THE HILL

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A catastrophe waiting to happen

By Jonathan Orszag

Although the 2009 hurricane season was a reasonably quiet one, the question still remains: Are we prepared as a nation for the next mega-catastrophe that will inevitably strike our country?

In one key respect, we are better prepared than when Hurricane Katrina roared through the Gulf states. We remember all too well the fumbling among the governmental entities involved with coordinating a response to the aftermath of Katrina. Fortunately, improvements have been made that will help the various levels of government more effectively work together following the next major natural catastrophe.

However, with respect to America's financial ability to respond, react, and recover from the occurrence of another massive natural catastrophe, we are no better off than we were four years ago, and, indeed, are in some ways exposed to a more precarious economic condition than ever before.

Earlier this year, I conducted a study with a colleague of mine, Doug Fontaine, in which we looked at the many significant issues that hinder the traditional insurance system from providing adequate and affordable coverage for the six in 10 American families that live in areas that have sustained massive hurricanes or devastating earthquakes.

This is an area of uncertainty rife with concerns about so-called timing risk (that is, when a natural catastrophe will happen) and the unpredictability of truly massive events (for example, how much destruction they will cause). The system is affected tremendously by global capital markets that are dominated by unregulated offshore risk underwriters. It is an inexact market that balances the information garnered from computerized risk analyses, the demand for capital from competing interests in all parts of the world, and the likelihood that a completely unpredictable act of Mother Nature could strike anywhere at any time.

Anywhere: A hurricane can hit many major American cities, such as Miami, Houston, or even New Orleans again. Earthquakes could devastate cities such as San Francisco, Los Angeles, Seattle or St. Louis.

Any time: We cannot control when a major natural catastrophe hits — it could be this year, next year, or sometime far into the future.

With the knowledge that an event will happen and an understanding that some of the most densely populated and economically significant cities in America are located in vulnerable areas, policymakers at the state and federal level should be "on notice" to take steps now to prepare for these events.

Action is needed because the current system for financial preparedness is riddled with inefficiencies and there is a significant gap between the ability of the private insurance and reinsurance sectors to deal with the financial consequences of major natural catastrophes and the protection that is required.

The inability of the current system to deal with mega-catastrophes inserts the federal government into the effective role of the insurer of last resort against major catastrophes in a way that is aptly characterized as ad hoc, backward-looking and unnecessarily inefficient.

In the aftermath of an event, such as Katrina, taxpayers from every corner of America help subsidize the uninsured and under-insured losses that occur in the devastated areas to the tune of tens of billions of dollars.

There is a better way. The federal government should implement a forward-looking policy that starting today prepares us financially for the catastrophes that we know are coming. One effective policy option is contained in legislation known as the Homeowners' Defense Act of 2009 (HDA), a bill introduced in the House and supported by then-Sen. and presidential candidate Barack Obama.

The HDA proposes a privately funded public partnership that helps to pre-fund the financial costs of a large-scale natural catastrophe. HDA simultaneously facilitates the risk participation of the private sector, expands the availability and sustainability of the catastrophic insurance system, and provides more potent incentives for residential property owners to undertake catastrophe loss mitigation efforts.

Our study, which was commissioned by ProtectingAmerica.org, found that this approach should add capacity, increase stability and lower costs overall. From an economic perspective, such an alliance of public and private resources best approaches the optimal manner to address the inefficiencies that plague the present system of federal disaster relief.

The type of integrated public-private partnership proposed in the HDA has the potential to expand greatly the available coverage for catastrophic events to more consumers at lower prices, while providing more stability to the insurance and reinsurance sectors (which would help alleviate the adverse shock to the U.S. economy that a major natural catastrophe could produce). According to one estimate based upon an earlier version of the HDA, direct reductions in homeowners' insurance premiums could exceed $11 billion annually, in part by encouraging greater use of reinsurance by state catastrophe plans.

We know that another major natural catastrophe will strike. Unfortunately, there is nothing we can do to change that. What we can do is prepare financially today for the catastrophe of tomorrow. If we don't, we are just allowing another catastrophe — this one man-made and financial — to happen.

Orszag is senior managing director at Compass Lexecon LLC, an economic consulting firm, and former economic policy adviser on President Bill Clinton's National Economic Council.

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Bill would share states' disaster cost

By Eun Kyung Kim
Gannett News Service

WASHINGTON — The recent wildfires in Southern California have raised the profile of legislation that would create a national catastrophe fund and potentially curb soaring insurance rates in disaster-plagued states.

