

Insuring Natural Catastrophes

- *The NAIC and state insurance departments are committed to developing a better way to insure large-scale natural disasters, based on the principle that any federal catastrophe response should capitalize on the expertise and strengths of the state insurance supervisory system.*
- *Natural catastrophes are local events that, in the extreme, become a national issue. The private insurance market should be the primary risk bearer for homeowners and small businesses, but a comprehensive, state-based, national plan is needed to help mitigate and manage large-scale natural catastrophes that exceed the capacity of insurance markets to address them.*
- *The NAIC endorses the concept of a commission of experts (including State insurance regulators) to examine various approaches to better managing natural catastrophes nationwide.*

Issue Background

The 2004 and 2005 hurricane seasons brought unprecedented devastation to the Gulf Coast, with seven million insurance claims costing more than \$100 billion in insured losses. Future mega catastrophes could be worse, and a reactive response will not suffice. The NAIC and state insurance regulators are working to develop a comprehensive national plan that combines new risk management techniques with a solid foundation of solvency and consumer protection inherent to state insurance regulation. Meanwhile, Congress continues to indicate interest in national catastrophe management, with the introduction of legislation related to a comprehensive national plan, a catastrophe commission, tax-deferred reserves, and wind vs. water coverage issues.

Key Points

- The NAIC endorses a commission of experts to examine various solutions, including legislation, to develop the best possible mix of measures to prepare for and respond to mega-catastrophes.
- The NAIC continues to develop a national catastrophe risk plan that includes an all-perils insurance policy, promotes reasonable building codes and mitigation tools, and emphasizes a private market response backed by state and federal reinsurance pools. The plan would allow insurance companies to set aside tax-deferred reserves—as is common in other countries—specifically for use during large natural catastrophes. Likewise, the NAIC plan considers a national catastrophe fund that could be developed to provide reinsurance coverage to state or regional catastrophe funds.
- A comprehensive strategy is essential to move the nation from a reactive “catastrophe management” approach to a proactive posture that involves mitigation programs, effective and enforced building codes, and incentives and disincentives to encourage appropriate building and land use policies.
- The financial impact of certain mega catastrophes could reach into the hundreds of billions of dollars and overwhelm the insurance industry. Pre-funding for such events is imperative, and federal involvement via taxpayer dollars is inevitable. It is better to plan for and manage these future loss costs now than to try to secure funding after an event has occurred.