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HOUSE OF REPRESENTATIVES

REPORT
110–419

HOMEOWNERS' DEFENSE ACT OF 2007

OCTOBER 31, 2007.—Committed to the Committee of the Whole House on the State of the Union and ordered to be printed

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

REPORT

together with

ADDITIONAL VIEWS

[To accompany H.R. 3355]

[Including cost estimate of the Congressional Budget Office]

The Committee on Financial Services, to whom was referred the bill (H.R. 3355) to ensure the availability and affordability of homeowners' insurance coverage for catastrophic events, having considered the same, report favorably thereon with an amendment and recommend that the bill as amended do pass.

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69–006

AMENDMENT

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

SECTION 1. SHORT TITLE; TABLE OF CONTENTS.

(a) SHORT TITLE.—This Act may be cited as the "Homeowners' Defense Act of 2007".

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

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

TITLE I—NATIONAL CATASTROPHE RISK CONSORTIUM

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

TITLE II—NATIONAL HOMEOWNERS' INSURANCE STABILIZATION PROGRAM

Sec. 201. Establishment.
Sec. 202. Liquidity loans and catastrophic loans for state and regional reinsurance programs.
Sec. 203. Reports and audits.
Sec. 204. Funding.

TITLE III—GENERAL PROVISIONS

Sec. 301. Qualified reinsurance programs.
Sec. 302. Definitions.
Sec. 303. Regulations.

SEC. 2. FINDINGS AND PURPOSES.

(a) FINDINGS.—The Congress finds that—

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

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

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

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

(5) historically, when a natural disaster eclipses the ability of the private industry and a State to manage the loss, the Federal Government has stepped in to provide the funding and services needed for recovery;

(6) the cost of such Federal "bail-outs" are borne by all taxpayers equally, as there is no provision to repay the money and resources provided, which thereby unfairly burdens citizens who live in lower risk communities;

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

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

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

(10) since 2004, the Congress has appropriated more than $58,000,000,000 in disaster relief to the States affected by natural catastrophes;

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

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

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

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

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

(16) State insurers and reinsurers, if appropriately backstopped themselves, can absorb catastrophic risk borne by private insurers without bearing timing risk, and thus enable all insurers (whether State-operated or privately owned) to underwrite and price insurance without timing risk and in such a way to encourage property owners to pay for the appropriate insurance to protect themselves and to take steps to mitigate against the risks of disaster by locally appropriate methods.

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

TITLE I—NATIONAL CATASTROPHE RISK CONSORTIUM

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

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

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

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

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

SEC. 102. FUNCTIONS.

The Consortium shall—

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

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

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

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

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

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

(7) submit annual reports to Congress describing the activities of the Consortium for the preceding year.

SEC. 103. POWERS.

The Consortium—

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

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

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

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

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

(c) AUDITS.—

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

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

SEC. 105. MANAGEMENT.

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

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

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

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

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

(B) a member from each State participating in the Consortium, who shall be appointed by such State.

(b) BYLAWS.—The Board may prescribe, amend, and repeal such bylaws as may be necessary for carrying out the functions of the Consortium.

(c) COMPENSATION, ACTUAL, NECESSARY, AND TRANSPORTATION EXPENSES.—

(1) NON-FEDERAL EMPLOYEES.—A member of the Board who is not otherwise employed by the Federal Government shall be entitled to receive the daily equivalent of the annual rate of basic pay payable for level IV of the Executive Schedule under section 5315 of title 5, United States Code, as in effect from time to time, for each day (including travel time) during which such member is engaged in the actual performance of duties of the Consortium.

(2) FEDERAL EMPLOYEES.—A member of the Board who is an officer or employee of the Federal Government shall serve without additional pay (or benefits in the nature of compensation) for service as a member of the Consortium.

(3) TRAVEL EXPENSES.—Members of the Consortium shall be entitled to receive travel expenses, including per diem in lieu of subsistence, equivalent to those set forth in subchapter I of chapter 57 of title 5, United States Code.

(d) QUORUM.—A majority of the Board shall constitute a quorum.

(e) EXECUTIVE DIRECTOR.—The Board shall appoint an executive director of the Consortium on such terms as the Board may determine.

SEC. 106. STAFF; EXPERTS AND CONSULTANTS.

(a) STAFF.—

(1) APPOINTMENT.—The Board of the Consortium may appoint and terminate such other staff as are necessary to enable the Consortium to perform its duties.

(2) COMPENSATION.—The Board of the Consortium may fix the compensation of the executive director and other staff.

(b) EXPERTS AND CONSULTANTS.—The Board shall procure the services of experts and consultants as the Board considers appropriate.

SEC. 107. FEDERAL LIABILITY.

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

SEC. 108. AUTHORIZATION OF APPROPRIATIONS.

There are authorized to be appropriated to carry out this title $20,000,000 for each of fiscal years 2008 through 2013.

TITLE II—NATIONAL HOMEOWNERS' INSURANCE STABILIZATION PROGRAM

SEC. 201. ESTABLISHMENT.

The Secretary of the Treasury shall carry out a program under this title to make liquidity loans and catastrophic loans under section 202 to qualified reinsurance programs to ensure the solvency of such programs, to improve the availability and affordability of homeowners' insurance, to incent risk transfer to the private capital and reinsurance markets, and to spread the risk of catastrophic financial loss resulting from natural disasters and catastrophic events.

SEC. 202. LIQUIDITY LOANS AND CATASTROPHIC LOANS FOR STATE AND REGIONAL REINSURANCE PROGRAMS.

(a) CONTRACTS.—The Secretary may enter into a contract with a qualified reinsurance program to carry out the purposes of this Act as the Secretary may deem appropriate. The contract shall include, at a minimum, the conditions for loan eligibility set forth in this section.

(b) CONDITIONS FOR LOAN ELIGIBILITY.—A loan under this section may be made only to a qualified reinsurance program and only if—

(1) before the loan is made—

(A) the State or regional reinsurance program submits to the Secretary a report setting forth, in such form and including such information as the Secretary shall require, how the program plans to repay the loan; and

(B) based upon the report of the program, the Secretary determines that the program can meet its repayment obligation under the loan and certifies that the program can meet such obligation;

(2) the program cannot access capital in the private market, including through catastrophe bonds and other securities sold through the facility created in title I of this Act, as determined by the Secretary, and a loan may be made to such a qualified reinsurance program only to the extent that such program cannot access capital in the private market;

(3) the Secretary determines that an event has resulted in insured losses in a State with a qualified reinsurance program;

(4) the loan complies with the requirements under subsection (d) and or (e), as applicable; and

(5) the loan is afforded the full faith and credit of the State and the State demonstrates to the Secretary that it has the ability to repay the loans.