The fires illustrated that the legislation, crafted by two House Democrats from hurricane-prone Florida, has appeal far beyond the state, supporters say.

"It's more than just Florida; it's more than just hurricanes," said Ed Collins of ProtectingAmerica.org. "It's all about protecting consumers and, frankly, taxpayers."

The Homeowners Defense Act, as the bill is formally known, is expected to go for a vote this week on the House floor. If passed, it would be the first such program, despite dozens of attempts.

Participating states would pool together to sell catastrophe bonds and reinsurance contracts to the private market. The program also would provide federal loans to states hit hard by disasters.

Much of the insurance industry opposes the bill, saying it could crowd out private industry.

"We'll always have a concern when any government entity interferes with the private market," said Dennis Kelley of the American Insurance Association.

The White House opposes the bill and has promised a veto.

Allstate applauds House passage of landmark Homeowners' Defense Act H.R. 3355

Prepares and protects America from major natural catastrophes.

BusinessWire

NORTHBROOK, Ill. — Allstate Insurance Co. last week lauded U.S. House passage of a bill designed to prepare and protect communities ahead of major natural catastrophes. The Homeowners' Defense Act of 2007 (HR 3355), approved Thursday by a wide margin, offers a comprehensive solution to communities hit by catastrophic events such as massive hurricanes, earthquakes and wildfires.

"We applaud this first step in creating a public and private partnership to properly address the devastation caused by large natural disasters. The current system was created before the recent warming of the oceans and is no longer adequate to deal with the increased frequency and devastation caused by hurricanes. This bill will help the 60 percent of Americans who live in danger of hurricanes or earthquakes destroying their homes, without requiring major support from low risk areas," said Tom Wilson, Allstate's chief executive officer. "We are proud to be a part of ProtectingAmerica.org, which has more than 300 members that have been actively advocating solutions to this problem."

The Homeowners' Defense Act establishes a national catastrophe program to increase access to insurance and protect consumers. The bill provides for federal loans and a financial backstop to state catastrophe funds that will help provide more protection at a lower cost to consumers. This encourages states to properly structure insurance regulations and pricing to accurately reflect risk. If losses exceed a fund's financial capacity, then the role of the federal government would be determined in advance of a loss.

"Passage of this landmark legislation provides additional momentum needed to bring this concept to reality," Wilson said. "Now that a companion bill has been introduced, we urge the Senate immediately to begin to take the additional steps needed to address this top national priority."

The Allstate Corp. (NYSE: ALL) is the nation's largest publicly held personal lines insurer. Widely known through the "You're In Good Hands With Allstate" slogan, Allstate helps individuals in approximately 17 million households protect what they have today and better prepare for tomorrow through approximately 14,600 exclusive agencies and financial representatives in the U.S. and Canada. Customers can access Allstate products and services such as auto insurance and homeowners insurance through Allstate agencies, or in select states at allstate.com and 1-800 Allstate. Encompass and Deerbrook Insurance brand property and casualty products are sold exclusively through independent agents. The Allstate Financial Group provides life insurance, supplemental accident and health insurance, annuity, banking and retirement products designed for individual, institutional and worksite customers that are distributed through Allstate agencies, independent agencies, financial institutions and broker-dealers.

The problem of natural disasters

What to do about natural disasters? We can't really prevent them and while many people are skeptical about dire predictions regarding climate change as the probable cause of an increase in weather-related catastrophes, others are convinced that we are indeed in for more and stronger "stormy weather" as a result of global warming.

Whatever the reason for their cause, natural catastrophes rack up big bills, for insureds and non-insureds alike. For those whose property is fully covered for wind, fire, hail and water, insurance should be there to pick up the pieces after disasters like this summer's massive flooding and tornadoes in the Midwest and South Central states, and wildfires in the Southeast and West. But what if — for whatever reason — it is not?

Greensburg, Kan. May 23, 2007. Photo by Greg Henshall / FEMA

After the onslaught of hurricane-related losses from 2004 and 2005, the question of how to pay for recovery after natural disasters has been raised time and time again. A bill — H.R. 3355, the Homeowners' Defense Act of 2007 — recently was introduced in the U.S. House of Representatives by Ron Klein (D-Fla.) and Tim Mahoney (D-Fla.), directed at providing relief from and planning for natural disasters through the use of state run catastrophe pools and private market mechanisms. Insurers for the most part expressed skepticism over such a plan, while agents say the legislation, while not perfect, is at least deserving of discussion. See page N2 for further analysis of H.R. 3355.

Whatever the reason for their cause, natural catastrophes rack up big bills for insuredsand non-insureds alike.

