

Hurricane Season of 2005:

Impacts on US P/C Insurance Markets in 2006 & Beyond

**Casualty Actuaries of Greater New York
New York, NY**

December 7, 2005

Download at:



<http://www.disasterinformation.org/disaster2/facts/presentation/>

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Presentation Outline

- **2006 Hurricane Season: Preview to Disaster?**
- **Katrina, Rita & Wilma: Their Place in History**
- **Catastrophe Review:**
 - **Loss estimate overview**
 - **Hurricanes Katrina & Rita's place in history**
 - **Loss distribution (geographic & by line)**
 - **Impact on financial & underwriting performance**
 - **Influence of legal environment on Katrina claims**
- **Energy Market Overview**
- **P/C Financial Overview & Impacts**
- **Industry Claims-Paying Resources**
- **Underwriting Performance pre-Katrina**
- **Pricing Impacts**
- **Q & A**

The 2006 Hurricane Season:

Preview to Disaster?





Outlook for 2006 Hurricane Season

	Average*	2005**	2006F
Named Storms	9.6	26	17
Named Storm Days	49.1	115.5	85
Hurricanes	5.9	14	9
Hurricane Days	24.5	47.5	45
Intense Hurricanes	2.3	7	5
Intense Hurricane Days	2.3	7	5
Net Tropical Cyclone Activity	100%	263%	195%

*Average over the period 1950-2000.

**As of December 4, 2005.

Source: Dr. William Gray, Colorado State University, December 6, 2005.



Probability of Major Hurricane Landfall (CAT 3, 4, 5) in 2006

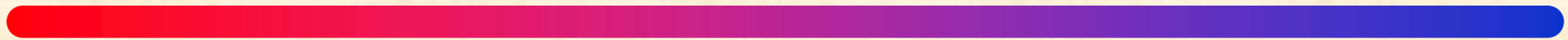
	Average*	2006F
Entire US Coast	52%	81%
US East Coast Including Florida Peninsula	31%	64%
Gulf Coast from FL Panhandle to Brownsville, TX	30%	47%
<i>Above-Average Major Hurricane Landfall in Caribbean</i>		

*Average over past century.

Source: Dr. William Gray, Colorado State University, December 6, 2005.

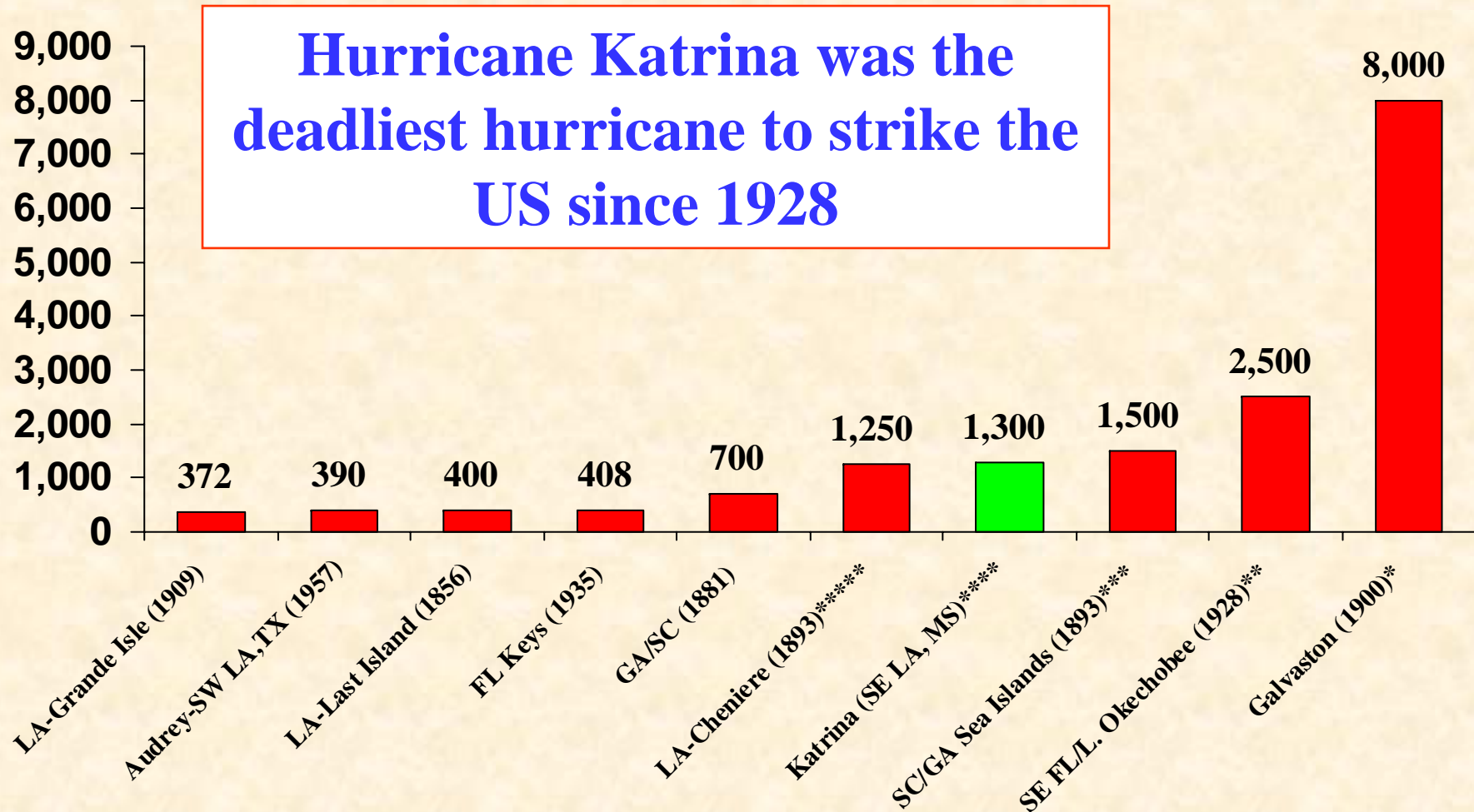
Hurricanes Katrina, Rita & Wilma:

Their Place in History





Top 10 Deadliest Hurricanes to Strike the US: 1851-2005



*Could be as high as 12,000

**Could be as high as 3,000

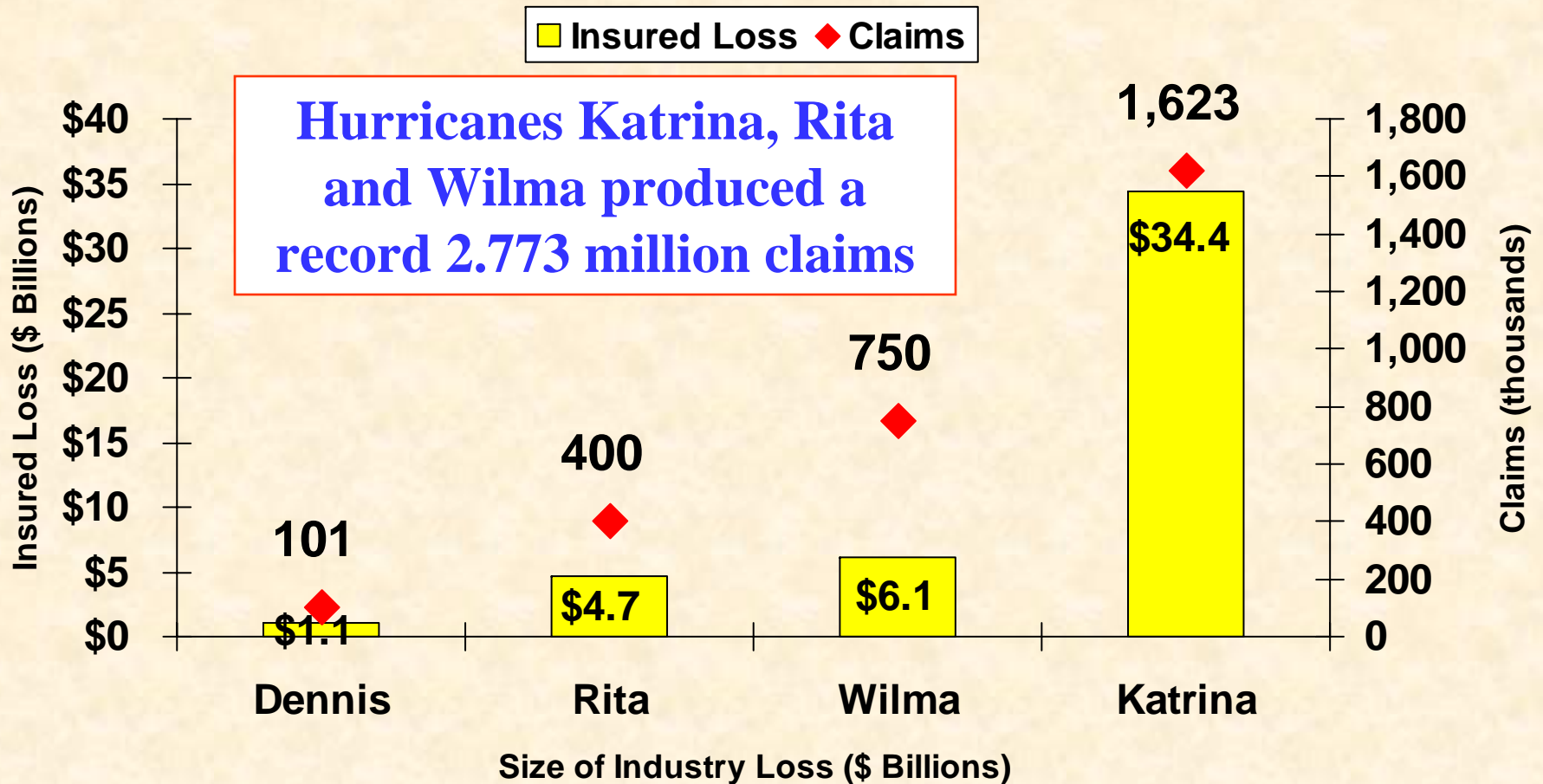
***Midpoint of 1,000 – 2,000 range

****Preliminary as of Oct. 14, 2005 *****Midpoint of 1,100-1,400 range.

Sources: NOAA; Insurance Information Institute.



Insured Loss & Claim Count for Major Storms of 2005*

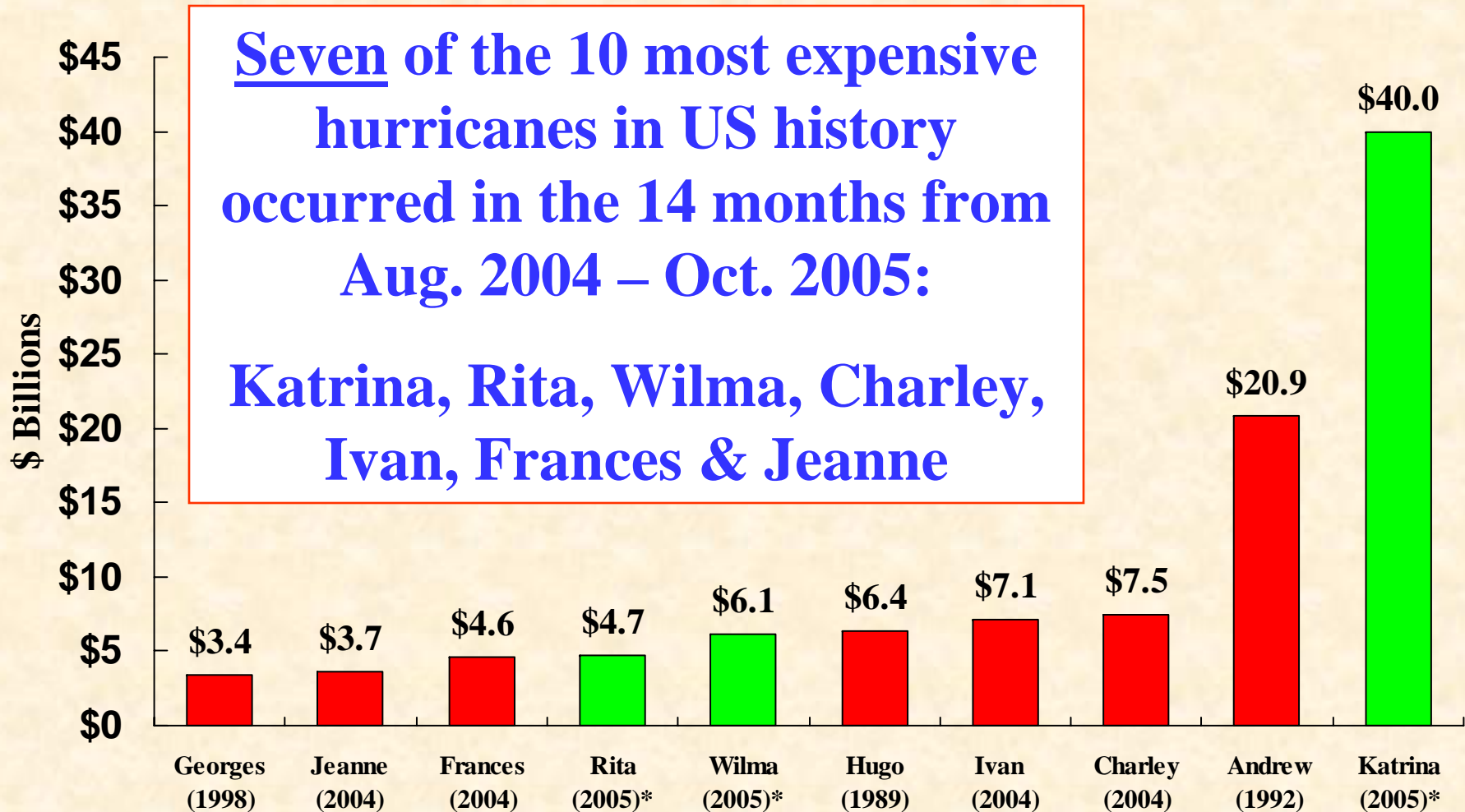


*Property and business interruption losses only. Excludes offshore energy & marine losses.

Source: ISO/PCS



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



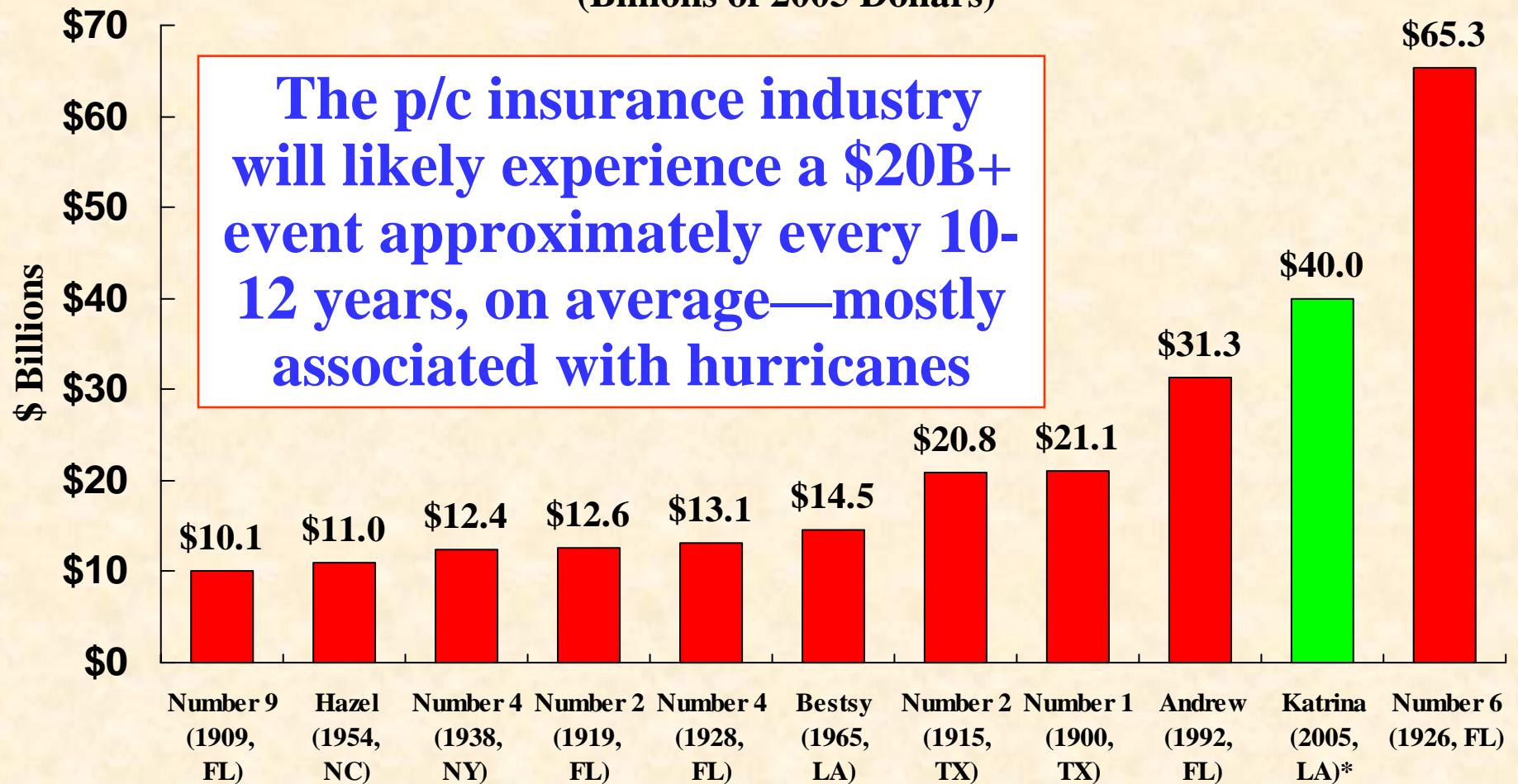
*Hurricanes Katrina, Rita and Wilma stated in 2005 dollars.

Sources: ISO/PCS; Insurance Information Institute.



Insured Losses from Top 10 Hurricanes Since 1990 & Katrina Adjusted for Inflation, Growth in Coastal Properties, Real Growth in Property Values & Increased Property Insurance Coverage

(Billions of 2005 Dollars)



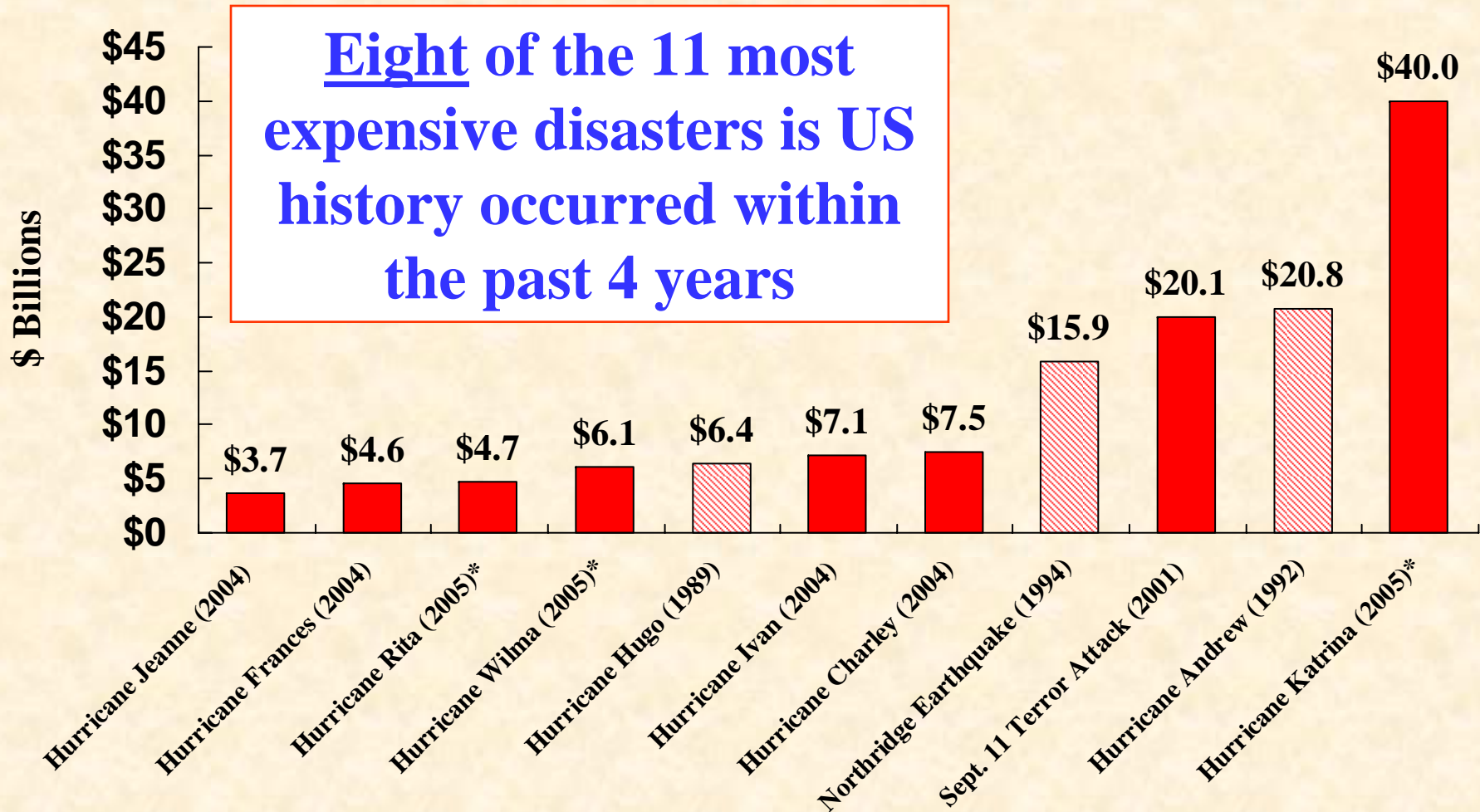
The p/c insurance industry will likely experience a \$20B+ event approximately every 10-12 years, on average—mostly associated with hurricanes

*ISO/PCS estimate as of October 10, 2005.

Source: *Hurricane Katrina: Analysis of the Impact on the Insurance Industry*, Tillinghast, October 2005; Insurance Info. Institute.



Top 11 Insured Property Losses in US (\$2004)



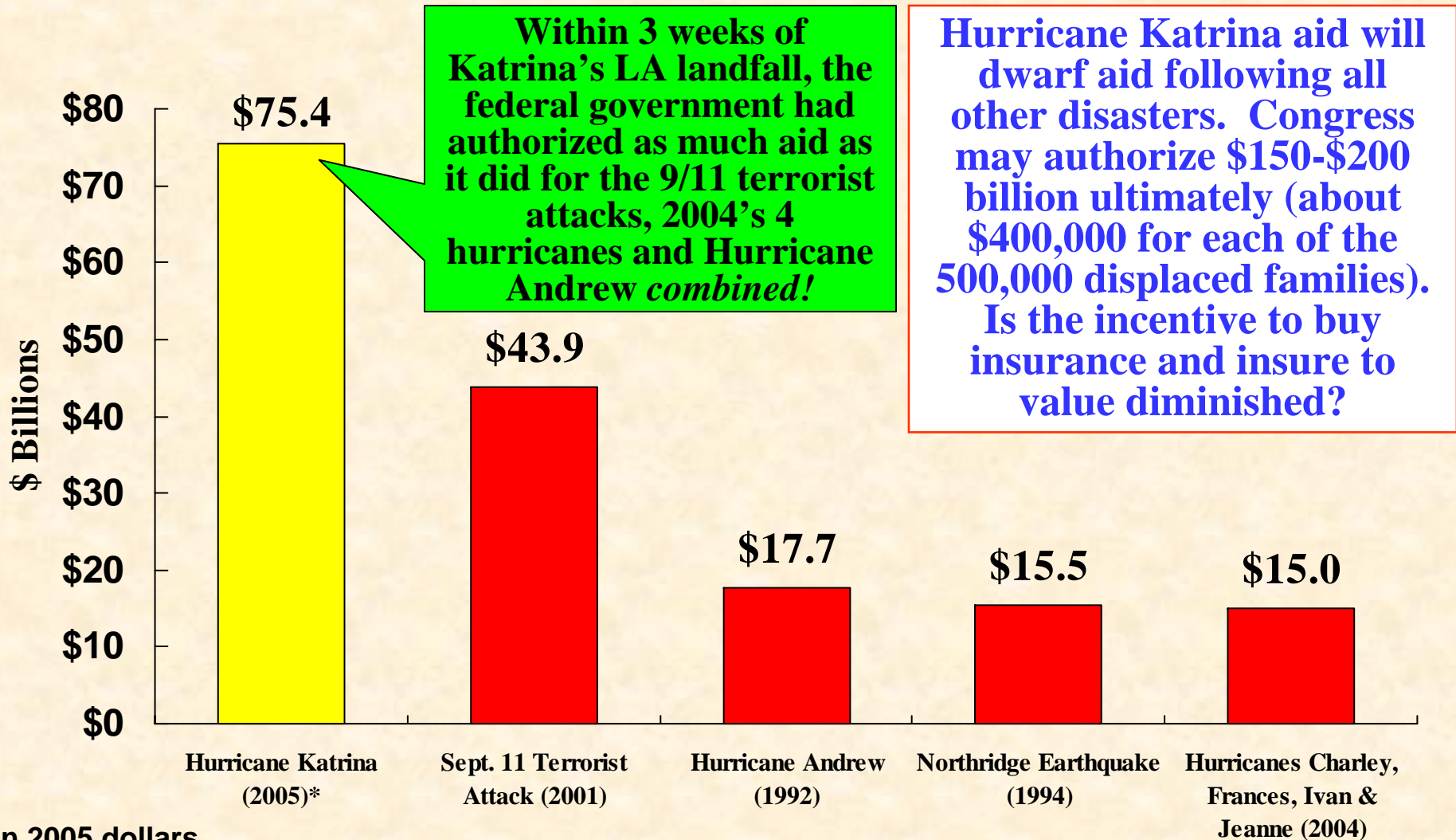
*Stated in 2005 dollars.

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

Sources: ISO/PCS; Insurance Information Institute.



Government Aid After Major Disasters (Billions)*



*In 2005 dollars.

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

CATASTROPHE LOSS MANAGEMENT

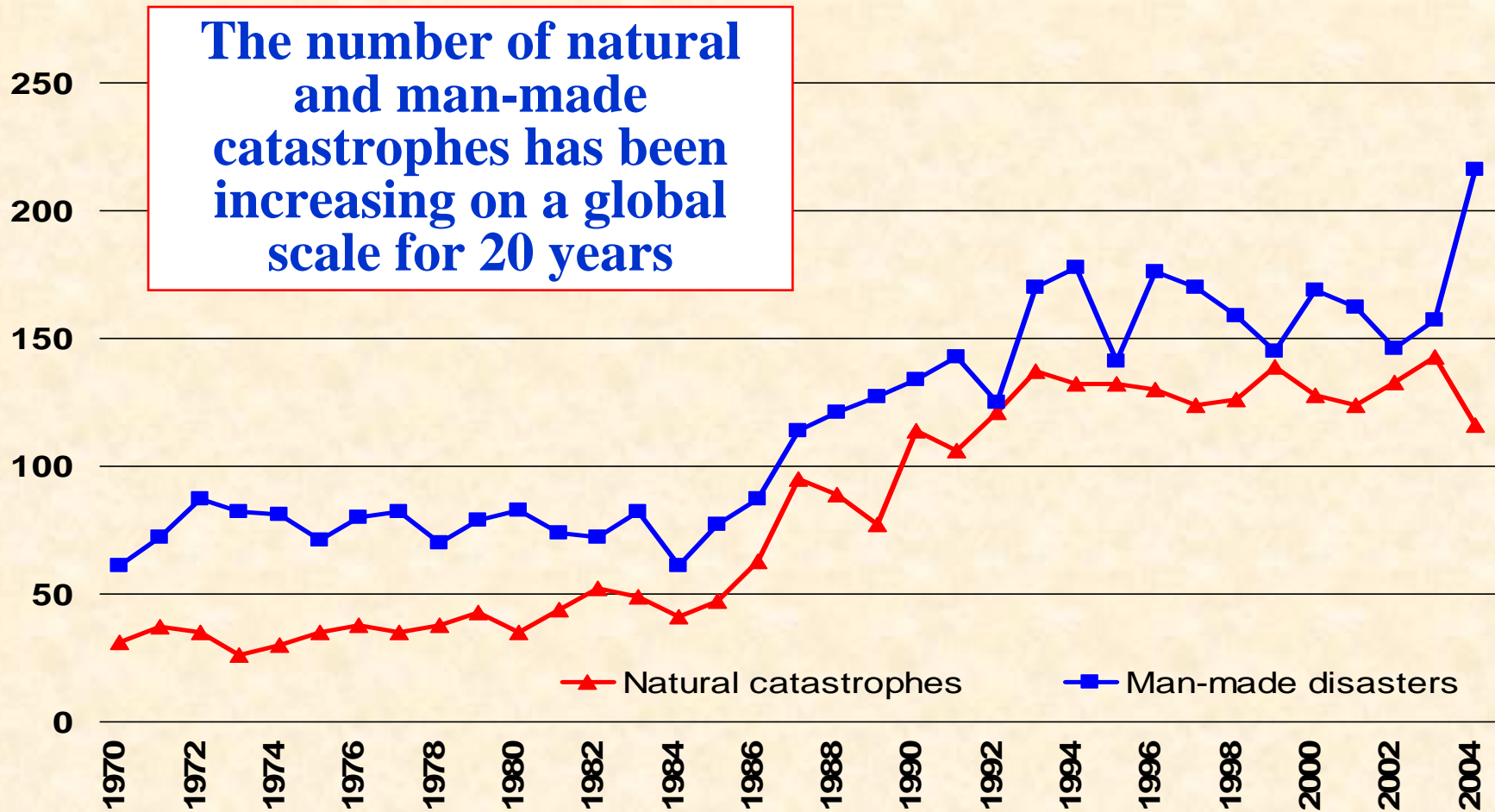
Focus on the Hurricane

iii

Season of 2005



Global Number of Catastrophic Events, 1970–2004





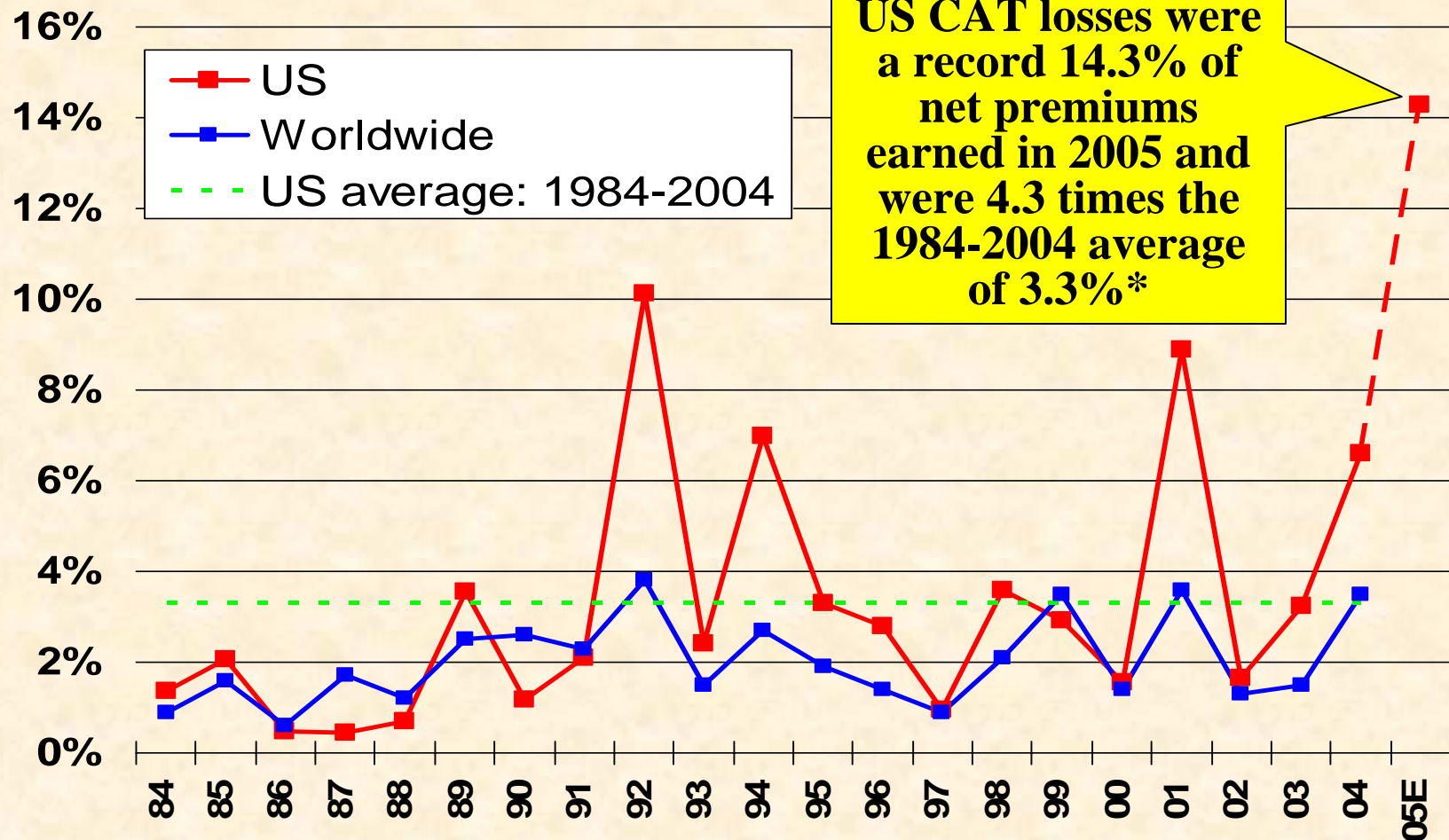
U.S. Insured Catastrophe Losses (\$ Billions)

2005 will be by far the worst year ever for insured catastrophe losses in the US at more than twice 2004's record.