(c) MANDATORY ASSISTANCE FOR QUALIFIED REINSURANCE PROGRAMS.—The Secretary shall upon the request of a qualified reinsurance program and subject to subsection (b), make a loan under subsection (d) or (e) for such program in the amount requested by such program (subject to the limitations under subsections (d)(2) and (e)(2), respectively).

(d) LIQUIDITY LOANS.—A loan under this subsection for a qualified reinsurance program shall be subject to the following requirements:

(1) PRECONDITIONS.—The Secretary shall have determined that the qualified reinsurance program—

(A) has a capital liquidity shortage, in accordance with regulations that the Secretary shall establish; and

(B) cannot access capital markets at effective rates of interest lower than those provided in paragraph (3).

(2) AMOUNT.—The principal amount of the loan may not exceed the ceiling coverage level for the qualified reinsurance program.

(3) RATE OF INTEREST.—The loan shall bear interest at an annual rate 3 percentage points higher than marketable obligations of the Treasury having the same term to maturity as the loan and issued during the most recently completed month, as determined by the Secretary, or such higher rate as may be necessary to ensure that the amounts of interest paid under such loans exceed the sum of the costs (as such term is defined in section 502 of the Federal Credit Reform Act of 1990 (2 U.S.C. 661a)) of such loans, the administrative costs involved in carrying out a program under this title for such loans, and any incidental effects on governmental receipts and outlays.

(4) TERM.—The loan shall have a term to maturity of not less than 5 years and not more than 10 years.

(e) CATASTROPHIC LOANS.—A loan under this subsection for a qualified reinsurance program shall be subject to the following requirements:

(1) PRECONDITIONS.—The Secretary shall have determined that an event has resulted in insured losses in a State with a qualified reinsurance program and that such insured losses in such State are in excess of 150 percent of the aggre-

gate amount of direct written premium for privately issued property and casualty insurance, for risks located in that State, over the calendar year preceding such event, in accordance with regulations that the Secretary shall establish.

(2) AMOUNT.—The principal amount of the loan made pursuant to an event referred to in paragraph (1) may not exceed the amount by which the insured losses sustained as a result of such event exceed the ceiling coverage level for the qualified reinsurance program.

(3) RATE OF INTEREST.—The loan shall bear interest at an annual rate 0.20 percentage points higher than marketable obligations of the Treasury having a term to maturity of not less than 10 years and issued during the most recently completed month, as determined by the Secretary, or such higher rate as may be necessary to ensure that the amounts of interest paid under such loans exceed the sum of the costs (as such term is defined in section 502 of the Federal Credit Reform Act of 1990 (2 U.S.C. 661a)) of such loans, the administrative costs involved in carrying out a program under this title for such loans, and any incidental effects on governmental receipts and outlays.

(4) TERM.—The loan shall have a term to maturity of not less than 10 years.

(f) USE OF FUNDS.—Amounts from a loan under this section shall only be used to provide reinsurance or retrocessional coverage to underlying primary insurers or reinsurers for losses arising from all personal real property or homeowners' lines of insurance, as defined in the Uniform Property & Casualty Product Coding Matrix published and maintained by the National Association of Insurance Commissioners. Such amounts shall not be used for any other purpose.

SEC. 203. REPORTS AND AUDITS.

The Secretary shall submit a report to the President and the Congress annually that identifies and describes any loans made under this title during such year and any repayments during such year of loans made under this title, and describes actions taken to ensure accountability of loan funds. The Secretary shall provide for regular audits to be conducted for each loan made under this title and shall make the results of such audits publicly available.

SEC. 204. FUNDING.

(a) PROGRAM FEE.—

(1) IN GENERAL.—The Secretary may establish and collect, from qualified reinsurance programs that are precertified pursuant to section 301(c), a reasonable fee, as may be necessary to offset the expenses of the Secretary in connection with carrying out the responsibilities of the Secretary under this title, including—

(A) costs of developing, implementing, and carrying out the program under this title; and

(B) costs of providing for precertification pursuant to section 301(c) of State and regional reinsurance programs as qualified reinsurance programs.

(2) ADJUSTMENT.—The Secretary may, from time to time, adjust the fee under paragraph (1) as appropriate based on expenses of the Secretary referred to in such paragraph.

(3) USE.—Any fees collected pursuant to this subsection shall be credited as offsetting collections of the Department of the Treasury and shall be available to the Secretary only for expenses referred to in paragraph (1).

(b) COSTS OF LOANS; ADMINISTRATIVE COSTS.—To the extent that amounts of negative credit subsidy are received by the Secretary in any fiscal year pursuant to loans made under this title, such amounts shall be available for costs (as such term is defined in section 502 of the Federal Credit Reform Act of 1990 (2 U.S.C. 661a)) of such loans and for costs of carrying out the program under this title for such loans.

(c) FULL TAXPAYER REPAYMENT.—The Secretary shall require the full repayment of all loans made under this title. If the Secretary determines at any time that such full repayment will not made, or is likely not to be made, the Secretary shall promptly submit a report to the Congress explaining why such full repayment will not be made or is likely not to be made.

TITLE III—GENERAL PROVISIONS

SEC. 301. QUALIFIED REINSURANCE PROGRAMS.

(a) IN GENERAL.—For purposes of this Act only, a program shall be considered to be a qualified reinsurance program if the program—

(1) is authorized by State law for the purposes described in this section;

(2) is an entity in which the authorizing State maintains a material, financial interest;

(3) provides reinsurance or retrocessional coverage to underlying primary insurers or reinsurers for losses arising from all personal residential lines of insurance, as defined in the Uniform Property & Casualty Product Coding Matrix published and maintained by the National Association of Insurance Commissioners;

(4) has a governing body, a majority of whose members are public officials;

(5) provides reinsurance or retrocessional coverage to underlying primary insurers or reinsurers for losses in excess of such amount that the Secretary has determined represents a catastrophic event in that particular State;

(6) is authorized by a State that has in effect such laws, regulations, or other requirements, as the Secretary shall by regulation provide, that—

(A) ensure, to the extent that reinsurance coverage made available under the qualified reinsurance program results in any cost savings in providing insurance coverage for risks in such State, such cost savings are reflected in premium rates charged to consumers for such coverage;

(B) require that any new construction, substantial rehabilitation, and renovation insured or reinsured by the program complies with applicable State or local government building, fire, and safety codes;

(C) require State authorized insurance entities within that State to establish an insurance rate structure that takes into account measures to mitigate insurance losses;

(D) require State authorized insurance and reinsurance entities within that State to establish rates at a level that annually produces expected premiums that shall be sufficient to pay the expected annualized cost of all claims, loss adjustment expenses, and all administrative costs of reinsurance coverage offered; and

(E) encourage State authorized insurance and reinsurance entities within that State to establish rates that do not involve cross-subsidization between any separate property and casualty lines covered under the State authorized insurance or reinsurance entity; and

(7) complies with such additional organizational, underwriting, and financial requirements as the Secretary shall, by regulation, provide to carry out the purposes of this Act.

