOR GUARANTEES; AMOUNT; COLLECTION.**

The Secretary shall charge and collect fees for each guarantee in amounts specified in the commitment to guarantee, which shall be in amounts sufficient in the judgment of the Secretary at the time of issuance of the commitment to guarantee to cover applicable administrative costs and probable losses on the guaranteed obligations covered by the commitment to guarantee, but in any event not to exceed

one-half of 1 per centum per annum of the outstanding indebtedness covered by each guarantee.

**SEC. 206. PAYMENT OF LOSSES.**

(a) **IN GENERAL.**—The Secretary agrees to pay to the duly appointed paying agent or trustee (in this section referred to as the “Fiscal Agent”) for the eligible State program that portion of the principal and interest on any debt guaranteed under this title that shall become due for payment but shall be unpaid by the eligible State program as a result of such program having provided insufficient funds to the Fiscal Agent to make such payments. The Secretary shall make such payments on the date such principal or interest becomes due for payment or on the business day next following the day on which the Secretary shall receive notice of failure on the part of the eligible State program to provide sufficient funds to the Fiscal Agent to make such payments, whichever is later. Upon making such payment, the Secretary shall be subrogated to all the rights of the ultimate recipient of the payment. The Secretary shall be entitled to recover from the eligible State program the amount of any payments made pursuant to any guarantee entered into under this title.

(b) **ROLE OF THE ATTORNEY GENERAL.**—The Attorney General shall take such action as may be appropriate to enforce any right accruing to the United States as a result of the issuance of any guarantee under this title.

(c) **RIGHT OF THE SECRETARY.**—Notwithstanding any other provision of law relating to the acquisition, handling, or disposal of property by the United States, the Secretary shall have the right in the discretion of the Secretary to complete, recondition, reconstruct, renovate, repair, maintain, operate, or sell any property acquired by the Secretary pursuant to the provisions of this title.

**SEC. 207. REGULATIONS.**

The Secretary shall issue any regulations necessary to carry out the debt-guarantee program established under this title.

## **TITLE III—REINSURANCE COVERAGE FOR ELIGIBLE STATE PROGRAMS**

**SEC. 301. PROGRAM AUTHORITY.**

The Secretary of the Treasury, shall make available for purchase, only by eligible State programs, contracts for reinsurance coverage under this title.

**SEC. 302. CONTRACT PRINCIPLES.**

Contracts for reinsurance coverage made available under this title—

- (1) shall be priced on an actuarially sound basis;
- (2) shall minimize the administrative costs of the Federal Government; and
- (3) shall provide coverage based solely on insured losses covered by the eligible State program purchasing the contract.

**SEC. 303. TERMS OF REINSURANCE CONTRACTS.**

(a) **MINIMUM ATTACHMENT POINT AND LEVELS OF COVERAGE.**—The Secretary shall establish attachment points at which reinsurance coverage under this title is provided to eligible State programs. In setting attachment points and in determining the levels of reinsurance coverage provided, the Secretary shall take into consideration—

- (1) the coverage available through eligible State programs;
- (2) the availability and accessibility of reinsurance in the private market; and
- (3) other factors as deemed appropriate by the Secretary.

(b) **NINETY PERCENT COVERAGE OF INSURED LOSSES IN EXCESS OF RETAINED LOSSES.**—Each contract for reinsurance coverage under this title shall provide that the amount paid out under the contract shall be equal to 90 percent of the amount of insured losses of the eligible State program in excess of the amount of retained losses that the contract requires, pursuant to subsection (a), to be incurred by such program.

(c) **MATURITY.**—The term of each contract for reinsurance coverage under this title shall not exceed 1 year or such other term as the Secretary may determine.

(d) **PAYMENT CONDITION.**—Each contract for reinsurance coverage under this title shall authorize claims payments to the eligible State program purchasing the coverage only for insured losses provided under the contract.

(e) **MULTIPLE EVENTS.**—The contract shall cover any insured losses from one or more events that may occur during the term of the contract and shall provide that if multiple events occur, the retained losses requirement under subsection (a) shall apply on a calendar year basis, in the aggregate and not separately to each individual event.

(f) **TIMING OF CLAIMS.**—Claims under a contract for reinsurance coverage under this title shall include only insurance claims that are reported to the eligible State program within the 3-year period beginning upon the event or events for which payment under the contract is provided.

(g) **ACTUARIAL PRICING.**—The price of coverage under a reinsurance contract under this title shall be an amount, established by the Secretary at a level that annually produces expected premiums that shall be sufficient to pay the reasonably anticipated cost of all claims (which may not be equal only to average annual costs), loss adjustment expenses, all administrative costs of reinsurance coverage offered under this title, and any such outwards reinsurance, as described in section 305(c)(3), as the Secretary considers prudent taking into consideration the demand for reinsurance coverage under this title. The anticipated cost of all claims shall be comparable to amounts being included in the price for similar layers of coverage in the private sector, taking into account the savings associated with non-profit and tax-exempt status of the Fund established under section 305.

(h) **INFORMATION.**—Each contract for reinsurance coverage under this title shall contain a condition providing that the Secretary may require the eligible State program that is covered under the contract to submit to the Secretary all information on the eligible State program relevant to the duties of the Secretary under this title.

(i) **OTHERS.**—Contracts for reinsurance coverage under this title shall contain such other terms as the Secretary considers necessary to carry out this title and to ensure the long-term financial integrity of the program under this title.

**SEC. 304. MAXIMUM FEDERAL LIABILITY.**

(a) **IN GENERAL.**—Subject to subsection (b) and notwithstanding any other provision of law, the aggregate potential liability for payment of claims under all contracts for reinsurance coverage under this title sold in any single year shall be determined by the Secretary based on review of the market for reinsurance coverage under this title.

(b) **LIMITATION.**—The authority of the Secretary to enter into contracts for reinsurance coverage under this title shall be effective for any fiscal year only to such extent or in such amounts as are or have been provided in appropriation Acts for such fiscal year for the aggregate potential liability for payment of claims under all contracts for reinsurance coverage under this title.

**SEC. 305. FEDERAL NATURAL CATASTROPHE REINSURANCE FUND.**

(a) **ESTABLISHMENT.**—There is established within the Treasury of the United States a fund to be known as the Federal Natural Catastrophe Reinsurance Fund (in this section referred to as the “Fund”).

(b) **CREDITS.**—The Fund shall be credited with—

- (1) amounts received annually from the sale of contracts for reinsurance coverage under this title;
- (2) any amounts appropriated for the aggregate potential liability for payment of claims under all contracts for reinsurance coverage under this title; and
- (3) any amounts earned on investments of the Fund pursuant to subsection (d).

(c) **USES.**—Amounts in the Fund shall be available to the Secretary only for the following purposes:

- (1) **CONTRACT PAYMENTS.**—For payments to purchasers covered under contracts for reinsurance coverage for eligible losses under such contracts.
- (2) **ADMINISTRATIVE EXPENSES.**—To pay for the administrative expenses incurred by the Secretary in carrying out the reinsurance program under this title.
- (3) **OUTWARDS REINSURANCE.**—To obtain retrocessional or other reinsurance coverage of any kind to cover risk reinsured under contracts for reinsurance coverage made available under this title.

(d) **INVESTMENT.**—The Secretary shall invest such amounts in the Fund as the Secretary considers advisable in obligations issued or guaranteed by the United States. For purposes of the grant mandate in section 401(e) for a fiscal year, the Secretary shall disclose the annual net investment income available not later than 60 days after the conclusion of such fiscal year and disperse appropriate funds not later than 90 days after the conclusion of such fiscal year.

**SEC. 306. REGULATIONS.**

The Secretary shall issue any regulations necessary to carry out the program for reinsurance coverage under this title.



## TITLE IV—MITIGATION GRANT PROGRAM

### SEC. 401. MITIGATION GRANT PROGRAM.

(a) **ESTABLISHMENT.**—The Secretary of Housing and Urban Development shall establish and carry out a program to provide grants to eligible entities to develop, enhance, or maintain programs to prevent and mitigate losses from natural catastrophes.

(b) **GRANTS.**—A grant provided under subsection (a) shall be used to reduce loss of life and property by—

(1) encouraging awareness of risk factors and what steps can be taken to eliminate or reduce them, including public education campaigns to promote citizen and community preparedness;

(2) assisting in the determination of the location of risk by giving careful consideration to the natural risks for the location of a property;

(3) providing inspections of homes to identify areas to strengthen such homes and reduce exposure to natural catastrophes;

(4) providing financial assistance to homeowners to retrofit homes to reduce exposure to natural catastrophes; or

(5) supporting disaster response readiness programs, including initiatives that develop, enhance, or maintain the capacity of a public safety organization to be better prepared, equipped, and trained to respond to natural catastrophes.

(c) **CONSULTATION WITH EXPERTS.**—In carrying out the program established under subsection (a), the Secretary of Housing and Urban Development shall consult with—

(1) disaster preparedness and response organizations;

(2) homebuilders;

(3) real estate professionals;

(4) building code enforcement agencies; and

(5) any other person that the Secretary considers appropriate.

(d) **ELIGIBLE ENTITY DEFINED.**—In this section, the term “eligible entity” means a State or local government, a part or program of a State or local government, or a nationally recognized, congressionally chartered disaster response non-profit organization.