*Includes \$50.3 billion per ISO/PCS plus \$5B offshore energy losses from Hurricanes Katrina & Rita.
Note: 2001 figure includes \$20.3B for 9/11 losses reported through 12/31/01. Includes only business and personal property claims, business interruption and auto claims. Non-prop/BI losses = \$12.2B.
Source: Property Claims Service/ISO; Insurance Information Institute

Insured Property Catastrophe Losses as % Net Premiums Earned, 1983–2005E

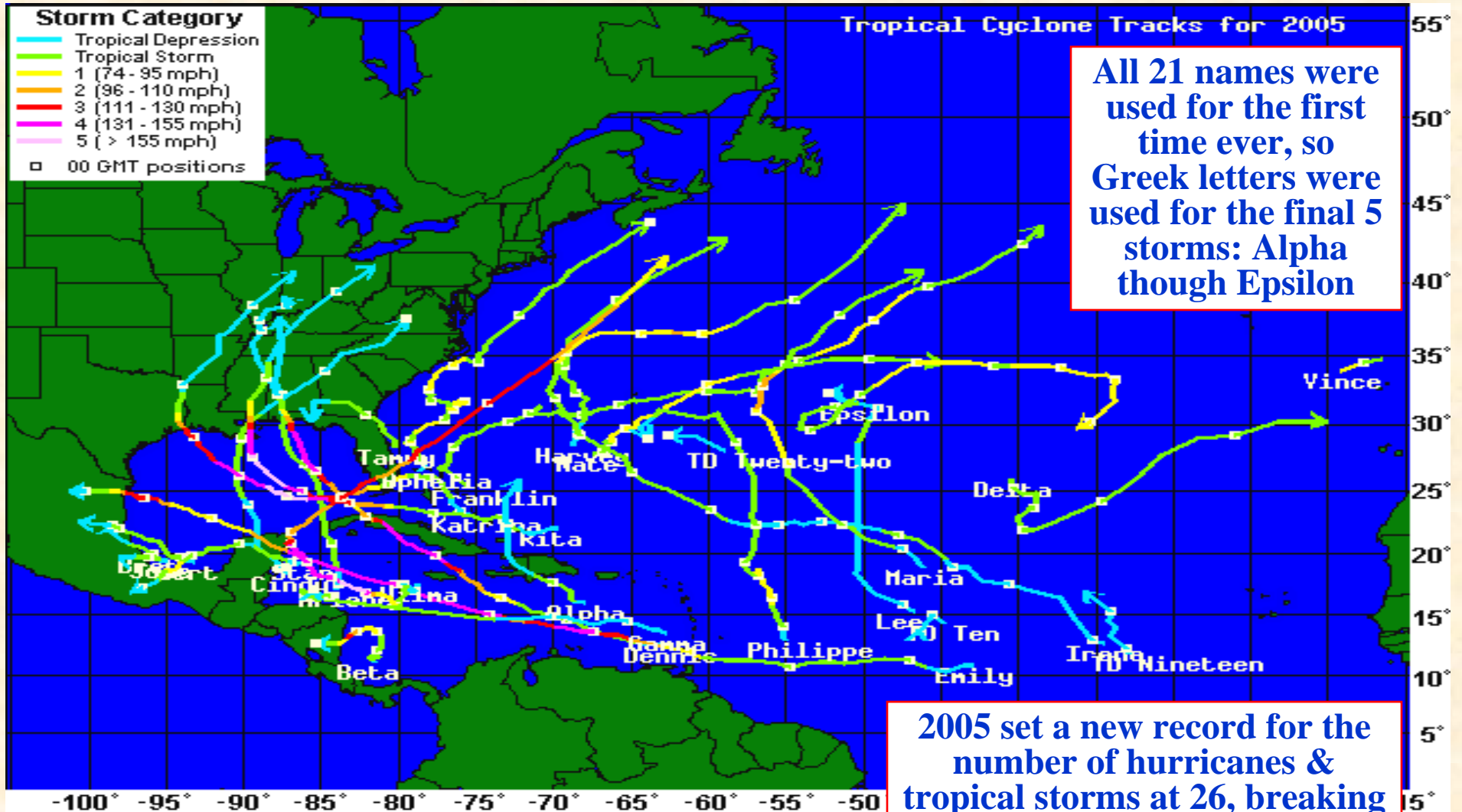


*Insurance Information Institute estimate of 14.3% for 2005 based estimated 2005 DPE of \$418.8B and estimated insured CAT losses of \$60B.

Sources: ISO, A.M. Best, Swiss Re Economic Research & Consulting; Insurance Information Institute.



2005 Has Been a Busy, Destructive, Deadly & Expensive Hurricane Season

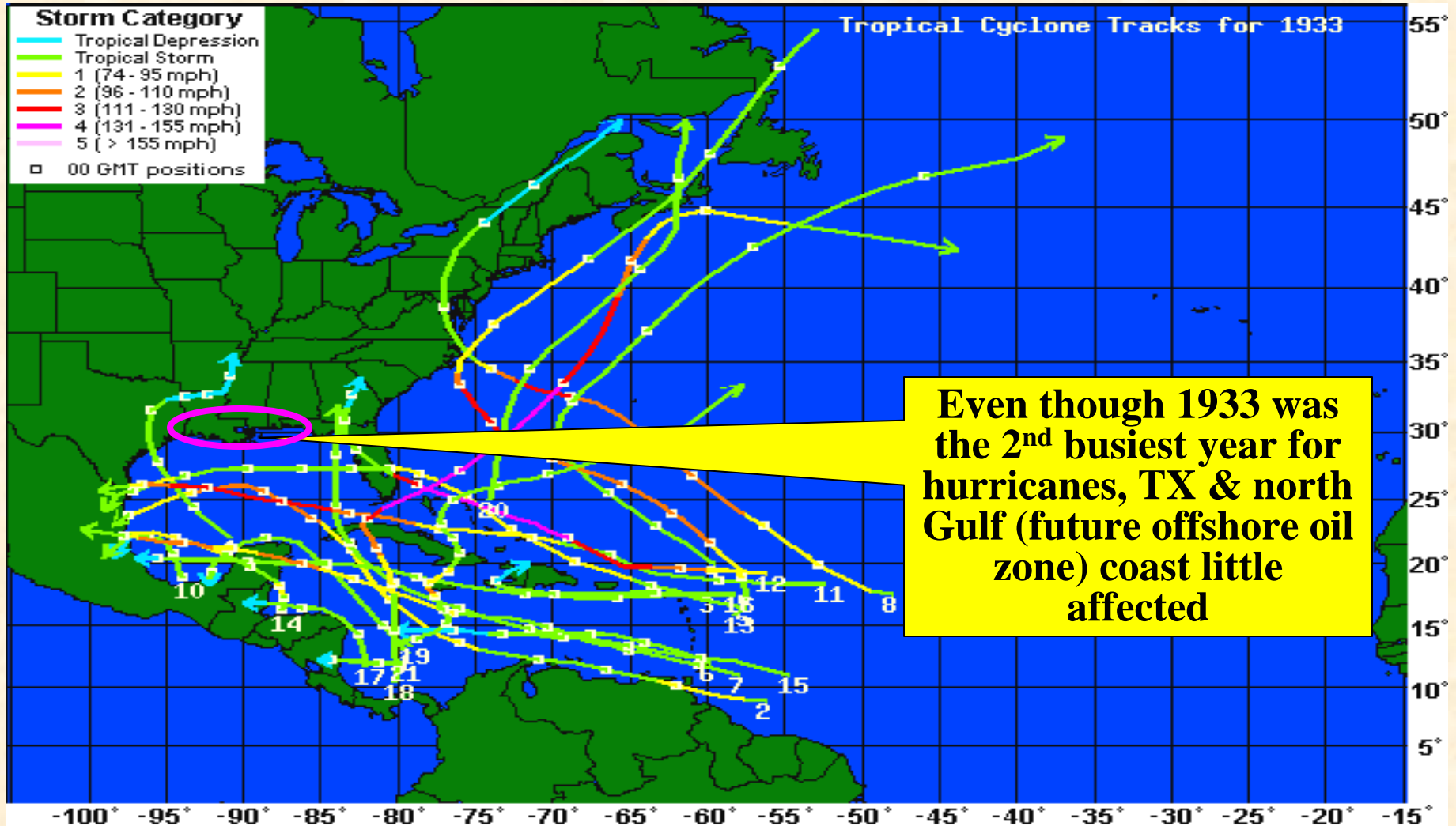


Source: WeatherUnderground.com, December 7, 2005.



Tropical Cyclone Activity in 1933

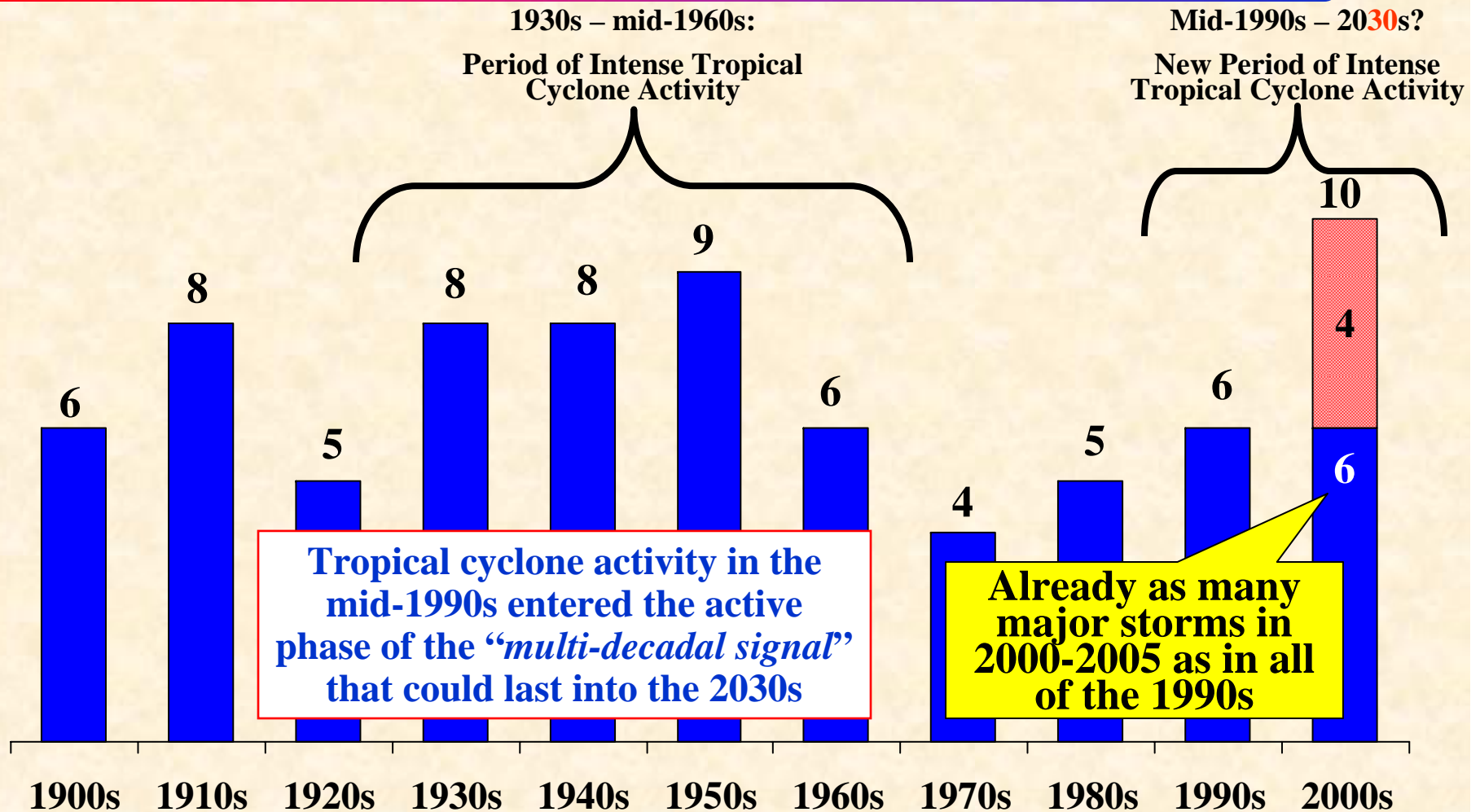
Held the Record Before 2005



Even though 1933 was the 2nd busiest year for hurricanes, TX & north Gulf (future offshore oil zone) coast little affected



Number of Major (Category 3, 4, 5) Hurricanes Striking the US by Decade



*Figure for 2000s is extrapolated based on data for 2000-2005 (6 major storms: Charley, Ivan, Jeanne (2004) & Katrina, Rita, Wilma (2005)).

Source: Tillinghast from National Hurricane Center: <http://www.nhc.noaa.gov/pastint.shtm>.

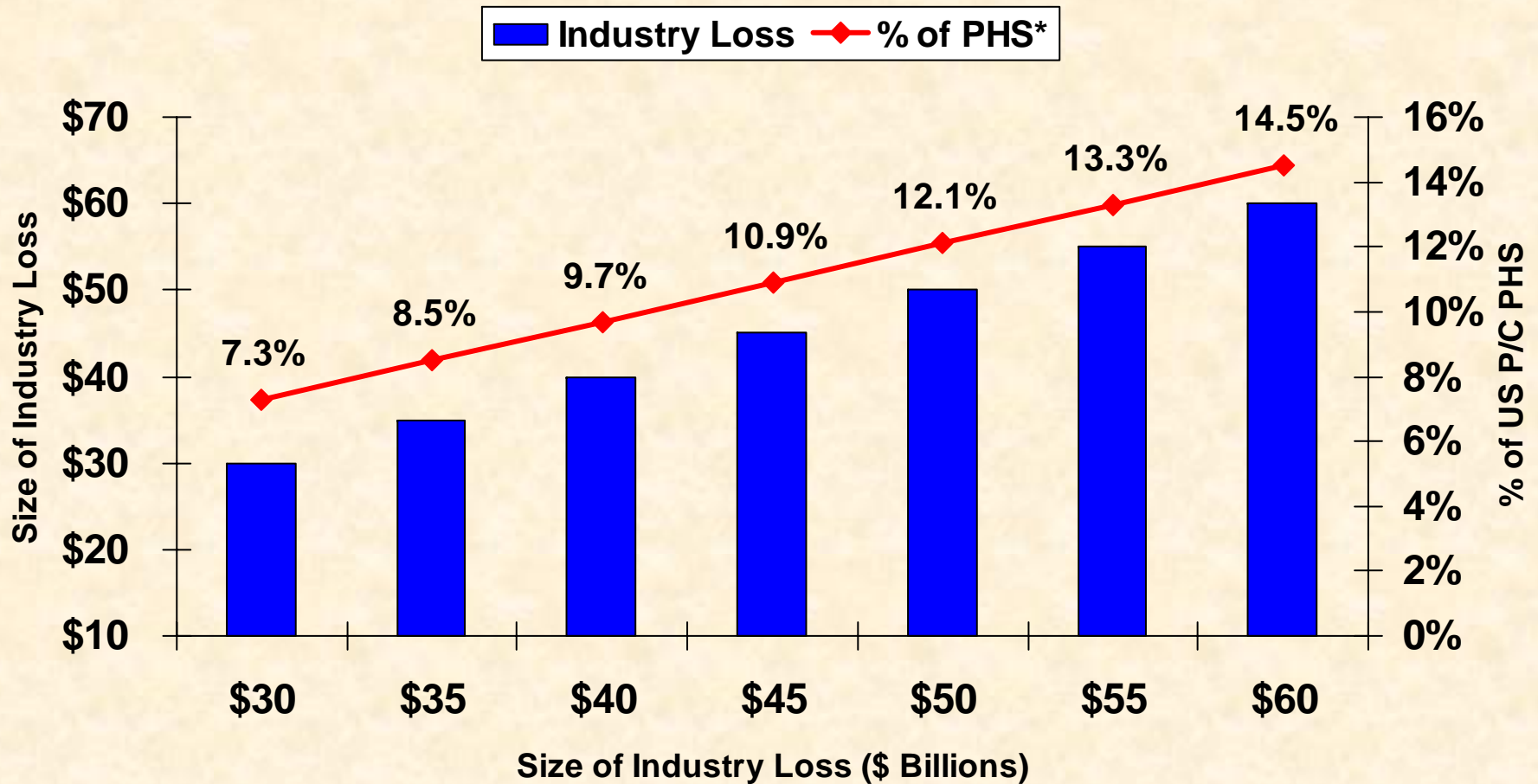


Breakdown of Tillinghast \$40-\$55 Billion Katrina Loss Estimate

Type of Loss	Low	High
Personal Property Lines		
Residential Property	\$14.0	\$17.0
Personal Auto	\$1.0	\$2.0
Personal Watercraft	\$0.2	\$0.3
Total	\$15.2	\$19.3
Commercial Property Lines		
Commercial Property (excl. Off-Shore)	\$13.5	\$16.0
Business Interruption (excl. marine & energy)	\$6.0	\$9.0
Commercial Auto	\$0.2	\$0.3
Sub-Total Personal & Commercial	\$19.7	\$25.3
Marine & Energy	\$4.0	\$6.0
Liability	\$1.0	\$3.0
Other	\$0.0	\$1.0
Total All Lines	\$39.9	\$54.6



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

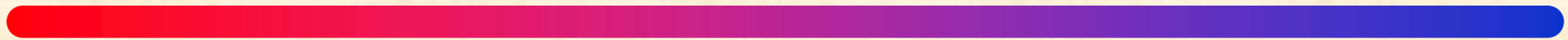


*Policyholder surplus as of 6/30/05 of \$412.5 billion (ISO).

Source: Insurance Information Institute.

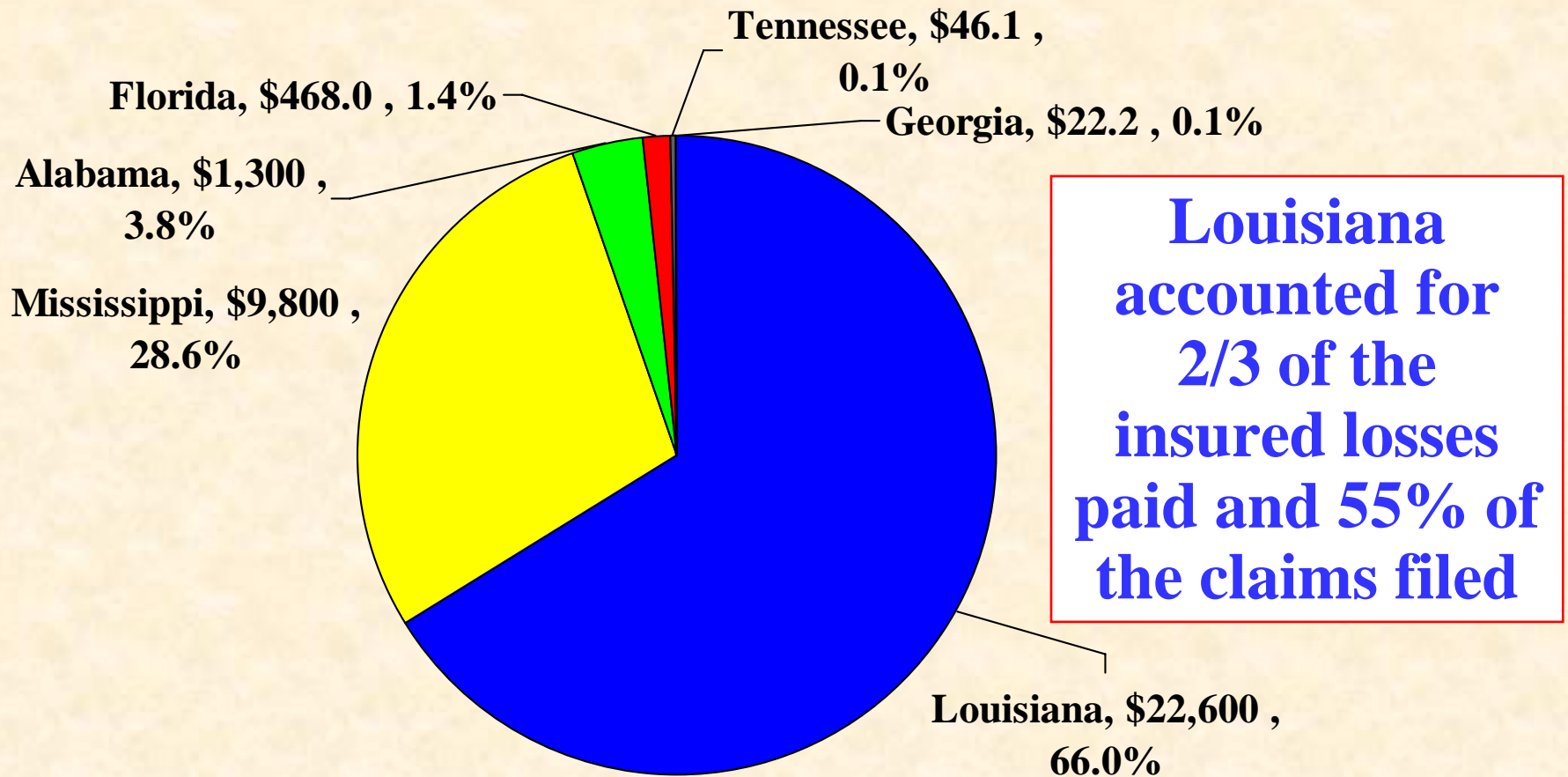
Hurricanes Katrina, Rita & Wilma:

Loss Distributions





*Hurricane Katrina Insured Loss Distribution by State (\$ Millions)**

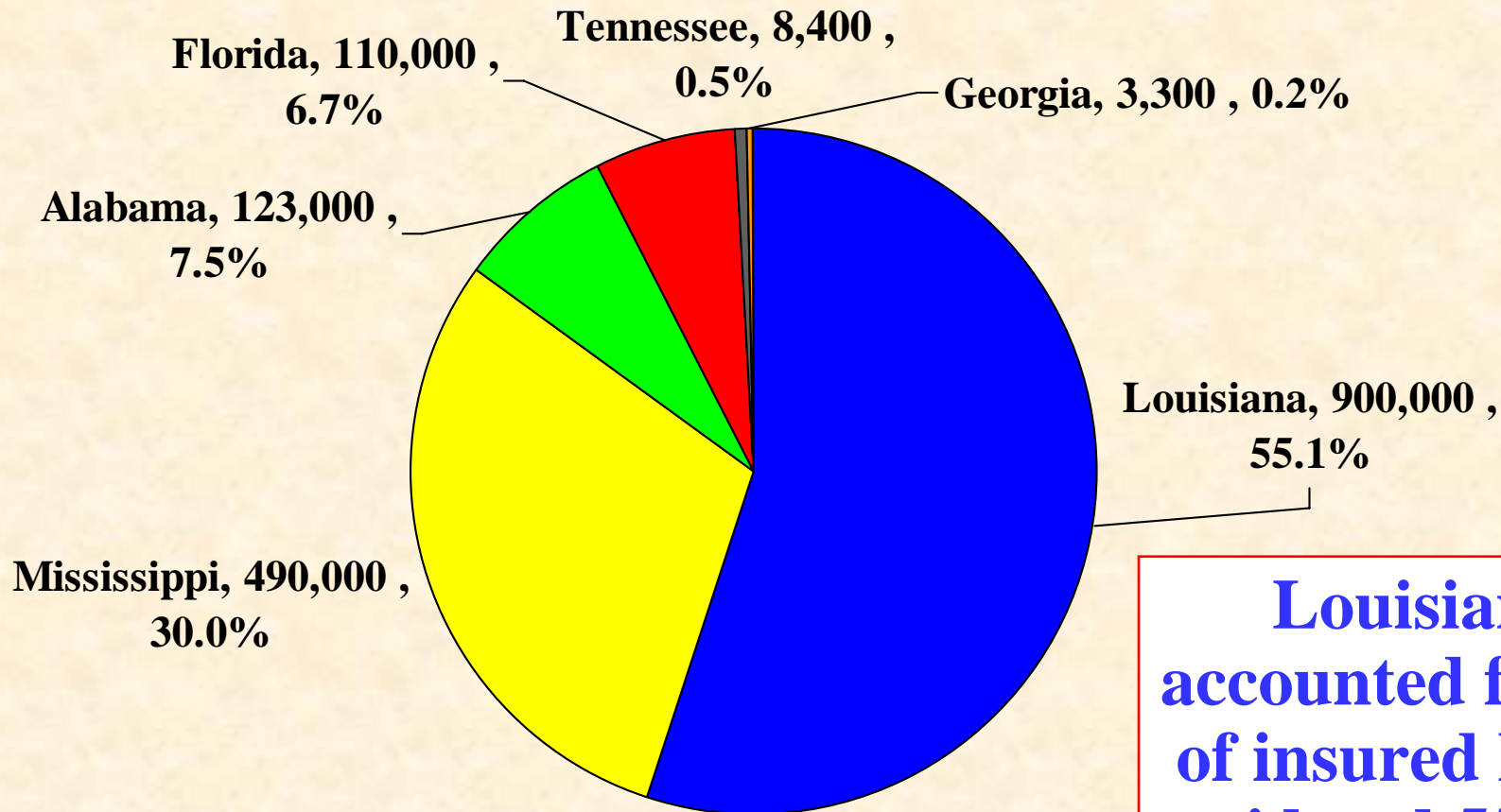


*As of October 4, 2005

Source: PCS division of ISO.



*Hurricane Katrina Claim Count Distribution by State**



**Louisiana
accounted for 2/3
of insured losses
paid and 55% of
claims filed**

*As of October 4, 2005

Source: PCS division of ISO.



Distribution of Katrina Losses by Market (\$Billions)

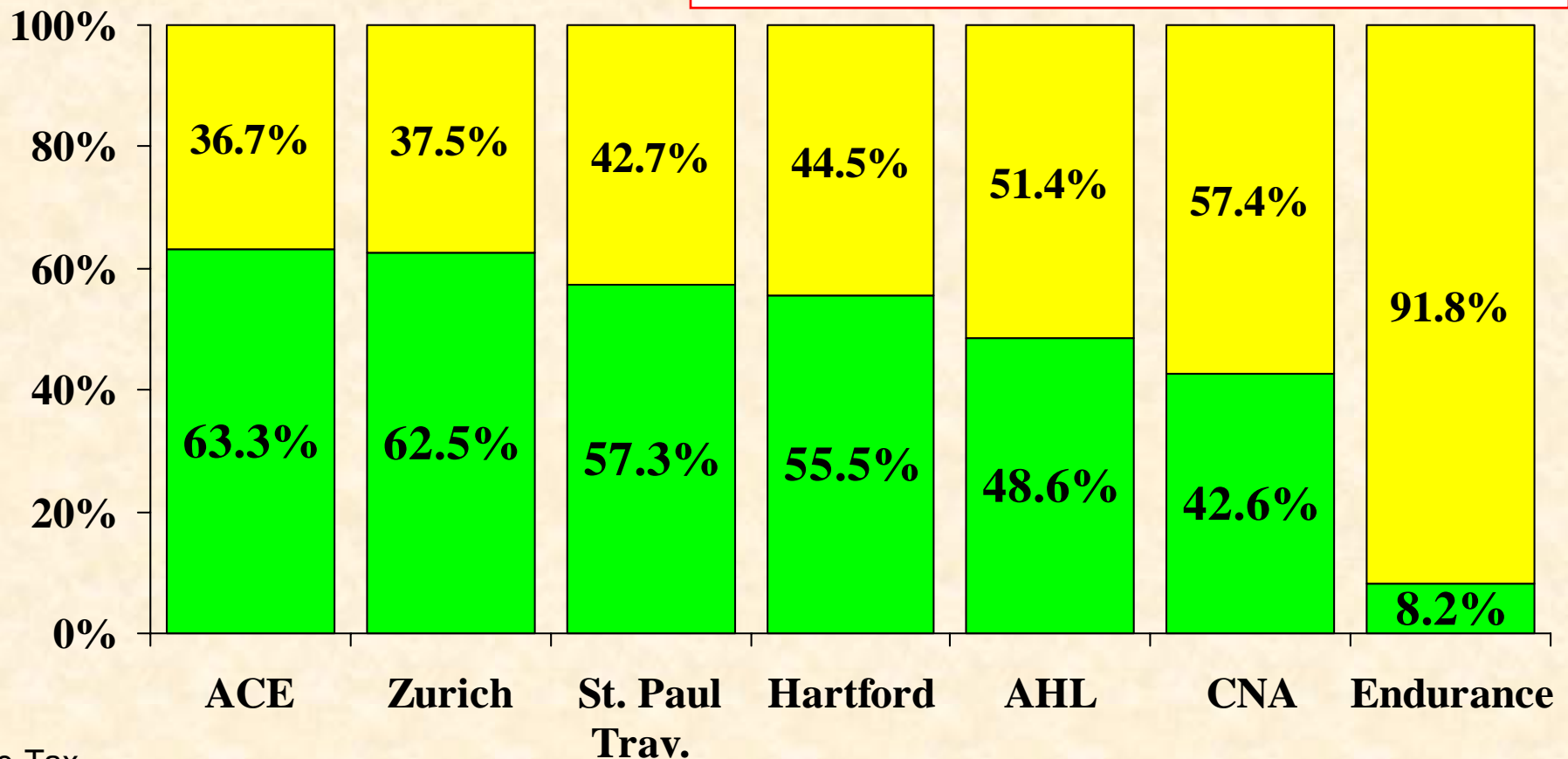
Market	Percentage	Amount
Insurers	47% - 53%	\$18.8 - \$28.9
Reinsurers	52% - 44%	\$20.7 - \$24.0
Capital Markets	1% - 3%	\$0.4 - \$1.6
TOTAL	100%	\$39.9 - \$54.6

Source: *Hurricane Katrina: Analysis of the Impact on the Insurance Industry*, Tillinghast, October 2005.

