



PREPARING FOR AND PROTECTING AMERICA FROM CATASTROPHE

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**STATEMENT OF**

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**Before the**

**House of Representatives Committee on Financial Services**  
**Subcommittee on Housing and Community Opportunity**  
**and**  
**Subcommittee on Capital Markets, Insurance, and Government**  
**Sponsored Enterprises**

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## Statement for the Record

Mr. Chairman, Ranking Member Bachus, and members of the committee, I want to thank you for the opportunity to appear before you today to discuss ways to better prepare and protect American families from the devastation caused by natural disasters. Congressman Klein, I also want to thank you for your leadership on this very important issue.

As you know, I am no stranger to the field of disaster management and emergency preparedness. I was honored to serve as the Director of FEMA under the Clinton Administration from 1993 until 2001. Today, I will speak to these issues in my capacity as co-chairman of ProtectingAmerica.Org, an organization formed in 2005, to raise the national awareness about the important responsibility we all have to prepare and protect consumers, families, businesses, and communities from natural catastrophes.

My fellow co-chairman is Admiral James Loy, former Deputy Secretary of Homeland Security and Commandant of the U.S. Coast Guard (Ret.). Together we have built a coalition and campaign to create a comprehensive and integrated management solution that protects homes and property at a lower cost, improves preparedness, and reduces the financial burden on consumers and taxpayers – all in an effort to speed recovery, protect property, and save money and lives. There are over 300 organizations in our coalition including the American Red Cross, the International Association of Fire Fighters, State Farm, Allstate, municipalities, small businesses, Fortune 100 companies, and more than 20,000 individual members. The membership is truly broad, diverse, and representative of virtually every state in the nation.

We all believe that this hearing is timely. With headlines around the world relaying stories from the recent tragedies in both Haiti, Chile and on Monday, Turkey, many here at home are taking a harder look at whether or not we would be prepared if a similar catastrophic event were to happen in the U.S.. Unfortunately, recent experiences, such as the aftermath of Hurricane Katrina in 2005, as well as the continuing economic troubles in our housing and lending sectors prove that we have a lot of work to be better prepared.

A catastrophic event, whether an earthquake striking one of our great American cities, or a massive hurricane making landfall near any of the metropolitan areas from New York to Houston, would cause such enormous damage that our economy would be stunned, private resources quickly depleted, and an immediate federal bailout of hundreds of billions of dollars could potentially be required. This Committee is very familiar with the fact that the American taxpayers have lost their appetite for bailouts. As a result, they would be far better served by a program that uses private insurance dollars to pre-fund coverage for the eventuality of a catastrophic natural catastrophe.

I believe that there are three key points critical to any comprehensive solution to the homeowners' insurance crisis.

First, a National Reinsurance Program will generate additional capacity, bring more stability to the market, make high-quality insurance more available, and ensure that consumers realize

significant cost-savings on their homeowners insurance. The best way to accomplish this is to enable and encourage more states to create well-structured, actuarially-sound catastrophe funds and to supplement the protection offered by the current state catastrophe programs in California and Florida.

To deliver meaningful premium savings for consumers and to allow for the maximum use of the reinsurance by differing programs in multiple states, the reinsurance provisions of the national program should allow flexibility on the attachment point. In addition, the Committee may wish to consider alternative means to fund the reinsurance program other than upfront appropriations of the entire potential liability since the odds of incurring this liability are very small. This is one area of the bill we believe can be improved by placing a lower federal catastrophic attachment point to provide a seamless level of protection for policy holders.

Second, Catastrophe Obligation Guarantees will provide helpful support to the debt issuances of state programs that could serve those programs well in distressed market conditions. The guarantee or loan concepts should be constructed to work together seamlessly with the reinsurance program. They should complement each other, with the guarantee and/or loan option covering a certain layer of loss and the reinsurance option another.

Finally, we believe that a hybrid approach to the prevention and mitigation provisions is important. This approach would keep the program under Housing and Urban Development (HUD) but incorporate a privately financed National Catastrophe Fund that provides significant investment income to groups like the Red Cross and others. We are pleased to have been working with the Committee to strengthen this particular piece of the legislation.