Meanwhile in this issue of *Insurance Journal*, our "Closing Quote" column, which regularly features contributed "opinions" by industry leaders, proponents of opposite sides of the national cat fund debate go back-to-back with arguments supporting both fully private and private-public mechanisms for insuring against natural catastrophes.

In "Closing Quote 'A'" on page 96, Dennis C. Burke, vice president, State Relations, with the Reinsurance Association of America, explains that the "private insurance market can pay and has recently paid extraordinary natural catastrophe losses." According to Burke, the private market is "the most efficient way to address and insure risk," and one that has proved itself time and time again.

Edward T. Collins, national director for ProtectingAmerica.org and managing counsel for The Allstate Corporation, on the other hand, thinks "we can do better." In "Closing Quote 'B'" on page 98, Collins says a strong "public-private partnership at the local, state and national levels is the best way to maximize the respective strengths of both the public and the private sectors." He says while the "current system seems to work well for some, especially unregulated foreign reinsurers," Collins believes that with the stakes climbing higher and higher, "reform is inevitable."

With Congress beginning to take action, the debate is underway. The question for each of us now is — will we join in the debate or let others decide?

Stephanie K. Jones

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Catastrophes: The time to act is now

By Edward T. Collins

Two years have passed since America's most shocking wake-up call regarding the devastation that follows the force and fury of Mother Nature. Since that time, a variety of legislative proposals have been offered at the state and national levels to address the shortcomings of our financial infrastructure, our first responder programs and our personal attitudes toward catastrophe preparation and protection.

The two years since Katrina hit have brought more and more policymakers to the clear and unambiguous conclusion that the status quo is unacceptable and that consumers and taxpayers deserve a better system.

Denying that a problem exists or offering as the solution to simply raise rates and hope for the best is unacceptable. The stakes are higher than ever. Reform is essential and inevitable.

We can do better. A stronger public-private partnership at the local, state and national levels is the best way to maximize the respective strengthens of both the public and the private sectors. The establishment of a comprehensive, integrated solution that leverages the public-private partnership model would provide more protection at lower cost to consumers.

The good news is that the solution is gaining momentum, and congressional leaders have predicted that a bill will be considered by the full House of Representatives by the end of the year. The solution is being embraced by a growing number of representatives from across the nation, including those who represent catastrophe-prone regions and others who represent lower-risk states who want to put an end to the massive policyholder and taxpayer subsidies upon which the current system relies.

Reports show that the typical taxpaying American family paid more than $800 to cover costs associated with Hurricane Katrina. That is an enormous nationwide catastrophe tax. We will probably always need some amount of public and charitable assistance to help catastrophe victims, but we propose a model that creates a new mindset and approach, reinforces the core America value of personal responsibility, and will reduce the cat tax.

The plan would be pre-funded and actuarially sound. The policyholder with risk would pay an actuarially-based rate that fully reflects all costs associated with the transfer of risk. The backstop would be operated on a tax-exempt and non-profit basis so it would cost much less to cover the losses that stem from massive natural events. No free lunch; just a less expensive way to better prepare and protect consumers.

Quality insurance for consumers would not only be more affordable but it would also become more available because primary insurers would be more willing to serve highly exposed areas with less fear of bankruptcy. This can reverse the current trend of a contracting primary homeowners insurance market and a growing residual market.

Moreover, we can help finance and facilitate other components of the solution at the same time. A small, but meaningful, portion of the investment income from the state and national backstop would provide a steady and dependable stream of funding for important mitigation programs like the establishment and enforcement of stronger building codes, effective retrofits and better land use planning. A portion of the investment stream would also be dedicated to provide additional funding for first responder programs so that families could be more effectively evacuated and so lives could be protected when catastrophe strikes.

The current system seems to work well for some, especially unregulated foreign reinsurers. It is, therefore, understandable why they would oppose change. However, we need to challenge their defense of the status quo, correct their mischaracterizations of what this solution is all about, and press forward to add capacity and improve stability, in a cost-effective way, beyond what the private reinsurance market alone can provide.

The exposure grows more and more extreme every year. The entire private homeowners insurance market faces a looming threat of total collapse if a major hurricane or series of hurricanes makes a direct hit on one of our metropolitan areas like Miami or New York. The same inevitability is true for major earthquakes, too, in California, along the New Madrid fault, and elsewhere.

> **Reports show that the typical taxpaying American family paid more than $800 to cover costs associated with Hurricane Katrina. That is an enormous nationwide catastrophe tax.**

Relying on state guaranty funds after such an event should give experts very little comfort. Even though these funds have broad assessment authority, this system assumes that enough insurers will remain capable of picking up the pieces following a potentially devastating event or series of events. They also assume these remaining companies, and their customers, will be able to absorb the potentially huge assessments that would be needed.