Percentage of Katrina Losses Ceded to Reinsurers for Select Insurers*

■ Ceded to Reinsurers ■ Net Loss

Share of loss ceded to reinsurers varies significantly, but underscores great importance of spread of risk

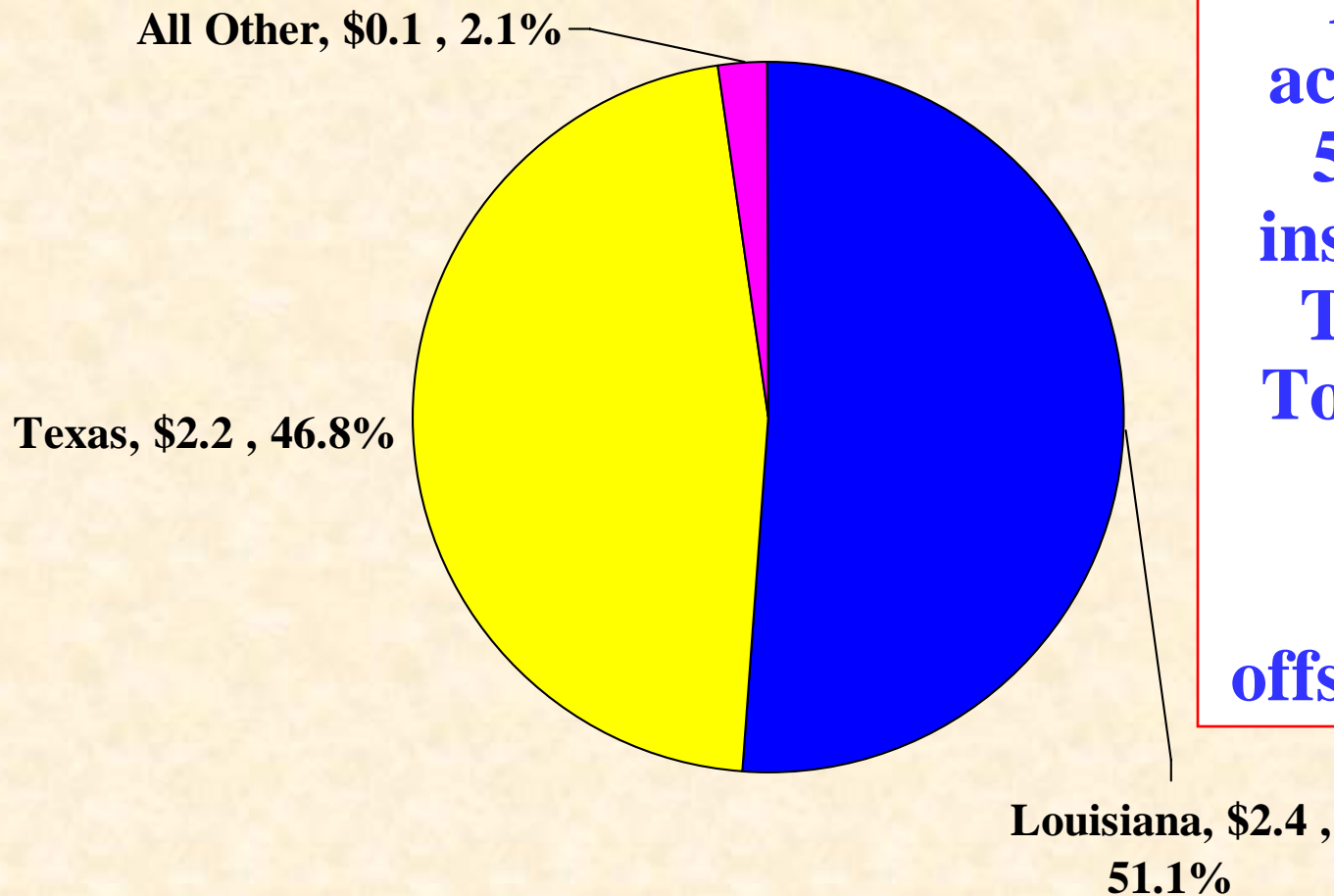


*Pre-Tax.

Source: Morgan Stanley from Company Reports as of October 13, 2005



*Hurricane Rita Insured Loss Distribution by State (\$ Billions)**



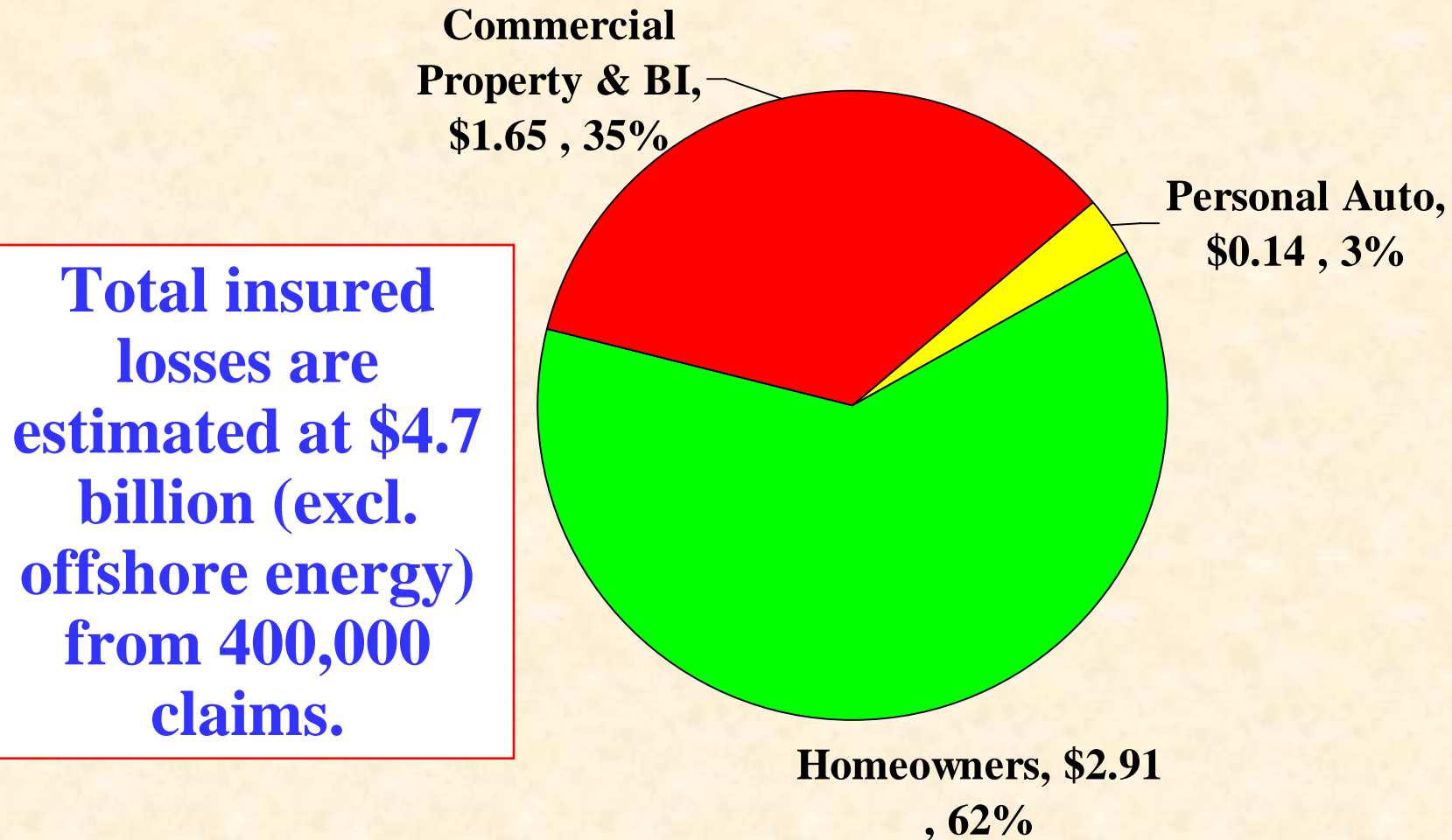
**Louisiana
accounted for
51% of the
insured losses,
Texas 47%.
Total claims =
400,000.**

**Excludes
offshore energy.**

*As of November 1, 2005
Source: PCS division of ISO.



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



Total insured losses are estimated at \$4.7 billion (excl. offshore energy) from 400,000 claims.

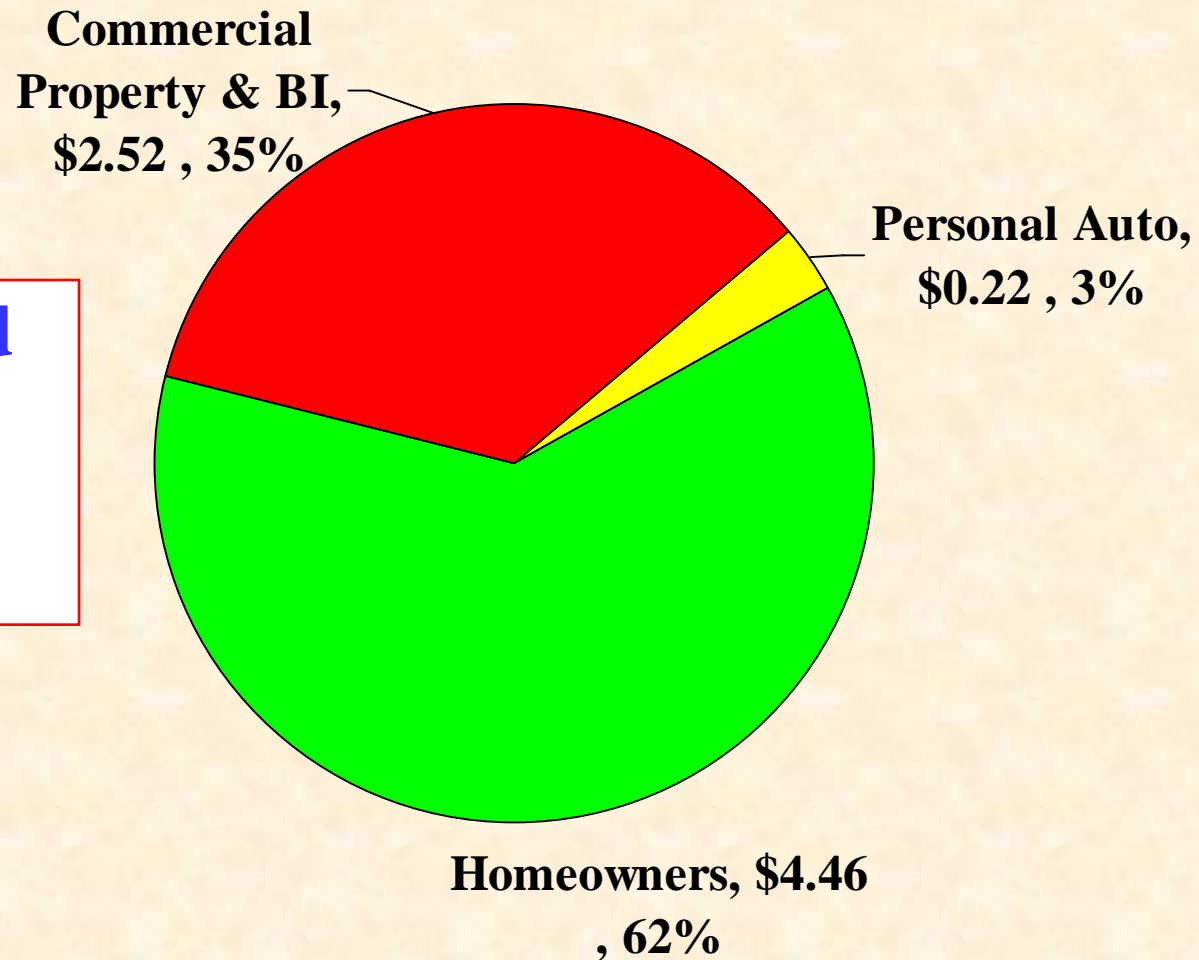
*Ill estimated breakdown based on PCS aggregate insured loss figure as of Nov. 1, 2005.
Source: Insurance Information Institute



Hurricane Wilma Loss

*Distribution by Line (\$ Billions)**

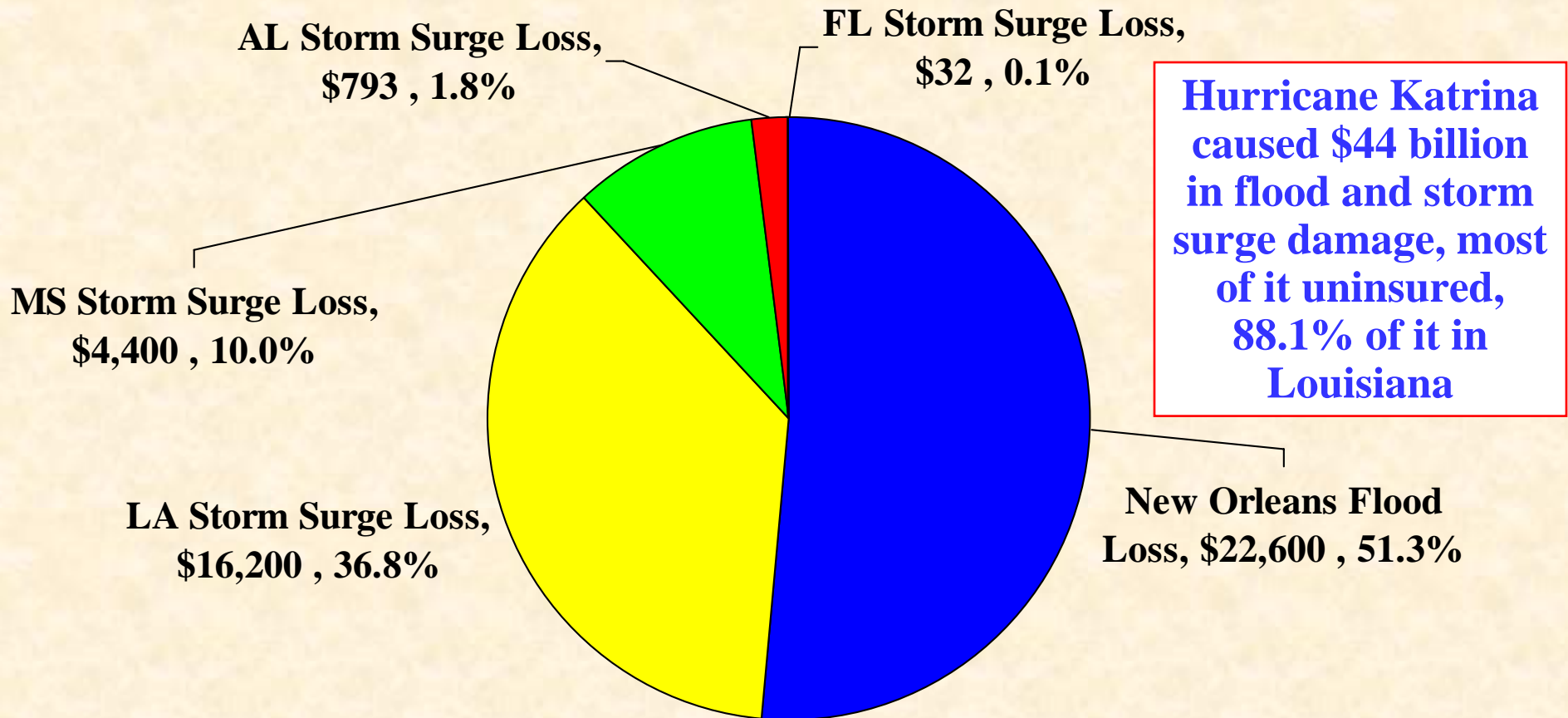
Total insured losses are estimated at \$7.2 billion



*Ill estimates as of November 1, 2005
Source: Insurance Information Institute



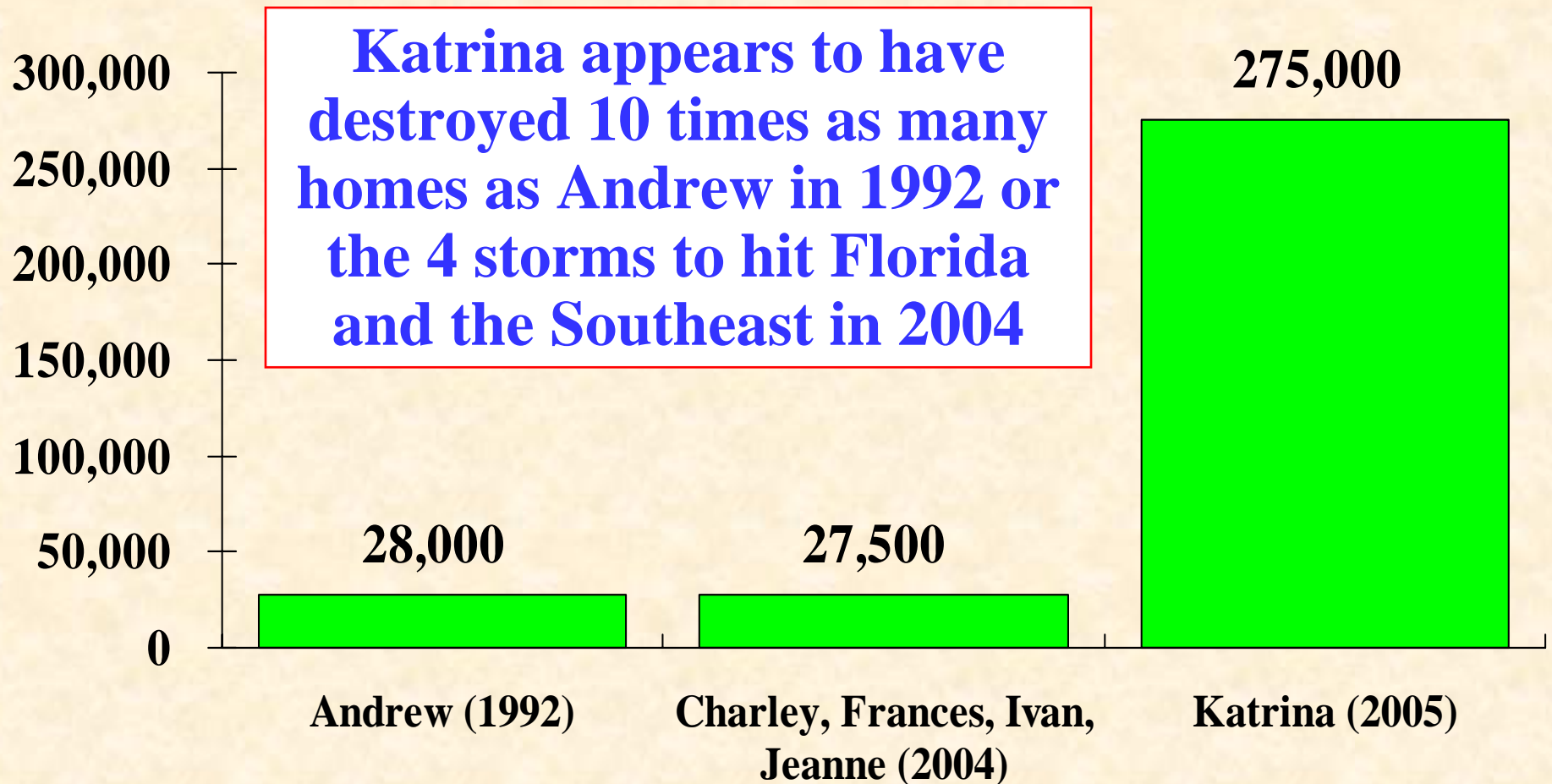
Property Damage from Hurricane Katrina Flood & Storm Surge (\$ Millions)*



*Value of property damage by flood and storm surge *whether or not insured*.
Source: AIR Worldwide, September 29, 2005.



*Number of Homes Destroyed by Major Hurricanes**

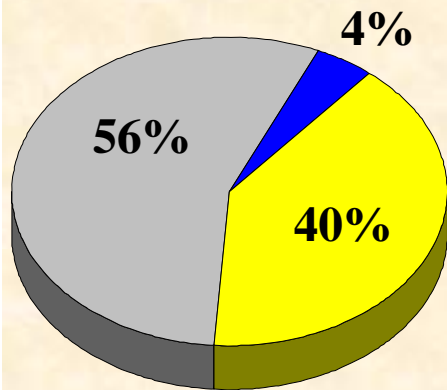


*Destruction is defined as a structure made uninhabitable or damaged beyond economic repair.
Source: National Association of Home Builders, National Red Cross (as of 9/15/05).

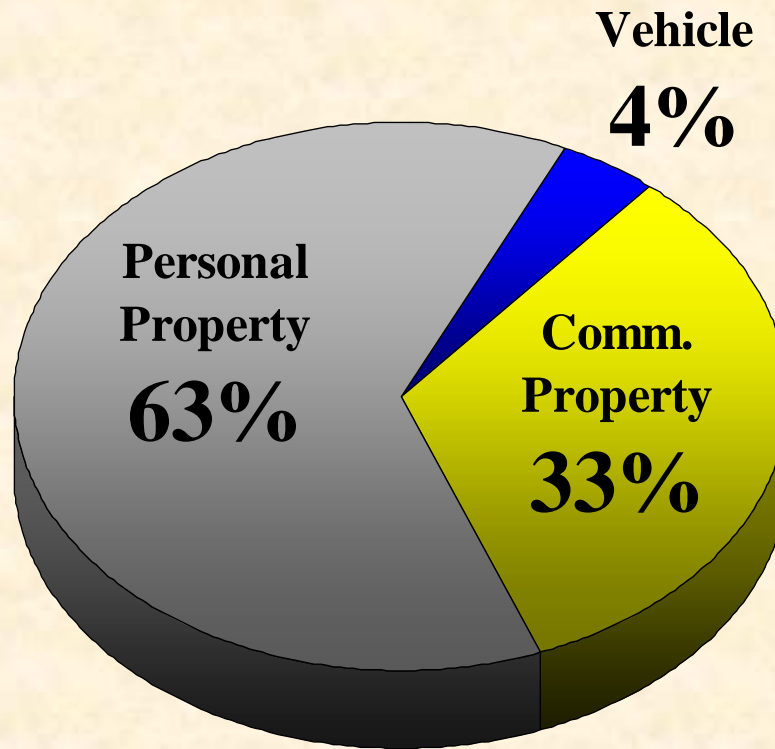


Personal Property Losses Accounted for Largest Share Damage from 2004 Hurricanes*

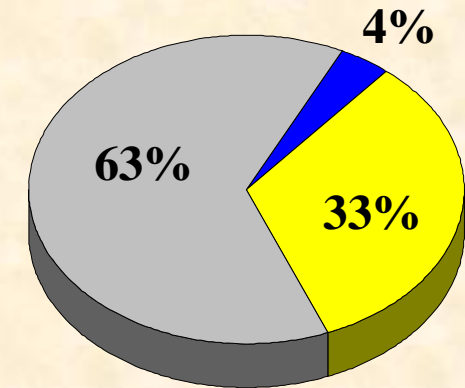
Charley



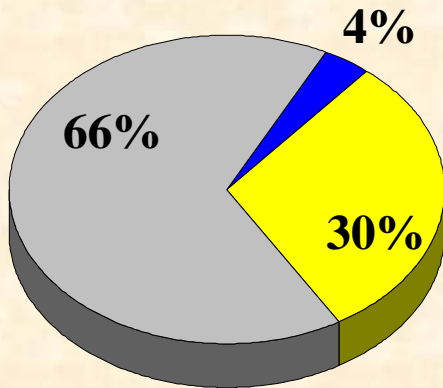
TOTAL



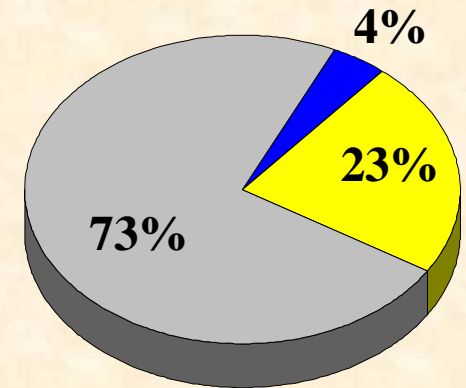
Ivan



Frances



Jeanne



Source: ISO/PCS; Insurance Information Institute.

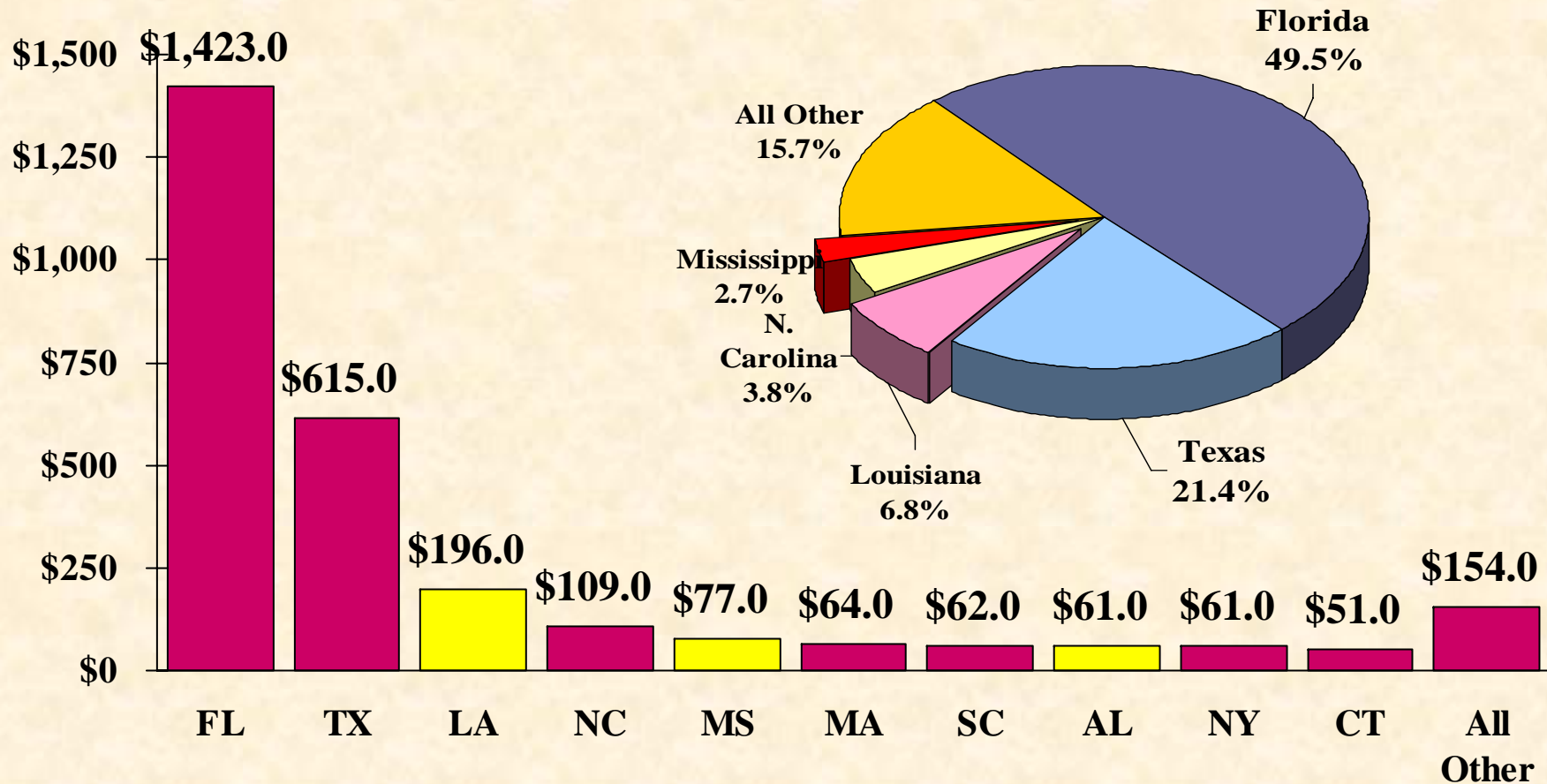
*Breakdowns based on FL losses, which accounted for 85% of losses for all affected states.