To state it simply, the status quo is not acceptable. A 2009 report by Jonathan Orszag, an economist who formerly served on President Clinton's National Economic Council, found that the current system for post-catastrophe financial preparedness is riddled with inefficiencies and there is a significant gap between the ability of the private insurance and reinsurance sectors to provide the protection that is required. Specifically, Mr. Orszag found that the current system is an ad hoc, backward-looking program that makes the government and the taxpayers, essentially, the insurers of last resort. Further, his report suggests that a better approach would be one that not only assures that resources are available to fund recovery, but also funds prevention, mitigation, and preparation.

To that end, we support a comprehensive, integrated plan linking a national catastrophe fund with support to first responders as well as strong education and mitigation provisions. A national catastrophe fund will create a privately financed and federally-administered layer of reinsurance to complement and stabilize private market reinsurance alternatives, and ensure greater availability and affordability for consumers of residential property insurance. It will do so by acting as a backstop for state catastrophe funds, which will protect the private market from collapse and ensure that resources are available to rebuild after a major catastrophe. In addition, it will save your constituents money on their homeowners' insurance and help states better manage the risk associated with mega-catastrophes, which are essentially uninsurable in the private market due to the timing risk.

Qualified state funds would also be able to purchase reinsurance from the national program. Rates for this coverage would be actuarially based and would only be available to state programs that have established the mandatory prevention and mitigation funding. In the event that a catastrophe strikes, private insurers would be required to meet all of their obligations to their policyholders. Should catastrophic losses exceed those obligations, the state catastrophe fund would be utilized. In the event of an extraordinary catastrophe, the national backstop program would provide benefits to the state and help pay remaining claims.

Because this is a state-by-state program based entirely on risk, the likelihood of a taxpayer subsidy is virtually eliminated. This approach requires pre-event funding and relies on private dollars from insurance companies in the areas that are most exposed to catastrophe. This approach is far preferable to the de facto bailout we have witnessed with natural disasters in recent memory. Following the devastation caused by Hurricane Katrina, a Brookings Institution study found that after-the-fact recovery funding resulted in an enormous taxpayer subsidy for effected uninsured and underinsured properties – of the first \$85 billion in taxpayer dollars spent more than \$10 billion funded losses for families lacking coverage.

ProtectingAmerica.org believes that a national catastrophe fund would also buffer the already fragile housing and lending markets during this time of economic downturn. The approach proposed in H.R. 2555 would reduce the threat of insurer insolvency and enhance the industry's capacity to pay claims. This in turn would create an important measure of stability to the catastrophic insurance industry and mitigates the shock to the U.S. economy that a major natural disaster might otherwise produce.

We recognize that not all areas of the country face equal threats of exposure to natural catastrophe. A recent report by Protecting America.org analyzed the demographic profiles of residents of counties that have been significantly affected by hurricane damage in recent years. The report found that persons who are most likely to be impacted by catastrophic events are disproportionately African American, poor, and living in homes with values well below state and national averages. This further reinforces the need for strong, complementary readiness, preparedness, and mitigation provisions. Ideally, the plan would require the national and state catastrophe fund to dedicate a significant portion of its investment income to local communities and non-profits to support efforts like building code development and enforcement, improved preparedness education and training, and additional equipment and personnel for first responders.

When catastrophe strikes, our response programs, such as those through the American Red Cross, do a remarkable job of getting victims into shelters and mobilizing emergency supplies and personnel so that the situation does not get worse.. All Americans, regardless of whether or not they have been victimized by catastrophe, owe our first responders an enormous debt of gratitude. Their service is invaluable. Clearly, programs that would improve preparedness, increase public education, enhance prevention and mitigation programs, and augment support for first responder programs would improve our national capability to prepare and protect those of us who live in harm's way.

I truly believe that this needs to continue to be a top national priority. It reflects strong leadership to act before the next crisis. It is time for the federal government to take action on this important issue and with your assistance, we can, together, get this critical legislation passed into law. Congressman Klein, thank you again for your leadership and continued persistence on this important issue, and thank you again to the Committee for this opportunity to testify. I would be happy to answer any questions that you may have.