(b) TRANSITIONAL MECHANISMS.—For the five-year period beginning on the date of the enactment of this Act, in the case of a State that does not have a qualified reinsurance program for the State, a State residual insurance market entity for such State shall be considered to be a qualified reinsurance program, but only if such State residual insurance market entity was in existence before such date of enactment.

(c) PRECERTIFICATION.—The Secretary shall establish procedures and standards for State and regional reinsurance programs and the State residual insurance market entities described in section (b) to apply to the Secretary at any time for certification (and recertification) as qualified reinsurance programs.

(d) REINSURANCE TO COVER EXPOSURE.—This section may not be construed to limit or prevent any insurer from obtaining reinsurance coverage for insured losses retained by insurers pursuant to this section, nor shall the obtaining of such coverage affect the calculation of the amount of any loan under this title.

SEC. 302. DEFINITIONS.

For purposes of this Act, the following definitions shall apply:

(1) CEILING COVERAGE LEVEL.—The term "ceiling coverage level" means, with respect to a qualified reinsurance program, the maximum liability, under law, that could be incurred at any time by the qualified reinsurance program.

(2) INSURED LOSS.—The term "insured loss" means any loss insured by a qualified reinsurance program.

(3) QUALIFIED REINSURANCE PROGRAM.—The term "qualified reinsurance program" means a State or regional program that meets the requirements under section 301.

(4) SECRETARY.—The term "Secretary" means the Secretary of the Treasury.

(5) STATE.—The term "State" includes the several States, the District of Columbia, the Commonwealth of Puerto Rico, Guam, the Commonwealth of the Northern Mariana Islands, the United States Virgin Islands, and American Samoa.

SEC. 303. REGULATIONS.

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

PURPOSE AND SUMMARY

H.R. 3355, the Homeowners' Defense Act of 2007, is intended to provide Federal support for State-sponsored reinsurance programs designed to help homeowners prepare for and recover from damage caused by natural catastrophes, to encourage mitigation of such damage and to promote the transfer of insured natural catastrophe risk into the capital markets.

H.R. 3355 has two main components designed to achieve these goals. First, Title I of the legislation establishes a voluntary Federal/State consortium to encourage and facilitate the ceding of risk from qualified reinsurance programs and State residual insurance market entities into the private markets, particularly the catastrophe bond markets. Second, Title II of the legislation creates a Federal loan program to provide a reliable source of post-event financing for qualified reinsurance programs.

Two types of loans are available through the Federal loan program created by Title II of the legislation. First, Title II provides liquidity loans to qualified reinsurance programs that have capital liquidity shortages, in amounts not exceeding the programs' ceiling coverage levels. Title II also makes available catastrophic loans to cover losses in excess of each State program's total liabilities. In order to receive either type of loan available under Title II, the Treasury Secretary must verify that the State program can meet its repayment obligations under the loan.

BACKGROUND AND NEED FOR LEGISLATION

The increasing costs of natural catastrophes have significantly stressed insurance markets. Insurance markets tend to respond adversely to mega-catastrophes. Mega-catastrophes can reduce insurers' surplus and cause them to remodel their analysis of risk and pricing, sometimes resulting in reduced availability and rates increased to match the increased perception of risk. This occurred, for example, following Hurricane Andrew in 1992 and the Northridge earthquake in 1994.

The recent spate of natural disasters has caused insurance companies to reexamine their exposure and business models for insuring natural disasters. This process has resulted in insurers and reinsurers pulling out of or reducing their portfolios in certain areas of the country. This resulting insurance availability loss has, in part, caused homeowners insurance rates to spike by up to 100 percent to over 600 percent in certain higher-risk areas.

The programs created in Titles I and II of H.R. 3355 work together to achieve the legislation's stated purposes. Title I establishes the National Catastrophe Risk Consortium, an organization that States can, but need not, join for the purposes of transferring catastrophe risk into the private capital markets. The desired risk transfer would be achieved through the issuance of risk-linked securities or through the coordination of reinsurance contracts. The Consortium is designed to function as a conduit, so that at no time would risk transfer either to or from the Federal Government. Likewise, the Consortium is prohibited from incurring debt.

The Consortium is to be governed by a board comprised of up to three Federal designees and one representative from each participating State program. All States' qualified reinsurance programs

are eligible to join. Much of the Consortium's needs for risk modeling, financial consulting, and relations with the capital markets can be arranged for on a contract basis rather than provided by permanent staff.

The Consortium is intended to facilitate State efforts to group catastrophic risk for resale. The Consortium staff will work in coordination with participating States' qualified reinsurance programs to catalogue inventories of catastrophic risk. Catastrophe bond underwriters and other market participants will be able to access this database to structure bonds or reinsurance contracts and treaties. In addition, the Consortium will aid participating States' qualified reinsurance programs in transferring catastrophic risk, such as by issuance of catastrophe bonds or the coordination reinsurance agreement, without actually taking possession of any bond proceeds, coupon payments or underlying risk.

The Consortium will aggregate and maintain relevant statistics that can assist market participants in the development of industry standards. Such standards could include, but are not limited to, the terms of bond offerings, the nature of triggers used, and the definitions of risks. Standardization is expected to contribute to the efficiency of the catastrophe bond market.

Title II of the legislation creates the National Homeowners Insurance Stabilization Program under which the Treasury Secretary can extend Federal loans to qualified reinsurance programs, which the Secretary has previously certified as qualified reinsurance programs, in states where natural disasters have occurred. Specifically, Title II makes two types of loans available: liquidity loans and catastrophic loans.

Liquidity loans can be extended to States' qualified reinsurance programs, which the Secretary has previously certified as qualified, that have insured losses and a capital liquidity shortage following a natural catastrophe. The amount of the loan cannot exceed a State qualified reinsurance program's ceiling coverage level. As reported, H.R. 3355's liquidity loans have an interest rate set at three percentage points higher than marketable obligations of the Treasury having the same term to maturity and have a term of maturity of between five and ten years. The interest rate and limited loan duration are intended to encourage sound financial management on the part of the States' qualified reinsurance programs by making the loans attractive only as a last option.

In the event insured losses in a state with a qualified reinsurance program exceed 150 percent of that state's direct written premium for privately issued property and casualty insurance, the Treasury Secretary can extend catastrophic loans to qualified reinsurance programs that the Secretary has previously certified as qualified reinsurance programs As reported, H.R. 3355's catastrophic loans have an annual interest rate 0.20 percentage points higher than marketable obligations of the Treasury and have a term to maturity of no less than ten years.