Average Annual Tropical Cyclone Insured Losses*

(Top 10 States, \$ Millions)

Distribution of Annual Losses

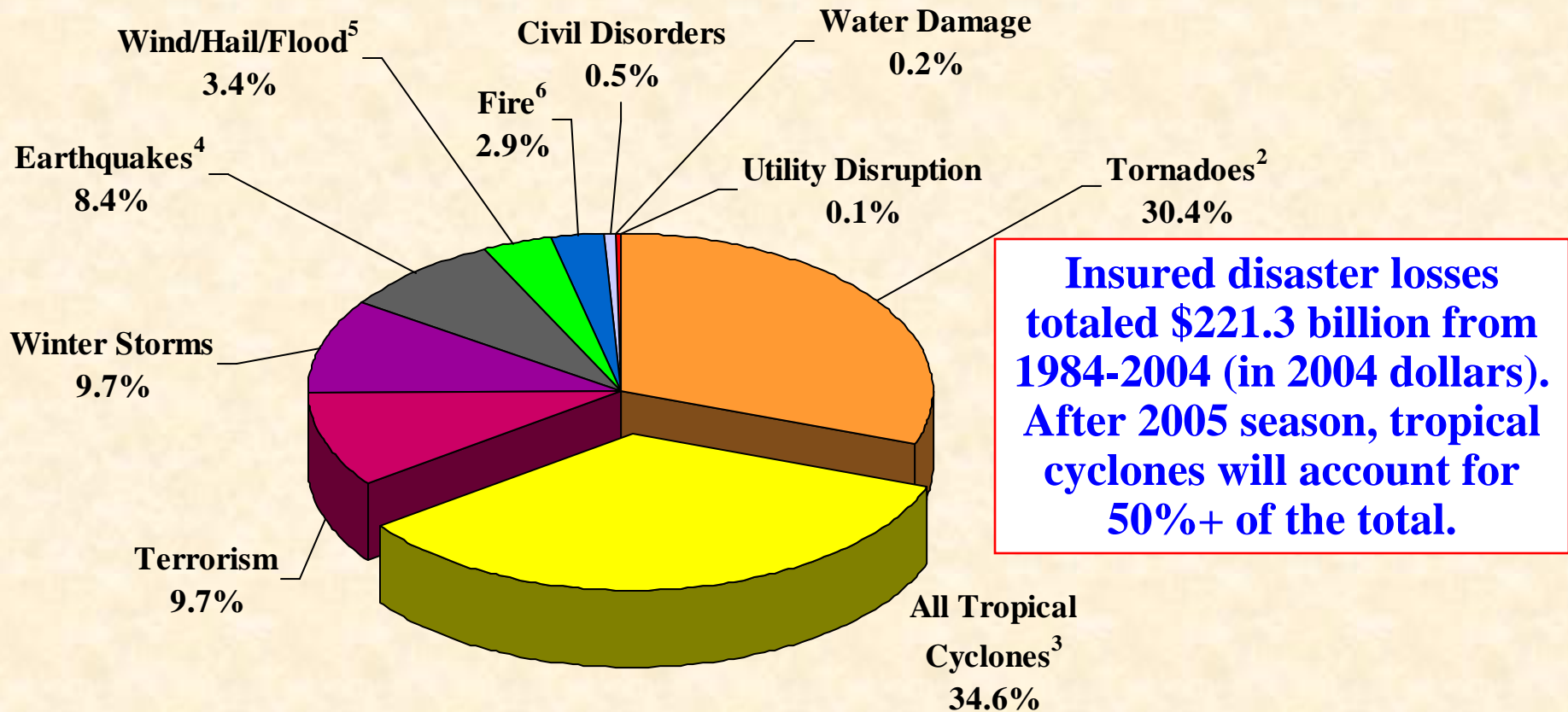


*Normalized losses adjusted for inflation, housing density, wealth and wind insurance coverage, based on historical data for 100-year period 1900-1999.

Source: Tillinghast-Towers Perrin



Inflation-Adjusted U.S. Insured Catastrophe Losses By Cause of Loss, 1985-2004¹



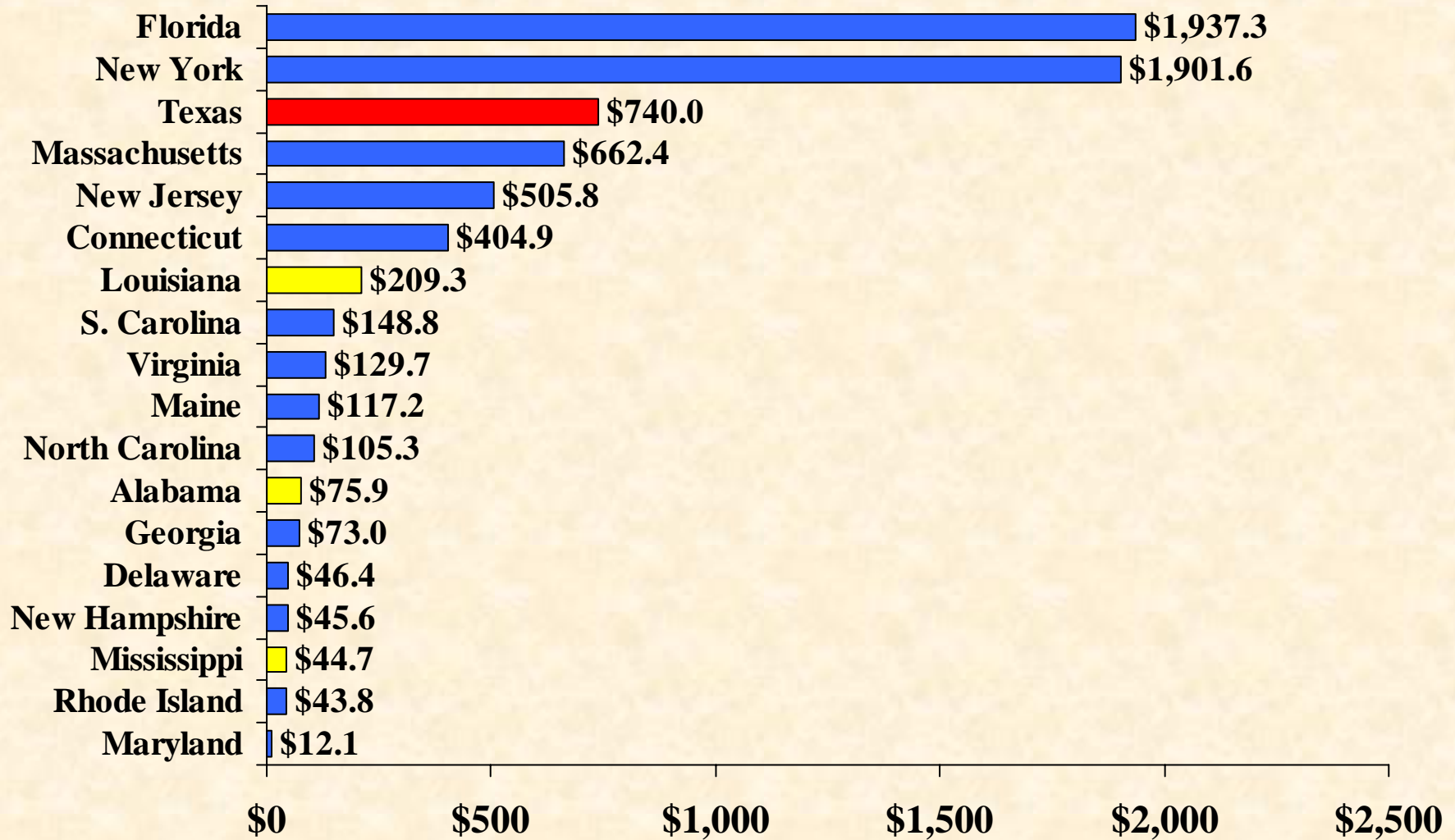
¹ Catastrophes are all events causing direct insured losses to property of \$25 million or more in 2004 dollars. Catastrophe threshold changed from \$5 million to \$25 million beginning in 1997. Adjusted for inflation by the III.

² Excludes snow. ³ Includes hurricanes and tropical storms. ⁴ Includes other geologic events such as volcanic eruptions and other earth movement. ⁵ Does not include flood damage covered by the federally administered National Flood Insurance Program. ⁶ Includes wildland fires.

Source: Insurance Information Institute estimates based on ISO data.



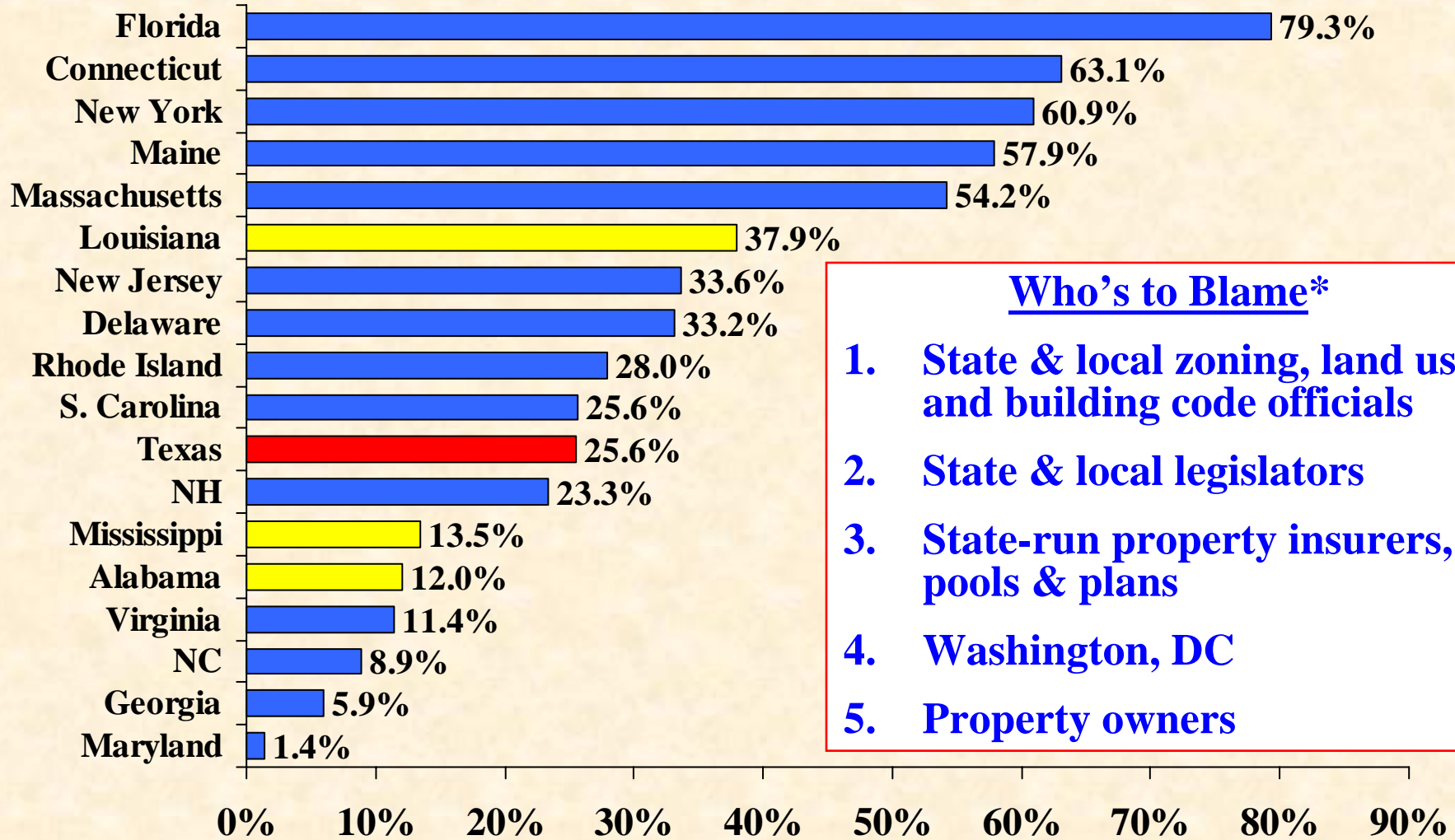
Total Value of Insured Coastal Exposure (2004, \$ Billions)



Source: AIR Worldwide



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



Who's to Blame*

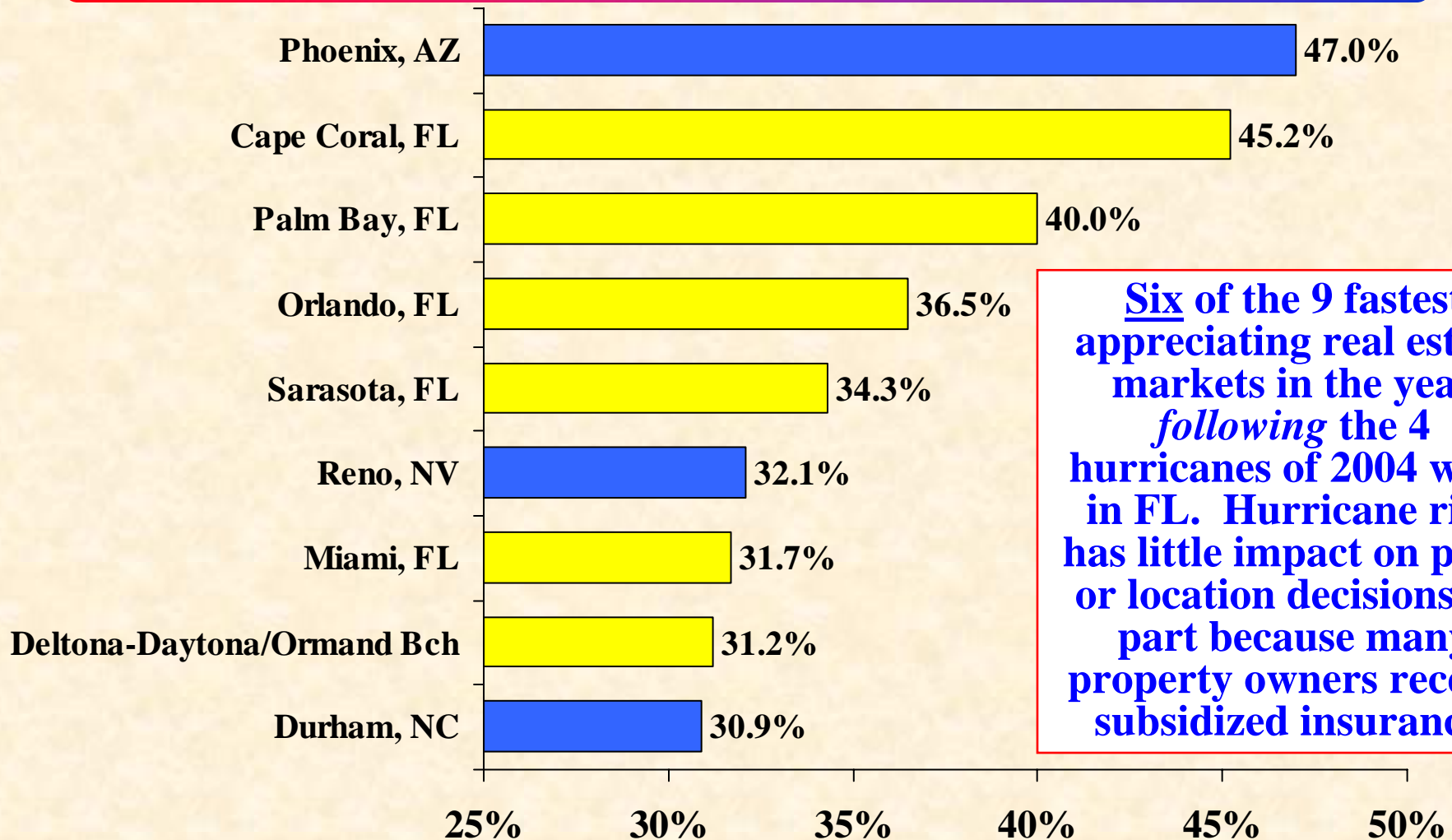
1. State & local zoning, land use and building code officials
2. State & local legislators
3. State-run property insurers, pools & plans
4. Washington, DC
5. Property owners

*Ill list

Source: AIR Worldwide



Metro Areas w/ Biggest Increase in Median Home Price Over Past Year (through Sept. 2005)



Six of the 9 fastest appreciating real estate markets in the year following the 4 hurricanes of 2004 were in FL. Hurricane risk has little impact on price or location decisions, in part because many property owners receive subsidized insurance.

Source: National Association of Realtors, US Dept. of Commerce.

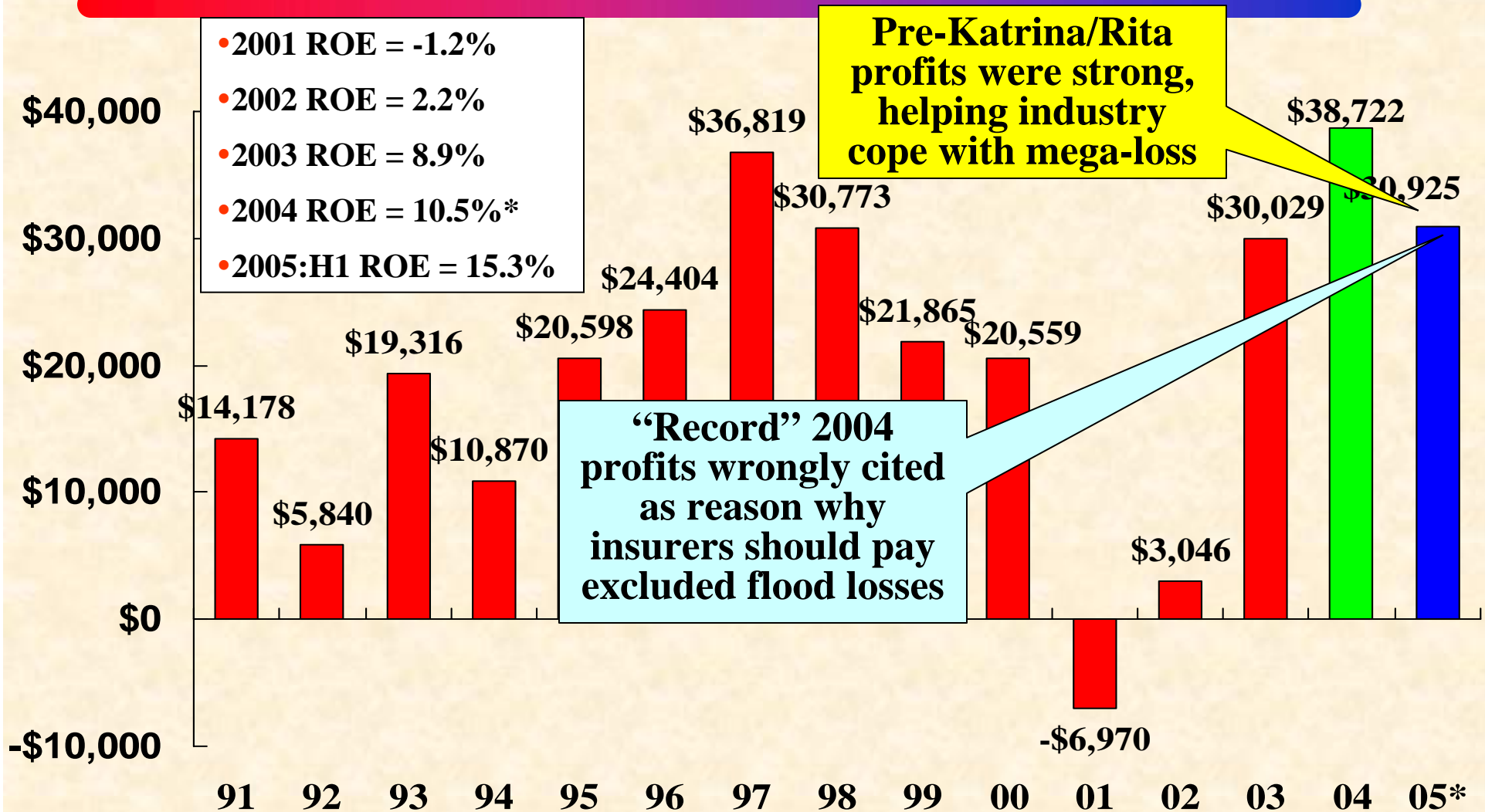
P/C Financial Overview

*Strong Pre-Katrina
Results Help Industry*

!!! *Meet the Challenge*



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



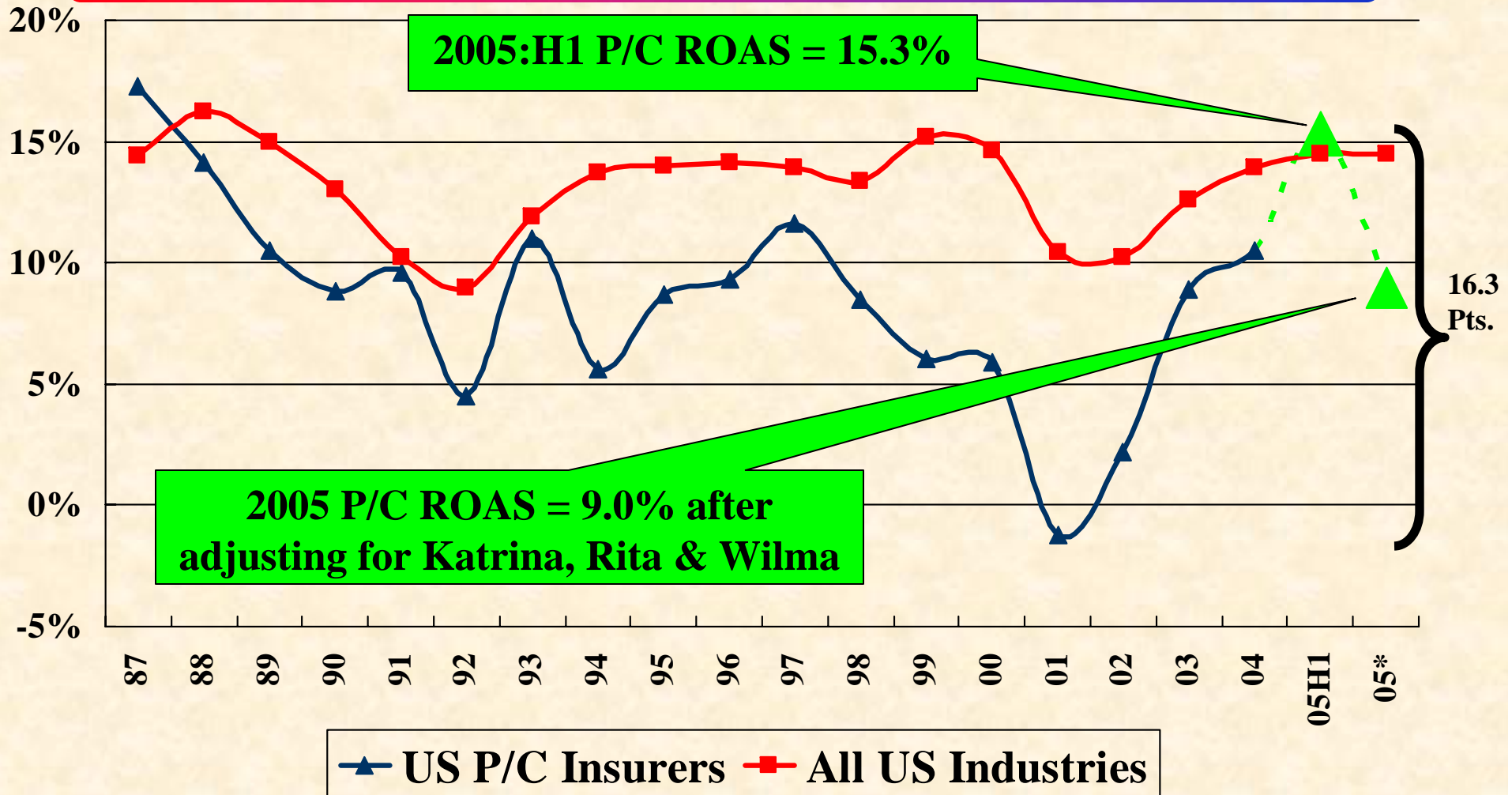
*ROE figures are GAAP; 2004 figure is return on average surplus. 2005 figure is for first half of year.

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



ROE: P/C vs. All Industries

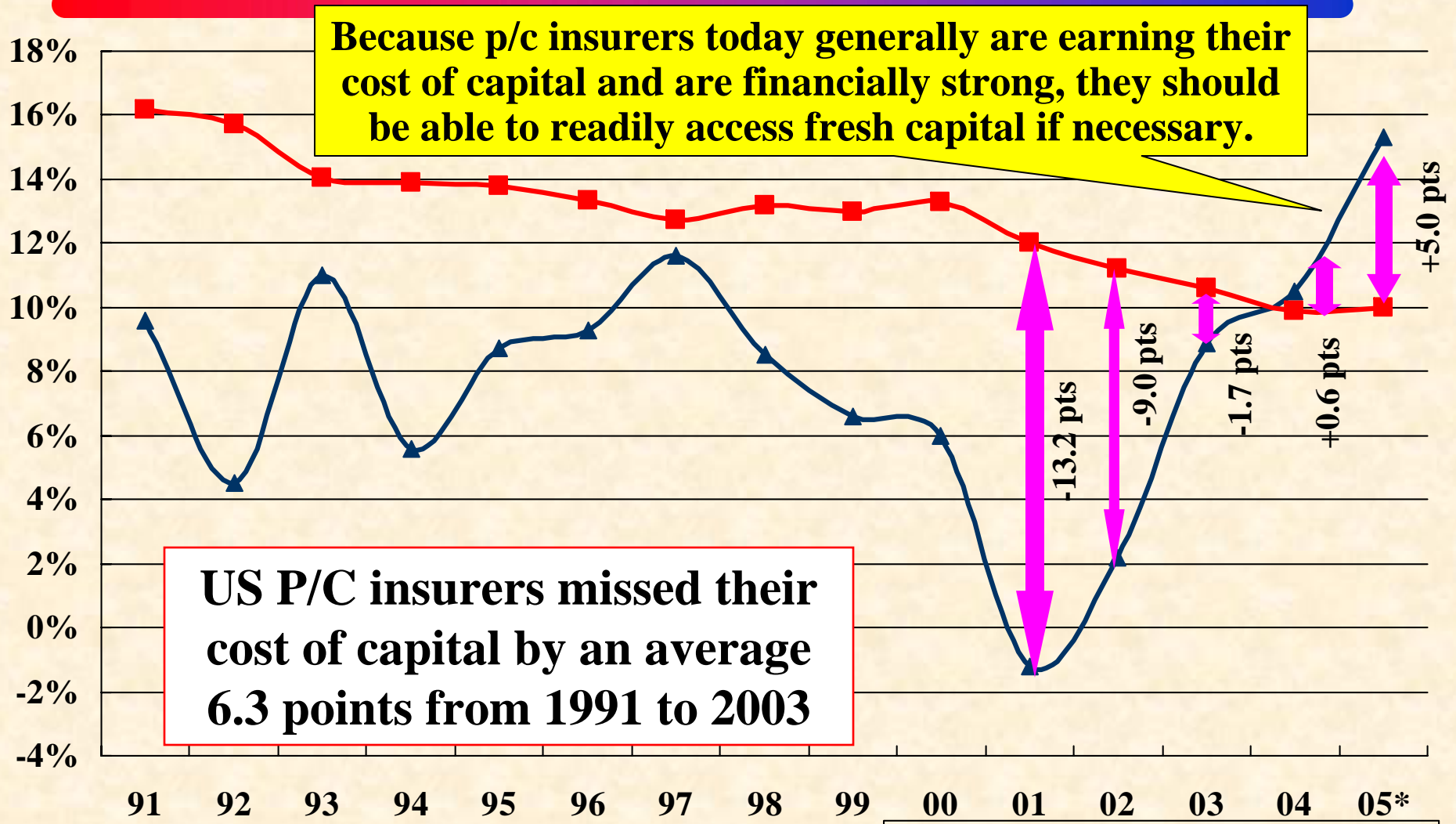
1987–2005F*



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



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

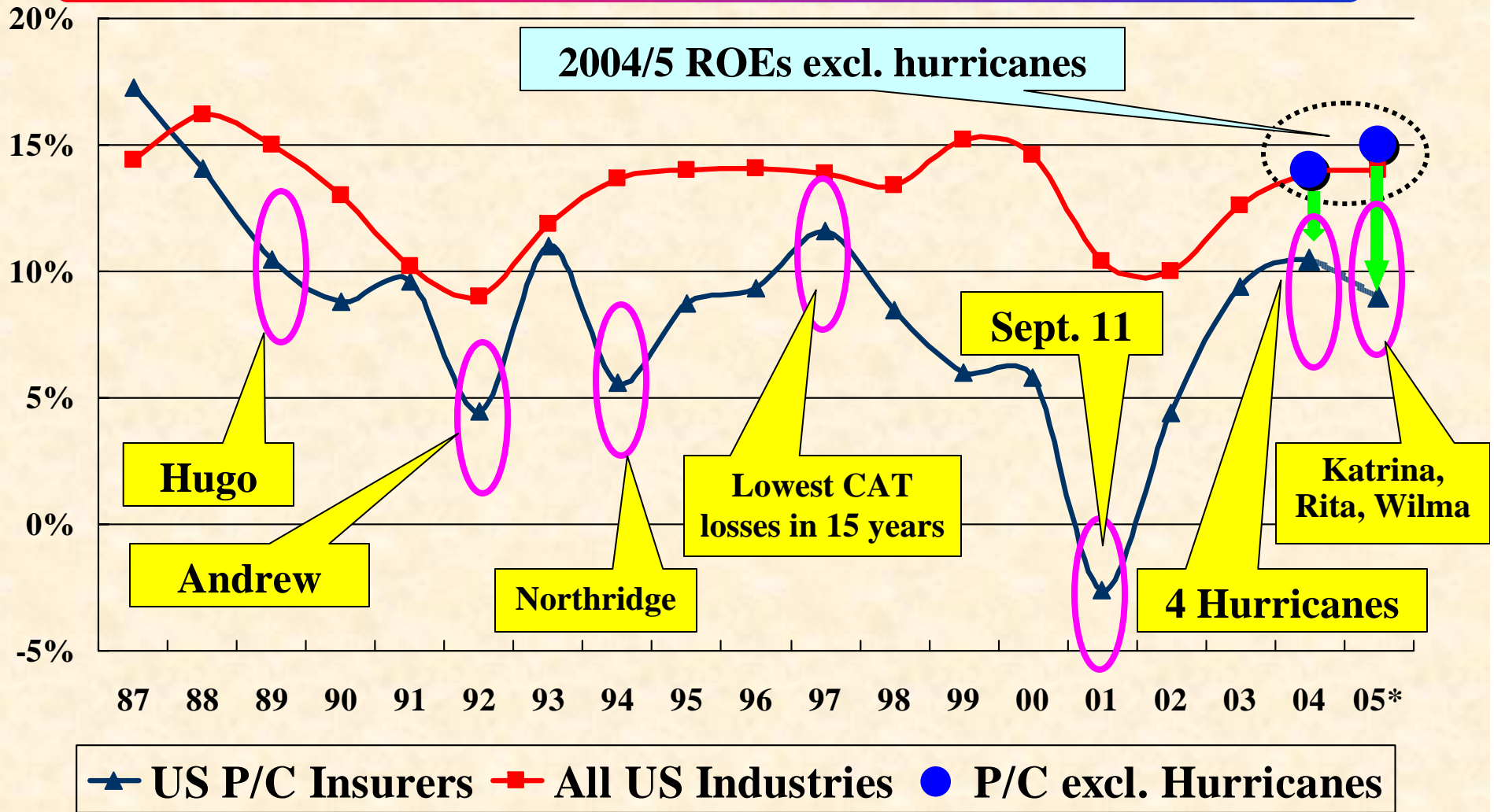


*First half 2005.

Source: The Geneva Association, Ins. Information Inst.