(e) **GRANT MANDATE.**—The Secretary shall, to the extent provided in advance in appropriation Acts, use not less than 35 percent of the net investment income from the Federal Natural Catastrophe Reinsurance Fund earned in each fiscal year pursuant to section 305(d) for grants under this section.

## TITLE V—GENERAL PROVISIONS

### SEC. 501. ELIGIBLE STATE PROGRAMS.

(a) **ELIGIBLE STATE PROGRAMS.**—A State program shall be considered an “eligible State program” for purposes of this Act if the Secretary certifies, in accordance with the procedures established under subsection (c), that the State program complies with the following requirements:

(1) **STATE PROGRAM DESIGN.**—The State program is established and authorized by State law as an insurance program or a reinsurance program that is designed to improve private insurance markets and that offers residential property insurance coverage for losses arising from any personal residential line of insurance, as defined in the Uniform Property and Casualty Product Coding Matrix of the National Association of Insurance Commissioners.

(2) **OPERATION.**—The State program shall meet the following requirements:

(A) A majority of the members of the governing body of the State program shall be public officials or appointed by public officials.

(B) The State shall have a financial interest in the State program.

(C) If the State has at any time appropriated amounts from the State program’s funds for any purpose other than payments for losses insured under the State program, or payments made in connection with any of the State program’s authorized activities, the State shall have returned such amounts to the State fund, together with interest on such amounts.

(3) **TAX STATUS.**—The State program shall have received from the Secretary (or the Secretary’s designee) a written determination, within the meaning of section 6110(b) of the Internal Revenue Code of 1986, that the program either—

(A) constitutes an “integral part” of the State that has created it; or

(B) is otherwise exempt from Federal income taxation.

(4) EARNINGS.—The State program may not provide for any distribution of any part of any net profits of the State program to any insurer that participates in the State program.

(5) PREVENTION AND MITIGATION.—

(A) MITIGATION OF LOSSES.—The State program shall include provisions designed to encourage and support programs to mitigate losses from natural catastrophes for which the State insurance or reinsurance program was established to provide insurance coverage.

(B) OPERATIONAL REQUIREMENTS.—The State program shall operate in a State that—

(i) requires that an appropriate public body within the State shall have adopted adequate mitigation measures with effective enforcement provisions which the Secretary finds are consistent with the criteria for construction described in the International Code Council building codes;

(ii) has taken actions to establish an insurance rate structure that takes into account measures to mitigate insured losses; and

(iii) ensures, to the extent that reinsurance coverage made available under the eligible State program results in any cost savings in providing insurance coverage for risks in such State, such cost savings are reflected in premium rates charged to consumers for such coverage.

(6) REQUIREMENTS REGARDING COVERAGE.—The State program—

(A) may not, except for charges or assessments related to post-event financing or bonding, involve cross-subsidization between any separate property and casualty insurance lines covered under the State program pursuant to paragraph (1);

(B) shall be subject to a requirement under State law that for any insurance coverage made available under the State insurance program or for any reinsurance coverage for such insurance coverage made available under the State reinsurance program, the premium rates charged shall cover the expected value of all future costs associated with insurance policies or reinsurance contracts written by such program, in accordance with the principles under section 303(g);

(C) shall make available to all qualifying policyholders insurance or reinsurance coverage, as applicable, and mitigation services on a basis that is not unfairly discriminatory; and

(D) publishes, and displays in a prominent location on a Website for the State insurance program, information for the State insurance program of estimated assessments and surcharges on policyholders, in accordance with State laws, regulations, or other requirements, for a range of natural disaster or catastrophic events having a varying magnitude of losses, including an event projected to result in losses of such magnitude that they have a 1 percent chance of being equaled or exceeded in any single year, based on the current year estimated aggregate funding capacity of the State insurance program and State reinsurance program.

(7) LAND USE AND ZONING.—The State program, to the extent possible, seeks to encourage appropriate State and local government units to develop comprehensive land use and zoning plans that include natural hazard mitigation.

(8) RISK-BASED CAPITAL REQUIREMENTS.—The State program—

(A) complies with such risk-based capital requirements as applicable State law may impose and shall take into consideration asset risk, credit risk, underwriting risk, and such other relevant risk as determined by the Secretary; and

(B) for each calendar year, prepares and submits to the Secretary a report identifying its claim-paying capacity at such time after the conclusion of such year, and containing such information and in such form, as the Secretary shall require.

(9) OTHER REQUIREMENTS.—The State program complies with such additional organizational, underwriting, and financial requirements as the Secretary shall, by regulation, provide to carry out the purposes of this Act.

(b) CERTIFICATION.—The Secretary shall establish procedures for initial certification and recertification as an eligible State program.

(c) TRANSITIONAL MECHANISMS.—For the 5-year period beginning on the date of the enactment of this Act, in the case of a State that does not have an eligible State program for the State, a State residual insurance market entity, or State-sponsored provider of natural catastrophe insurance, for such State shall be considered to be an eligible State program, but only if such State residual insurance market entity, or State-sponsored provider of natural catastrophe insurance, was in existence before such date of enactment.

(d) REINSURANCE TO COVER EXPOSURE.—This section may not be construed to limit or prevent any eligible State program from obtaining reinsurance coverage for insured losses retained by insurers pursuant to this section.

**SEC. 502. STUDY AND CONDITIONAL COVERAGE OF COMMERCIAL RESIDENTIAL LINES OF INSURANCE.**

The Secretary shall study, on an expedited basis, the need for and impact of expanding the programs established by this Act to apply to insured losses of eligible State programs for losses arising from all commercial insurance policies which provide coverage for properties that are composed predominantly of residential rental units. The Secretary shall consider the catastrophic insurance and reinsurance market for commercial residential properties, and specifically the availability of adequate private insurance coverage when an insured event occurs, the impact any such capacity restrictions have on housing affordability for renters, and the likelihood that such an expansion of the program would increase insurance capacity for this market segment.

**SEC. 503. STUDY OF RISK-BASED PRICING AND STATE PROGRAM RATES.**

The Comptroller General of the United States shall conduct a study to analyze—

- (1) risk-based rate pricing, to determine the use of actuarially sound pricing for State insurance, reinsurance, or residual market programs, including what measures States are taking to implement actuarially sound rates; and
- (2) rates for State insurance, reinsurance, or residual market programs that fail to cover the expected value of all future costs, including the cost of capital, associated with insurance policies or reinsurance contracts written by such programs or fail to have sufficient assets above their indebtedness to meet their obligations.

Not later than 6 months after the date of the enactment of this Act, the Comptroller General shall submit a report to the Congress on the results of the study under this section.

**SEC. 504. DEFINITIONS.**

In this Act:

- (1) COMMITMENT TO GUARANTEE.—The term “commitment to guarantee” means a commitment to make debt guarantees to an eligible State program pursuant to section 202(c).
- (2) ELIGIBLE STATE PROGRAM.—The term “eligible State program” means a State program that the Secretary certifies as an eligible State program under section 501.
- (3) INSURED LOSS.—The term “insured loss” means any loss that is determined by an eligible State program as being covered by insurance or reinsurance made available under that eligible State program.
- (4) QUALIFYING ASSETS.—The term “qualifying assets” means the policyholder surplus of the eligible State program as stated in the most recent quarterly financial statement filed by the program with the domiciliary regulator of the program in the last quarter ending prior to the event or events.
- (5) SECRETARY.—The term “Secretary” means the Secretary of the Treasury.
- (6) STATE.—The term “State” includes the several States, the District of Columbia, the Commonwealth of Puerto Rico, Guam, the Commonwealth of the Northern Mariana Islands, the United States Virgin Islands, and American Samoa, and any other territory or possession of the United States.

**SEC. 505. REGULATIONS.**

The Secretary shall issue such regulations as may be necessary to carry out this Act.

PURPOSE AND SUMMARY

H.R. 2555, the Homeowners’ Defense Act of 2010, addresses the issues of homeowners’ insurance affordability and availability by: (1) fostering the efficient transfer of natural catastrophe risk equitably throughout the private insurance marketplace and the broader capital markets; and (2) helping homeowners and communities prepare for and recover from catastrophic natural catastrophes. As both efficient risk transfer and aggressive mitigation are equally vital to any attempt to stabilize the homeowners’ insurance marketplace, the Homeowners’ Defense Act includes three different, though related, means of risk transfer that each require partici-

pating States to maintain reasonable, market-based underwriting practices and require individuals and communities to commit to and maintain mitigation efforts identified as effective in reducing losses following a natural catastrophe.

#### BACKGROUND AND NEED FOR LEGISLATION

The increasing costs of natural catastrophes have significantly stressed property and casualty insurance markets, particularly the homeowners' insurance market. This market stress is due in large part to the fact that participants in the insurance marketplace have the most experience with and are best prepared to deal with high-frequency, low-severity events. In contrast, catastrophic events, and particularly mega-catastrophes, such as the recent earthquakes in Chile and Haiti and hurricanes like Katrina, are low-frequency, high-severity events that violate standard loss models by affecting many insured exposures at one time and subject insurers to near unsustainable losses in a given year.

Insurance markets tend to respond adversely to mega-catastrophes. They respond to large events, particularly those that cause them to reevaluate their estimates of the probability and severity of loss, by restricting the supply of insurance and raising the price of the limited coverage that is made available. This occurred, for example, following Hurricane Andrew in 1992 and the Northridge earthquake in 1994.