As a transitional mechanism, during the first five years after enactment, states without qualified reinsurance programs would be eligible to participate in the National Homeowners Insurance Stabilization Program through their residual insurance market entities (e.g., State FAIR and windstorm plans) until they create qualified reinsurance programs, provided the State residual insurance

market entity is in place before enactment of this legislation. State residual insurance market entities remain eligible to participate in Title I's National Catastrophe Risk Consortium at anytime following enactment.

Title III of H.R. 3355 includes general provisions, regarding eligibility for and operations of the programs created in Titles I and II, intended to ensure responsible insurance and reinsurance underwriting. Most importantly, Title III defines, for the purposes of this legislation, a "qualified reinsurance program" as a State-authorized entity that provides reinsurance or retrocessional coverage to underlying primary insurers or reinsurers for losses arising from all personal residential lines of insurance. The definition of qualified reinsurance program also mandates that participating States have enacted statutes or regulations that: (i) ensure any cost savings realized through State insurance or reinsurance programs pass through to policyholders; (ii) require compliance with applicable building codes; (iii) require an insurance rate structure that takes into account measures to mitigate losses; (iv) require State insurance and reinsurance entities to establish risk-based rates; and (v) encourage State insurance and reinsurance entities to establish rates that do not involve cross-subsidization between various insurance lines of coverage.

HEARINGS

The Subcommittee on Housing and Community Opportunity and the Subcommittee on Capital Markets, Insurance, and Government Sponsored Enterprises held a joint legislative hearing on H.R. 3355 on September 6, 2007. The following witnesses testified: The Honorable Phillip Swagel, Assistant Secretary for Economic Policy, U.S. Department of the Treasury; The Honorable J.P. Schmidt, Insurance Commissioner, State of Hawaii, on behalf of the National Association of Insurance Commissioners; The Honorable Matthew Patrick, Massachusetts House of Representatives; The Honorable Tom Evans, Chairman, Florida Coalition for Preservation; Mr. Danyal Ozizmir, Head of Asset Back Securities-Insurance Linked Securities, Swiss Re Financial Products Corporation; Mr. John Seo, Co-founder and Managing Member, Fermat Capital Management; Mr. Franklin Nutter, President, The Reinsurance Association of America; Mr. Vince Malta, Malta & Co., Inc., on behalf of the National Association of Realtors; Mr. Robert Joyce, Chairman and Chief Executive Officer, The Westfield Group, on behalf of the Property Casualty Insurance Association of America; Mr. Steve Spiro, Spiro Risk Management, Inc., on behalf of the Independent Insurance Agents of America; and Mr. John D. Echeverria, Executive Director, Georgetown Environmental Law & Policy Institute, Georgetown University Law Center.

On March 27, 2007, the Subcommittee on Housing and Community Opportunity held a hearing entitled "Perspectives on Natural Disaster Insurance" at which witnesses testified regarding the general need to provide financial security against the natural disasters plaguing our nation. The following witnesses testified: The Honorable Ron Klein; The Honorable Tim Mahoney; The Honorable Ginny Brown-Waite; The Honorable Gene Taylor; Commissioner Kevin M. McCarty, Office of Insurance Regulation, State of Florida; Mr. Andrew Valdivia, President, White & Company Insurance Inc.;

Mr. Malcolm N. Bennett, President, International Realty and Investments; Mr. Robert L. Porter, Executive Director, ProtectingAmerica.org; Mr. Gary Thomas, President's Liaison to the Public and Federal Issues Group, National Association of Realtors; Gov. Marc Racicot, President, American Insurance Association; Mr. Franklin Nutter, President, Reinsurance Association of America; and Ms. Ann Spragens, Senior Vice President, Secretary and General Counsel, Property Casualty Insurers Association of America.

COMMITTEE CONSIDERATION

The Committee on Financial Services met in open session on September 25, 2007, and ordered H.R. 3355, the Homeowners' Defense Act of 2007, as amended, reported with a favorable recommendation by a record vote of 36 yeas and 27 nays.

COMMITTEE VOTES

Clause 3(b) of rule XIII of the Rules of the House of Representatives requires the Committee to list the record votes on the motion to report legislation and amendments thereto. A motion by Mr. Frank to report the bill, as amended, to the House with a favorable recommendation was agreed to by a record vote of 36 yeas and 27 nays (Record vote FC–71). The names of Members voting for and against follow:

Representative	Aye	Nay	Present	Representative	Aye	Nay	Present
Mr. Frank	X			Mr. Bachus		X	
Mr. Kanjorski	X			Mr. Baker		X	
Ms. Waters	X			Ms. Pryce (OH)		X	
Mrs. Maloney	X			Mr. Castle		X	
Mr. Gutierrez	X			Mr. King (NY)		X	
Ms. Velázquez				Mr. Royce		X	
Mr. Watt	X			Mr. Lucas		X	
Mr. Ackerman	X			Mr. Paul		X	
Ms. Carson				Mr. LaTourette		X	
Mr. Sherman	X			Mr. Manzullo		X	
Mr. Meeks				Mr. Jones	X		
Mr. Moore (KS)	X			Mrs. Biggert		X	
Mr. Capuano	X			Mr. Shays		X	
Mr. Hinojosa				Mr. Miller (CA)		X	
Mr. Clay	X			Mrs. Capito		X	
Mrs. McCarthy	X			Mr. Feeney	X		
Mr. Baca	X			Mr. Hensarling		X	
Mr. Lynch	X			Mr. Garrett (NJ)		X	
Mr. Miller (NC)	X			Ms. Brown-Waite	X		
Mr. Scott	X			Mr. Barrett (SC)		X	
Mr. Green	X			Mr. Gerlach		X	
Mr. Cleaver				Mr. Pearce		X	
Ms. Bean	X			Mr. Neugebauer		X	
Ms. Moore (WI)	X			Mr. Price (GA)		X	
Mr. Davis (TN)	X			Mr. Davis (KY)		X	
Mr. Sires	X			Mr. McHenry		X	
Mr. Hodes	X			Mr. Campbell	X		
Mr. Ellison	X			Mr. Putnam			
Mr. Klein	X			Mrs. Bachmann		X	
Mr. Mahoney (FL)	X			Mr. Roskam		X	
Mr. Wilson	X			Mr. Marchant		X	
Mr. Perlmutter	X			Mr. McCotter		X	
Mr. Murphy	X						
Mr. Donnelly	X						
Mr. Wexler	X						
Mr. Marshall	X						