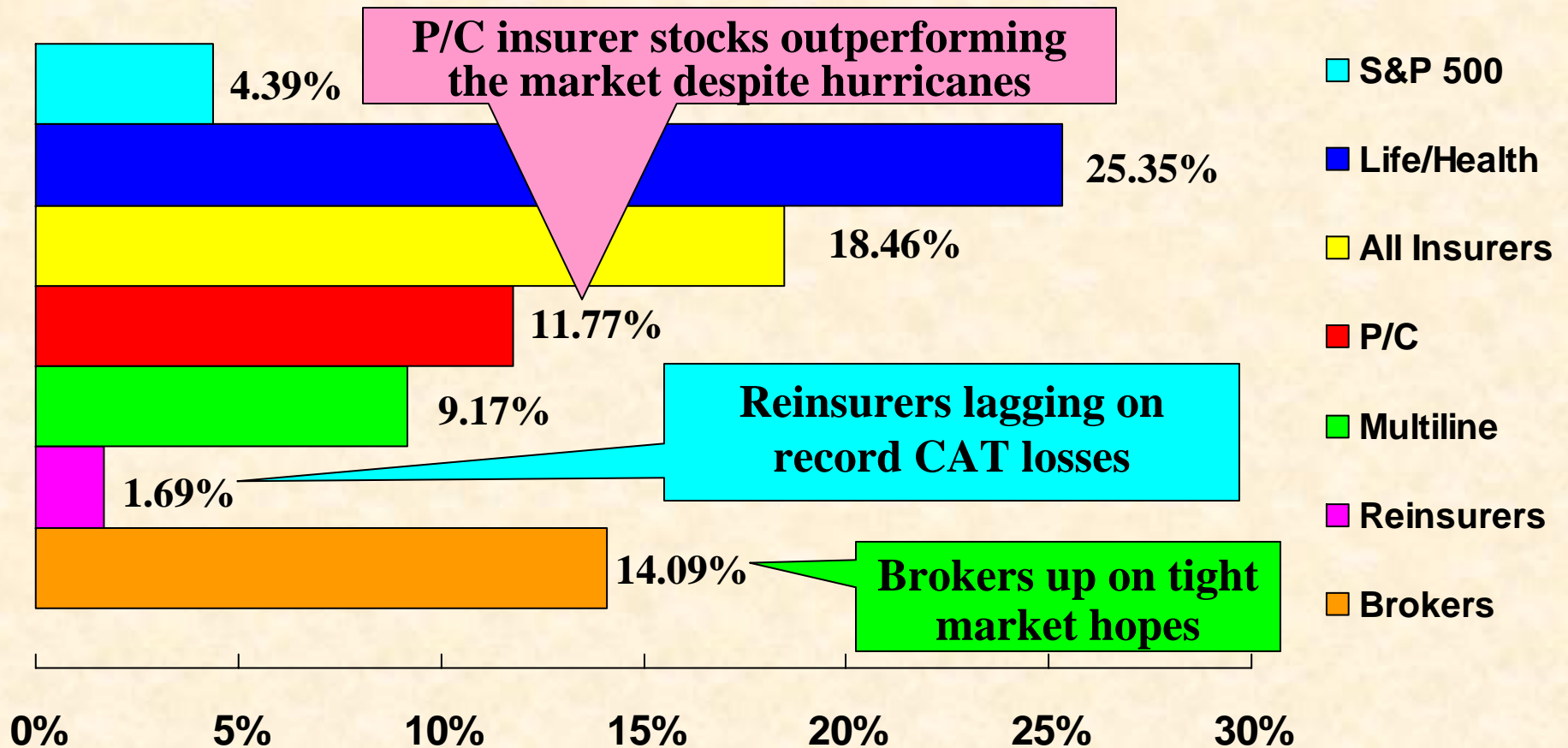
ROE: P/C vs. All Industries 1987-2005E



Source: Insurance Information Institute; *Fortune*

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

Total Return 2005 YTD Through December 2, 2005

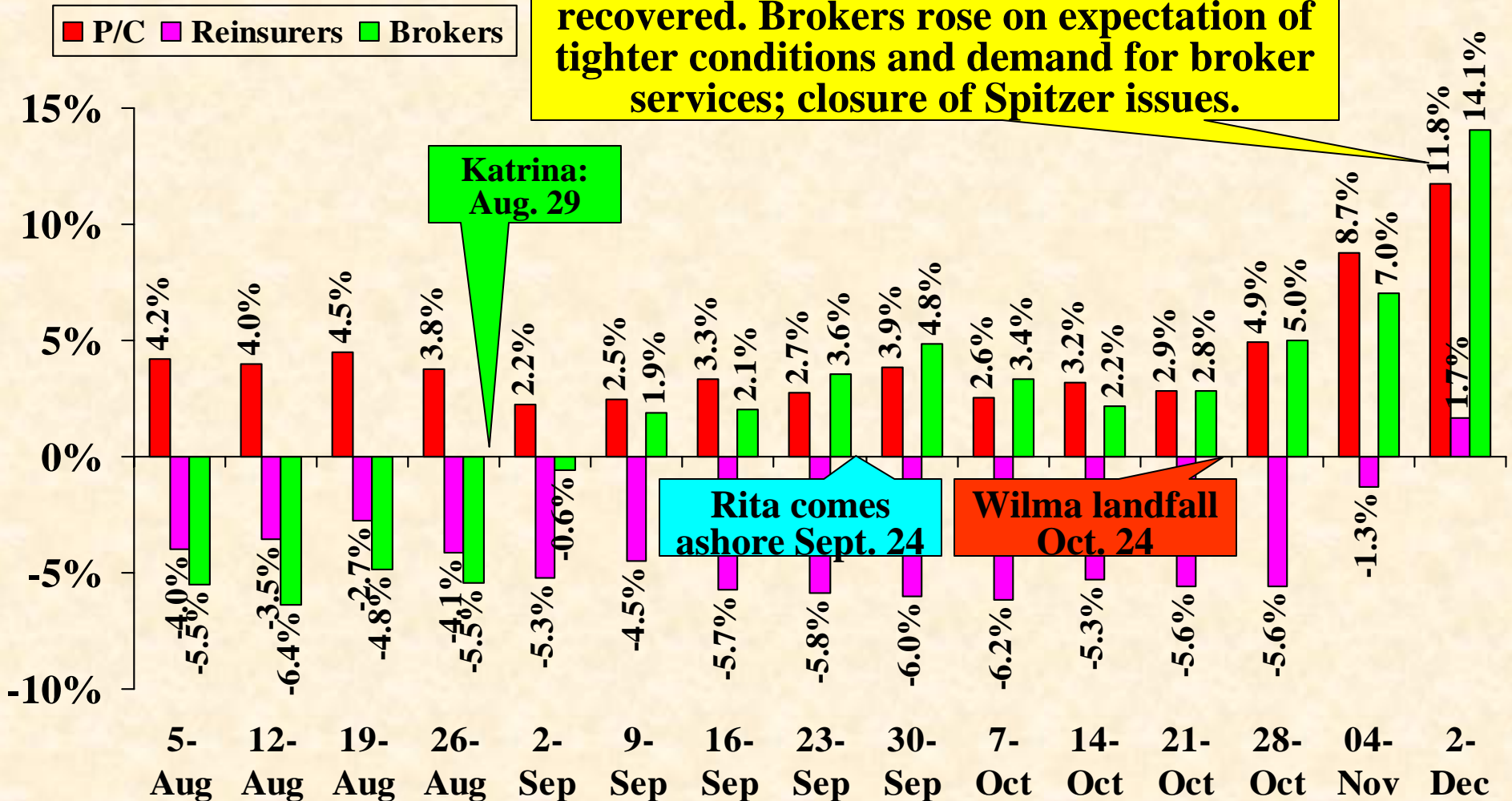


Source: SNL Securities, Standard & Poor's, Insurance Information Institute



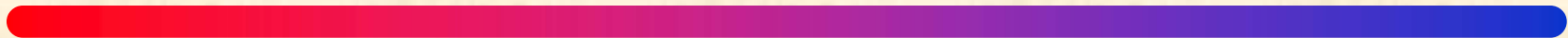
Change in YTD Stock Performance by Sector Pre- & Post-Katrina/Rita/Wilma

P/C & reinsurer stocks hurt by, now fully recovered. Brokers rose on expectation of tighter conditions and demand for broker services; closure of Spitzer issues.



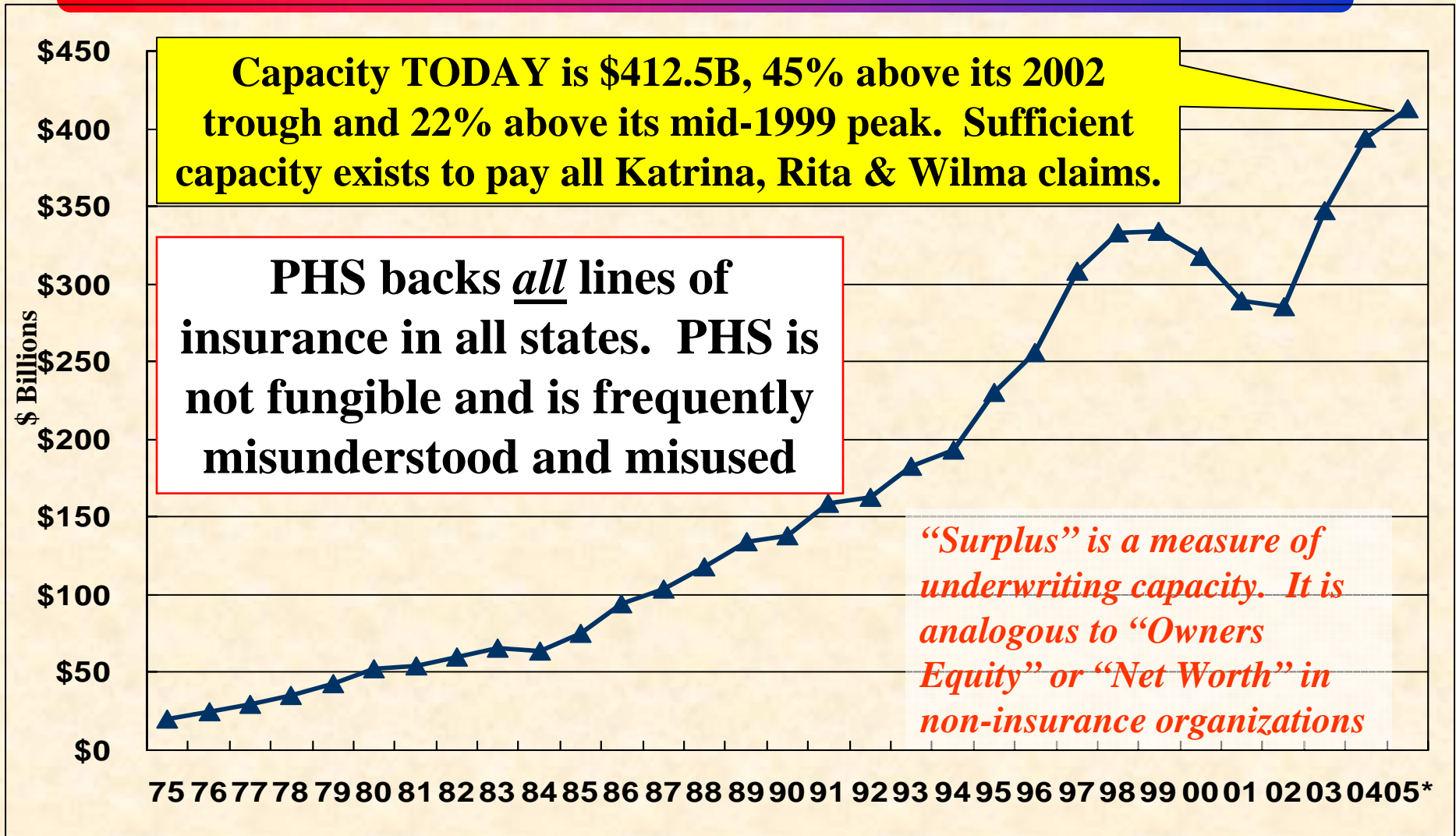
Source: SNL Securities; Insurance Information Institute

Insurer Claims Paying Resources





U.S. Policyholder Surplus: 1975-2005*

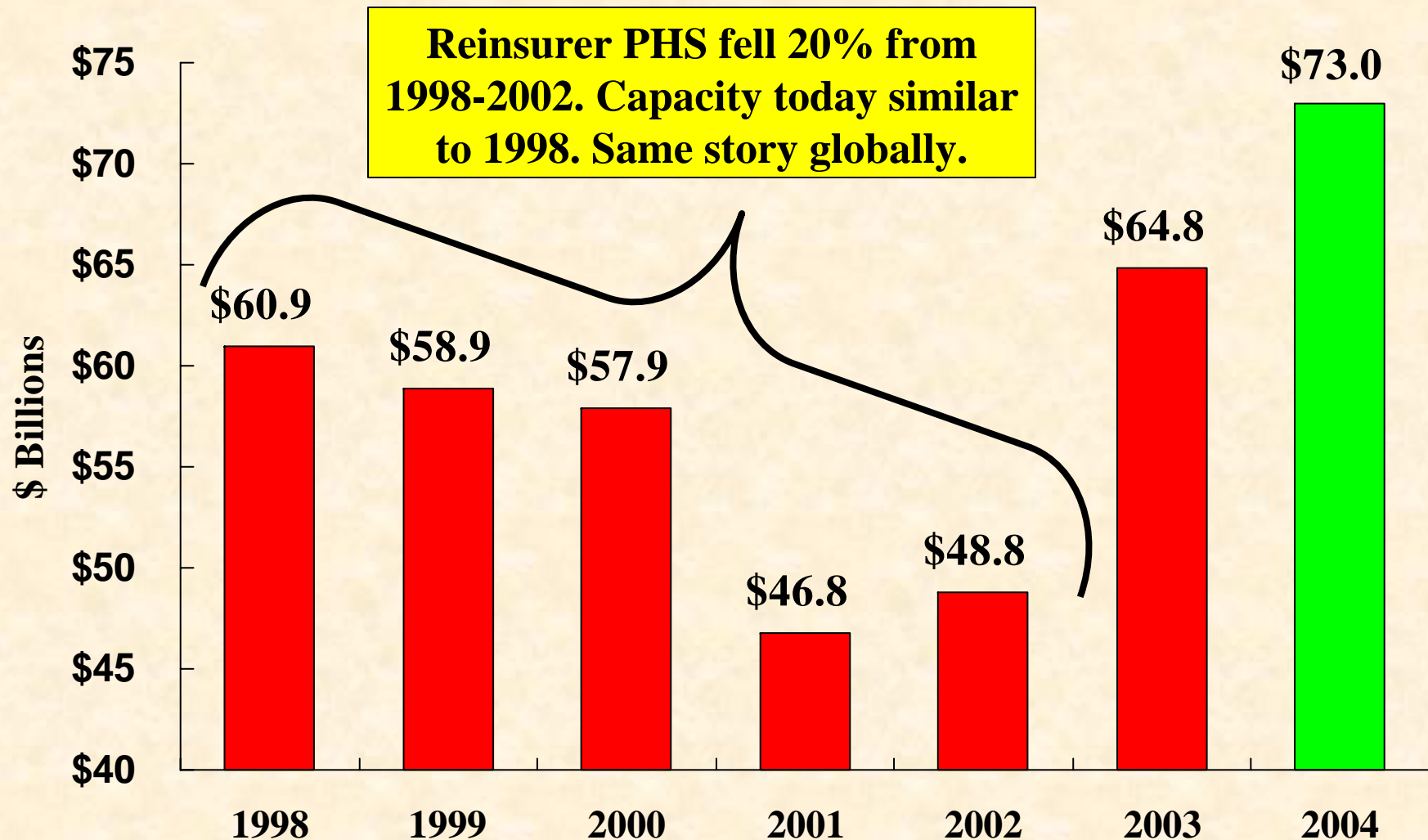


Source: A.M. Best, ISO, Insurance Information Institute

*As of 6/30/05.



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

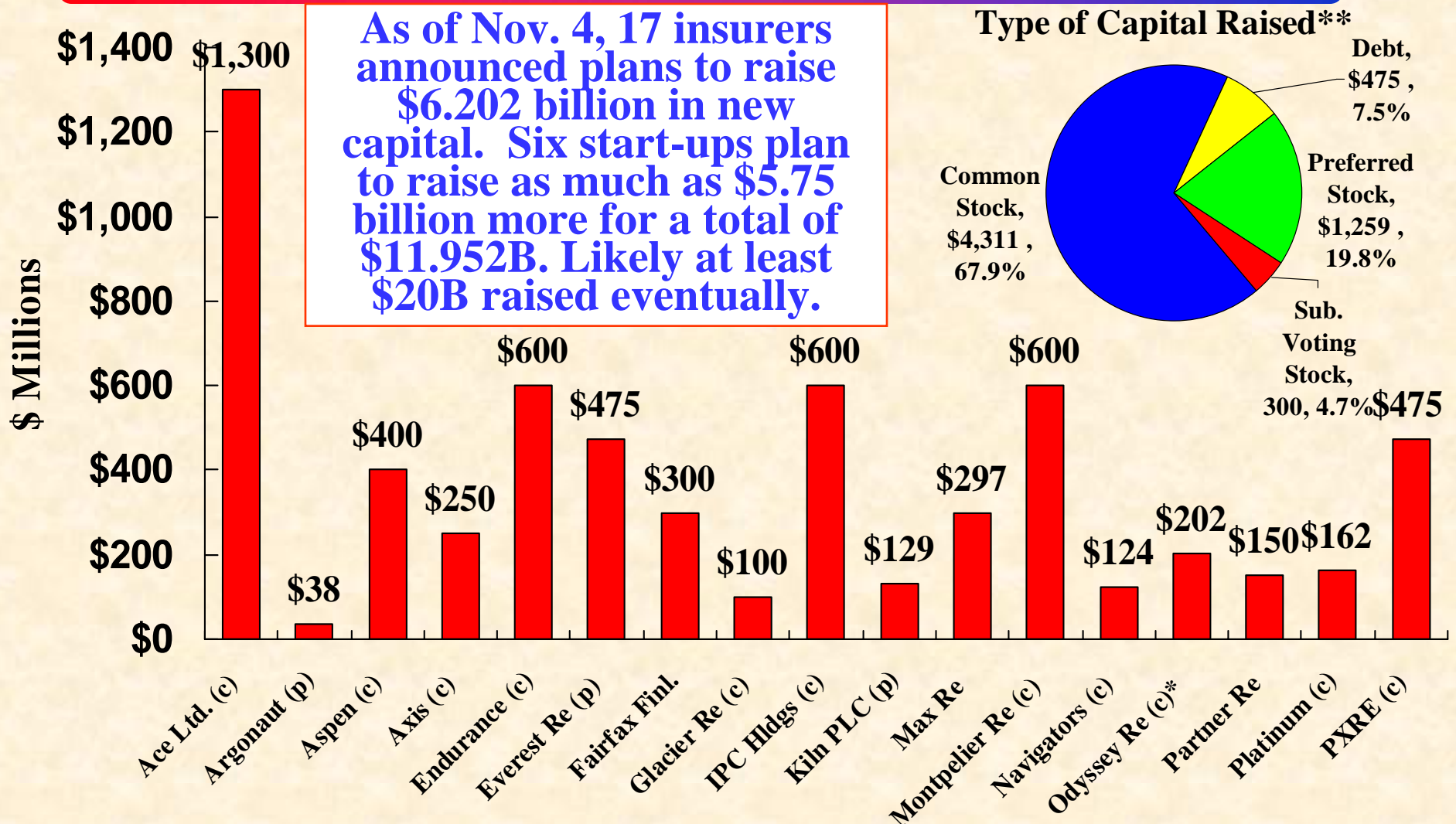


Source: A.M. Best; Insurance Information Institute



Announced Insurer Capital Raising*

(\$ Millions, as of November 4, 2005)

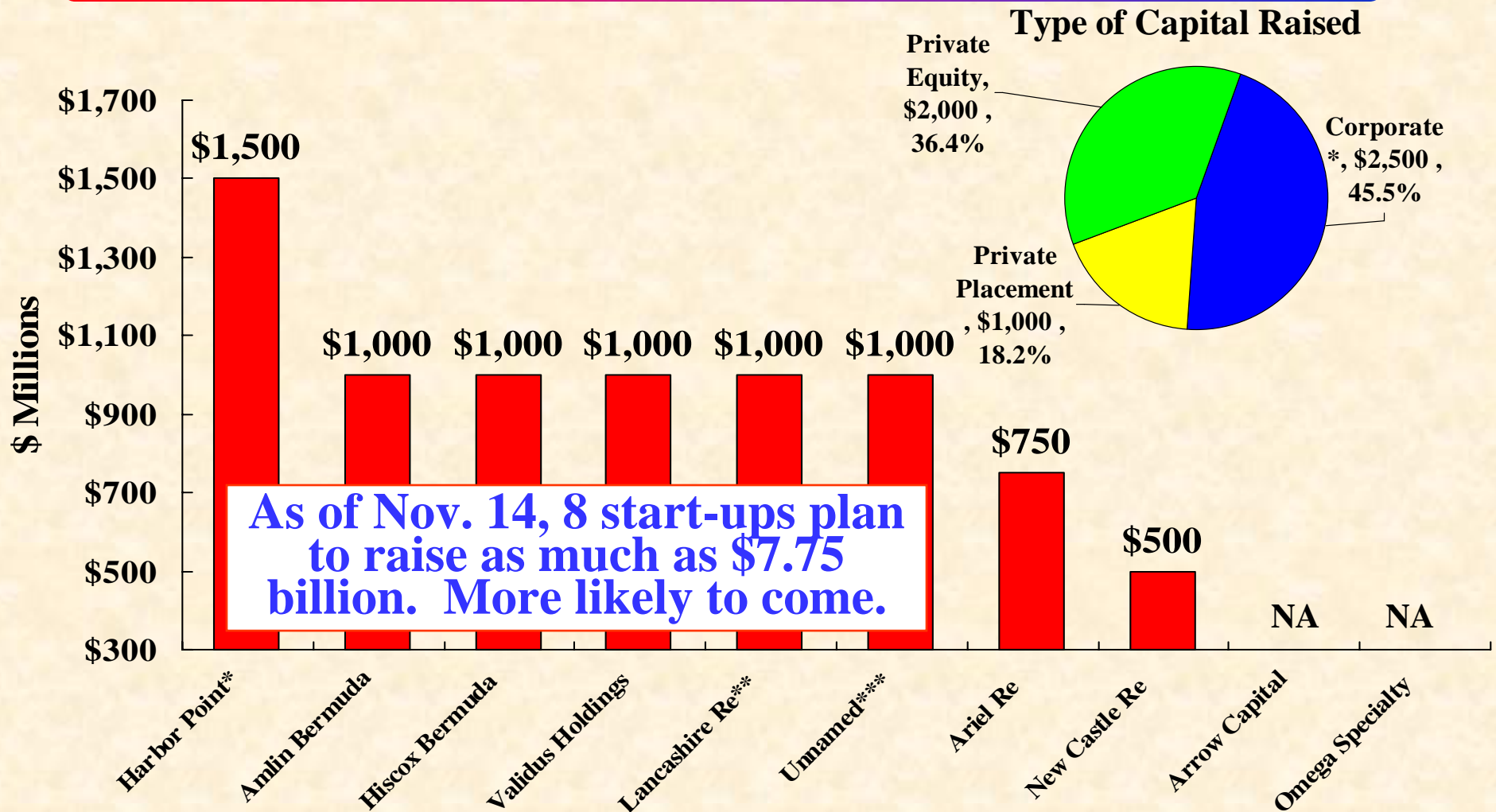


*Existing (re) insurers. Announced amounts may differ from sums actually raised. Odyssey Re: \$102 m out of \$202m still pending. **As of Oct. 25. Sources: Morgan Stanley, Company Reports; Insurance Information Institute.



Announced Capital Raising by Insurance Start-Ups

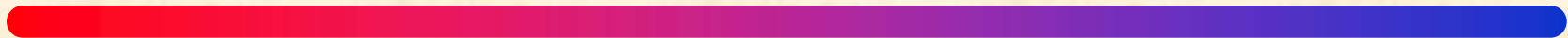
(\$ Millions, as of November 14, 2005)



*Chubb, Trident are funding Harbor Point. Announced amounts may differ from sums actually raised. **Stated amount is \$750 million to \$1 billion. ***XL Capital/Hedge Fund venture. Arrow Capital formed by Goldman Sachs. Sources: Morgan Stanley, Company Reports; Insurance Information Institute.

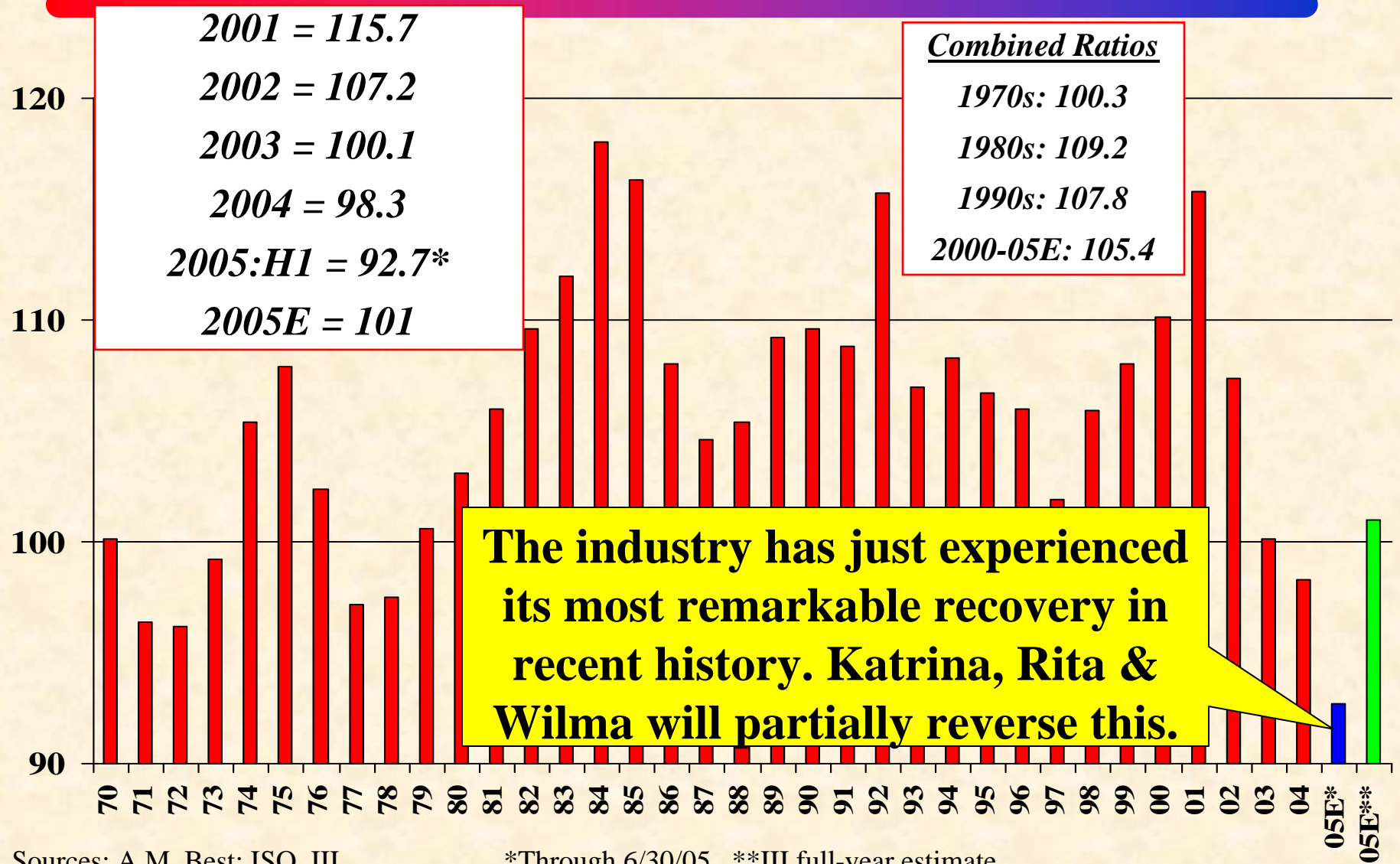
UNDERWRITING

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





*P/C Industry Combined Ratio**



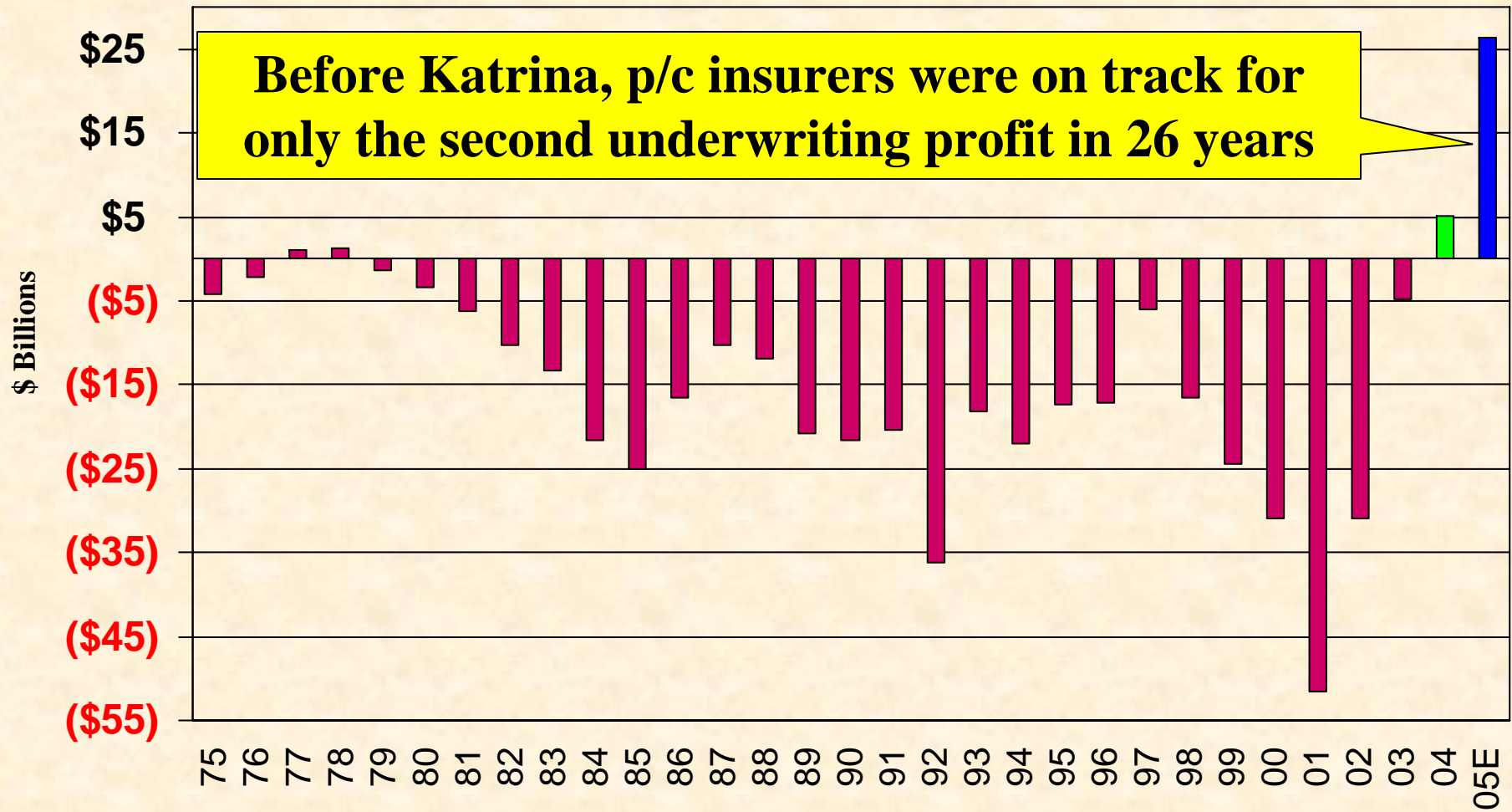
Sources: A.M. Best; ISO, III.

*Through 6/30/05 **III full-year estimate.