We can not responsibly ignore these threats. A stronger financial infrastructure is needed, and the time to act is now, before the next crisis.

Congress can't do this alone. Let's roll up our sleeves and work together to design a system that is fair to everyone and that creates a culture of preparedness, helps strengthen first responders, saves lives and protects the homes and communities that Americans spend their whole lives building.

Edward T. Collins is the national director for ProtectingAmerica.org, a member of the Board of Directors and the Executive Committee of the Institute for Business and Home Safety, and managing counsel for The Allstate Corporation.

Admiral James M. Loy, National Co-Chair
Former Deputy Secretary, Department of Homeland Security
Commandant, U.S. Coast Guard (Retired)

James Lee Witt, National Co-Chair
Former Director, Federal Emergency Management Agency
Former Chief Executive Officer, International Code Council

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For Further Details:
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America's Mayors Join the Call for National Catastrophe Fund
US Conference of Mayors to Congress: We Need a CAT Plan Now

The US Conference of Mayors, an organization that includes more than 1,000 mayors from across the nation, this week voted unanimously in support of a resolution calling on Congress to create a comprehensive, integrated national catastrophe plan that includes a national catastrophe fund to enhance the availability of homeowners insurance in states across the country that are prone to natural disasters.

"The fact is that mayors are on the front lines before, during and after a catastrophe, and their unanimous support should send a strong signal to Capitol Hill that the time for action is now, before the next catastrophe strikes," said James Lee Witt, co-chair of ProtectingAmerica.org and former director of the Federal Emergency Management Agency.

In its resolution, the nation's mayors noted that the national catastrophe fund is essential to reducing the amount of after-the-fact expenditures of taxpayers' funds that the Congress appropriates to address damages that could otherwise be minimized by a national catastrophe fund and an integrated catastrophe preparedness program.

"The mayors' resolution echoes and amplifies ProtectingAmerica.org's findings that a national catastrophe program and fund would protect homes and lives, would save homeowners an estimated $8.4 billion in insurance premiums each year, and would remove an enormous burden on taxpayers," said Admiral James M. Loy, also a co-chair of ProtectingAmerica.Org and former deputy secretary of the US Department of Homeland Security.

In addition to the $8.4 billion that homeowners would save through a national catastrophe fund, an analysis by the leading international actuary Milliman Company found that a total of $11.6 billion could be saved if states established similar privately funded catastrophe funds.

About ProtectingAmerica.org

ProtectingAmerica.org is a non-profit organization consisting of emergency management officials, first responders, disaster relief experts, insurers and others. Its members include the American Red Cross and more than 275 other organizations and businesses.

At the core of ProtectingAmerica.org's mission is the establishment of a comprehensive, integrated national catastrophe management solution that will better prepare and protect American families, communities, consumers and the American economy from catastrophe. ProtectingAmerica.org is working to increase public awareness and enhance consumer education; advocate for better coordination with local, state and federal mitigation and recovery efforts, and strengthen emergency response and financial mechanisms to rebuild after a major catastrophe.

The organization supports comprehensive federal legislation that would establish a privately financed national catastrophe fund that would serve as a backstop to state catastrophe funds. The funds' private deposits and the majority of its earnings could only be used to cover replacement and rebuilding costs following major catastrophic events. A portion of the funds' earnings would be dedicated to increase public and consumer education, strengthen first responders, and enhance building codes and their enforcement.

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PREPARING FOR AND PROTECTING AMERICA FROM CATASTROPHE

Admiral James M. Loy, National Co-Chair
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NEWS RELEASE

FOR IMMEDIATE RELEASE:
May 14, 2007

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Homeowners Poised to Annually Save $11.6 Billion if Catastrophe Protections Enacted
Only a Matter of Time for Catastrophe to Strike According to Weather Experts

(Washington, D.C.) - American homeowners will save $11.6 billion annually if privately funded catastrophe protection programs are established in disaster-prone states and backed up by a similar national program, according to Milliman, Inc., one of the nation's leading actuarial and consulting firms.

'An integrated program that includes a state catastrophe fund and a national backstop in addition to the traditional insurance market, while helping to fund mitigation efforts, enhance first responder programs and expand homeowner education, would save American homeowners an estimated $11.6 billion per year,' according to Dr. David Appel, Principal and Director of Economics Consulting for Milliman.