Representative	Aye	Nay	Present	Representative	Aye	Nay	Present
Mr. Boren	X						

The following amendments were disposed of by record votes. The names of Members voting for and against follow:

An amendment in the nature of a substitute by Mr. Shays, No. 1c, establishing a Commission on Natural Catastrophe Risk management, was not agreed to by a record vote of 22 yeas and 32 nays (Record vote FC–67):

Representative	Aye	Nay	Present	Representative	Aye	Nay	Present
Mr. Frank		X		Mr. Bachus			
Mr. Kanjorski		X		Mr. Baker	X		
Ms. Waters		X		Ms. Pryce (OH)	X		
Mrs. Maloney		X		Mr. Castle			
Mr. Gutierrez		X		Mr. King (NY)	X		
Ms. Velázquez				Mr. Royce	X		
Mr. Watt		X		Mr. Lucas	X		
Mr. Ackerman		X		Mr. Paul	X		
Ms. Carson				Mr. LaTourette			
Mr. Sherman				Mr. Manzullo	X		
Mr. Meeks				Mr. Jones		X	
Mr. Moore (KS)		X		Mrs. Biggert	X		
Mr. Capuano		X		Mr. Shays	X		
Mr. Hinojosa				Mr. Miller (CA)	X		
Mr. Clay		X		Mrs. Capito	X		
Mrs. McCarthy		X		Mr. Feeney		X	
Mr. Baca		X		Mr. Hensarling	X		
Mr. Lynch		X		Mr. Garrett (NJ)	X		
Mr. Miller (NC)		X		Ms. Brown-Waite		X	
Mr. Scott		X		Mr. Barrett (SC)	X		
Mr. Green		X		Mr. Gerlach	X		
Mr. Cleaver				Mr. Pearce	X		
Ms. Bean		X		Mr. Neugebauer	X		
Ms. Moore (WI)				Mr. Price (GA)	X		
Mr. Davis (TN)		X		Mr. Davis (KY)	X		
Mr. Sires				Mr. McHenry	X		
Mr. Hodes		X		Mr. Campbell		X	
Mr. Ellison		X		Mr. Putnam			
Mr. Klein		X		Mrs. Bachmann			
Mr. Mahoney (FL)		X		Mr. Roskam	X		
Mr. Wilson		X		Mr. Marchant			
Mr. Perlmutter		X		Mr. McCotter	X		
Mr. Murphy		X					
Mr. Donnelly		X					
Mr. Wexler		X					
Mr. Marshall				.			
Mr. Boren		X					

An amendment by Mr. Price (GA), No. 1f, authorizing the Secretary of the Treasury to adjust the trigger for loan eligibility, was not agreed to by a record vote of 27 yeas and 32 nays (Record vote FC–68):

Representative	Aye	Nay	Present	Representative	Aye	Nay	Present
Mr. Frank		X		Mr. Bachus	X		
Mr. Kanjorski		X		Mr. Baker	X		
Ms. Waters		X		Ms. Pryce (OH)	X		
Mrs. Maloney		X		Mr. Castle			
Mr. Gutierrez		X		Mr. King (NY)	X		
Ms. Velázquez				Mr. Royce	X		
Mr. Watt		X		Mr. Lucas	X		
Mr. Ackerman		X		Mr. Paul	X		
Ms. Carson				Mr. LaTourette	X		

Representative	Aye	Nay	Present	Representative	Aye	Nay	Present
Mr. Sherman		X		Mr. Manzullo	X		
Mr. Meeks				Mr. Jones		X	
Mr. Moore (KS)		X		Mrs. Biggert	X		
Mr. Capuano		X		Mr. Shays	X		
Mr. Hinojosa				Mr. Miller (CA)	X		
Mr. Clay		X		Mrs. Capito	X		
Mrs. McCarthy		X		Mr. Feeney	X		
Mr. Baca		X		Mr. Hensarling	X		
Mr. Lynch		X		Mr. Garrett (NJ)	X		
Mr. Miller (NC)		X		Ms. Brown-Waite		X	
Mr. Scott		X		Mr. Barrett (SC)	X		
Mr. Green		X		Mr. Gerlach	X		
Mr. Cleaver				Mr. Pearce	X		
Ms. Bean		X		Mr. Neugebauer	X		
Ms. Moore (WI)				Mr. Price (GA)	X		
Mr. Davis (TN)		X		Mr. Davis (KY)	X		
Mr. Sires				Mr. McHenry	X		
Mr. Hodes		X		Mr. Campbell	X		
Mr. Ellison		X		Mr. Putnam			
Mr. Klein		X		Mrs. Bachmann	X		
Mr. Mahoney (FL)		X		Mr. Roskam	X		
Mr. Wilson		X		Mr. Marchant			
Mr. Perlmutter		X		Mr. McCotter	X		
Mr. Murphy		X					
Mr. Donnelly		X					
Mr. Wexler		X					
Mr. Marshall		X					
Mr. Boren		X					

An amendment by Mr. Price (GA), No. 1g, adding an additional requirement to the definition of "qualified reinsurance program", was not agreed to by a record vote of 31 yeas and 32 nays (Record vote FC–69):

Representative	Aye	Nay	Present	Representative	Aye	Nay	Present
Mr. Frank		X		Mr. Bachus	X		
Mr. Kanjorski		X		Mr. Baker	X		
Ms. Waters		X		Ms. Pryce (OH)	X		
Mrs. Maloney		X		Mr. Castle	X		
Mr. Gutierrez		X		Mr. King (NY)	X		
Ms. Velázquez				Mr. Royce	X		
Mr. Watt		X		Mr. Lucas	X		
Mr. Ackerman		X		Mr. Paul	X		
Ms. Carson				Mr. LaTourette	X		
Mr. Sherman		X		Mr. Manzullo	X		
Mr. Meeks				Mr. Jones	X		
Mr. Moore (KS)		X		Mrs. Biggert	X		
Mr. Capuano		X		Mr. Shays	X		
Mr. Hinojosa				Mr. Miller (CA)	X		
Mr. Clay		X		Mrs. Capito	X		
Mrs. McCarthy		X		Mr. Feeney	X		
Mr. Baca		X		Mr. Hensarling	X		
Mr. Lynch		X		Mr. Garrett (NJ)	X		
Mr. Miller (NC)		X		Ms. Brown-Waite	X		
Mr. Scott		X		Mr. Barrett (SC)	X		
Mr. Green		X		Mr. Gerlach	X		
Mr. Cleaver				Mr. Pearce	X		
Ms. Bean		X		Mr. Neugebauer	X		
Ms. Moore (WI)		X		Mr. Price (GA)	X		
Mr. Davis (TN)		X		Mr. Davis (KY)	X		
Mr. Sires		X		Mr. McHenry	X		
Mr. Hodes		X		Mr. Campbell	X		
Mr. Ellison		X		Mr. Putnam			
Mr. Klein		X		Mrs. Bachmann	X		
Mr. Mahoney (FL)		X		Mr. Roskam	X		