Underwriting Gain (Loss)

*1975-2005E**



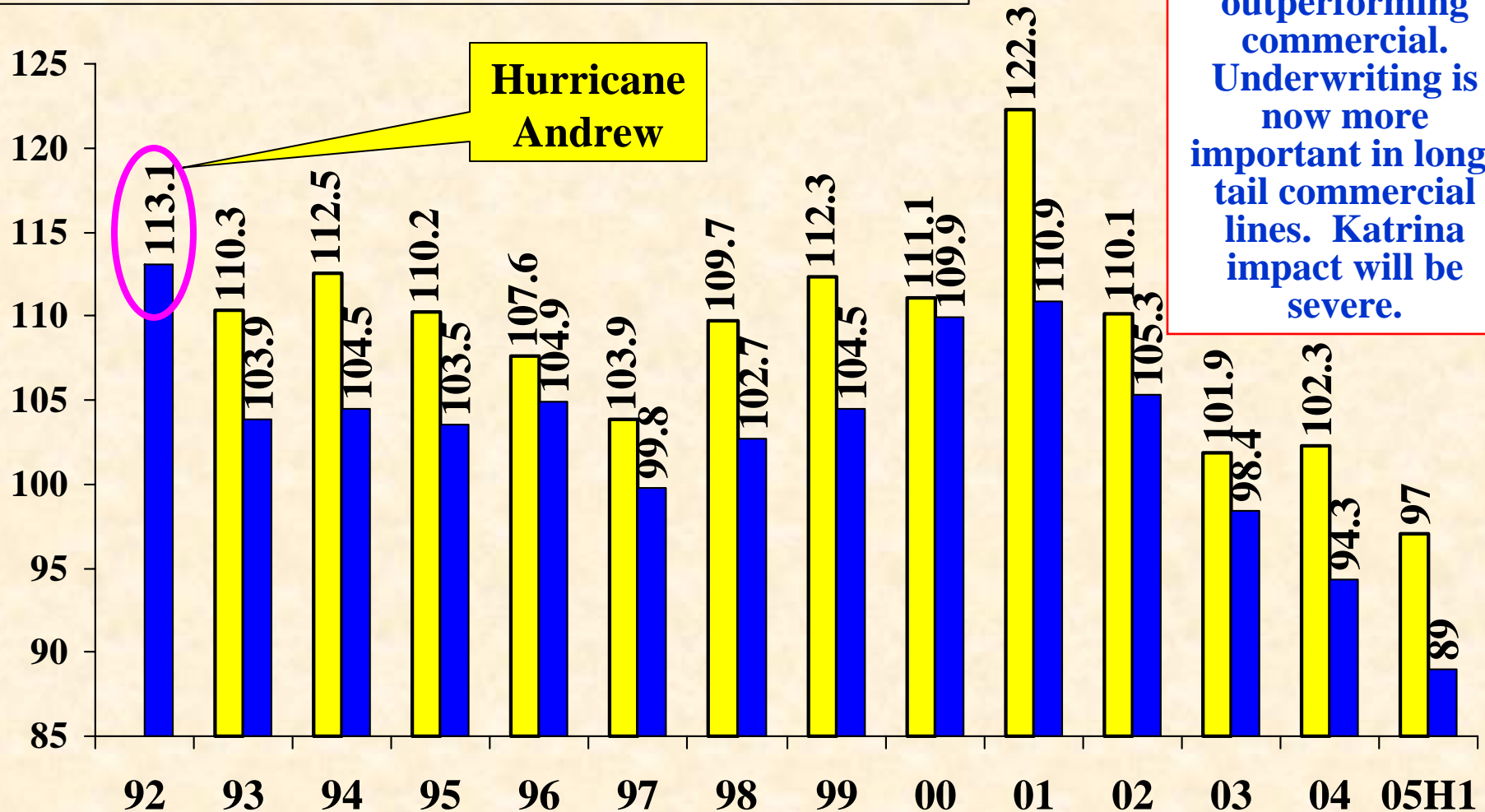
*2005 estimate is based on annualized actual 05H1 net underwriting profit of \$13.2 billion.

Source: A.M. Best, Insurance Information Institute



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

Commercial--Net Basis Personal--Net Basis



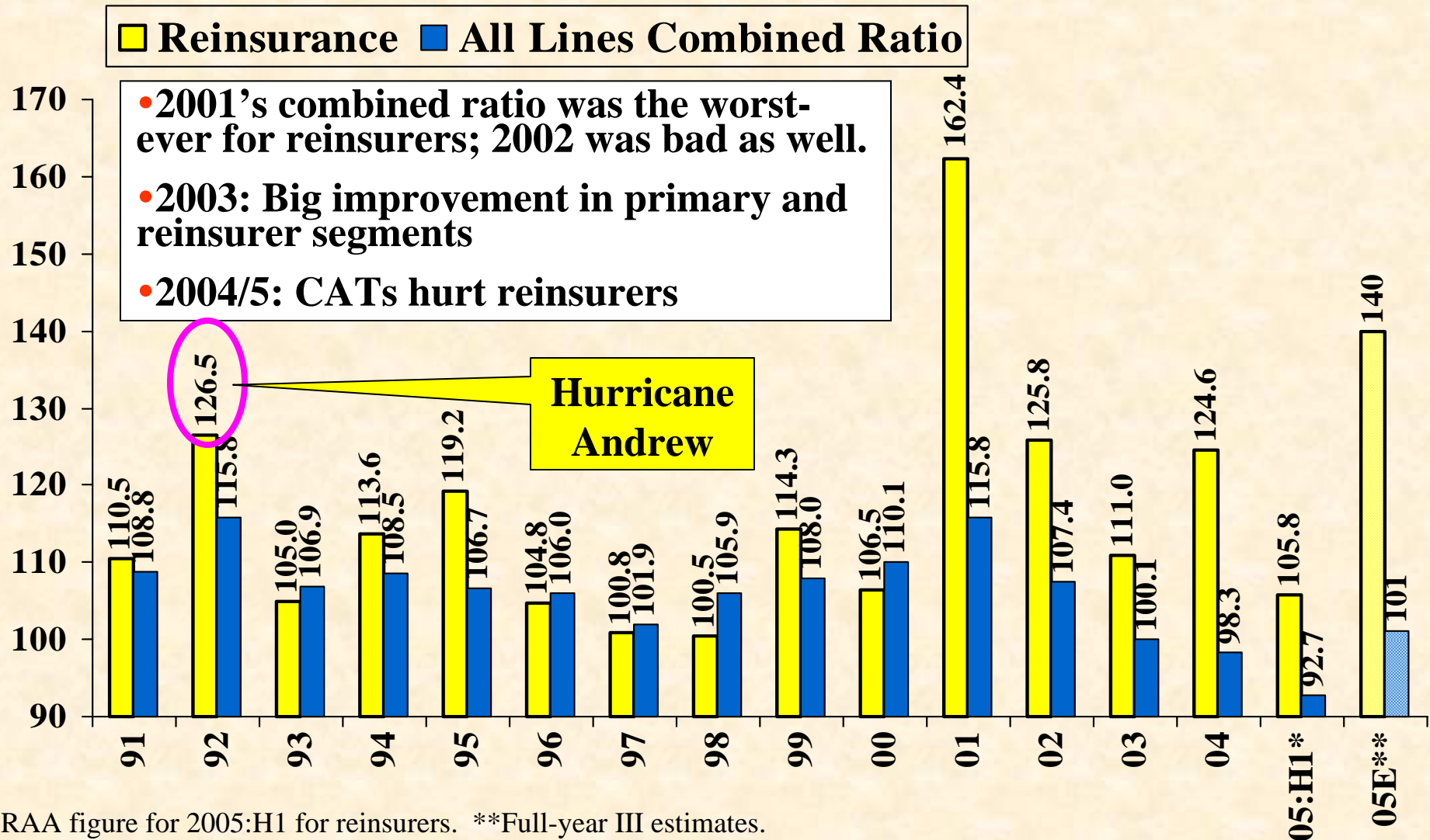
Personal lines outperforming commercial. Underwriting is now more important in long-tail commercial lines. Katrina impact will be severe.

Source: A.M. Best; Insurance Information Institute

*III estimate for first half 2005. Actual 1H05 combined ratio all lines was 92.7.



Combined Ratio: Reinsurance vs. P/C Industry



*RAA figure for 2005:H1 for reinsurers. **Full-year III estimates.

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



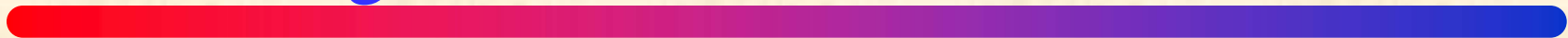
TRIA Extension?

(Focus on Senate Bill)

- **Term:**
 - 2-Year Extension, 3rd Possible if progress toward long-term solution
- **Trigger Increased:**
 - Up from \$5MM now to \$50MM in 2006 and \$100MM in 2007
- **Lines Dropped**
 - Commercial Auto, Prof. Liability, Surety, Burglary & Theft, FMP
 - H.B. 4314 would add Group Life
- **Deductibles Increase for Individual Companies:**
 - 15% Now → 17.5% in 2006 → 20% in 2007 for all lines
 - Would vary by line in House 4314 version
- **Retentions Increase for Industry Aggregate:**
 - \$15B Now → \$17.5B in 2006 → \$20B in 2007
- **Co-Pays Increase for Amount Above Industry Aggregate**
 - 10% Now → 10% in 2006 → 15% in 2007
- **Study to Develop Long-Term Solutions**
 - Senate version requires study to find long-term solution
- **Nuclear, Biological, Chemical & Radiological Risk**
 - No mention in Senate bill; House bill creates new NBCR liability for insurers

UNDERWRITING AFFECTS FINANCIAL STRENGTH

*Is There Cause
for Concern?*





Rating Agency Actions Following

Hurricane Katrina (as of Oct. 6, 2005)*

Companies Under Review w/ Negative Implications

	<u>Company</u>	<u>A.M. Best Rating</u>
1.	Allied World	A+
2.	Allmerica Financial P&C Cos .	A-
3.	American Re	A
4.	Balboa Insurance Grp.	A
5.	DaVinci Re	A
6.	Endurance Specialty	A
7.	Florists Mutual Grp.	A-
8.	Glencoe	A
9.	Imagine Insurance Co. Ltd.	A-
10.	IPCRe	A+
11.	Louisiana Farm Bureau Mutual	A-
12.	Mississippi Farm Bureau Mutual	A+
13.	Munich Re	A+
14.	Mutual Savings Fire Ins. Co.	B-
15.	Mutual Savings Life Ins. Co.	B-
16.	Odyssey Re	A
17.	PartnerRe Group	A+
18.	PXRE	A-
19.	Renaissance Re	A+
20.	Rosemont Reinsurance Ltd.	A-
21.	Transatlantic Re	A+
22.	XL Capital	A+
23.	XL Life Insurance & Annuity	A+
24.	XL Life Ltd.	A+

Companies on Credit Watch with Negative Implications

	<u>Company</u>	<u>S&P Rating</u>
1.	Allmerica	BBB+
2.	Allstate Corp.	AA
3.	Aspen Group	A
4.	Oil Casualty Insurance Ltd.	A-
5.	Society of Lloyd's	A
6.	State Farm	AA
7.	Swiss Re	AA
8.	United Fire Group	A

Downgrades

	<u>Company</u>	<u>S&P Rating</u>	<u>A.M. Best</u>
1.	Alea	A- to BBB+	A- to B++
2.	Olympus Re	not rated	A- to B+
3.	PXRE	A to A-	A to A-
4.	Advent Synd. 780	3pi to 2pi	not rated

“...the replenishment of capital alone may not be sufficient to sustain a company’s rating.” A.M. Best press release Sept. 15, 2005

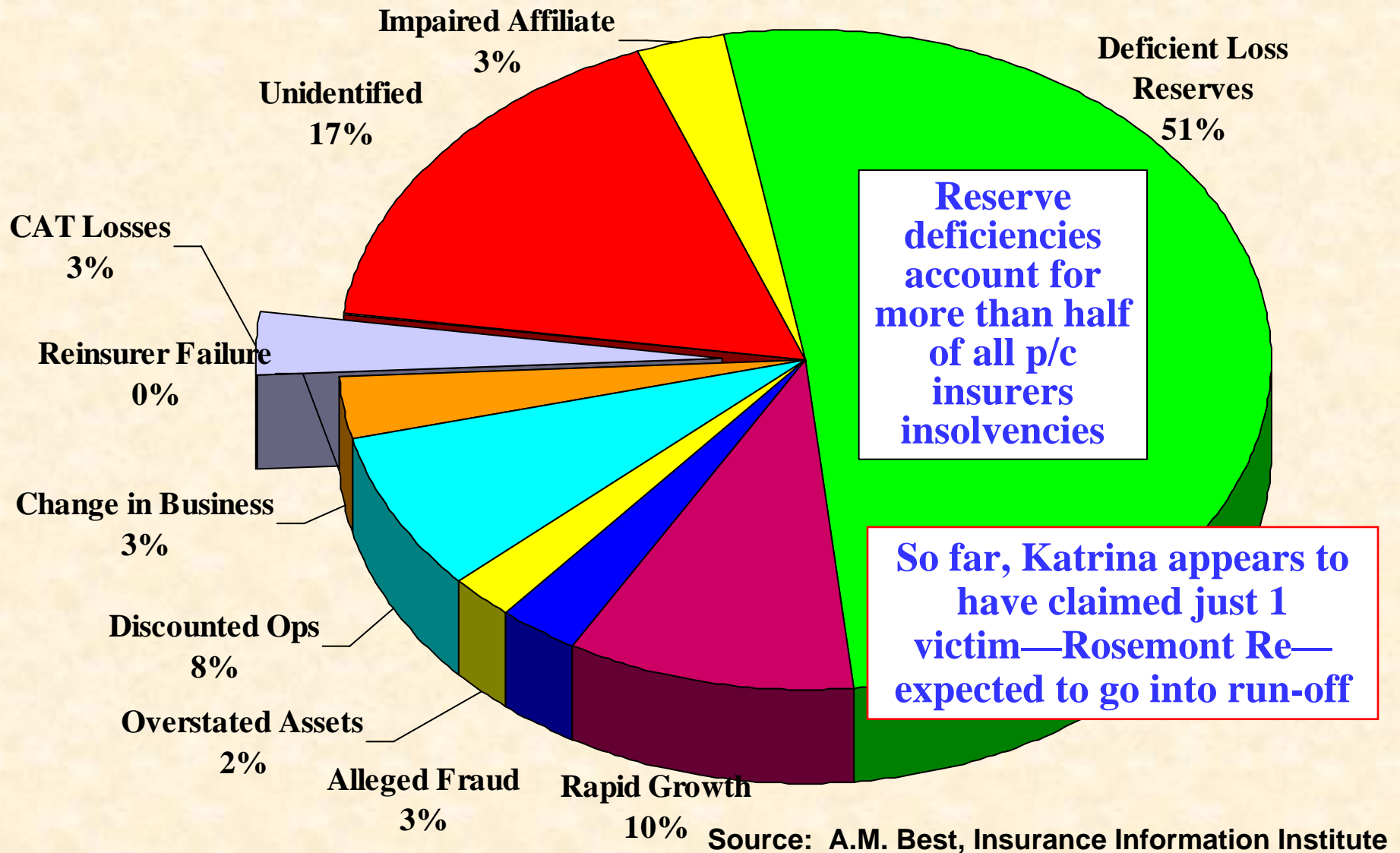
*ACE and Montpelier Re were originally placed on watch/review but have been removed.

Source: Hurricane Katrina: Analysis of the Impact on the Insurance Industry, Tillinohast. October 2005.



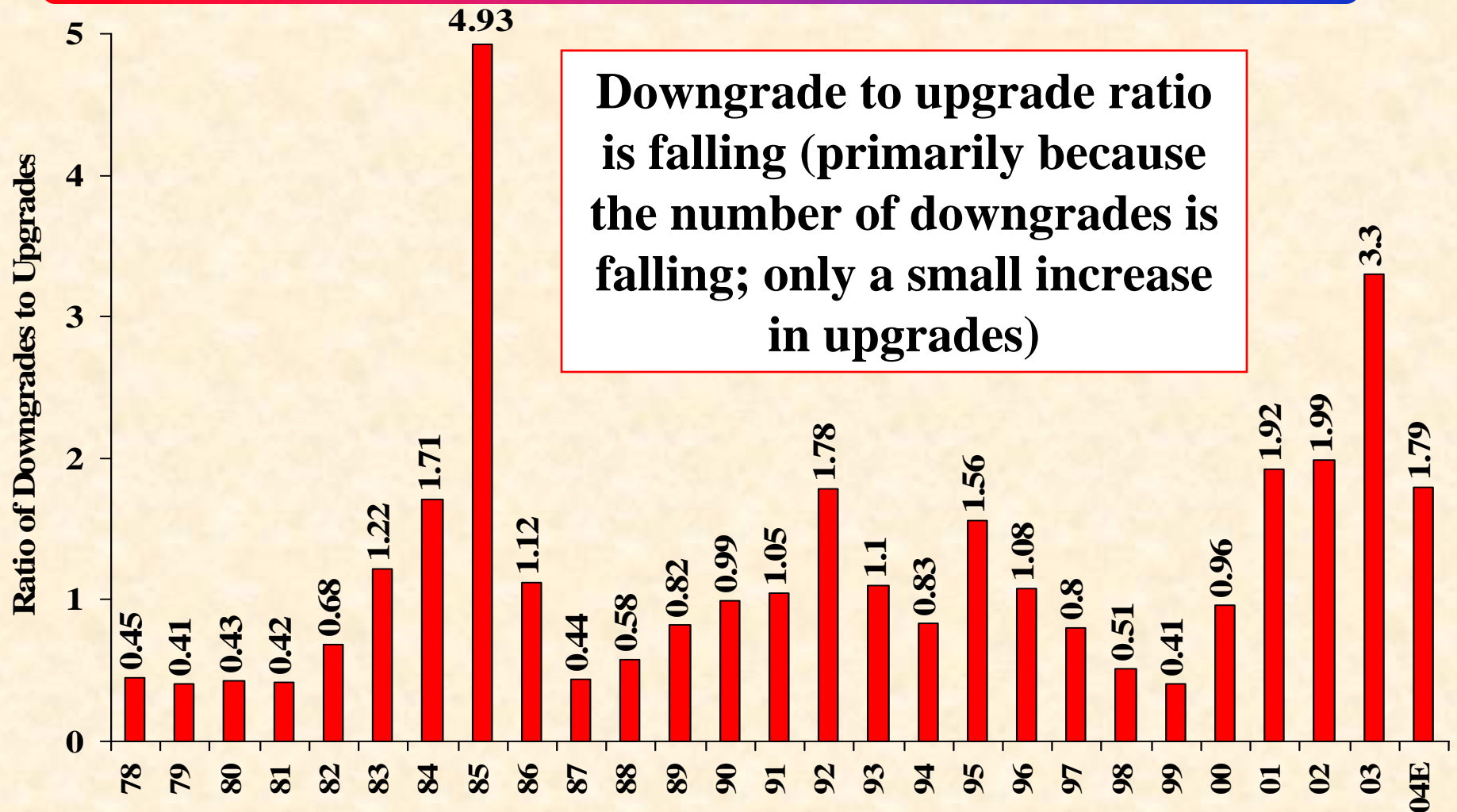
Reason for P/C Insolvencies

(218 Insolvencies, 1993-2002)





Downgrade/Upgrade Ratio*



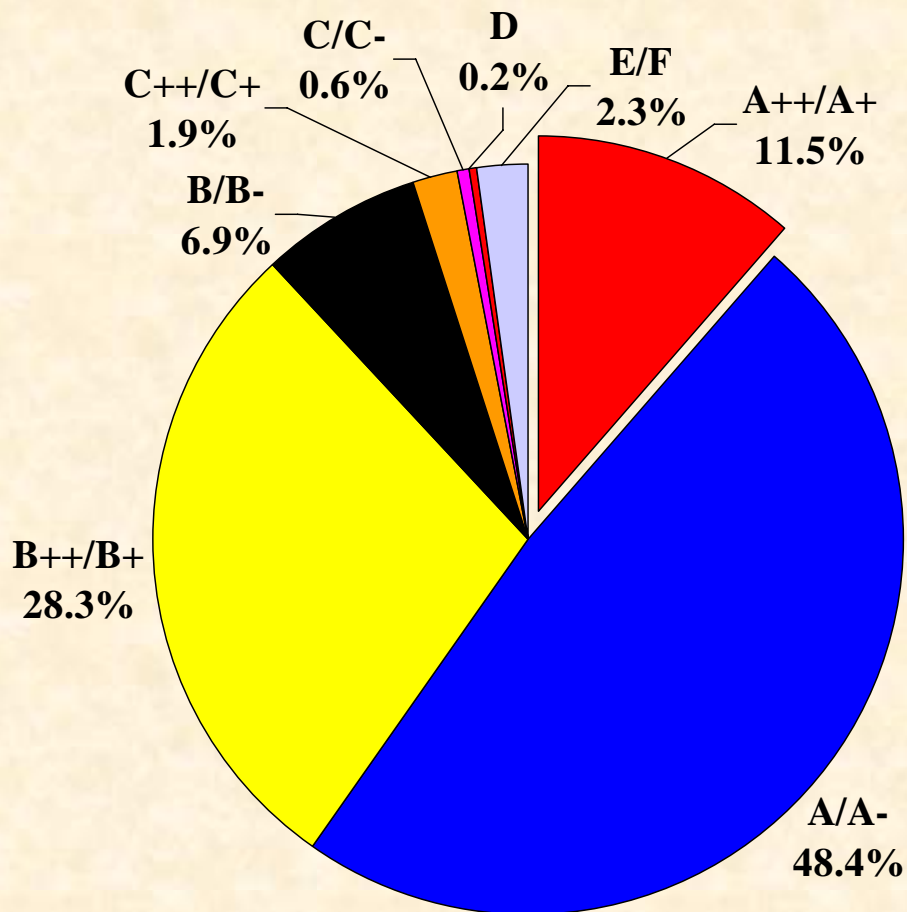
Sources: *Impairment Rate and Rating Transition Study—1977 to 2002*, A.M. Best & Co.

*U.S. property/casualty and life/health insurers before 2000; P/C only 2000-2004.

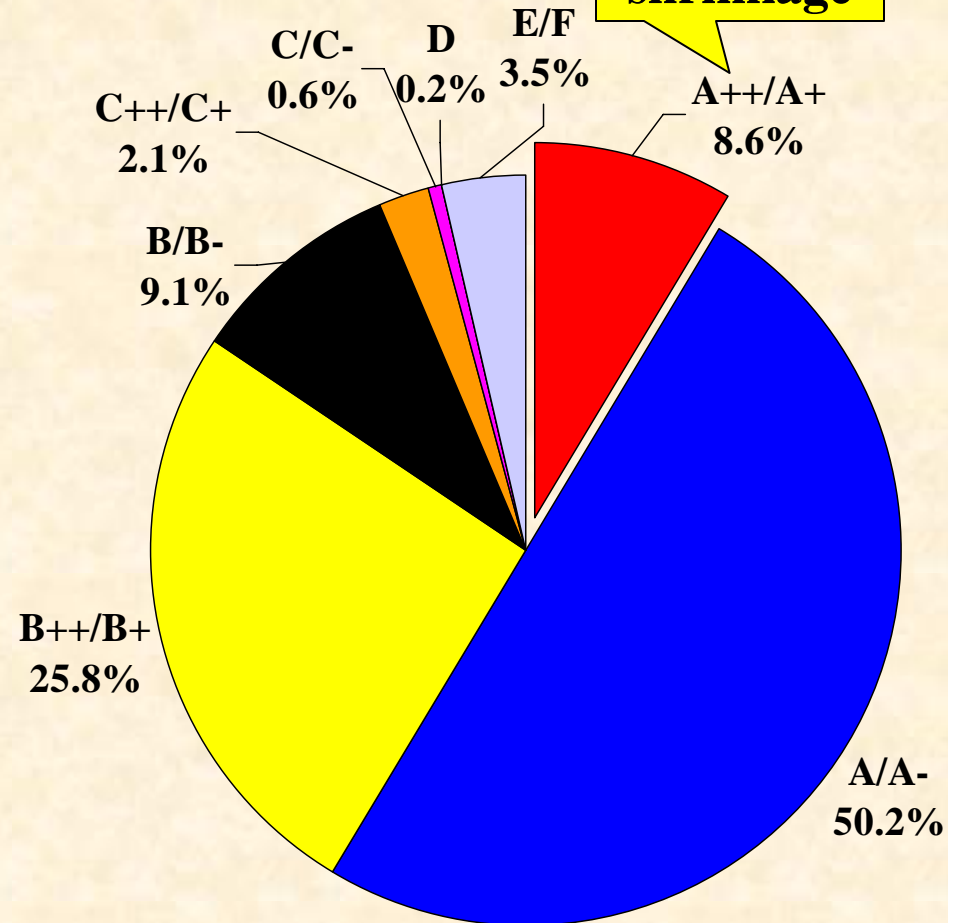


Historical Ratings Distribution, US P/C Insurers, 2000 vs. 2004

2000



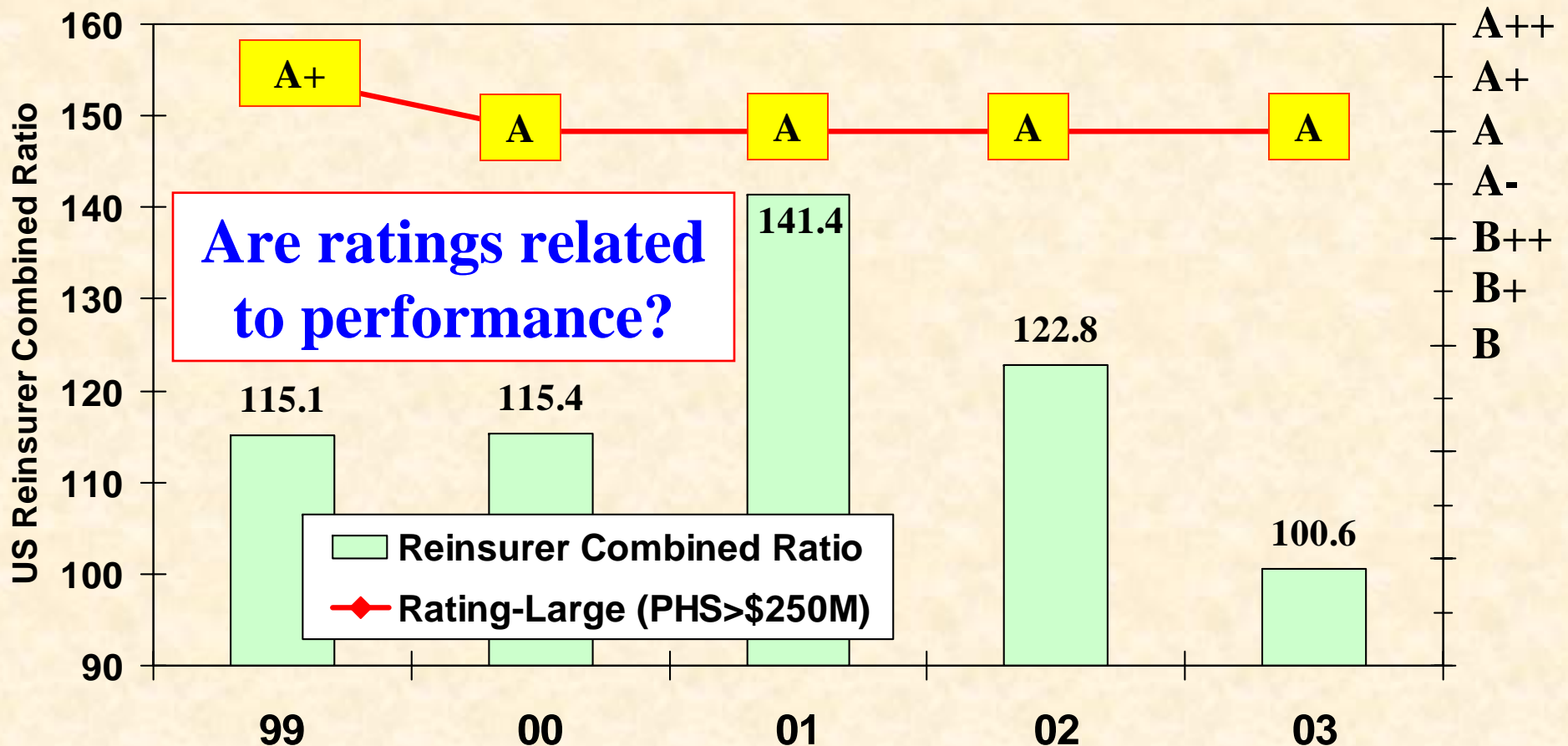
2004



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



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

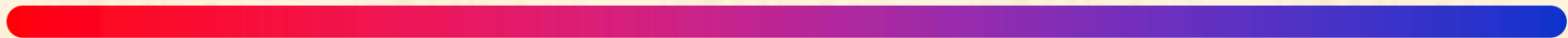


*Combined ratio is for all US reinsurers. Rating is for large reinsurers (policyholder surplus exceeding \$250 million). The median rating for small reinsurers (PHS < \$250M) was A- throughout the 1999-2003 period.