'Our actuarial analysis confirms and validates the notion that such an integrated program which transfers some of the cost of private reinsurance into tax exempt catastrophe funds would produce significant annual savings for American homeowners,' he added.

Comprehensive catastrophe preparation and protection programs are critical to the nation, based on general weather predictions offered today by Kenneth Reeves, Expert Senior Meteorologist and Director of Forecast Operations at AccuWeather.com, the nation's largest private weather forecasting agency.

'As the population expands and continues to gravitate to the nation's coastline, catastrophic weather events such as hurricanes will have an ever-greater impact on some of the most densely populated regions of the county,' according to AccuWeather.com's Reeves.

'Hurricane Katrina was a warning to the rest of the country that we need to be better prepared,' said Reeves. 'Despite several days of advance notice, many people were still not ready for the fury it unleashed on the Gulf Coast. Those who were could do little or nothing to save their property and possessions. And the lesson of Katrina does not just apply to coastal communities—as we just saw, virtually the entire town of Greensburg, KS, was destroyed by a tornado less than two weeks ago.'

'These reports should serve as a wake-up call to everyone in America. Our country needs to be better prepared and protected before the next catastrophe strikes,' said James Lee Witt, former FEMA Director and co-chair of ProtectingAmerica.org, a coalition of more than 200 organizations calling for action by Congress and state legislatures to enact comprehensive catastrophe protection programs.

'Our current financial recovery mechanisms, which rely primarily on the private insurance market, federal assistance in the form of low-interest loans and a handful of state catastrophe funds, are incapable of meeting the needs of victims and the immeasurable costs that follow a catastrophe. It is our obligation to retool the system today to be prepared for what can happen tomorrow,' Witt continued.

'Beyond helping to insure for monetary losses, state and federal catastrophe funds will improve the way America is prepared for and protected from catastrophe. Our solution calls for new programs and processes that would speed relief, recovery and rebuilding,' said Admiral James Loy, former Deputy Secretary of Homeland Security and ProtectingAmerica.org co-chair.

'When a hurricane is on the radar screen, it is too late to begin thinking about preparedness. As afforded by the establishment of a national catastrophe fund, programs to improve preparedness and enhance prevention and mitigation programs are invaluable in advancing our nation's capability to minimize damage and recover efficiently,' Loy continued.

The Milliman report found that if a national backstop mechanism is enacted and state catastrophe funds are created in the states outlined in the report, consumers will realize annual savings in excess of $11 billion in their homeowner's insurance premiums. State-by-state savings would vary according to a number of factors, including the likelihood of a natural catastrophe, population density and the value of residential property. For example, annual savings per household in California would average $256; Louisiana, $224; North Carolina, $132; and Oregon, $127.

'Part of the beauty of this approach is that residents of risk-free states would not pay a dime into a catastrophe fund. This would significantly reduce the current cross-subsidy that occurs when the federal government steps in to repair and rebuild in the aftermath of regional catastrophes,' said Admiral Loy.

Florida Insurance Commissioner Kevin McCarty estimated that the 2004/2005 hurricane season cost every American taxpaying family more than $800 to cover the costs of repairing and rebuilding damaged areas of the Gulf region.

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Washington Times
March 3, 2006

When the Next Catastrophe strikes

By James M. Loy

There are few places in America that are immune from the physical threat of catastrophe, and none would be exempt from the economic consequences if catastrophe struck today.

The onslaught of Hurricanes Katrina, Wilma and Rita provided sobering insights into the shortcomings of our preparedness for catastrophic storms. To this day, the nightly news and the daily newspapers remind us of the devastation of the 2005 hurricane season.

So terrifying were the storms of 2005 that many people fail to remember that just one year earlier, Florida was hit with four major hurricanes in six weeks. Seven of the 10 most damaging hurricanes in U.S. history have occurred within the past five years.

It would be easy to think that the force and fury of major hurricanes are reserved for the coasts on the Gulf and Southeast. That would be wrong. Since 1900, 11 hurricanes have made direct hits on New England, six have made landfall squarely in New York. In 1938, the most powerful of those hurricanes landed with such force that it became known as "The Long Island Express." It killed 700 people and left 63,000 homeless. If a hurricane of the same force struck New York today, the economic damages could exceed $100 billion. The potential loss of life would be extraordinary.

Earthquakes, often associated only with California, pose a tremendous threat not just to the West Coast, but to America's heartland as well. April will mark the 100th anniversary of the Great San Francisco Earthquake, the costliest earthquake to ever rock America. Replacement costs for a similar quake today are estimated at $400 billion.