Successive, increasingly expensive natural disasters have caused insurance companies to reexamine their business models for insuring natural disasters. This process has resulted in insurers and reinsurers pulling out of or reducing their portfolios in certain areas of the country. This resulting insurance capacity loss has caused homeowners insurance rates to spike from 100 percent to over 600 percent in certain higher-risk areas and left many areas of the country without effectively functioning private insurance markets.

The programs created in Titles I–V of H.R. 2555 work together to help smooth post-incident spikes in the homeowners' insurance marketplace and protect consumers from the financial devastation that can result from natural catastrophes.

The first method by which the Homeowners' Defense Act facilitates the transfer of insurance risk into the private capital and reinsurance markets is through the creation of the National Catastrophe Risk Consortium, an organization that States can voluntarily join for the purposes of transferring catastrophe risk. Risk transfer would be achieved through the issuance of risk-linked securities or through reinsurance contracts. Eligible State insurance programs are defined in Title V of the legislation (see below). The Consortium is designed to function as a conduit, so that at no time would actual risk transfer either to or from the Federal Government.

The Consortium offers States and private market participants a unique opportunity to benefit from a combining of catastrophic risk diversified by type of peril and geographic region. The Consortium staff will work in coordination with participating States to catalogue inventories of catastrophic risk. Catastrophe bond underwriters and other market participants will be able to access this database to structure bonds or reinsurance contracts and treaties. The Consortium will serve as a conduit issuer of catastrophe bonds

on behalf of the participating States, but not actually take possession of any bond proceeds, coupon payments or underlying risk.

Through the aggregation and maintenance of market statistics, the Consortium will develop industry standards for the catastrophe bond and risk transference markets. Such standards include but are not limited to the terms of bond offerings, the nature of triggers used and the definitions of risks.

The Consortium would be governed by a board comprised of Federal and State representatives with each member having a single vote. The Consortium would be jointly funded by the Federal government and participating States. A minimal Federal appropriation will be matched by State obligations prorated according to each State's participation in the Consortium.

The legislation authorizes \$20 billion for Fiscal Years 2010 through 2014 to carry out Title I.

The second method by which the Homeowners' Defense Act facilitates risk transfer into the private capital markets is the Catastrophe Obligation Program created in Title II of the bill. Title II permits the Treasury to offer to holders of the debt of State catastrophe insurance or reinsurance programs a guarantee that principal and interest on the debt will be paid. Treasury may guarantee a total of up to: (1) \$3.5 billion for programs that insure against earthquake loss; and (2) \$17 billion for programs that insure against all other natural disasters. These Treasury guarantees cover a period of three years that at each anniversary may be extended for a period of one year (not to exceed 30 years in total). The principal amount guaranteed for an individual State program may be up to the total amount of insured losses sustained by the State program less 80 percent of the State program's capital as stated in the State program's last quarterly report. Treasury may charge a fee to cover administrative costs and probable losses on the guarantee that does not exceed one half of one percent of the outstanding debt guaranteed. Treasury may recover any payments made on guarantees from the appropriate State program.

In order to request a guarantee, at the time of a request for a guarantee and annually on request for extension, a State program must submit a report describing how the State program plans to repay the debt. Before providing any guarantee, the Treasury must review the State program's debt repayment report, verify that the State program is in compliance with the guarantee program's underwriting and loss mitigation requirements, and assure the State program agrees not to use any Federal funds to repay the underlying guaranteed debt.

In Title III, the Homeowners' Defense Act establishes the Federal Natural Catastrophe Reinsurance Fund in the Department of the Treasury. Qualified reinsurance programs can purchase one-year reinsurance contracts from the Fund provided the coverage does not displace or compete with the private market. The Fund can enter into reinsurance contracts for any band of reinsurance coverage that responds to losses in excess of the certain amount of loss as defined in the legislation. Of the insured losses in excess of this amount, the reinsurance contract will pay 90 percent.

The contracts shall cover insured losses from one or more events that may occur during the term of the contract and shall provide that if multiple events do occur, the retained losses requirement

shall apply on a calendar year basis in the aggregate. The contracts shall be priced at a level that provides sufficient premium income to the fund to pay the reasonably anticipated cost of all claims, including those resulting from catastrophic natural disasters, and administrative expenses.

The aggregate liability for payment of claims under reinsurance contracts the Fund can assume is determined by the Secretary after assessing the availability of needed catastrophic coverage in the national and international marketplace. The Fund can be credited with amounts received from the sale of reinsurance contracts, and amounts earned on investments of the Fund.

The Secretary can use amounts in the Fund to pay purchasers covered under contracts for reinsurance, administrative expenses and payments for reinsurance coverage of the risk assumed by the Fund in reinsurance contracts. Should the Fund issue obligations to pay claims, all such obligations must be repaid with interest paid in the form of premiums charged to purchasers of reinsurance contracts. If the Fund is deemed by the Secretary to have funds in excess of current needs, the excess may be invested in obligations of the United States. No money is appropriated for the operation of the Fund.

Finally, Title IV authorizes the Secretary of Housing and Urban Development to establish a grant program to develop, enhance and maintain State or local government programs that relate to prevention and mitigation of losses from natural catastrophes. Such programs focus on: (1) encouraging awareness of risk factors and steps taken to reduce or eliminate them; (2) assisting in the determination of risk based on location of a property; (3) providing inspections of homes; (4) providing financial assistance to retrofit homes to reduce exposure to loss; and (5) supporting disaster response readiness programs. Title IV directs the Secretary to use no less than 35 percent of the net investment income from the Federal Natural Catastrophe Reinsurance Fund earned in each fiscal year for funding.

#### HEARINGS

The Subcommittee on Housing and Community Opportunity and the Subcommittee on Capital Markets, Insurance, and Government Sponsored Enterprises held a joint legislative hearing entitled “Approaches to Mitigating and Managing Natural Catastrophe Risk: H.R. 2555, The Homeowners’ Defense Act” on Wednesday, March 10, 2010. The following witnesses testified:

#### **Hearing Witnesses**

- Mr. James Lee Witt, former Director of the Federal Emergency Management Agency on behalf of Protect-ingAmerica.org
- Mr. Glenn Pomeroy, Chief Executive Officer, California Earthquake Authority
- Mr. Steve Ellis, Vice President, Taxpayers for Common Sense
- Mr. Charles McMillan, Coldwell Banker Residential Brokerage, Dallas-Fort Worth and Immediate Past President, National Association of REALTORS®

## COMMITTEE CONSIDERATION

The Committee on Financial Services met in open session on April 27, 2010, and ordered H.R. 2555, the Homeowners' Defense Act of 2009, as amended, favorably reported to the House by a record vote of 39 yeas and 26 nays.

## COMMITTEE VOTES

Clause 3(b) of rule XIII of the Rules of the House of Representatives requires the Committee to list the record votes on the motion to report legislation and amendments thereto. A motion by Mr. Frank to report the bill, as amended, to the House with a favorable recommendation was agreed to by a record vote of 39 yeas and 26 nays (Record vote no. FC-115). The names of Members voting for and against follow:

## RECORD VOTE NO. FC-115

Representative	Aye	Nay	Present	Representative	Aye	Nay	Present
Mr. Frank .....	X			Mr. Bachus .....		X	
Mr. Kanjorski .....	X			Mr. Castle .....		X	
Ms. Waters .....	X			Mr. King (NY) .....		X	
Mrs. Maloney .....	X			Mr. Royce .....		X	
Mr. Gutierrez .....				Mr. Lucas .....		X	
Ms. Velázquez .....	X			Mr. Paul .....		X	
Mr. Watt .....	X			Mr. Manzullo .....		X	
Mr. Ackerman .....	X			Mr. Jones .....		X	
Mr. Sherman .....	X			Mrs. Biggert .....		X	
Mr. Meeks .....	X			Mr. Miller (CA) .....		X	
Mr. Moore (KS) .....	X			Mrs. Capito .....		X	
Mr. Capuano .....	X			Mr. Hensarling .....			
Mr. Hinojosa .....	X			Mr. Garrett (NJ) .....		X	
Mr. Clay .....	X			Mr. Barrett (SC) .....			
Mrs. McCarthy .....	X			Mr. Gerlach .....		X	
Mr. Baca .....	X			Mr. Neugebauer .....		X	
Mr. Lynch .....	X			Mr. Price (GA) .....			
Mr. Miller (NC) .....	X			Mr. McHenry .....		X	
Mr. Scott .....	X			Mr. Campbell .....	X		
Mr. Green .....	X			Mr. Putnam .....	X		
Mr. Cleaver .....	X			Mrs. Bachmann .....		X	
Ms. Bean .....	X			Mr. Marchant .....		X	
Ms. Moore (WI) .....				Mr. McCotter .....		X	
Mr. Hodes .....				Mr. McCarthy .....		X	
Mr. Ellison .....	X			Mr. Posey .....	X		
Mr. Klein .....	X			Ms. Jenkins .....		X	
Mr. Wilson .....	X			Mr. Lee .....		X	
Mr. Perlmutter .....	X			Mr. Paulsen .....		X	
Mr. Donnelly .....	X			Mr. Lance .....		X	
Mr. Foster .....	X						
Mr. Carson .....	X						
Ms. Speier .....	X						
Mr. Childers .....	X						
Mr. Minnick .....	X						
Mr. Adler .....	X						
Ms. Kilroy .....		X					
Mr. Driehaus .....		X					
Ms. Kosmas .....	X						
Mr. Grayson .....	X						
Mr. Himes .....		X					
Mr. Peters .....	X						
Mr. Maffei .....	X						