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

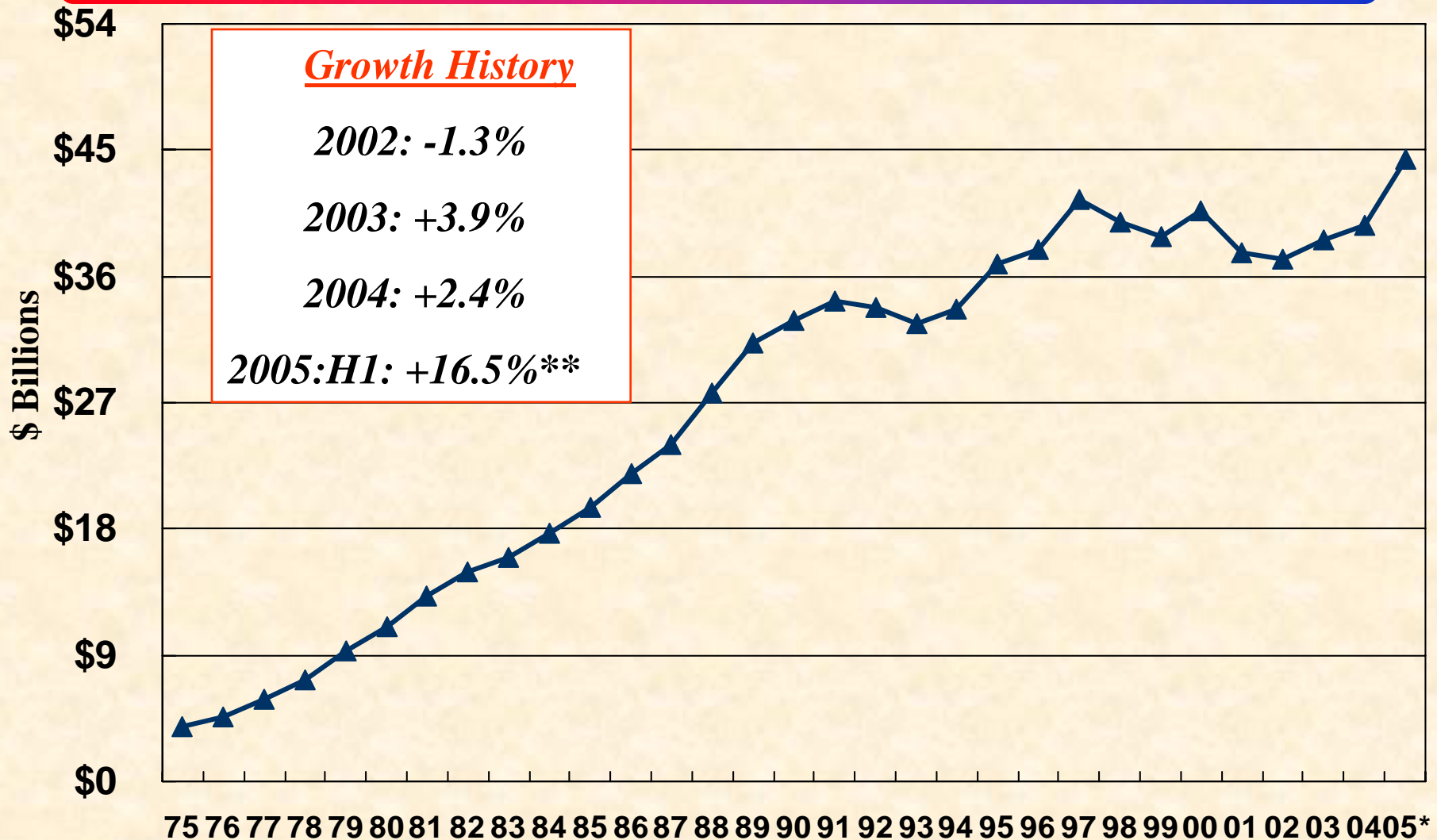
INVESTMENTS

*Improvements Still
Support Cash Flow
Underwriting*





Net Investment Income



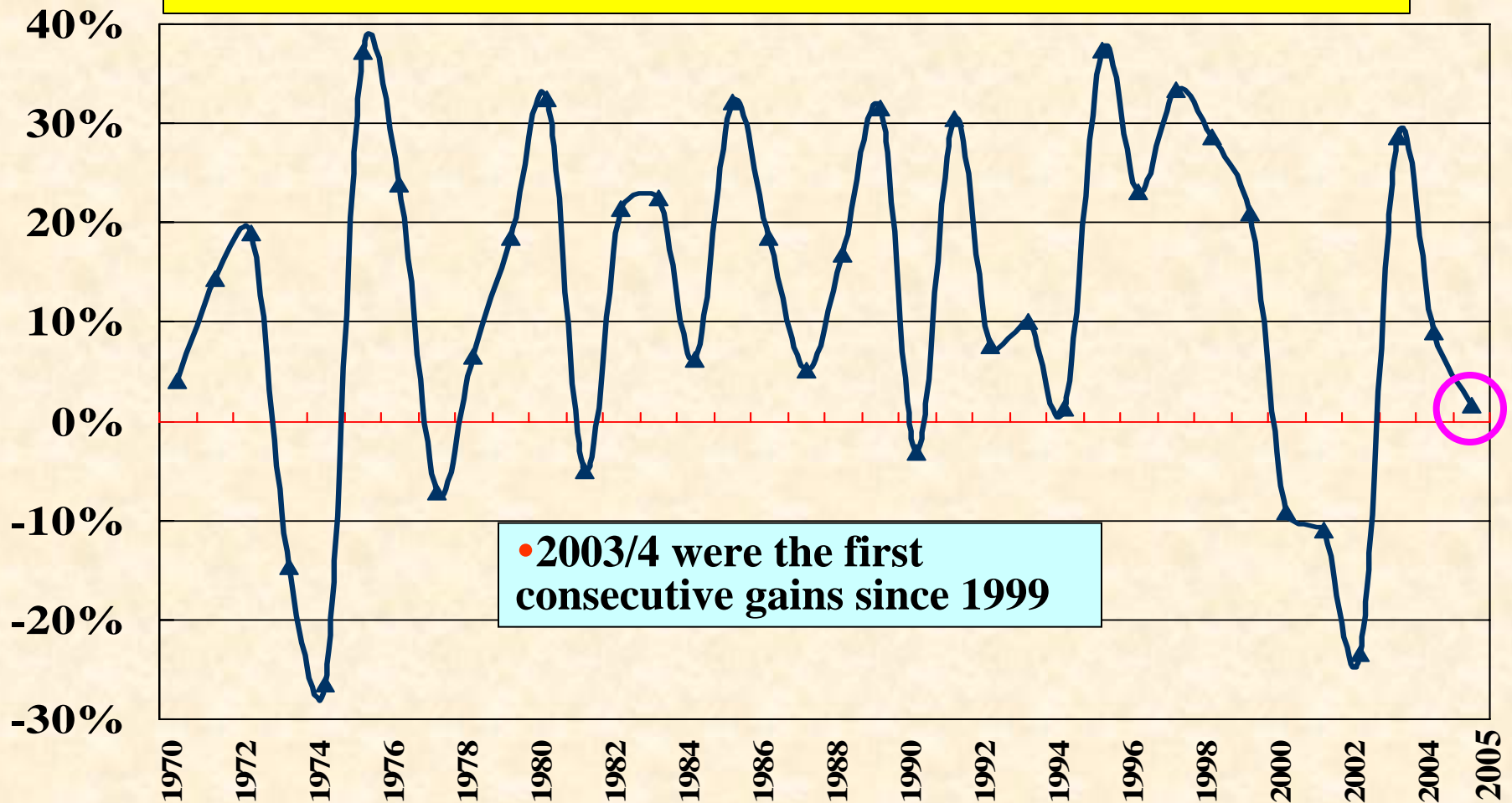
Source: A.M. Best, ISO, Insurance Information Institute;

*Annualized. **2005:H1 over 2004:H1, adjusted for special dividend of \$3.1B.



Total Returns for Large Company Stocks: 1970-2005*

S&P 500 was up 9% in 2004. Fears of higher interest rates, inflation, the falling dollar, resurgent oil prices are concerns in 2005



Source: Ibbotson Associates, Insurance Information Institute.

*Through November 16, 2005.



Property/Casualty Insurance Industry Investment Gain*



*Investment gains consist primarily of interest, stock dividends and realized capital gains and losses. Annualized 2005 figure based on data as of 6/30/05, adjusted for special dividend of \$3.1B. Source: Insurance Services Office; Insurance Information Institute.

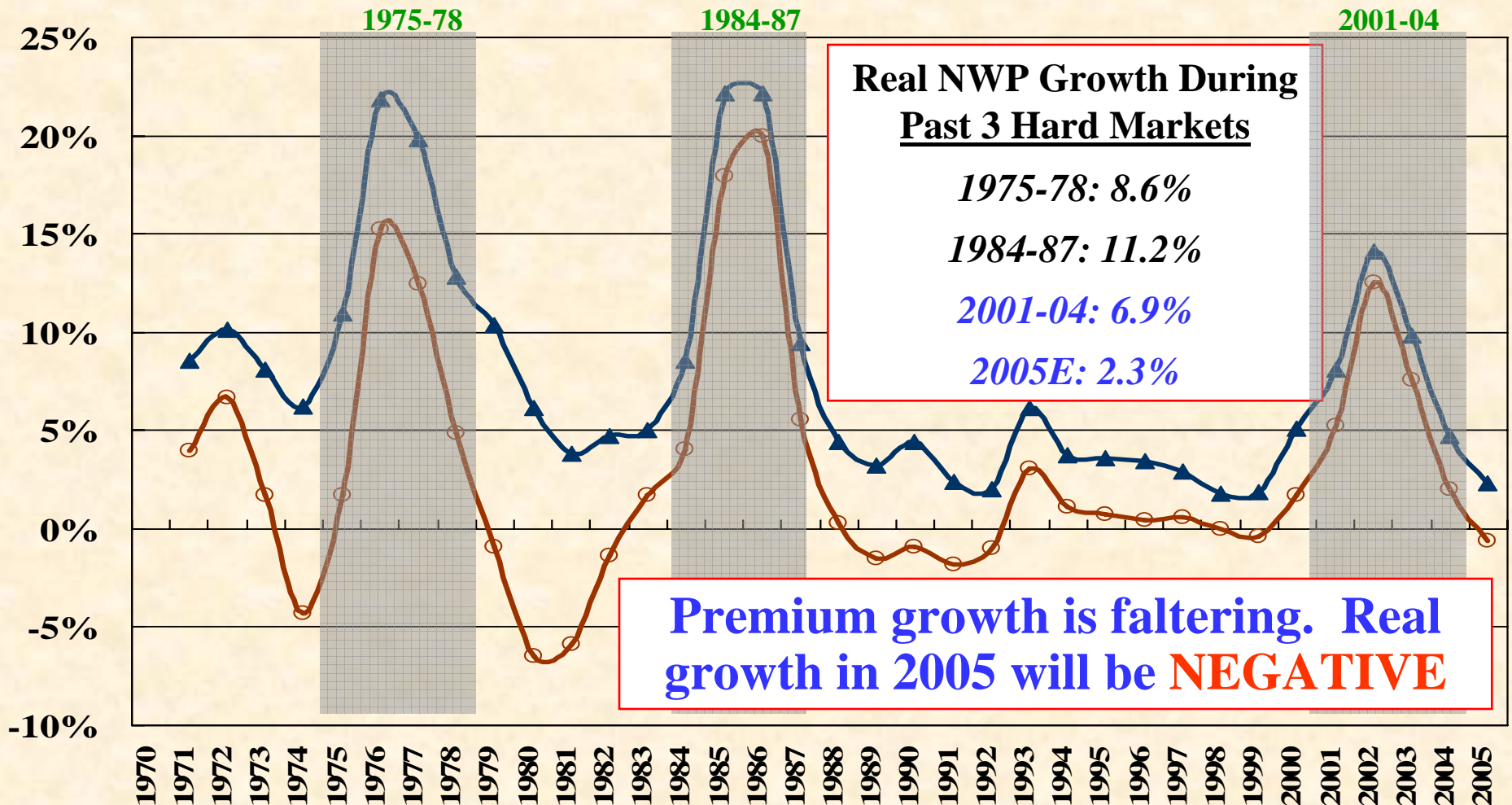
PRICING TRENDS

*Will Katrina & Rita
Harden Markets?*





Strength of Recent Hard Markets by NWP Growth*



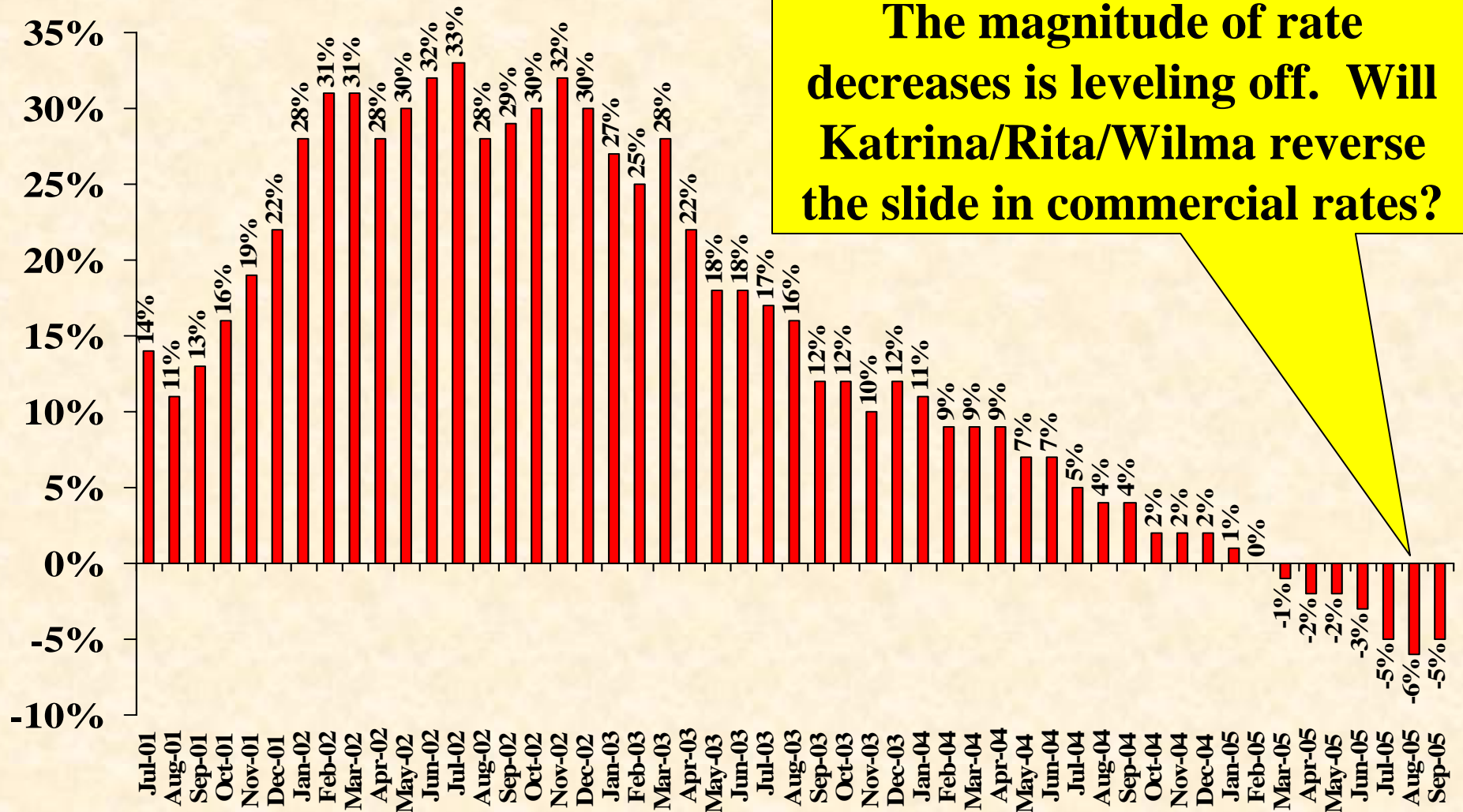
Note: Shaded areas denote hard market periods.

Source: A.M. Best, Insurance Information Institute

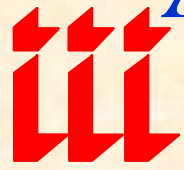
*2005 figure is III forecast based on 05H1 result.



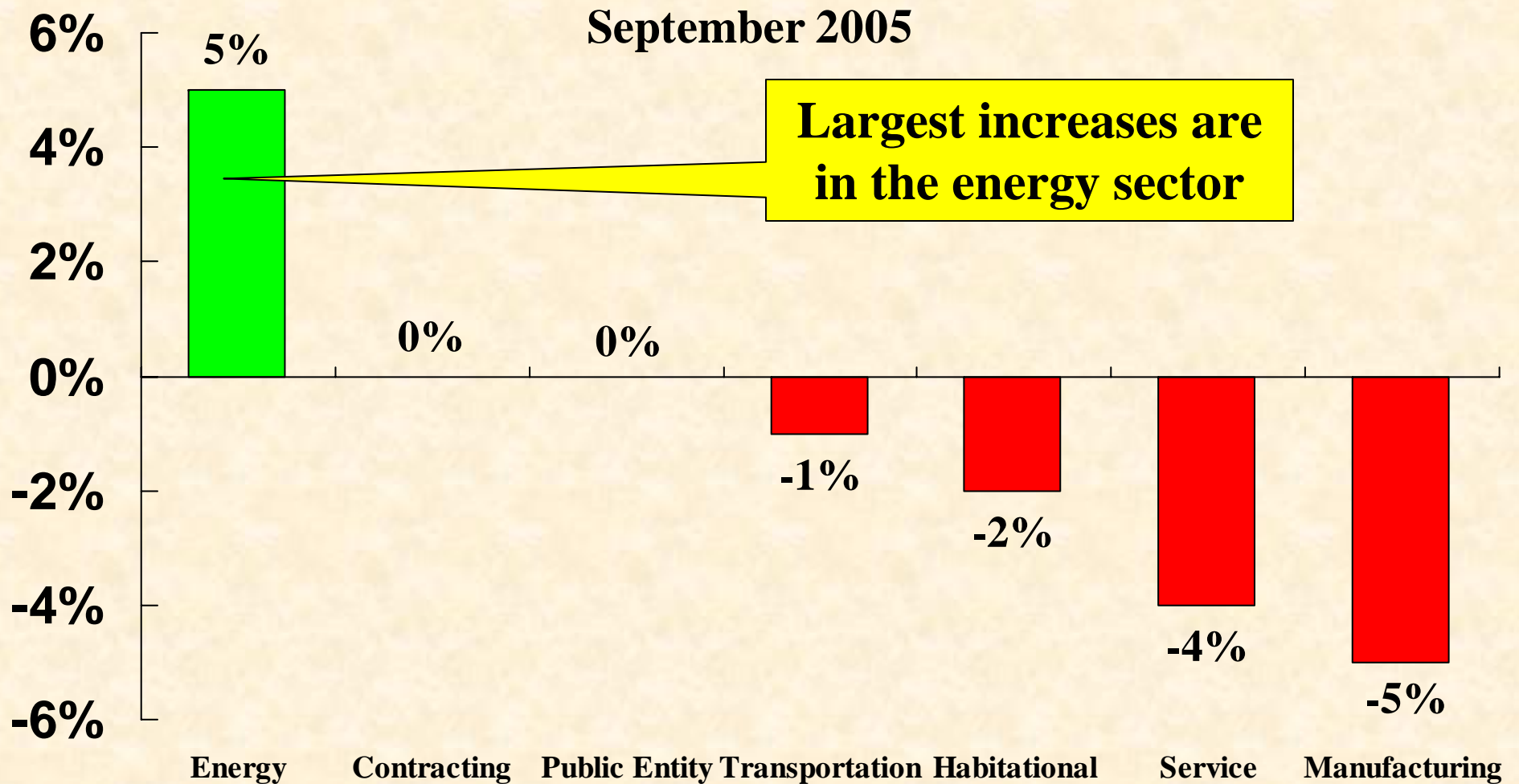
Commercial Premium Rate Changes Are Sharply Lower



Source: MarketScout.com



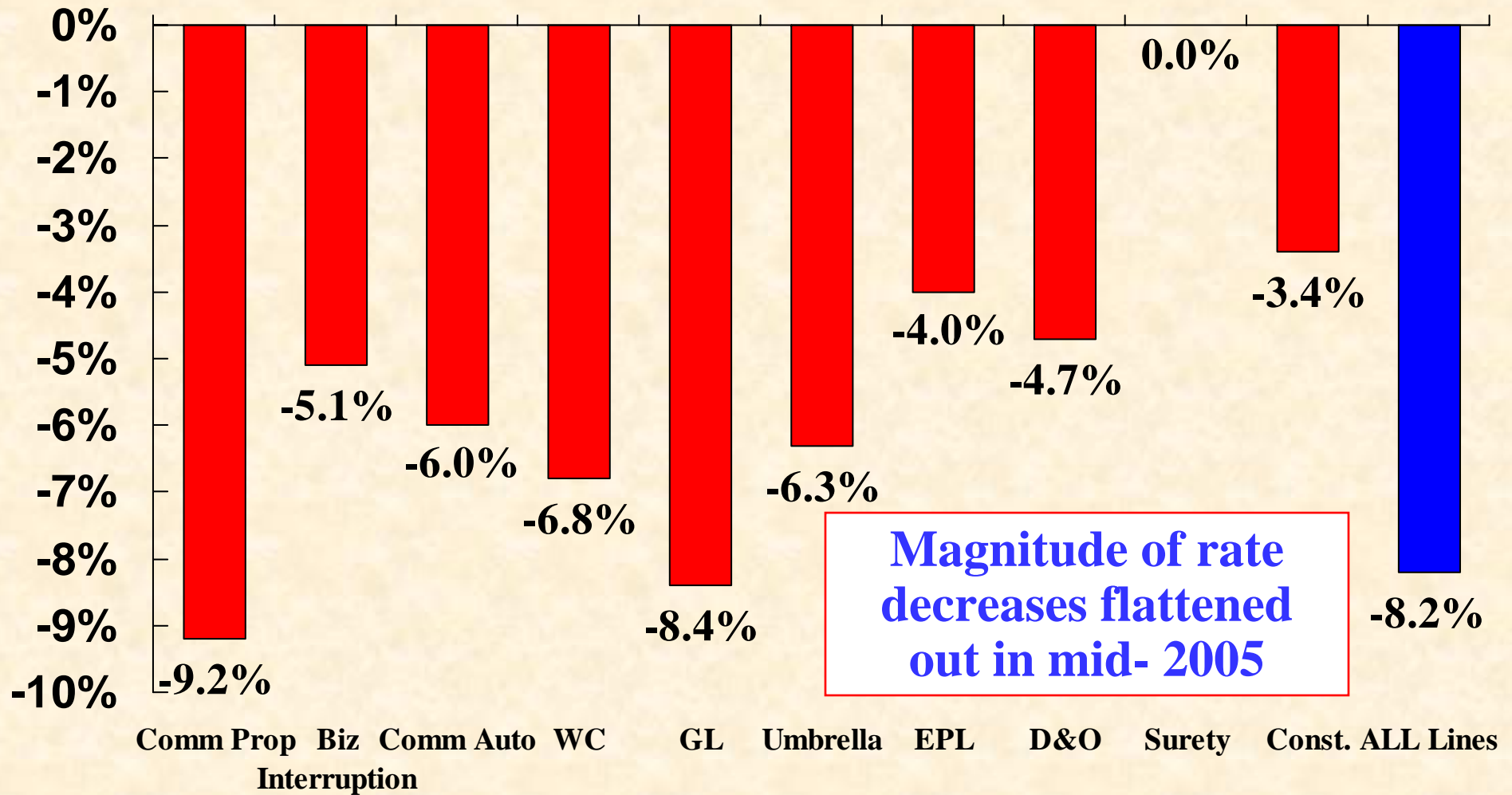
Average Rate Increase/Decrease by Industry Class



Source: MarketScout.com



Rate Changes by Line, 3rd Qtr. 2005

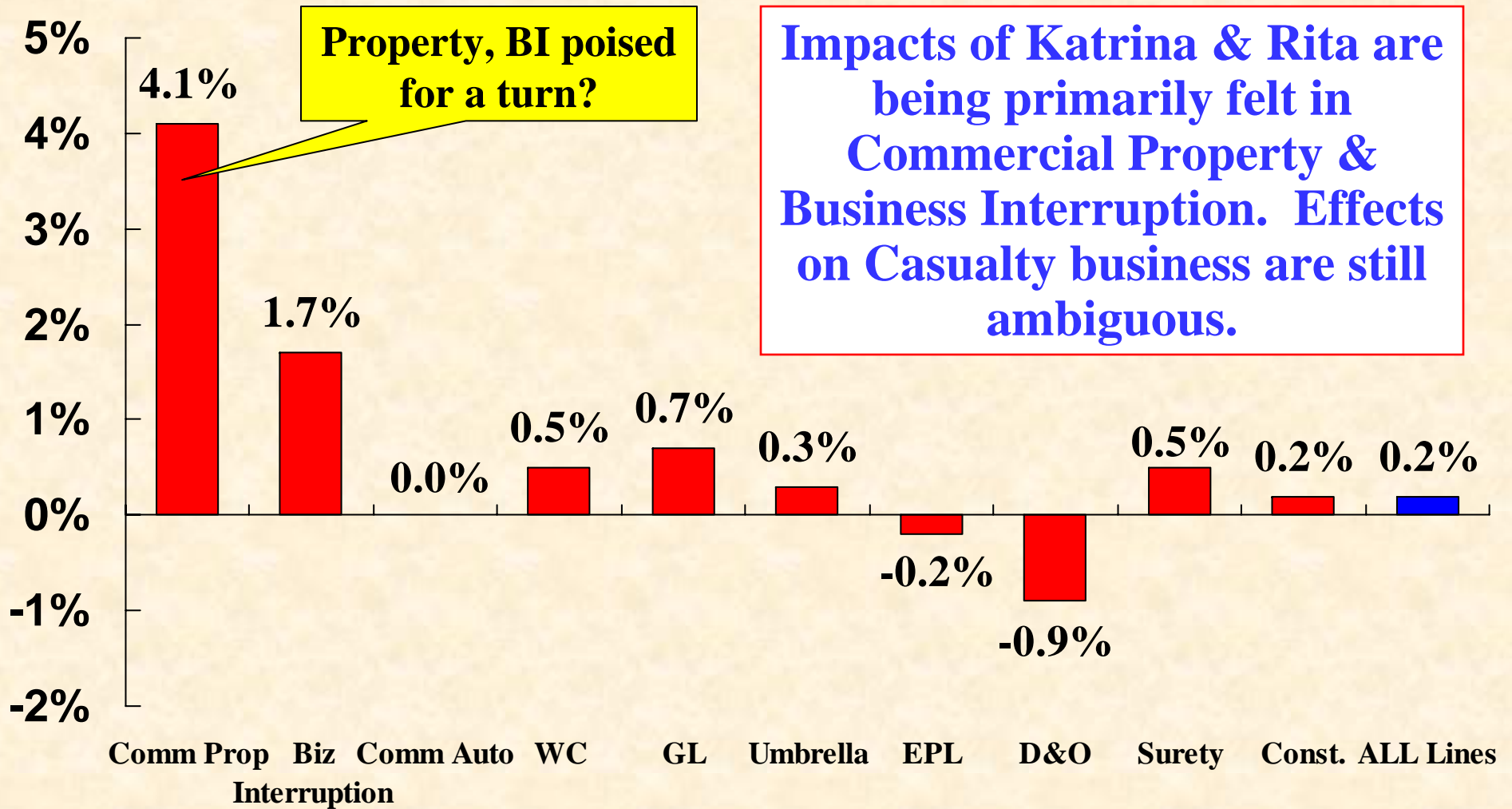


Source: Council of Insurance Agents & Brokers; Insurance Information Institute



Absolute Change in Price by Line,

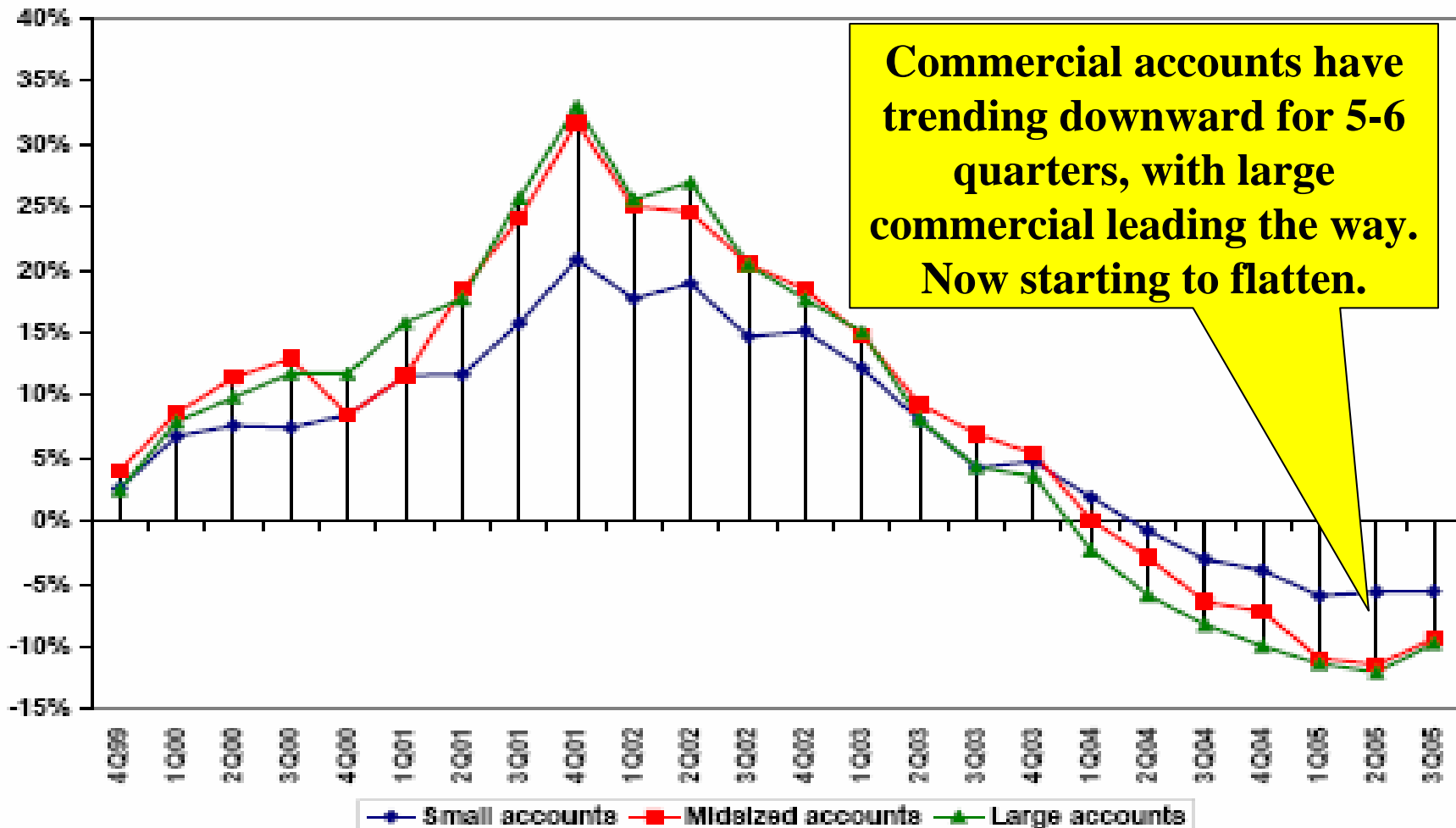
3rd Qtr. 2005 vs. 2nd Qtr. 2005



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

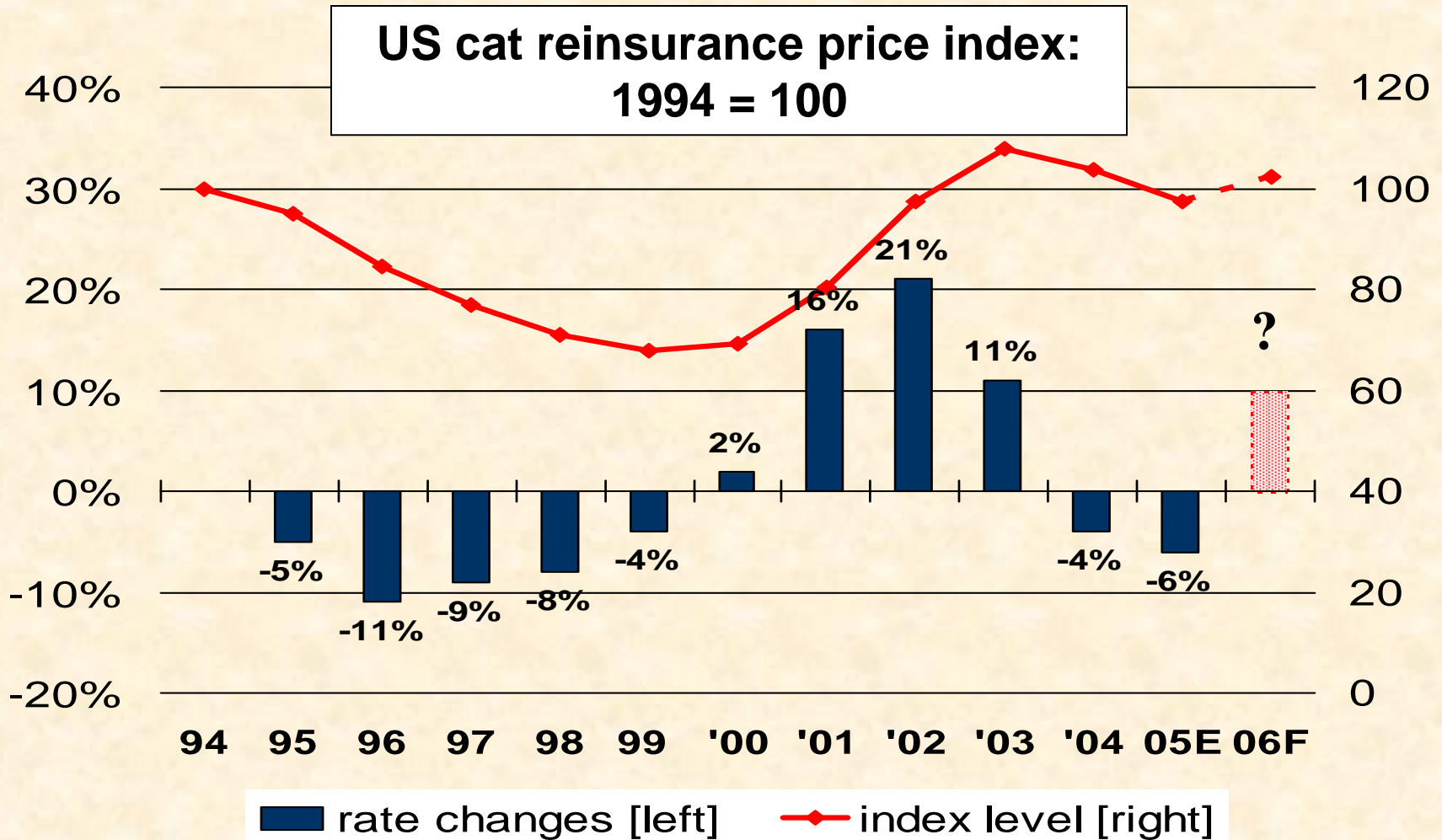


Average Commercial Rate Change by Account Size





Reinsurance Prices are Only at 1995 Levels, Despite Increased Risk



Sources: Swiss Re, Cat Market Research; Insurance Information Institute estimate for 2006.