But there have been worse earthquakes in America. In 1811, the first of a series of earthquakes hit near New Madrid, Mo. Newspaper and eyewitness accounts indicate that these earthquakes probably exceeded the strength of San Francisco's 1906 earthquake.

The epicenter of the New Madrid quakes was midway between St. Louis and Memphis. Those earthquakes changed the course of the Mississippi River and damaged structures for hundreds of miles. Their shock waves covered more than a million square miles, from Mississippi to Michigan, from Pennsylvania to Nebraska.

Damage was limited because those earthquakes struck in an area that at the time was a vast wilderness, a part of the newly acquired Louisiana Purchase. Today, millions of American families make their homes right on top of the New Madrid fault. Families in middle-America cities -- like Nashville, St. Louis, Memphis and Little Rock -- would all suffer were we to experience a replay of the New Madrid earthquakes.

Fortunately, policy-makers have finally begun to recognize that catastrophe can strike anywhere in America, and that better preparation and protection must be national priorities. Unfortunately, the debate has been limited primarily to investigating the failures in the government response to Katrina, on the rebuilding of New Orleans and on structural changes to the federal bureaucracy.

In addition to debating the government response and structure, we need to find private-sector solutions as well. We need comprehensive, integrated solutions at the local, state and federal levels that leverage the knowledge and expertise of the private sector in an effort to mitigate the potential damage during a catastrophic event and to ensure that adequate financial resources are available to lessen the economic consequences in catastrophe's aftermath.

America's private insurance industry is efficient and effective in providing financial resources to families that have been victims of foreseeable losses and small-scale catastrophes. But, in total, the property and casualty insurance industry has only about $400 billion of capital to cover all claims for all lines of insurance. While this amount is adequate to cover predictable losses, it may well be inadequate to cover unpredictable mega-catastrophes. Why take that chance?

Supplementing those reserves to make sure consumers will be protected could be easily accomplished by creating privately funded state and national catastrophe funds. These funds would include deposits of private insurance-company revenues that could grow free and would be used to pay the extraordinary claims following a catastrophe. A limited amount of the investment income could be used to support consumer education, expand first-responder programs, strengthen building codes and improve code enforcement.

A bipartisan group of representatives has introduced legislation that would allow for a IRA-like national financial backstop. It is important legislation that should be considered before the next catastrophe strikes.

Adm. James M. Loy (Coast Guard Ret.) is co-chairman of ProtectingAmerica.Org. He also served as deputy secretary of the Department of Homeland Security.

NATIONAL UNDERWRITER
February 13, 2006

National Catastrophe Fund Will Pay Dividends For All

BY JAMES LEE WITT AND JAMES M. LOY

California Insurance Commissioner John Garamendi took a bold step last year to alert America that as a nation we are not as prepared as we should be for the consequences of catastrophe.

The step the commissioner took to convene a summit of the nation's insurance regulators, for the purpose of preparing for and protecting America from disaster losses, came at a critical moment as the threat of catastrophic events continues to rise.

The fact that Mr. Garamendi was joined by top regulators from New York, Florida and Illinois underscores the nationwide concern and acknowledges that catastrophes are not contained and isolated events. These policymakers question whether we will have the mechanisms in place to enable families to be prepared for and protected from catastrophes when they strike.

A new coalition of first responders, emergency personnel, building code experts, insurers and others began calling for the creation of a privately funded national catastrophe fund even before the onset of the devastating hurricane season of 2005.

The members of this coalition-ProtectingAmerica.org-applaud the vision and leadership of these insurance regulators from across the country.

The national economic impact of catastrophes is shouldered not by the residents of individual states, but by all Americans. Earthquake faults run all along the West Coast and throughout the Midwest, while hurricanes run throughout the Gulf and eastern shores. Had state, local and federal officials paid closer attention to preparing for natural disasters, the consequences from the 2005 hurricane season might have been less tragic.

As California marks the 100th anniversary of the Great Earthquake of 1906, it is worth noting that if an earthquake struck today at the same location with the same magnitude as that of only a century ago, the likely economic losses are estimated to exceed $400 billion. Financial recovery in the wake of such a catastrophic event would be an unrivaled national economic challenge for our families, our communities and our nation.

San Francisco's experience in 1906 is thought by many Americans as the largest of all earthquakes to hit the United States, but the fact is that San Francisco's earthquake doesn't even rank in the top-10 strongest in U.S. history.

Eight of the top-10 U.S. earthquakes occurred in remote parts of Alaska, but two enormous earthquakes occurred along the New Madrid Fault, right in the middle of our nation, in 1810 and 1811. Had the Richter Scale been in use at the time, these quakes would have registered an eight.