Representative	Aye	Nay	Present	Representative	Aye	Nay	Present
Mr. Wilson		X		Mr. Marchant	X		
Mr. Perlmutter		X		Mr. McCotter	X		
Mr. Murphy		X					
Mr. Donnelly		X					
Mr. Wexler		X					
Mr. Marshall		X					
Mr. Boren		X					

An amendment by Mr. Price (GA), No. 1h, limiting federal loans to only catastrophic events, was not agreed to by a record vote of 29 yeas and 34 nays (Record vote FC–70):

Representative	Aye	Nay	Present	Representative	Aye	Nay	Present
Mr. Frank		X		Mr. Bachus	X		
Mr. Kanjorski		X		Mr. Baker	X		
Ms. Waters		X		Ms. Pryce (OH)	X		
Mrs. Maloney		X		Mr. Castle	X		
Mr. Gutierrez		X		Mr. King (NY)	X		
Ms. Velázquez				Mr. Royce	X		
Mr. Watt		X		Mr. Lucas	X		
Mr. Ackerman		X		Mr. Paul	X		
Ms. Carson				Mr. LaTourette	X		
Mr. Sherman		X		Mr. Manzullo	X		
Mr. Meeks				Mr. Jones		X	
Mr. Moore (KS)		X		Mrs. Biggert	X		
Mr. Capuano		X		Mr. Shays	X		
Mr. Hinojosa				Mr. Miller (CA)	X		
Mr. Clay		X		Mrs. Capito	X		
Mrs. McCarthy		X		Mr. Feeney	X		
Mr. Baca		X		Mr. Hensarling	X		
Mr. Lynch		X		Mr. Garrett (NJ)	X		
Mr. Miller (NC)		X		Ms. Brown-Waite	X		
Mr. Scott		X		Mr. Barrett (SC)	X		
Mr. Green		X		Mr. Gerlach	X		
Mr. Cleaver				Mr. Pearce	X		
Ms. Bean		X		Mr. Neugebauer	X		
Ms. Moore (WI)		X		Mr. Price (GA)	X		
Mr. Davis (TN)		X		Mr. Davis (KY)	X		
Mr. Sires		X		Mr. McHenry	X		
Mr. Hodes		X		Mr. Campbell		X	
Mr. Ellison		X		Mr. Putnam			
Mr. Klein		X		Mrs. Bachmann	X		
Mr. Mahoney (FL)		X		Mr. Roskam	X		
Mr. Wilson		X		Mr. Marchant	X		
Mr. Perlmutter		X		Mr. McCotter	X		
Mr. Murphy		X					
Mr. Donnelly		X					
Mr. Wexler		X					
Mr. Marshall		X					
Mr. Boren		X					

The following other amendments were also considered by the Committee:

An amendment by Mr. Frank, No. 1, a manager's amendment in the nature of a substitute, as amended, was agreed to by a voice vote.

An amendment by Ms. Brown-Waite, No. 1a, providing reinsurance coverage for state natural catastrophe insurance programs, was offered and withdrawn.

An amendment by Mr. Murphy, No. 1b, inserting "requires" regarding qualified reinsurance programs, was agreed to by a voice vote.

An amendment by Mr. Feeney, No. 1d, regarding direct assistance to homeowners, was offered and withdrawn.

An amendment by Mr. Bachus, No. 1e, adding a precondition for qualified reinsurance programs, was offered and withdrawn.

An amendment by Mr. Campbell, No. 1i, including commercial property, was offered and withdrawn.

COMMITTEE OVERSIGHT FINDINGS

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

PERFORMANCE GOALS AND OBJECTIVES

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

H.R. 3355 is intended to provide Federal support for State-sponsored reinsurance programs designed to help homeowners prepare for and recover from damage caused by natural catastrophes, to encourage mitigation of such damage and to promote the transfer of insured natural catastrophe risk into the capital markets.

NEW BUDGET AUTHORITY, ENTITLEMENT AUTHORITY, AND TAX EXPENDITURES

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

COMMITTEE COST ESTIMATE

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

CONGRESSIONAL BUDGET OFFICE ESTIMATE

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

OCTOBER 30, 2007.

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

DEAR MR. CHAIRMAN: The Congressional Budget Office has prepared the enclosed cost estimate for H.R. 3355, the Homeowners' Defense Act of 2007.

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

Sincerely,

PETER R. ORSZAG.

Enclosure.

H.R. 3355—Homeowners' Defense Act of 2007

Summary: H.R. 3355 would authorize the appropriation of $120 million over the 2008–2013 period to establish a National Catastrophe Risk Consortium to help coordinate the availability of reinsurance contracts between state reinsurance entities and the private market. The consortium also would act as an information repository for states on the risk of natural disasters and research on the standardization of risk-linked securities (for example, catastrophe bonds). Assuming the appropriation of the specified amounts, CBO estimates that implementing this provision would cost $75 million over the 2008–2012 period.

The bill also would establish two new federal direct loan programs within the Department of the Treasury for state reinsurance programs facing certain levels of insured losses following a natural disaster. Loans could be made only if a reinsurer could not access capital in the private market and repayment was secured by the full faith and credit of the state. Treasury would develop procedures for state reinsurance programs to prequalify for loans, including the assessment of fees to cover the cost of administering the program. CBO expects that such loans would be made very rarely and would involve a minimal subsidy cost under the terms specified in the legislation. As such, CBO estimates that loans made under the bill would have an insignificant cost over the next five years. Enacting H.R. 3355 would not affect direct spending or revenues.

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

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

	By fiscal year, in millions of dollars—				
	2008	2009	2010	2011	2012
Authorization Level	20	20	20	20	20
Estimated Outlays	3	12	20	20	20

Note: H.R. 3355 also would authorize the appropriation of $20 million in fiscal year 2013.

Basis of estimate: For this estimate, CBO assumes that the bill will be enacted in early fiscal year 2008 and that the necessary amounts will be appropriated for each fiscal year.

National Catastrophe Risk Consortium

H.R. 3355 would authorize the appropriation of $20 million for each of fiscal years 2008 through 2013 to establish the National Catastrophe Risk Consortium. The consortium would be a federal entity managed by a board of directors made up of designees from the Departments of the Treasury, Commerce, and Homeland Security, and members from each participating state. Responsibilities of the Consortium would include: encouraging and facilitating different avenues for state insurers to enter into reinsurance agreements with the private market, conducting research and analysis into the standardization of risk-linked securities, and gathering insurance information. Assuming the appropriation of the specified

amounts, CBO estimates that implementing this provision would cost $3 million in 2008 and $75 million over the 2008–2012 period for staff and research expenses.