During the consideration of the bill, the following amendments were disposed of by record votes. The names of Members voting for and against follow:

An amendment in the nature of a substitute offered by Mrs. Capito (and Mr. Garrett (NJ)), was not agreed to by a record vote of 24 yeas and 42 nays (Record vote no. FC-111):

RECORD VOTE NO. FC-111

Representative	Aye	Nay	Present	Representative	Aye	Nay	Present
Mr. Frank		X		Mr. Bachus	X		
Mr. Kanjorski		X		Mr. Castle	X		
Ms. Waters		X		Mr. King (NY)	X		
Mrs. Maloney		X		Mr. Royce	X		
Mr. Gutierrez				Mr. Lucas	X		
Ms. Velázquez		X		Mr. Paul	X		
Mr. Watt		X		Mr. Manzullo	X		
Mr. Ackerman		X		Mr. Jones	X		
Mr. Sherman		X		Mrs. Biggert	X		
Mr. Meeks		X		Mr. Miller (CA)	X		
Mr. Moore (KS)		X		Mrs. Capito	X		
Mr. Capuano		X		Mr. Hensarling	X		
Mr. Hinojosa		X		Mr. Garrett (NJ)	X		
Mr. Clay		X		Mr. Barrett (SC)			
Mrs. McCarthy		X		Mr. Gerlach	X		
Mr. Baca		X		Mr. Neugebauer	X		
Mr. Lynch		X		Mr. Price (GA)			
Mr. Miller (NC)		X		Mr. McHenry	X		
Mr. Scott		X		Mr. Campbell		X	
Mr. Green		X		Mr. Putnam		X	
Mr. Cleaver		X		Mrs. Bachmann	X		
Ms. Bean		X		Mr. Marchant	X		
Ms. Moore (WI)				Mr. McCotter	X		
Mr. Hodes				Mr. McCarthy	X		
Mr. Ellison		X		Mr. Posey		X	
Mr. Klein		X		Ms. Jenkins	X		
Mr. Wilson		X		Mr. Lee	X		
Mr. Perlmutter		X		Mr. Paulsen	X		
Mr. Donnelly		X		Mr. Lance	X		
Mr. Foster		X					
Mr. Carson		X					
Ms. Speier		X					
Mr. Childers		X					
Mr. Minnick		X					
Mr. Adler		X					
Ms. Kilroy		X					
Mr. Driehaus		X					
Ms. Kosmas		X					
Mr. Grayson		X					
Mr. Himes		X					
Mr. Peters		X					
Mr. Maffei		X					

An amendment by Mr. Royce, no. 4, striking title III relating to reinsurance coverage for eligible State programs, was not agreed to by a record vote of 27 yeas and 38 nays (Record vote no. FC-112):

RECORD VOTE NO. FC-112

Representative	Aye	Nay	Present	Representative	Aye	Nay	Present
Mr. Frank		X		Mr. Bachus	X		
Mr. Kanjorski		X		Mr. Castle	X		
Ms. Waters		X		Mr. King (NY)	X		
Mrs. Maloney		X		Mr. Royce	X		
Mr. Gutierrez				Mr. Lucas	X		



RECORD VOTE NO. FC-112—Continued

Representative	Aye	Nay	Present	Representative	Aye	Nay	Present
Ms. Velázquez		X		Mr. Paul	X		
Mr. Watt		X		Mr. Manzano	X		
Mr. Ackerman		X		Mr. Jones	X		
Mr. Sherman		X		Mrs. Biggert	X		
Mr. Meeks		X		Mr. Miller (CA)	X		
Mr. Moore (KS)		X		Mrs. Capito	X		
Mr. Capuano		X		Mr. Hensarling			
Mr. Hinojosa		X		Mr. Garrett (NJ)	X		
Mr. Clay		X		Mr. Barrett (SC)			
Mrs. McCarthy		X		Mr. Gerlach	X		
Mr. Baca		X		Mr. Neugebauer	X		
Mr. Lynch		X		Mr. Price (GA)			
Mr. Miller (NC)		X		Mr. McHenry	X		
Mr. Scott		X		Mr. Campbell	X		
Mr. Green		X		Mr. Putnam	X		
Mr. Cleaver		X		Mrs. Bachmann	X		
Ms. Bean		X		Mr. Marchant	X		
Ms. Moore (WI)				Mr. McCotter	X		
Mr. Hodes				Mr. McCarthy	X		
Mr. Ellison		X		Mr. Posey	X		
Mr. Klein		X		Ms. Jenkins	X		
Mr. Wilson		X		Mr. Lee	X		
Mr. Perlmutter		X		Mr. Paulsen	X		
Mr. Donnelly		X		Mr. Lance	X		
Mr. Foster		X					
Mr. Carson		X					
Ms. Speier		X					
Mr. Childers		X					
Mr. Minnick		X					
Mr. Adler		X					
Ms. Kilroy		X					
Mr. Driehaus		X					
Ms. Kosmas		X					
Mr. Grayson		X					
Mr. Himes	X						
Mr. Peters		X					
Mr. Maffei		X					

An amendment by Mr. Garrett (NJ), no. 6, relating to the effective date, was not agreed to by a record vote of 24 yeas and 41 nays (Record vote no. FC-113):

RECORD VOTE NO. FC-113

Representative	Aye	Nay	Present	Representative	Aye	Nay	Present
Mr. Frank		X		Mr. Bachus	X		
Mr. Kanjorski		X		Mr. Castle	X		
Ms. Waters		X		Mr. King (NY)	X		
Mrs. Maloney		X		Mr. Royce	X		
Mr. Gutierrez				Mr. Lucas	X		
Ms. Velázquez		X		Mr. Paul	X		
Mr. Watt		X		Mr. Manzano	X		
Mr. Ackerman		X		Mr. Jones	X		
Mr. Sherman		X		Mrs. Biggert	X		
Mr. Meeks		X		Mr. Miller (CA)	X		
Mr. Moore (KS)		X		Mrs. Capito	X		
Mr. Capuano		X		Mr. Hensarling			
Mr. Hinojosa		X		Mr. Garrett (NJ)	X		
Mr. Clay		X		Mr. Barrett (SC)			
Mrs. McCarthy		X		Mr. Gerlach	X		
Mr. Baca		X		Mr. Neugebauer	X		
Mr. Lynch		X		Mr. Price (GA)			
Mr. Miller (NC)		X		Mr. McHenry	X		

RECORD VOTE NO. FC-113—Continued

Representative	Aye	Nay	Present	Representative	Aye	Nay	Present
Mr. Scott		X		Mr. Campbell		X	
Mr. Green		X		Mr. Putnam		X	
Mr. Cleaver		X		Mrs. Bachmann	X		
Ms. Bean		X		Mr. Marchant	X		
Ms. Moore (WI)				Mr. McCotter	X		
Mr. Hodes				Mr. McCarthy	X		
Mr. Ellison		X		Mr. Posey	X		
Mr. Klein		X		Ms. Jenkins	X		
Mr. Wilson		X		Mr. Lee	X		
Mr. Perlmutter		X		Mr. Paulsen	X		
Mr. Donnelly		X		Mr. Lance	X		
Mr. Foster		X					
Mr. Carson		X					
Ms. Speier		X					
Mr. Childers		X					
Mr. Minnick		X					
Mr. Adler		X					
Ms. Kilroy		X					
Mr. Driehaus		X					
Ms. Kosmas		X					
Mr. Grayson		X					
Mr. Himes		X					
Mr. Peters		X					
Mr. Maffei		X					

An amendment by Mr. Neugebauer, no. 10, relating to the effective date of catastrophe obligation guarantee and reinsurance programs, was not agreed to by a record vote of 22 yeas and 43 nays (Record vote no. FC-114):

RECORD VOTE NO. FC-114

Representative	Aye	Nay	Present	Representative	Aye	Nay	Present
Mr. Frank		X		Mr. Bachus	X		
Mr. Kanjorski		X		Mr. Castle	X		
Ms. Waters		X		Mr. King (NY)		X	
Mrs. Maloney		X		Mr. Royce	X		
Mr. Gutierrez				Mr. Lucas	X		
Ms. Velázquez		X		Mr. Paul	X		
Mr. Watt		X		Mr. Manullo	X		
Mr. Ackerman		X		Mr. Jones	X		
Mr. Sherman		X		Mrs. Biggert	X		
Mr. Meeks		X		Mr. Miller (CA)	X		
Mr. Moore (KS)		X		Mrs. Capito	X		
Mr. Capuano		X		Mr. Hensarling			
Mr. Hinojosa		X		Mr. Garrett (NJ)	X		
Mr. Clay		X		Mr. Barrett (SC)			
Mrs. McCarthy		X		Mr. Gerlach	X		
Mr. Baca		X		Mr. Neugebauer	X		
Mr. Lynch		X		Mr. Price (GA)			
Mr. Miller (NC)		X		Mr. McHenry	X		
Mr. Scott		X		Mr. Campbell		X	
Mr. Green		X		Mr. Putnam		X	
Mr. Cleaver		X		Mrs. Bachmann	X		
Ms. Bean		X		Mr. Marchant	X		
Ms. Moore (WI)				Mr. McCotter	X		
Mr. Hodes				Mr. McCarthy	X		
Mr. Ellison		X		Mr. Posey		X	
Mr. Klein		X		Ms. Jenkins	X		
Mr. Wilson		X		Mr. Lee	X		
Mr. Perlmutter		X		Mr. Paulsen	X		
Mr. Donnelly		X		Mr. Lance	X		
Mr. Foster		X					

RECORD VOTE NO. FC-114—Continued

Representative	Aye	Nay	Present	Representative	Aye	Nay	Present
Mr. Carson .....	.....	X	.....				
Ms. Speier .....	.....	X	.....				
Mr. Childers .....	.....	X	.....				
Mr. Minnick .....	.....	X	.....				
Mr. Adler .....	.....	X	.....				
Ms. Kilroy .....	.....	X	.....				
Mr. Driehaus .....	.....	X	.....				
Ms. Kosmas .....	.....	X	.....				
Mr. Grayson .....	.....	X	.....				
Mr. Himes .....	.....	X	.....				
Mr. Peters .....	.....	X	.....				
Mr. Maffei .....	.....	X	.....				