Their tremors were felt from Mississippi to Michigan, from Pennsylvania to Nebraska.

When the New Madrid series of earthquakes struck, our heartland was vast and uninhabited. Were either of the New Madrid quakes to occur today, the damage would be enormous.

The point is, catastrophes can strike anywhere in America. They are not an issue for our coastlines alone, but for every American in every state.

The 2005 hurricane season brought with it the most extensive and expensive damages our nation has ever incurred. In fact, eight of the most costly catastrophes in U.S. history occurred in the past four years.

As the National Geographic noted at the outset of the 2005 hurricane season, "The mighty Atlantic conveyor belt is in high gear, and sea-surface temperatures are up. That means we could be in for decades of coast-crushing hurricanes."

With every possibility that America will be facing years of record-shattering catastrophes, the commissioners are absolutely right to call for a national financial backstop standing behind the private insurance market to help us repair, rebuild and recover from catastrophe.

The creation of a national catastrophe fund would assure the viability of the private market and its ability to provide coverage to families, businesses and communities.

Such a catastrophe fund would function much in the same way as personal IRAs. Insurers would be required to deposit a portion of homeowners insurance premiums into the fund, where they would grow free of taxes, just like in an IRA. And, just like IRAs, those funds could only be tapped for very restrictive purposes. The fund would only be used to help pay claims in the aftermath of a true catastrophe.

Shortly after the national catastrophe summit, H.R. 4366-the Homeowners Insurance Protection Act of 2005-was introduced in the House of Representatives by two Florida Republican representatives, Ginny Brown-Waite and Clay Shaw. These members of Congress recognize that America can do a better job preparing for and protecting its citizens from natural catastrophes.

H.R. 4366 is a comprehensive approach that protects homes and property at a lower cost. It improves preparedness, strengthens first responders, mitigates the impact of a catastrophe on our economy, and reduces the financial burden on consumers and taxpayers.

The bill would use private premium dollars to fund a backstop to the private market and state catastrophe funds. This Consumer HELP Fund will stand behind state catastrophe funds and pay claims when the state fund has exceeded its capacity.

Contributions to the fund would be based on actuarially sound and self-sufficient rates according to local exposures to ensure there will be no subsidization of catastrophe-prone states by other states.

H.R. 4366 is a market-based approach to a true national challenge that should be embraced by all members of the House of Representative and the Senate before the next catastrophe strikes.

James Lee Witt and James M. Loy are co-chairs of ProtectingAmerica.org.

Mr. Witt formerly served as the director of the Federal Emergency Management Agency in the Clinton administration. James Loy, a retired admiral, previously served as the deputy secretary of the U.S.

Department of Homeland Security in the administration of President George W. Bush.

FINANCIAL TIMES

Monday, September 12, 2005

JAMES LEE WITT

America can prepare for what it cannot control

Tom Wilson, the president of Allstate Insurance Company, delivered a speech to the Executives' Forum of Houston last month and issued a critical warning: America must become better prepared to address the financial consequences of catastrophe. A week later, Hurricane Katrina struck the Gulf coast.

The financial mechanisms we have in place to help families, businesses and communities repair, respond and recover after the onslaught of a man-made or natural catastrophe are inefficient, ineffective and insufficient. Additionally, we need to better educate homeowners, builders and emergency responders about ways we can prepare for and protect ourselves from potential catastrophes.

Mr Wilson understands the costs, both human and financial, that the nation would face in the aftermath of a catastrophe. It is his business to think about the unthinkable and to calculate the incalculable.

When I served as the director of the Federal Emergency Management Agency (Fema), it was my job to think about how America will recover from inevitable disasters and catastrophes – terrorism, earthquakes, hurricanes, floods and tornadoes. The numbers are staggering.

If the 1906 San Francisco Earthquake occurred today, the replacement costs would exceed $400bn. The 1938 hurricane known as the "Long Island Express" missed Manhattan by less than 10 miles, killed 700 people, left 63,000 people homeless and caused more than $300m in damages. The costs today of a similar storm would be massive – easily in the tens of billions of dollars.

When Hurricane Andrew slammed the Florida coast in 1992 it caused $20bn in damages. If the storm had veered slightly north and hit Miami, recovery costs would have easily doubled. The terrorist attacks of September 11 2001 cost $30bn, the most expen-

The 10 most costly catastrophes in US history occurred within the past 15 years. There is little doubt that more are on the way

sive catastrophe in history. The economic damage reverberated throughout the nation. Hurricane Katrina is expected to cause an estimated $26bn payout by the insurance industry.