Liquidity and catastrophe loans for state reinsurance programs

H.R. 3355 would establish two new direct loan programs within the Department of the Treasury for state reinsurance programs facing a certain level of insured losses following a natural disaster. Reinsurance programs insure primary insurers or other reinsurers against losses in excess of amounts specified by contract or law. Reinsurance programs eligible for the new loan programs created under the bill would only be those in which the authorizing state maintained a financial interest. Examples of such reinsurance programs include the Florida Hurricane Catastrophe Fund (FHCF) and the California Earthquake Authority. In cases where a state does not have a reinsurance program that meets the requirements for a loan under the bill, a state residual insurer (for example, wind pool programs) would be eligible to apply during the five-year period following enactment.

Procedures to Establish Loan Eligibility. H.R. 3355 would direct the Secretary of the Treasury to develop procedures for reinsurance programs to establish loan eligibility prior to a natural disaster. At a minimum, insurance entities covered by the reinsurer would be required to establish rate structures sufficient to cover expected annualized costs and ensure that any new construction or substantial renovation of insured properties comply with applicable state and local building codes. As a part of the precertification process, the Secretary would assess a fee on state reinsurance programs to cover the costs of administering the loan program. Those fees would be credited in the budget as an offsetting collection and would be available upon subsequent appropriation of a loan subsidy.

Based on information about the characteristics of existing state reinsurance programs and on information from the Treasury, CBO expects that most state reinsurance programs would meet the eligibility requirements set forth under the bill and thus would be eligible to receive loans. In addition, other qualified reinsurance programs may be established in the future that also would be eligible to receive loans.

Liquidity Loans. Under H.R. 3355, a qualified reinsurance program would be eligible to receive a liquidity loan if the program demonstrates it is facing a liquidity shortage and is not able to access capital at a reasonable rate in the private market. The principal of such loans could not exceed the ceiling coverage level—the maximum amount of liability the program could incur under law. In addition, the full faith and credit of the state in which the reinsurance program is authorized would be required. Loans would be made at a rate of not less than 3 percentage points above the applicable Treasury rate and for a term of between five and ten years.

Based on information from the state of Florida, CBO expects that those loans would most likely be used to address short-term liquidity shortages and would be repaid once adequate capital became available through established reinsurance agreements or through the private market. In cases where a liquidity loan is held to term (which CBO expects would be unlikely to occur because of the high

interest rate of the loan), CBO estimates that those loans would have no significant cost to the federal government. As of June 2007, rating agencies like Standard and Poor's have not issued a credit rating below "A" for new general obligation bonds issued by a state. Based on historical default rates and the minimum terms specified in the bill, CBO estimates that the default risk associated with a state's general obligation bond rating would have to increase significantly before such a loan would be estimated to have more than a negligible subsidy cost. While the default risk of loans backed by the full faith and credit of a state would likely increase following a disaster, CBO expects that this increase would not be significant. (Following Hurricane Katrina, for example, Standard and Poor's announced it would adjust a state's credit rating for the first time as a result of a natural disaster by lowering Louisiana's rating from an A+ to an A.) As such, CBO estimates that any liquidity loan made under the bill would have an insignificant cost over the next five years.

Catastrophe Loans. Under the bill, a qualified reinsurance program would be eligible to receive a catastrophe loan following a disaster if insured losses exceeded 150 percent of the aggregate amount of premiums assessed (whether collected or not) for private property and casualty insurance issued in the state over the previous 12-month period. The principal of such a loan could not exceed the difference between the total insured loss and the program's ceiling coverage level, and repayment would be afforded the full faith and credit of the state. Loans would be made at a rate of not less than 20 basis points above the applicable Treasury rate and for a term of not less than 10 years.

Based on information from the states, CBO expects that few, if any, reinsurance programs would apply for a catastrophe loan following a disaster. State insurance commissions and rating agencies often require that primary insurers are able to cover at least a 100-year event to maintain their credit rating. As such, not only would losses exceeding the ceiling coverage level be outside the responsibility of the reinsurer, they likely would be covered through existing reinsurance agreements between the primary insurer and the private market.

For example, as a result of Hurricane Katrina, the Gulf Coast faced insured losses of over $40 billion. Such losses well exceeded the minimum eligibility threshold for a catastrophe loan under the bill. (Based on the aggregate amount of direct written premium for private property and casualty insurance, CBO estimates that the threshold probably would have been around $12 billion for Louisiana in 2005.) However, CBO expects that there would have been little demand for a catastrophe loan following Katrina because a state reinsurance program (if one had existed) would not have been responsible for losses above its ceiling coverage level. Furthermore, such losses would have been covered by existing reinsurance agreements between primary insurers and the private market. For those reasons, CBO estimates that implementing this provision would have no cost over the next five years.

Intergovernmental and private-sector impact: H.R. 3355 contains no intergovernmental or private-sector mandates as defined in UMRA and would impose no costs on state, local, or tribal governments.

Estimate prepared by: Federal Costs: Daniel Hoople; Impact on State, Local, and Tribal Governments: Melissa Merrell; Impact on the Private Sector: MarDestinee C. Perez.

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

FEDERAL MANDATES STATEMENT

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

ADVISORY COMMITTEE STATEMENT

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

CONSTITUTIONAL AUTHORITY STATEMENT

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

APPLICABILITY TO LEGISLATIVE BRANCH

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

EARMARK IDENTIFICATION

H.R. 3355 does not contain any congressional earmarks, limited tax benefits, or limited tariff benefits as defined in clause 9 of rule XXI.

SECTION-BY-SECTION ANALYSIS OF THE LEGISLATION

Sec. 1.—Short title

This section establishes the short title of the bill, the "Homeowners' Defense Act of 2007."

Sec. 2.—Findings and purpose

This section sets findings that support the creation of a National Catastrophe Risk Consortium and the National Homeowners Insurance Stabilization Program.

Title I—National Catastrophe Risk Consortium

Sec. 101.—Establishment; status; principal office; membership

This Title establishes a National Catastrophe Risk Consortium that would consist of qualified reinsurance programs that join on a voluntary basis. The Consortium is not a part of the Federal Government.

Sec. 102.—Functions

The Consortium will maintain an inventory of catastrophe risk obligations held by participating States and will issue securities and other financial instruments linked to catastrophe risks in the capital markets. Furthermore, the Consortium can coordinate reinsurance contracts with private parties.

The Consortium will also act as a database of State catastrophe risk information that can be accessed by private participants and perform research and analysis that encourages standardization of the risk-linked securities market.