The following other amendments were also considered by the Committee:

An amendment by Mr. Putnam, no. 2, requiring publishing and display of State coverage information on Website, was agreed to by a voice vote.

An amendment by Mr. Minnick, no. 3, precluding properties in the 100 year floodplain from being eligible for debt guarantees, was offered and withdrawn, then later re-offered as amendment no. 5, and was then agreed to by a voice vote.

An amendment by Mr. Putnam, no. 7, requiring State law to sue catastrophe loan comparable to private market, risk-based rate pricing, and actuarial principles, was offered and withdrawn.

An amendment by Mr. Campbell, no. 8, regarding future costs associated with insurance and reinsurance contracts, was agreed to by a voice vote.

An amendment by Mr. Minnick, no. 9, stating that debt guarantees cannot be applied to properties within the Coastal Barrier Resources System, was offered and withdrawn.

An amendment by Mrs. Bachmann, no. 11, relating to prohibition on election and lobbying activities, was amended by unanimous consent and then agreed to by a voice vote.

An amendment by Mrs. Bachmann, no. 12, relating to the repeal of the Act, was not agreed to by a voice vote.

An amendment by Mr. Campbell, no. 13, to lower earthquake perils and all other perils coverage, was amended by unanimous consent and then agreed to by a voice vote.

An amendment by Mr. Campbell, no. 14, relating to working capital requirement, was offered and withdrawn.

An amendment by Mr. Klein, no. 15, a manager’s amendment, was agreed to by a voice vote.

COMMITTEE OVERSIGHT FINDINGS

Pursuant to clause 3(c)(1) of rule XIII of the Rules of the House of Representatives, the Committee has held a hearing and made findings that are reflected in this report.

PERFORMANCE GOALS AND OBJECTIVES

Pursuant to clause 3(c)(4) of rule XIII of the Rules of the House of Representatives, the Committee establishes the following performance related goals and objectives for this legislation:

H.R. 2555, the Homeowners' Defense Act of 2010, would address the issues of homeowners insurance affordability and availability by: (1) fostering the efficient transfer of natural catastrophe risk equitably throughout the private insurance marketplace and the broader capital markets; and (2) help homeowners and communities prepare for and recover from catastrophic natural catastrophes.

NEW BUDGET AUTHORITY, ENTITLEMENT AUTHORITY, AND TAX  
EXPENDITURES

In compliance with clause 3(c)(2) of rule XIII of the Rules of the House of Representatives, the Committee adopts as its own the estimate of new budget authority, entitlement authority, or tax expenditures or revenues contained in the cost estimate prepared by the Director of the Congressional Budget Office pursuant to section 402 of the Congressional Budget Act of 1974.

COMMITTEE COST ESTIMATE

The Committee adopts as its own the cost estimate prepared by the Director of the Congressional Budget Office pursuant to section 402 of the Congressional Budget Act of 1974.

CONGRESSIONAL BUDGET OFFICE ESTIMATE

Pursuant to clause 3(c)(3) of rule XIII of the Rules of the House of Representatives, the following is the cost estimate provided by the Congressional Budget Office pursuant to section 402 of the Congressional Budget Act of 1974:

U.S. CONGRESS,  
CONGRESSIONAL BUDGET OFFICE,  
*Washington, DC, June 2, 2010.*

Hon. BARNEY FRANK,  
*Chairman, Committee on Financial Services,  
House of Representatives, Washington, DC.*

DEAR MR. CHAIRMAN: The Congressional Budget Office has prepared the enclosed cost estimate for H.R. 2555, the Homeowners' Defense Act of 2010.

If you wish further details on this estimate, we will be pleased to provide them. The CBO staff contact is Daniel Hoople.

Sincerely,

DOUGLAS W. ELMENDORF.

Enclosure.

*H.R. 2555—Homeowners' Defense Act of 2010*

Summary: H.R. 2555 is aimed at increasing the availability and affordability of homeowners' insurance by improving the ability of certain state-sponsored insurers and reinsurers to access resources to pay claims following a natural disaster. Based on data from state-sponsored entities that would likely be eligible to participate in the new federal programs and historical expenditure patterns for disaster mitigation programs, CBO estimates that implementing this legislation would cost \$1.7 billion over the 2011–2015 period, assuming appropriation of the necessary amounts beginning in 2011.

The legislation would authorize appropriations to establish a federal disaster reinsurance program. Reinsurance is insurance for insurers (or other reinsurers); it allows insurance programs to transfer risk to other entities. Under the bill, the Secretary of the Treasury would be authorized to sell reinsurance to state-sponsored insurers and reinsurers (private entities would not be eligible) in amounts to be determined by the Secretary. Such reinsurance could only be offered to the extent that appropriations for the maximum potential liability of the federal government were provided in advance for each year of insurance coverage.

H.R. 2555 also would authorize appropriations for the Treasury to enter into commitments to guarantee the principal and interest of bonds issued by eligible insurers and reinsurers following a disaster. The total principal of outstanding bonds guaranteed by the Treasury could not exceed \$3.5 billion for earthquake claims and \$17 billion for all other perils. H.R. 2555 would authorize the appropriation of \$75 million over the 2011–2014 period to provide grants for state and local governments to help prevent and mitigate losses from natural disasters. Additionally, CBO estimates that the bill would authorize the appropriation of about \$700 million from the new federal reinsurance program for the same purpose. The bill also would authorize the appropriation of \$100 million over the 2011–2014 period to establish a National Catastrophe Risk Consortium.

Pay-as-you-go procedures do not apply to this legislation because it would not affect direct spending or revenues.

H.R. 2555 contains no intergovernmental or private-sector mandates as defined in the Unfunded Mandates Reform Act (UMRA) and would impose no costs on state, local, or tribal governments.

Estimated cost to the Federal Government: The estimated budgetary impact of H.R. 2555 is shown in the following table. The costs of this legislation fall within budget function 450 (community and regional development).

	By fiscal year, in millions of dollars—					
	2011	2012	2013	2014	2015	2011–2015
CHANGES IN SPENDING SUBJECT TO APPROPRIATION						
Natural Catastrophe Reinsurance Fund:						
Estimated Authorization Level .....	3,440	7,035	7,190	7,350	7,515	32,539
Estimated Outlays .....	124	258	265	274	284	1,205
Catastrophe Obligation Guarantee Program:						
Estimated Authorization Level .....	65	2	2	23	23	115
Estimated Outlays .....	23	23	23	23	23	115
Mitigation Grant Program:						
Estimated Authorization Level .....	15	38	105	230	376	764
Estimated Outlays .....	2	8	28	73	156	267
National Catastrophe Risk Consortium:						
Authorization Level .....	20	20	20	20	0	80
Estimated Outlays .....	10	18	20	20	12	80
Total Changes:						
Estimated Authorization Level .....	3,540	7,095	7,317	7,623	7,914	33,489
Estimated Outlays .....	159	307	336	390	475	1,667

Basis of estimate: For this estimate, CBO assumes that the bill will be enacted by the end of fiscal year 2010 and that the necessary amounts will be appropriated for each fiscal year beginning in 2011.

Several factors make the costs of the legislation highly uncertain. Under the bill, the Treasury would have considerable discretion in implementing the federal reinsurance and debt guarantee programs, including establishing eligibility and setting the terms for reinsurance contracts. This discretion makes it difficult to determine which state-sponsored programs would participate. Second, because the structure of various insurers and reinsurers may be altered in response to this legislation or in response to a future disaster, it is unclear what the risk profile of those programs would look like each year. Unless otherwise indicated by historical experience or information provided by a program, CBO assumes for this estimate that potentially eligible entities would operate under their current structure for the next five years and that reinsurance terms offered by the Treasury would encourage participation in the federal program.

*Programs that increase access to capital*

H.R. 2555 would establish two new programs within the Treasury to allow certain state-sponsored insurers and reinsurers to access funding to pay claims following a natural disaster—the National Catastrophe Reinsurance Fund and the Catastrophe Obligation Guarantee program. To be eligible for those programs, insurers or reinsurers would have to:

- Operate as a state-sponsored, nonprofit program that offers (or reinsures) residential property insurance, and in which the state has a financial interest;
- Be governed by a body made up of a majority of public officials;
- Charge premiums that are actuarially sound and do not cross-subsidize separate insurance lines;
- Be considered an “integral part” of the state or otherwise recognized as exempt from federal income taxation;
- Reflect hazard mitigation measures in premiums; and
- Reside in a state that has adopted mitigation measures consistent with the International Code Council building codes.