The 10 most costly catastrophes in US history occurred within the past 15 years. There is little doubt that more are on the way. Already, our naming system for hurricanes and tropical storms has moved deep into the alphabet. In previous years we worried about hurricanes named Andrew, Donna and Floyd. Reports from the National Hurricane Center hint that, for the foreseeable future, we should worry about Tammy, Vince and Wilma.

The National Geographic's August issue carried a feature on hurricanes in America entitled: "In Hot Water." The story notes that one in five homes in Florida was damaged by a hurricane last year. The story warns that: "The mighty Atlantic conveyor belt is in high gear and sea-surface temperatures are up. That means we could be in for decades of coast-crushing hurricanes."

So what can America do to be better financially prepared and protected from catastrophe? From a financial standpoint, a backstop for families, businesses and communities is needed in the case of catastrophic events. Florida and California have funds in place that deal with hurricanes and earthquakes. Legislation has been announced by a bipartisan team of New York legislators calling for the creation of a similar fund.

Policymakers in disaster-prone states should follow the example of Florida, California and New York. States can move faster than the federal government and they should.

But catastrophes are not a state-by-state problem. Hurricanes that hit North Carolina wreak havoc on New England. Earthquakes centred in California cause damage well into the Pacific north-west. Terrorist attacks on a single metropolitan area could easily affect a multi-state region or the nation as a whole.

A national solution is every bit as important as the steps being taken in the states. That solution should include a national catastrophe fund that would shore up private insurers in instances when truly catastrophic events occur. Such a fund would be a financially responsible way to assure the viability of the private market and its ability to provide coverage for other perils.

We cannot control the ravages of nature or the savagery of mankind but we can be better prepared and better protected. Experts have given us stark and stern warnings. The time to heed those warnings is now.

The writer is chief executive and chairman of James Lee Witt Associates, a public safety and crisis management consulting firm. He served in President Bill Clinton's cabinet as the director of

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We can't afford not to plan for catastrophes

By James Lee Witt

Hundreds of thousands of residents jammed the highways to get out of Hurricane Katrina's path, which included 145-mph wind gusts and storm surges of more than 20 feet. That was just the beginning.

Local, state and federal resources were mobilized as one of the most powerful hurricanes in history made landfall along the Gulf Coast regions of Louisiana, Mississippi and Alabama.

During my years as director of the Federal Emergency Management Agency (FEMA), I witnessed the incredible abilities and dedication of our nation's emergency response personnel, of which we have the best trained and best equipped possible. Despite their skills, ability and technology, we must do more to be better prepared and protected in the case of such a catastrophe.

Our financial recovery mechanisms, which rely primarily on the private insurance market, federal assistance in the form of low-interest loans and a handful of state catastrophe funds, need to be retooled so that they are capable of meeting the immeasurable costs of a catastrophe.

Conservative estimates indicate that the costs of recovery from Hurricane Katrina will rival any natural catastrophe we've experienced in the USA. Initial predictions indicate that recovery costs could surpass the $30 billion cost of recovering from the attacks of Sept. 11, 2001.

A replay of any of our previous natural catastrophes would result in similarly astounding costs:

•A 1938 hurricane, the "Long Island Express," missed Manhattan by only a few miles and caused $308 million in damage. A replay of that storm today is projected to have a recovery cost of $24 billion in Suffolk County, alone.

•If the 1906 San Francisco earthquake happened in the same spot as it did a century ago, damages are estimated to exceed $400 billion.

From a financial standpoint, state and federal catastrophe funds provide a necessary backstop for families, businesses and communities in the case of extraordinary events. Florida has funds in place to deal with hurricanes; California has such funds for earthquakes. New York is considering a similar fund as well.

Policymakers in other disaster-prone states should follow their example. States can move faster than the federal government. And they should move now.

On the other hand, catastrophes are not a state-by-state problem. Hurricanes that hit North Carolina can wreak havoc on New England. Earthquakes in California can cause damage well into the Pacific Northwest.

A national solution is every bit as important as the steps being taken in the states. Steps to be taken include a national catastrophe fund that would shore up private insurers in instances when truly catastrophic events occur. Such a fund would be a financially responsible way to ensure the viability of the private market and its ability to provide coverage to families, businesses and communities.

James Lee Witt is the CEO and chairman of James Lee Witt Associates, a public safety and crisis management consulting firm. Witt served as the director of FEMA from 1993 to 2001. Witt has been hired by Louisiana to help advise the governor on hurricane recovery efforts.