Focus on the Energy Sector

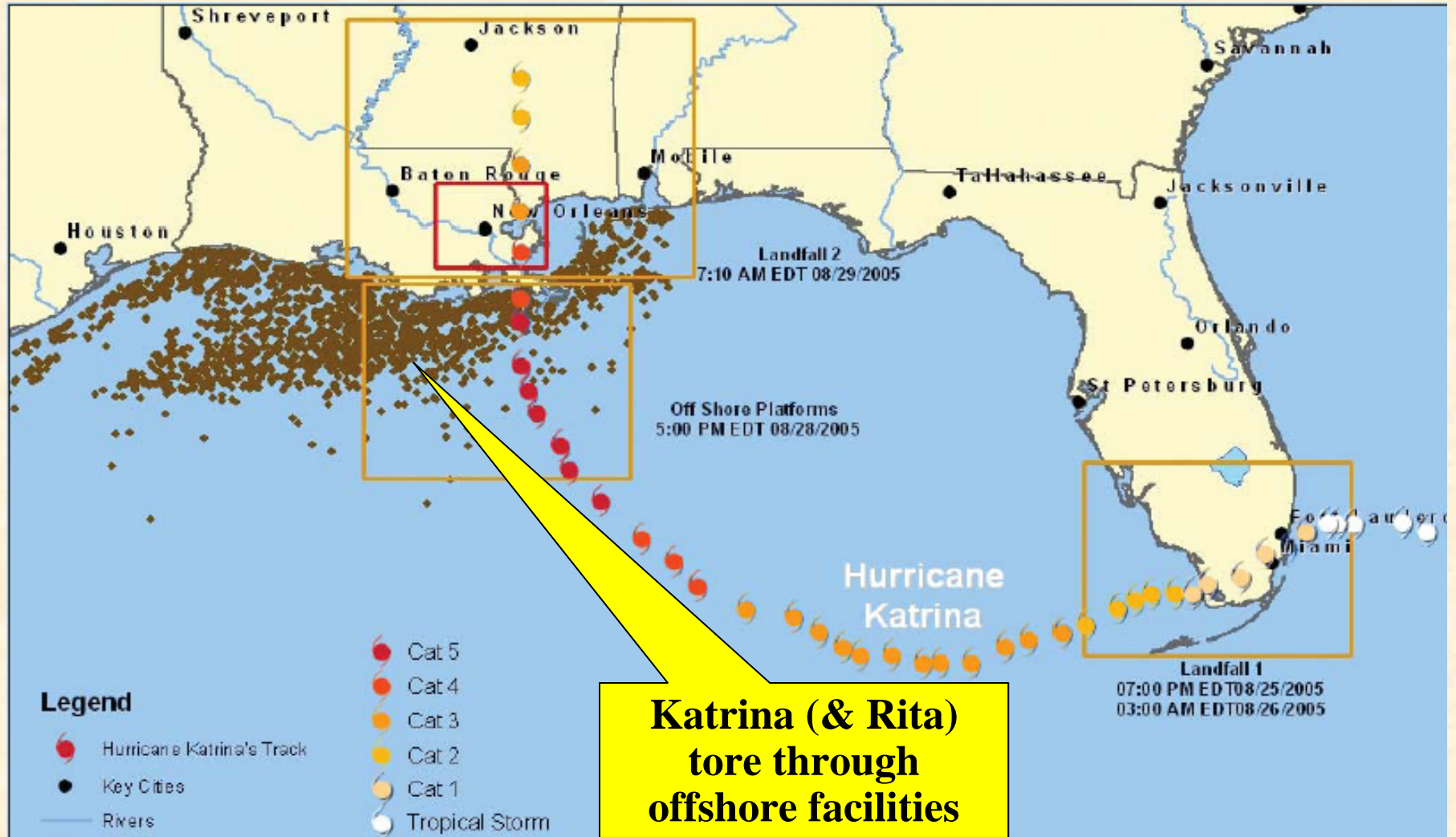


A wrecked oil platform washes ashore in Alabama in the wake of Hurricane Katrina.





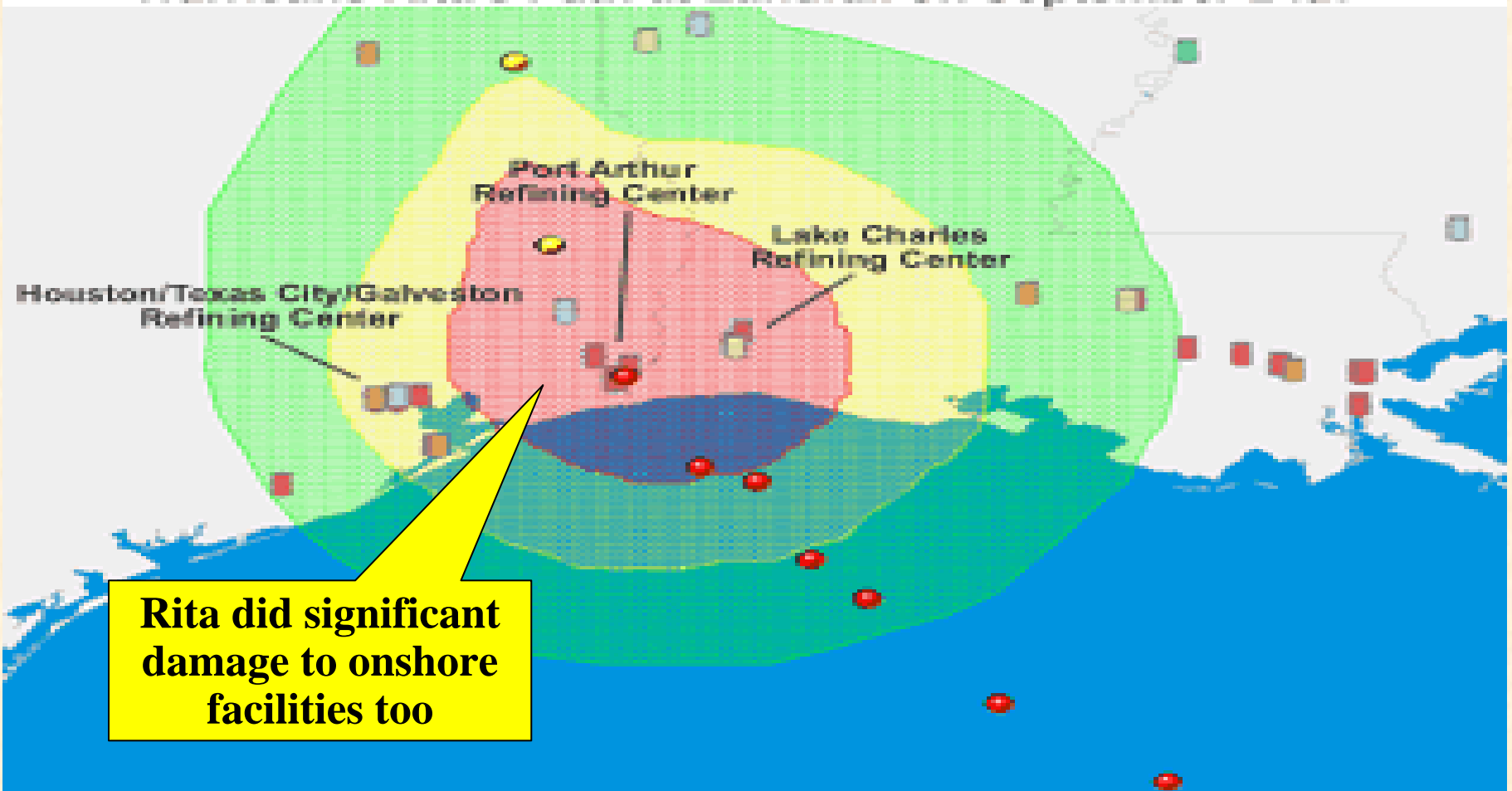
Katrina's Path of Destruction Through the Offshore Energy Industry



Source: "Hurricane Katrina: Profile of a Super Cat," RMS, October 2005.

Hurricane Rita's Path Was at Least as Devastating for Energy Concerns

Hurricane Rita's Path at Landfall on September 24th

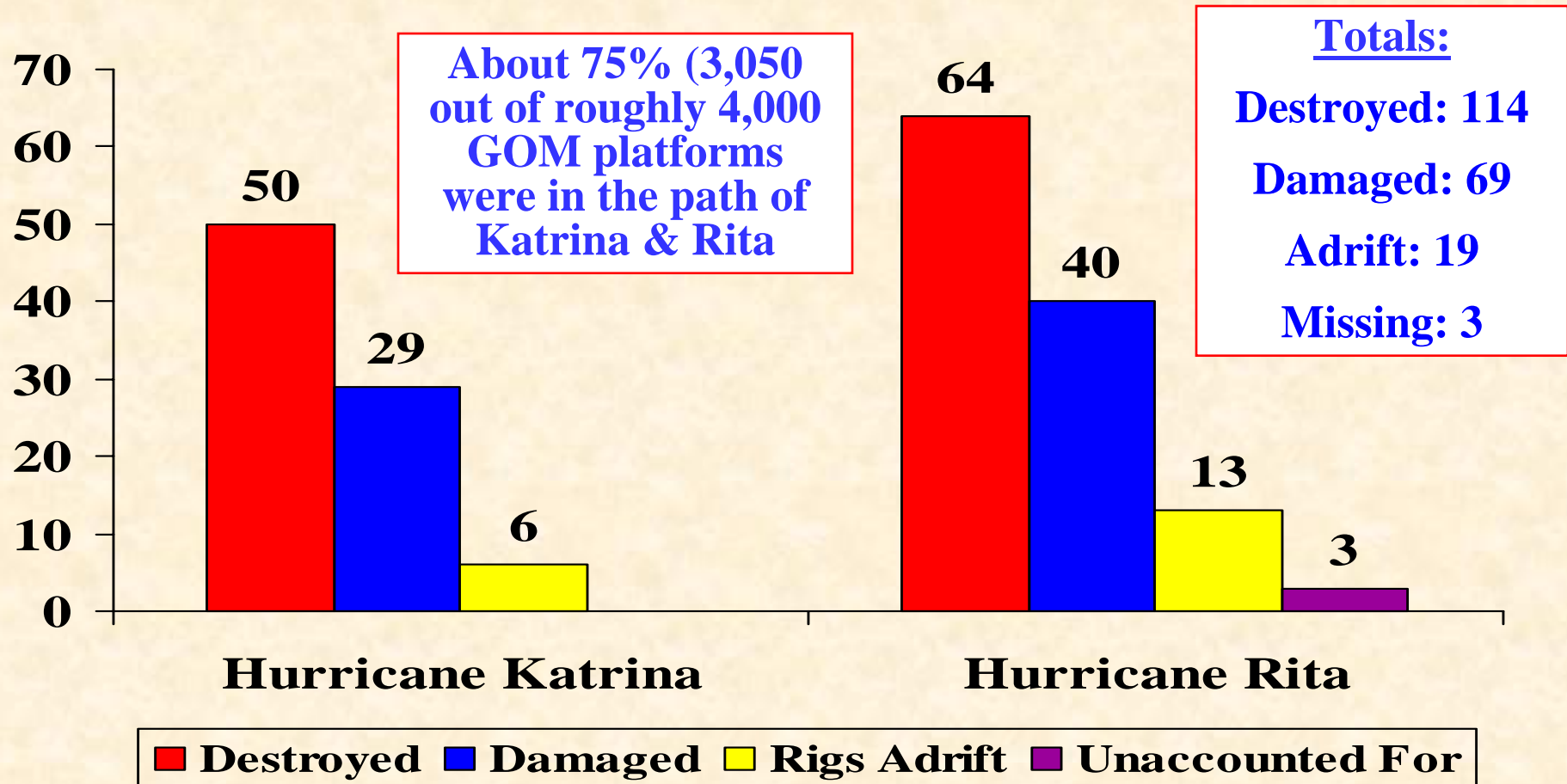


Source: Energy Information Administration; iMapData Inc.



Hurricanes Katrina/Rita: Damage to Oil Platforms and Rigs in Gulf of Mexico

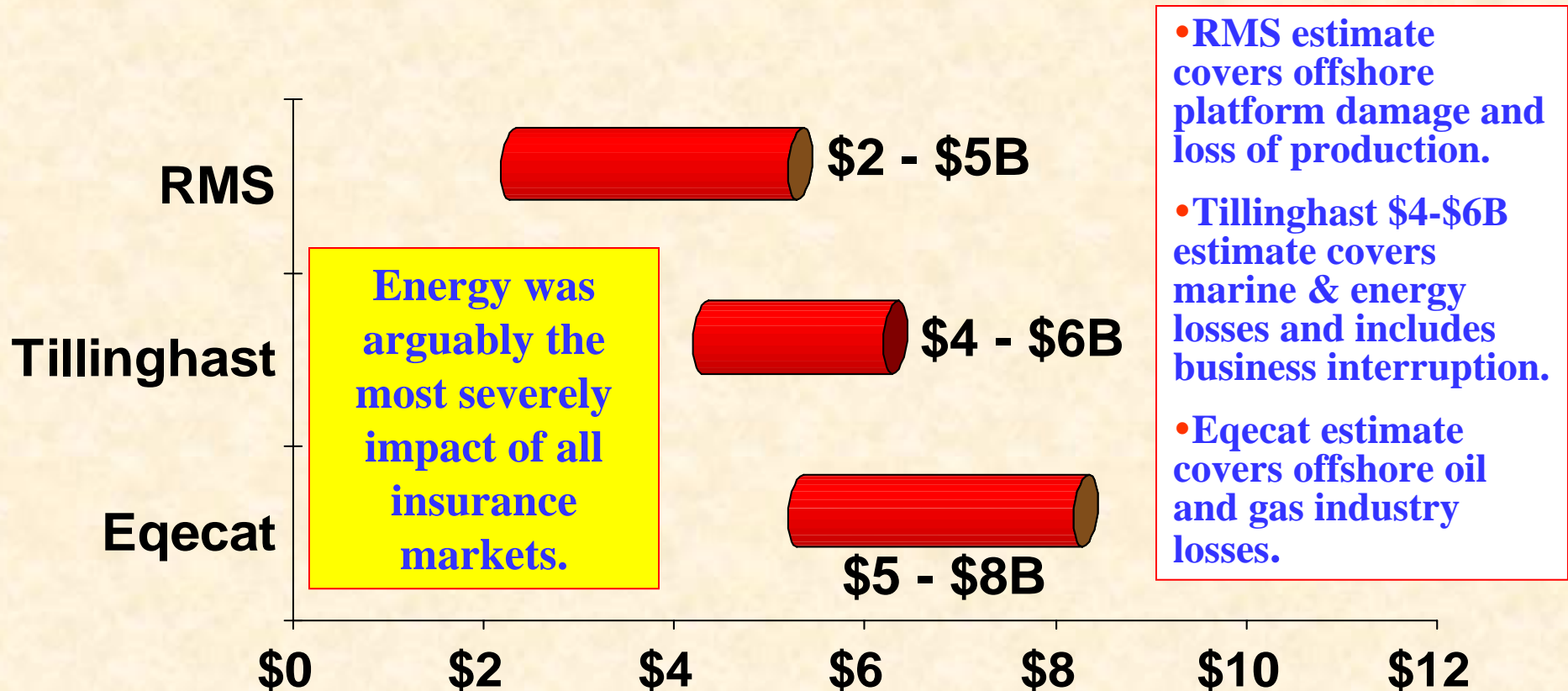
No. of Platforms/Rigs Destroyed, Damaged or Adrift, as of October 4, 2005.





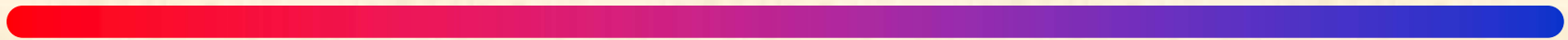
Hurricane Katrina Energy Insured Loss Estimates

(Billions of \$, As of October 10, 2005)



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

*Legal Environment
Will Affect
Katrina's Outcome*





Business Leaders Ranking of Liability Systems for 2005

Best States

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

New in 2005

ND, IN, SD, WY

Drop-Offs

ID, UT, NH, KS

Worst States

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

Newly Notorious

HI, FL

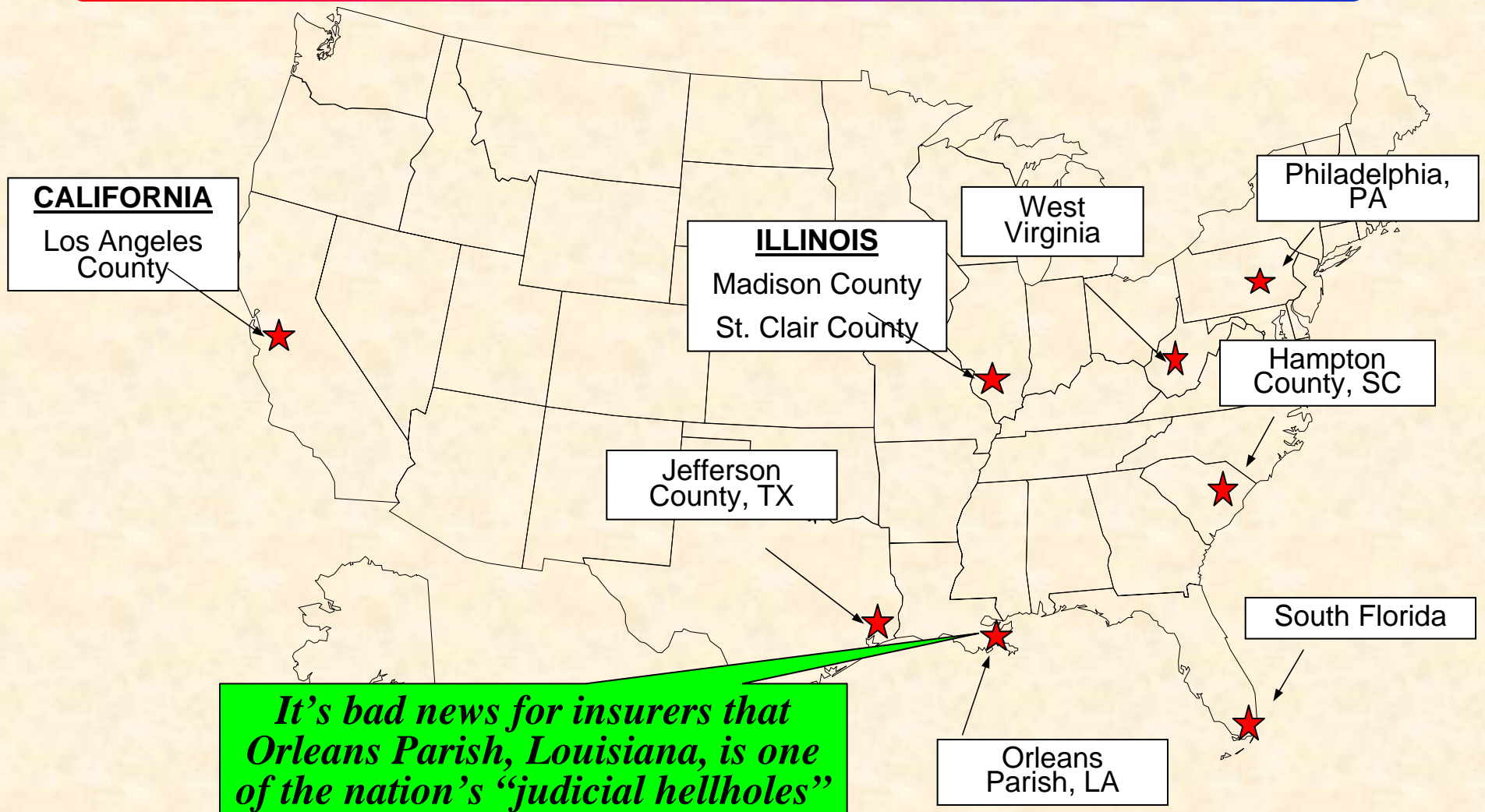
Rising Above

MO, MT

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



The Nation's Judicial Hellholes



Source: American Tort Reform Association; Insurance Information Institute



Accusations by MS Attorney General Jim Hood Against Insurers

- **Count 1: Violation of the Public Policy of the State of Mississippi**
 - Alleges flood exclusion is void since MS contract law does not allow exclusions that interfere with proximate cause
- **Count 2: Unconscionability**
 - Contracts (policies) are unreasonably complex
- **Count 3: “Water Damage” and/or “Flood” Exclusions are Ambiguous**
 - Alleges exclusions are ambiguous when read in conjunction with other policy provisions.
- **Count 4: Violation of MS Consumer Protection Act**
 - Alleges contracts (policies) are deceptive
- **Count 5: Irreparable Injury**
 - Alleges insurer enforcement contracts has and continues to harm MS policyholders



Types of Lawsuits Being Filed in the Wake of Hurricane Katrina

• **Homeowners Insurance**

- Lawyers (e.g., Dicky Scruggs) and Mississippi Attorney General Jim Hood are suing insurers over whether homeowners policies should cover flood.
- TX judge ordered one company to stop denying claims to people claim for additional living expense who could not provide immediate documentation of damage.
- Insurer being sued for not informing flood customer that excess flood coverage may have been available from a different private insurer

• **Oil Spills**

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

• **Fishing Grounds**

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

• **Wetlands**

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

Source: *Wall Street Journal*, 9/26/05, p. B1; *Houston Chronicle*, Oct. 12, 2005; Insurance Information Institute



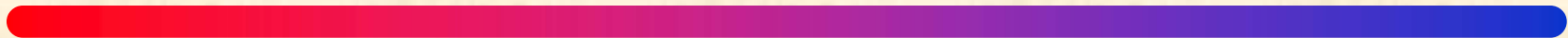
Typical Flood Exclusion in Homeowners Insurance Policy

- **Flood Exclusion**

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

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

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





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

- 1. National Natural Disaster Pool**
- 2. Regional Natural Disaster Pool(s)**
- 3. Federal Reinsurance Program**
- 4. Tax-Favored Pre-Event Reserving**
- 5. Personal “Savings” Accounts for Disaster Losses**

Regulators’ “Layered Approach”

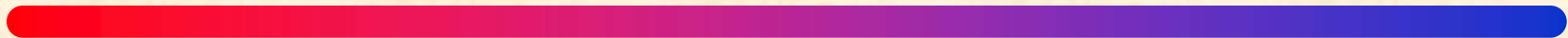
- 1. Max private insurer & reinsurer capacity**
- 2. State CAT funds**
- 3. Federal reinsurance facility**



Pros/Cons of Federal CAT (Re) Insurance Facility

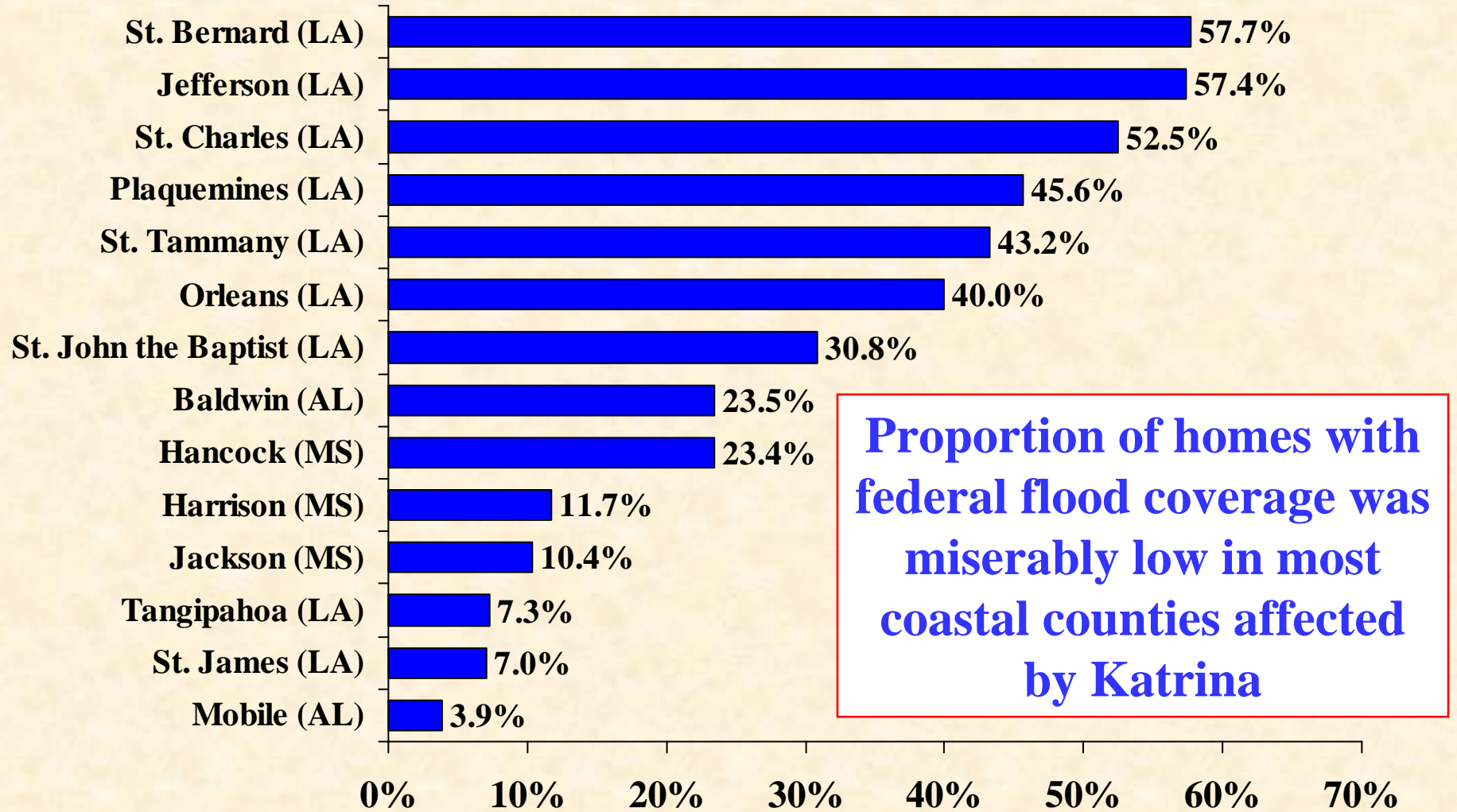
- **Rationale *FOR* Federal Involvement**
 - Insurance was not meant to handle mega-catastrophes
 - Such risks are fundamentally uninsurable
 - Federal government already heavily involved in insuring against weather-related mega-catastrophes (e.g., flood, crop)
 - Insurers are not allowed to charge risk appropriate rates (including rising reinsurance costs)
 - Price/availability of private reinsurance is volatile
- **Rationale *AGAINST* Federal Involvement**
 - Crowds-out pvt. insurance/reinsurance markets; stifles innovation
 - Relationship between price and risk assumed is diminished since fed insurance programs are seldom actuarially sound
 - Increases federal involvement and regulatory authority in p/c insurance (*not a negative for some market participants*)
 - Cost to US Treasury (esp. taxpayers in less disaster prone states)
 - Diminishes incentives for mitigation, tougher building codes and wiser land use policies if Fed rate are politically influenced

FEMA's National Flood Insurance Program





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



Source: Census Bureau, FEMA, New York Times.



What Needs to Happen for the NFIP To Be More Effective

- **Move to actuarially based rates**
 - **Include loading to build-up reserve fund**
 - **Expand refusals on irresponsible construction & repeats**
- **Expand mandatory purchase requirements beyond 1-in-100 year flood plain (250 or 500-year plain)**
- **Update & digitize flood maps**
 - **Need process for continuous updating**
 - **Coordinate inundation & flood maps**
- **Create/formalize central lender property tax-based authority for tracking properties subject to mandatory purchase requirement**



Summary

- **2005:H1 was likely the p/c insurance industry's zenith in the current cycle for underwriting/earnings**
- **Industry was financially strong and well capitalized pre-Katrina**
- **2005 CATs unlikely to provoke widespread hard market conditions (only about 5% of global p/c capital)**
- **Effects mostly confined mostly to specific lines & regions: HO, Commercial Property, Property CAT Reinsurance & retrocessional markets, PPA Comprehensive; Energy/Marine**
 - **Areas most impacted are Gulf & Atlantic coasts**
- **Cyclical concerns will quickly return as dominant issue**
- **Rising investment returns insufficient to support deep soft market in terms of price, terms & conditions**
- **Clear need to remain more underwriting focused**
- **Major Challenges:**
 - **Maintaining price/underwriting discipline**
 - **Managing variability/volatility of results**
 - **New/emerging/re-emerging risks**



*Insurance Information
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