During the first five years following enactment, if a state does not have an otherwise eligible program, a residual insurer or other state-sponsored provider of catastrophe insurance would be eligible to participate in the new federal programs if such insurance existed prior to enactment of H.R. 2555.

Based on the criteria set forth in the legislation, CBO expects that several existing insurance entities would be eligible to purchase reinsurance or obtain a debt guarantee commitment from the Treasury under the bill over the next five years. Examples of such programs include the Florida Hurricane Catastrophe Fund (FHCF), the California Earthquake Authority (CEA), the Texas Windstorm Insurance Association (TWIA), Louisiana Citizens Property Insurance, and other state Fair Access to Insurance Requirements (FAIR) plans. Actuaries from Florida Citizens Property Insurance (a state-regulated primary insurer for property owners unable to obtain coverage in the private market) as well as the state have recently acknowledged that the insurer is charging below actuarially sound premiums. Thus, CBO assumes that Florida Citizens would not be eligible for either of the new Treasury programs during the next five years. In addition, the program would not qualify for special treatment during the five-year transition period because Flor-

ida has another program (the FHCF) that meets the eligibility criteria under the legislation.

In addition to those state-sponsored entities already established, states could modify or create other programs that would become eligible to participate in the new federal programs. For example, following Hurricane Iniki, Hawaii created a Hurricane Relief Fund in 1993 to provide direct insurance to property owners. The state stopped writing coverage in 2000; however, it is possible that the fund (or a similar entity in another state) could write coverage in the future and become eligible to purchase reinsurance or obtain a debt guarantee under the legislation. For this estimate, CBO assumes that only active insurance programs currently established would participate. If programs not yet established participate in the future, the estimated costs of this legislation would be higher.

**National Catastrophe Reinsurance Fund.** Title III would establish a National Catastrophe Reinsurance Fund within the Treasury and would authorize such sums as may be necessary to cover the maximum potential liability of the federal government for reinsurance coverage purchased through the fund. Reinsurance contracts would cover 90 percent of insured losses above and below unspecified minimum retention and maximum coverage levels (set at the discretion of the Treasury) during a given year. The premium charged for such coverage would be set at an amount that the Treasury estimates would offset the expected cost of the reinsurance, including administrative expenses.

CBO estimates that eligible entities would seek about \$7 billion in reinsurance coverage from the proposed federal reinsurance fund in 2012 (the first full year that the fund would be effective under the legislation). We estimate that eligible entities would continue to seek the same level of coverage in future years, adjusted for increases in the value and volume of insurance coverage and reaching about \$7.5 billion by 2015. CBO's estimate of the expected cost of the reinsurance coverage—net of the premiums charged for that federal coverage—averages about \$270 million a year over the 2012–2015 period. As discussed below, CBO expects that premiums charged for the federal reinsurance program would be inadequate to compensate the government for the cost of that coverage.

*Premiums Would Likely Fall Below Those Offered by the Private Market.* Because insurers and reinsurers do not have perfect information, they face considerable uncertainty in setting premiums. For natural disaster coverage, the two main sources of uncertainty involve estimates of expected losses (underwriting risk) and timing of payments (timing risk).

Estimates of expected property damage from catastrophic natural disasters rely on historical data as well as projections of changes in weather patterns and property values. Because catastrophic natural disasters are infrequent, historical data are very limited. Therefore, reinsurers face considerable risk that their estimates of expected property damages, and thus premiums, will not be high enough to cover actual losses over time. Even if insurers and reinsurers knew the exact premium that would cover losses over time, there is still a risk that a high-cost, low-probability disaster could occur early in the program's history, before the program had time to collect enough premiums to accumulate a sufficient level of reserves.

Private insurers and reinsurers of catastrophic events attempt to address both of those risks (as well as others) by including a substantial “risk load”<sup>1</sup> in their premiums. Risk loads observed in private transactions for natural disaster reinsurance vary depending on the range of expected property damages (variance) for a given disaster. Estimates for infrequent events (very severe hurricanes or earthquakes, for example) have wider ranges of expected damages, and thus reinsurance premiums for those events tend to carry a higher risk load. Typical risk loads may be four to six times as large as the expected losses, but they can be 10 times or more.

There are several reasons why CBO believes that both the risk load and the overall premium offered by the Treasury would be less than a comparable premium charged by the private market:

- The federal program would have the capacity to absorb large levels of losses as soon as the program begins operation because of the requirement that the maximum potential liability be appropriated in advance of issuance; therefore, the federal reinsurance program would not have to include timing risk in its premium calculation.

- Other government insurance programs (for example, crop insurance and flood insurance) have not typically incorporated significant risk multiples into premiums to account for uncertainty in loss estimates.

- The Treasury would be required under the bill to account for savings associated with the nonprofit and tax-exempt status of the fund when setting premiums.

- Consumer and political pressures directed toward the proposed federal program would likely create a strong incentive for its managers to keep reinsurance premiums low to address homeowners’ concerns of price and availability in the property insurance market. The wide range of expected outcomes produced by catastrophic losses provides the ability for programs to choose lower expected losses while meeting the requirement of being actuarially sound.

*Demand for Reinsurance and Estimated Authorization Level.* CBO expects that FHCF, CEA, TWIA, Louisiana Citizens, and several state-sponsored FAIR plans would purchase federal reinsurance under H.R. 2555 over the next five years. Some of those insurance entities would cease purchasing coverage from the Treasury following 2015 because they would no longer be eligible. (Most FAIR plans would not qualify for the federal reinsurance program under the criteria set forth in the bill and would only participate for the five years after enactment—the transition period during which noneligible residual insurers and other state providers of catastrophe insurance could participate if no other state-sponsored entity was eligible.) Because CBO expects that premiums offered by the federal government would be below those offered by the private market, we estimate that over time, each participating program would purchase all of its reinsurance through the new federal program.

Under the bill, the total liability of the fund in any single year could not exceed the amount appropriated by the Congress for that purpose. In other words, a reinsurance contract that would reim-

<sup>1</sup>A “risk load” is a factor used by insurers to adjust premiums upward to account for uncertainties in the models used to estimate property damages and other risks inherent in issuing an insurance or reinsurance contract.



burse a state-sponsored insurer or reinsurer for up to \$10 billion in property damage claims from a natural disaster would require an appropriation of \$10 billion before the policy could be issued. CBO obtained data from many potential participants in the federal reinsurance program, including current and historical reinsurance purchases. Based on this information, CBO estimates that the National Catastrophe Reinsurance Fund would require about \$3.4 billion in appropriations in 2011 and almost \$33 billion over the 2011–2015 period to meet the demand for federal reinsurance.

*Federal Reinsurance Would Likely Be Priced Below Cost.* If the Treasury had perfect information needed to set premiums for the proposed reinsurance program, the expected net cost of the program would be zero. Actual costs from year to year would be positive or negative depending on the random occurrence of covered events; however, over time the program would generate enough income to cover all claims.

CBO has limited confidence in the accuracy of expected loss estimates used to set premiums for reinsurance of catastrophic natural disasters. The significant uncertainty inherent in the models used to forecast the frequency and severity of natural disasters and their effects on insured structures, the tendency of government programs to include relatively small or no risk loads, and political and consumer pressures to keep premiums low would lead, we expect, to premiums that are unlikely to cover future costs.

*Net Expenditures From the National Catastrophe Reinsurance Fund Would Be Positive.* Because the legislation would require the appropriation of the maximum potential loss of the federal government prior to the issuance of a reinsurance contract, insured losses could not exceed amounts appropriated to the fund. However, CBO expects that reinsurance claims resulting from property damage caused by natural disasters would exceed premium income, resulting in net outlays from the fund. Even if the federal government were just as likely to set some premiums too high as too low, the implications for net program costs would not be symmetric because low premiums would encourage sales, while high premiums would discourage sales. CBO estimates that the federal government would tend to sell more reinsurance at a loss than at a gain, resulting in net expenditures from the fund.

Based on current and historical data on probable maximum losses and reinsurance, CBO estimates that reinsurance claims would exceed premiums by \$1.2 billion over the next five years, resulting in net outlays from the National Catastrophe Reinsurance Fund of that amount.

**Catastrophe Obligation Guarantee Program.** Title II would authorize such sums as may be necessary for the Secretary of the Treasury to guarantee the principal and interest of debt obligations (for example, bonds) issued by eligible insurers and reinsurers to pay claims for property damages following a natural disaster. The guaranteed principal could not exceed expected insured losses less 80 percent of the issuing programs' reported assets, \$3.5 billion for earthquake damages, or \$17 billion for damages from all other perils, whichever is least. State programs receiving a guarantee under the bill would be assessed an annual fee not to exceed one-half of one percent of the outstanding debt.

The budgetary accounting for loan guarantees is governed by the Federal Credit Reform Act of 1990 (FCRA), which requires an appropriation of the subsidy and administrative costs associated with federal loan guarantees and federal direct loans. Under FCRA, the subsidy is the estimated lifetime cost to the government of a loan or loan guarantee, calculated on a net-present-value basis excluding administrative costs. FCRA further specifies that the present-value computation should be done by discounting the expected net cash flows from the government at interest rates on Treasury securities of comparable maturity.

CBO expects that FHCF, CEA, TWIA, and Louisiana Citizens would apply for a guarantee under H.R. 3555. In addition, other state FAIR plans (such as the Mississippi Windstorm Underwriting Association) may participate, although very few have the current authority to issue debt. Based on the current risk profiles and claims-paying capacities of those programs, the annualized volume of debt obligations that would be guaranteed under the bill would total about \$2.1 billion (mostly from TWIA and FHCF), we estimate. The relatively high credit rating of insurers and reinsurers likely to participate, combined with expected fee income, suggests a relatively low subsidy rate for those guarantees—between zero and 2 percent, depending on the size of the fee—for a total subsidy cost of about \$20 million per year.

Under the bill, the Treasury would enter into a three-year commitment (with optional single-year renewals thereafter) to guarantee debt issued by a participating program following a natural disaster. While it is unlikely that a natural disaster large enough to trigger a debt guarantee would occur, CBO believes that a commitment to guarantee debt would constitute an obligation of the federal government and would require an appropriation to cover the expected cost of any guarantees that might be entered into. CBO estimates that the Treasury would need \$63 million (three years of estimated subsidy costs) to enter into debt guarantee commitments covering the 2011–2013 period. For each one-year renewal period thereafter, CBO estimates about \$21 million would need to be provided.

Federal expenditures resulting from a default on a debt guarantee made under the bill would likely be infrequent (due to the low probability that a major disaster causing a participating insurer or reinsurer to borrow funds to pay claims would occur and the low probability that the issuing program would default on such borrowing). CBO's estimate of this provision is an annualized cost that reflects those low probabilities. However, if a large-scale natural disaster were to occur and if a state program were to default, spending would be much greater than the expected costs included in this estimate.

CBO estimates that the cost of guaranteeing debt obligations after a disaster would total about \$115 million over the next five years, including about \$2 million a year for program administration. (Such administrative costs for federal loan and loan guarantee programs are recorded in the budget on a cash basis.)

#### *Other discretionary programs*

H.R. 2555 also would authorize appropriations for hazard mitigation grants and the establishment of a National Catastrophic Risk

Consortium. CBO estimates that enacting those provisions would cost \$347 million over the 2011–2015 period, assuming appropriation of the specified and necessary amounts.

**Mitigation Grant Program.** Title IV would authorize the appropriation of \$15 million for each of fiscal years 2011 through 2014 for the Department of Housing and Urban Development to award grants to state and local governments to prevent and mitigate losses from natural disasters. In addition, the bill would authorize the appropriation of an amount equal to 35 percent of the investment income of the National Catastrophe Reinsurance Fund (which CBO estimates would total about \$704 million over the 2012–2015 period), for a total authorization level of \$764 million. Based on historical expenditures of existing mitigation programs, we estimate that implementing this program would cost \$267 million over the next five years.

**National Catastrophe Risk Consortium.** Title I would authorize the appropriation of \$20 million for each of fiscal years 2011–2014 to establish the National Catastrophe Risk Consortium. The consortium would be a federal entity managed by a board of directors made up of designees from the Departments of the Treasury, Commerce, and Homeland Security, and members of participating states that operate or have authorized a natural catastrophe or residual market insurance entity. Responsibilities of the consortium would include: gathering risk and insurance information, conducting research and analysis into the standardization of risk-linked securities, and facilitating different avenues (for example, securitization and reinsurance) for states to transfer risk to the private market. Under the bill, any security or other financial instrument coordinated by the consortium would be done on a conduit basis (that is, the consortium and the federal government would assume no risk). Based on the cost of similar efforts, CBO estimates that implementing this provision would cost \$80 million over the 2011–2015 period for staff and research expenses, assuming appropriation of specified amounts.

Pay-as-you-go considerations: None.

Intergovernmental and private-sector impact: H.R. 2555 contains no intergovernmental or private-sector mandates as defined in UMRA. Debt guarantees, reinsurance policies, and mitigation grants in the bill would benefit state and local governments. Any costs to those entities would be incurred voluntarily as conditions of participating in a voluntary federal program.

Estimate prepared by: Federal Costs: Daniel Hoople; Impact on State, Local, and Tribal Governments: Melissa Merrell; Impact on the Private Sector: Paige Piper/Bach.

Estimate approved by: Theresa Gullo, Deputy Assistant Director for Budget Analysis.

#### FEDERAL MANDATES STATEMENT

The Committee adopts as its own the estimate of Federal mandates prepared by the Director of the Congressional Budget Office pursuant to section 423 of the Unfunded Mandates Reform Act.

#### ADVISORY COMMITTEE STATEMENT

No advisory committees within the meaning of section 5(b) of the Federal Advisory Committee Act were created by this legislation.

## CONSTITUTIONAL AUTHORITY STATEMENT

Pursuant to clause 3(d)(1) of rule XIII of the Rules of the House of Representatives, the Committee finds that the Constitutional Authority of Congress to enact this legislation is provided by Article 1, section 8, clause 1 (relating to the general welfare of the United States) and clause 3 (relating to the power to regulate interstate commerce).

## APPLICABILITY TO LEGISLATIVE BRANCH

The Committee finds that the legislation does not relate to the terms and conditions of employment or access to public services or accommodations within the meaning of section 102(b)(3) of the Congressional Accountability Act.

## EARMARK IDENTIFICATION

H.R. 2555 does not contain any congressional earmarks, limited tax benefits, or limited tariff benefits as defined in clause 9 of rule XXI.

## SECTION-BY-SECTION ANALYSIS OF THE LEGISLATION

*Title I: The National Catastrophe Risk Consortium**Sec. 101—Establishment; status; principal office; membership*

This Title establishes a National Catastrophe Risk Consortium that would consist of States that join on a voluntary basis.

*Sec. 102—Functions*

The Consortium will maintain an inventory of catastrophe risk obligations held by participating States and will issue financial instruments linked to catastrophe risk in the capital markets. Furthermore, it can coordinate reinsurance contracts with private parties. The Consortium will also act as a database of State catastrophe risk information. Finally, the Consortium will perform research and analysis that encourages standardization of the risk-linked securities market.

*Sec. 103—Powers*

The Consortium can contract with any individual or public or private entity necessary for carrying out its functions.

*Sec. 104—Non-profit entity; conflict of interest; audits*

The Consortium is a non-profit organization with no capital stock. To ensure continued integrity, the Consortium's financial statements shall be audited annually by independent certified public accountants. The Consortium is prohibited from engaging in any election related and lobbying activities.

*Sec. 105—Management*

The Consortium shall be managed by a Board of Directors composed of the Secretaries of Treasury, Homeland Security and Commerce and a member from each participating State. The Chair of this Board shall be the Secretary of the Treasury or the Secretary's designee.

*Sec. 106—Staff; experts and consultants*

The Chair may appoint staff and set their compensation.

*Sec. 107—Federal liability*

The Federal Government will bear no liabilities from the actions of the Consortium.

*Sec. 108—Authorization of appropriations*

The Consortium is authorized for \$20 million for each year 2010–2014.

*Title II: Catastrophe Obligation Guarantees**Sec. 201—Purpose*

The Secretary of the Treasury (the Secretary) will guarantee the debt of a State catastrophe insurance program to provide liquidity so that the State program can expedite payment of claims and recovery from a significant natural catastrophe.

*Sec. 202—Establishment of debt guarantee program*

The Secretary is authorized to guarantee holders of debt issued by eligible State programs against loss of principal or interest, or both. The total principal amount of debt obligations guaranteed by the Secretary will not exceed 3.5 billion for earthquake coverage or 17 billion for all other perils. A commitment to guarantee debt by the Secretary is good for three years and may be extended for one year on an annual basis.

The Secretary may issue the commitment to guarantee only if the eligible State program submits a plan detailing how the program plans to repay the debt. Further eligibility conditions for the commitment to guarantee include: (i) specifying the fees for debt guarantee coverage; (ii) stipulating that the maximum term of the debt may not exceed 30 years; (iii) requiring that the eligible State program cannot use Federal funds of any kind to repay the debt; and (iv) ensuring that the commitment is not extended to State programs that cover losses arising from floods to properties in a special flood hazard area.

To obtain a debt guarantee under this section, an eligible State program must show that insured losses arising from the event or events covered by the commitment are likely to exceed the program's available cash resources on the date of the event.

The aggregate principal amount of the debt guaranteed following an event or events may not exceed 80 percent of the qualifying assets of the eligible State program as stated in the State program's most recent financial statement prior to the event or events.

*Sec. 203—Effect of guarantee*

The issuance of any guarantee by the Secretary shall be conclusive evidence that the guarantee has been properly obtained.

*Sec. 204—Full faith and credit*

The full faith and credit of the United States is pledged to the payment of all guarantees issued under this title.

*Sec. 205—Fees for guarantees; amount; collection*

The Secretary shall charge and collect fees for each guarantee that are sufficient to cover applicable administrative costs and probable losses on the guaranteed obligations.

*Sec. 206—Payment of losses*

The Secretary will pay the duly appointed agent for the eligible State program the principal and interest on any debt guaranteed under this title when the State program cannot make such payments.

*Title III: Reinsurance coverage for eligible state programs**Sec. 301—Program authority*

The Secretary shall offer reinsurance coverage subject to the requirements of this Act for eligible State programs.

*Sec. 302—Contract principles*

Reinsurance coverage made available under this title shall: (i) be priced on an actuarially sound basis; (ii) minimize the administrative costs of the Federal Government; and (iii) provide coverage based solely on insured losses covered by the eligible State program purchasing the contract.

*Sec. 303—Terms of reinsurance contracts*

The Secretary is to set attachment points for reinsurance coverage provided under this act based on the coverage available through eligible State programs and the availability and accessibility of reinsurance in the private market. This section also provides the Secretary with the flexibility to set the aggregate potential liability based on market conditions. Reinsurance coverage under this title shall not exceed one year or such other term as the Secretary may determine.

The Federal government will pay 90 percent of insured losses covered in the contract to the eligible State program in excess of the amount of retained losses that the contract requires.

The Secretary shall price reinsurance coverage at such a level that annual premiums are sufficient to pay: (i) the reasonably anticipated cost of all claims (which may not be equal only to average annual costs); (ii) loss adjustment expenses; (iii) the administrative costs of providing reinsurance coverage; and (iv) any retrocessional coverage the Secretary considers prudent. The anticipated cost of all claims shall be comparable to amounts being included in the price for similar layers of coverage in the private sector.

*Sec. 304—Maximum Federal liability*

The authority of the Secretary to enter into contracts for reinsurance coverage is effective only to such extent or in such amounts as are or have been provided in appropriations for the aggregate potential liability for payment of claims under all contracts for reinsurance coverage under this title.

The aggregate potential liability for reinsurance coverage sold by the Secretary in any single year shall be determined based on review of the market for reinsurance coverage under this title.

*Sec. 305—Federal Natural Catastrophe Reinsurance Fund*

The Secretary shall establish within the Treasury a Federal Natural Catastrophe Reinsurance Fund, which can collect reinsurance premiums, pay claims, obtain retrocessional coverage and invest excess funds in US government debt.

*Title IV: Mitigation Grant Program*

*Sec. 401—Mitigation grant program*

The Secretary of Housing and Urban Development shall establish and carry out a grant program to develop, enhance, or maintain programs to prevent and mitigate losses from natural catastrophes.

A grant under this program shall be used to: (i) encourage awareness of risk factors and ways reduce them; (ii) assist in the determination of the location of risk; (iii) provide inspections of homes to identify ways to strengthen such homes; (iv) provide financial assistance to retrofit homes; or to (v) support disaster response readiness programs.

Pursuant to section 305(d), for purposes of the grant mandate, the Secretary of the Treasury shall disclose the annual net investment income available not later than 60 days after the end of the fiscal year and disperse appropriate funds not later than 90 days after the end of the fiscal year.

*Title V: General Provisions*

*Sec. 501—Eligible State programs*

To qualify as an eligible State program under this Act, a program must: (i) be established and authorized by State law as an insurance or reinsurance program that is designed to improve the private insurance markets; (ii) have a majority of public officials or persons on its governing body; (iii) include provisions designed to encourage and support programs that mitigate losses from natural catastrophes; and (iv) comply with applicable risk-based capital requirements.

For five-years after enactment, if a State does not have an eligible State Program, a State residual insurance market entity or State-sponsored provider of natural catastrophe insurance will be considered an eligible State program if these programs were in existence before enactment.

*Sec. 502—Study and conditional coverage of commercial residential lines of insurance*

Directs the Secretary to study the need for and impact of expanding this Act to apply to insured losses arising from all commercial insurance policies which provide coverage for properties that are composed predominantly of residential rental units.

*Sec. 503—Study of risk-based pricing and state program rates*

Directs the Government Accountability Office (GAO) to present a report to Congress within six months on risk-based pricing in current State insurance and reinsurance funds, and rates for State in-

surance and reinsurance funds that fail to cover the expected value of all future costs.

*Sec. 504—Definitions*

Defines various terms in the bill, including commitment to guarantee, insured loss and qualifying asset.

*Sec. 505—Regulations*

The Secretary shall issue such regulations as may be necessary to carry out this Act.



## DISSENTING VIEWS

H.R. 2555, the Homeowner Defense Act, is ill-advised and unwarranted legislation that proposes to create new Federal programs that would shift the financial risks of property owners in catastrophe-prone states to U.S. taxpayers. This fiscally reckless and irresponsible measure would expose all Federal taxpayers to massive new liabilities that could potentially total billions of dollars. The bill would also undermine private insurance and reinsurance markets by setting up the Federal government to sell reinsurance and provide new debt guarantees; create new moral hazards by undermining market-based incentives for mitigation and risk management; and put taxpayers on the hook for yet another Federal bailout in the event that a state catastrophe insurance program cannot meet its obligations.

According to an estimate by the Congressional Budget Office (CBO), H.R. 2555 would cost \$1.7 billion over five years. We believe this estimate may represent only the tip of the iceberg. CBO expects that “premiums charged for the federal reinsurance program would be inadequate to compensate the government for the cost of that coverage.” The CBO report also expresses the concern that “consumer and political pressures directed toward the proposed federal program would likely create a strong incentive for its managers to keep reinsurance premiums low . . .” In addition, referring to the proposed catastrophic obligation guarantee program, the CBO report warns that “if a large-scale natural disaster were to occur and if a state program were to default, spending would be much greater than the expected costs included in this estimate.”

A broad range of taxpayer rights and environmental organizations have expressed strong opposition to H.R. 2555. In recent subcommittee testimony, the non-partisan budget watchdog group, Taxpayers for Common Sense asserted that “H.R. 2555 is fundamentally flawed” and “would actually end up putting taxpayers at risk and subsidizing people to live in harm’s way. Taxpayers across the country would be forced to pay for a narrow bailout that primarily helps the well off. It doesn’t make sense.”

In addition, the Smarter Safer Coalition, which includes environmental groups, taxpayer organizations and insurance industry representatives, strongly opposes H.R. 2555 because it would cost taxpayers billions of dollars, discourage the insurance and reinsurance private market, and result in incentives to build in unsafe and environmentally fragile areas. According to the Coalition, H.R. 2555 “creates a federal bailout program principally designed to benefit hurricane-threatened Florida at the expense of taxpayers in all 50 states. The legislation supports a Florida system that is based on artificially low premiums. Such a system encourages risky development behavior. It is a cost the federal government and taxpayers cannot afford.”

Furthermore, according to recent testimony by the National Wildlife Federation, the environmental community is concerned that “H.R. 2555 would create incentives for other states to create Florida-like state CAT funds, sending a signal that states could begin to move away from more sound policies toward higher risks and subsidies such as Florida has.” The Federation witness also stated, “In the long run we believe the overall effect of the legislation would be to exacerbate natural hazard risks and costs to homeowners and ultimately to the U.S. taxpayers. As a result, the National Wildlife Federation opposes H.R. 2555 in its current form.”

Natural catastrophes can be financially devastating to many of our citizens, and securing adequate insurance coverage against property losses is an ongoing challenge for some homeowners, businesses and communities located in certain high-risk regions of the United States. When the private insurance and reinsurance markets are allowed to function and charge premium rates based on actuarially sound data that projects the risk of losses, there is typically ample competition and an abundant supply of insurance capacity. After major storms, rates may increase, in some cases substantially, and availability may decrease as insurers seek to manage their risk more conservatively. While these insurance rate and availability fluctuations may present challenges for many people in the affected regions, they are part of the cost of living in high-risk areas.

In particular, the State of Florida faces extraordinary challenges in maintaining stable private insurance markets to provide financial protection against hurricanes and the severe and widespread property damage they can cause. While Florida has taken tentative steps recently to permit insurance premium rates to begin increasing gradually over time, rates have been artificially restrained for many years and remain far short of being actuarially sound and commensurate with the projected risk. Government-imposed rate controls, while they can provide short-term rate relief in the form of subsidized insurance premiums, will over time undermine the goal of maintaining competitive private insurance and reinsurance markets. Rate controls and premium subsidies will also erode market-based incentives for prudent risk management and loss mitigation.

After Hurricane Andrew in 1992, Florida established the Hurricane Catastrophe Fund as a tax-exempt state trust fund to provide insurance companies with reimbursement for a portion of their catastrophic hurricane losses. More recently, in 2002, the Florida Citizens Property Insurance Corporation was created to serve as an insurer of last resort but has grown to become the state’s largest property insurer. Both of these state insurance programs are part of a system that seeks to maintain low insurance rates, and both programs continue to face large funding shortfalls in meeting their potential obligations to pay claims.

H.R. 2555 seeks to shift a large portion of the financial burden of natural catastrophe risk management from underfunded state insurance programs, like those in Florida, to the Federal government. Even within the State of Florida, there is an ongoing debate over the fairness of imposing assessments on all residents across

the state to cover the shortfalls caused by charging inadequate insurance rates for properties located in vulnerable coastal areas.

During the Committee's consideration of H.R. 2555, Representatives Capito and Garrett offered a Republican substitute that would establish an independent blue-ribbon commission to study regional catastrophe risk management challenges and explore global risk management opportunities. We believe an independent commission of experts is needed to evaluate the full range of alternatives to promote more effective loss mitigation strategies and encourage more stable private insurance and reinsurance markets in high-risk regions. The Capito-Garrett amendment would direct the Commission to report to Congress before the beginning of the 2011 hurricane season. This would enable Congress to consider and act upon the Commission's recommendations in a timely fashion.

Instead of creating new programs that will lead to Federal bailouts for underfunded state catastrophe insurance programs, we should be exploring market-based risk-management alternatives and developing more comprehensive strategies to help minimize the financial threats of natural disasters.

Now is the wrong time to increase the American taxpayer's exposure to new liabilities while we are trying to rein in spending and reduce the deficit. The best way to drive insurance premium rates down and to expand capacity is to promote more private sector competition in the marketplace rather than intervening with costly new government programs.

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