The Consortium will also perform any other functions necessary to aid in catastrophe risk transfer and will submit a yearly report to Congress highlighting and explaining its activities.

Sec. 103.—Powers

The Consortium can enter into contracts as necessary to carry out its functions. The Consortium is given any other powers that may be necessary for carrying out this Act. It will not have the power to issue debt or assume risk.

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

The Consortium is a non-profit organization with no capital stock. The revenue, earnings, and all other income accrued to the Consortium shall only be used to carry out the provisions of this Act and not to enrich the Consortium personnel. Furthermore, to prevent conflicts of interest, no director, officer, or employee of the Consortium shall participate in the deliberation upon any question affecting his or her personal interests. Finally, to ensure continued integrity, the Consortium's financial statements shall be audited annually by independent certified public accountants. The audit shall be included in the Consortium's annual report to Congress.

Sec. 105.—Management

The Consortium shall be managed by a Board of Directors consisting of not fewer than three members. The Secretary of the Treasury or his designee shall serve as the chairperson. Designees of the Secretaries of Homeland Security and Commerce shall also serve as board members but only during such times there are fewer than two states participating in the Consortium. Furthermore, the Board has the authority to appoint an Executive Director.

Only Board members who are not Federal employees will be eligible for compensation.

Sec. 106.—Staff; experts and consultants

The Board of Directors may appoint and terminate staff and set their compensation as is deemed appropriate for the purposes of the Consortium. The Board also has the power to contract expert consultants as it deems appropriate.

Sec. 107.—Federal liability

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

Sec. 108.—Authorization of appropriations

The Consortium is authorized for five years at $20 million per year.

Title II—National Homeowners' Insurance Stabilization Program

Sec. 201.—Establishment

The Secretary shall carry out a program to make liquidity loans and catastrophic loans to qualified reinsurance programs.

Sec. 202.—Liquidity loans and catastrophic loans for state and regional reinsurance programs

To the extent that a qualified reinsurance program cannot access capital in the private market, a qualified program can be eligible to receive two types of Federal loans. The program must file a report with the Treasury Secretary explaining how it will repay the loan and the Secretary must find that—based on the report—the program will be able to meet the loan terms.

The Secretary can extend liquidity loans to a qualified reinsurance program after the Secretary determines that the qualified reinsurance program has a funding shortage and cannot borrow in the capital markets. The amount of the loan cannot exceed the ceiling coverage level for the qualified reinsurance program. The liquidity loan has a maturity of between five and ten years and an interest rate set at three percentage points higher than Treasury obligations of comparable maturity. In addition, the Secretary can set the rate higher if necessary to ensure the interest paid under a loan exceeds the sum of costs for that loan.

The Secretary can extend catastrophic loans to a State's qualified reinsurance program, if the Secretary determines that an event has occurred in that state resulting in insured losses that exceed 150 percent of that State's direct written premium for privately issued property and casualty insurance. The loan amount cannot exceed the amount by which the insured losses exceed the ceiling coverage level of the qualified reinsurance program. Catastrophic loans have an annual interest rate 0.20 percentage points higher than marketable obligations of the Treasury and a term to maturity of not less than ten years.

The loan proceeds may only be used to pay claims made to qualified reinsurance programs.

Sec. 203.—Reports and audits

The Secretary is required to submit an annual report to the President and Congress that identifies and describes loans made under this title.

Sec. 204.—Funding

The Secretary is directed to collect a reasonable fee from qualified reinsurance programs in order to offset the expenses associated with the loan program. The Secretary shall require the full repayment of loans made under Title II and must submit a report to Congress when and if it is determined that such loans will not be repaid.

Title III—General Provisions

Sec. 301.—Qualified reinsurance programs

A qualified reinsurance program is an entity authorized by the State that provides reinsurance or retrocessional coverage to underlying primary insurers or reinsurers for losses arising from all personal residential lines of insurance. Authorizing states must require that such programs pass any cost savings onto insurance consumers, ensure compliance with building codes, use a rate structure that reflects loss mitigation, and set rates at a level that generates sufficient premium to pay expected annualized claims. This section may not, however, be construed to limit or prevent any insurer from obtaining reinsurance coverage for insured losses retained by insurers.

In the case of states that do not have a qualified reinsurance program, State residual insurance programs can be considered qualified reinsurance programs for five years from the date of enactment. The Secretary will establish procedures and standards for state and regional reinsurance programs and residual insurance market entities to apply for pre-certification, certification, and recertification.

Sec. 302.—Definitions

Ceiling Coverage Level is the maximum aggregate amount of coverage provided at any time by a qualified reinsurance program.

Homeowners Insurance is as defined in the Uniform Property & Casualty Product Coding Matrix published and maintained by the National Association of Insurance Commissioners.

Insured Loss means any loss insured by a qualified reinsurance program.

Qualified Reinsurance Program is a program that meets the qualifications provided in section 301.

Sec. 303.—Regulations

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

ADDITIONAL VIEWS

It is unfortunate that the Committee has rushed to report legislation that does little more than provide federally subsidized loans to the insurance company of one state, at the expense of taxpayers across the country. Only one hearing was held on H.R. 3355, and practically every witness raised serious concerns with the legislation. Despite the negative witness testimony and opposition expressed by numerous environmental groups, consumer organizations, and insurance experts, H.R. 3355 was rammed through the committee less than two months after its introduction, on a near party-line vote. There are several alternative proposals that have been introduced by Members this year that directly address the tax, regulatory, and marketplace issues that are causing a crisis in certain states, and there is still an opportunity that the Committee should consider to develop bipartisan consensus legislation.

As the nation's most hurricane-prone state, Florida has repeatedly sought to secure more. affordable insurance for its residents. According to a recent report issued by the Georgetown University Law Center Environmental Law & Policy Institute, since Hurricane Andrew in 1992, Florida's real property values have increased from $421 billion to more than $1.2 trillion, with 80 percent of Florida's 16 million residents living within ten miles of the coast. Coastal development has expanded wildly, despite the increased threat of future hurricanes. In 2004, four huge storms—Charley, Frances, Ivan, and Jeanne—hit Florida, causing about $29 billion in insured losses. In 2005, Hurricanes Katrina, Rita, and Wilma ripped through the Atlantic and Gulf of Mexico, causing even higher losses.

The increased frequency and magnitude of storms in Florida, coupled with state regulations preventing insurers from charging risk-based prices, limits on capital movement, and uncertainty over legal and regulatory enforcement of contracts, has caused many private insurers to reduce their exposure and new underwriting in the state. Florida has tried to subsidize the affordability of property insurance for residents, such as requiring insurance companies to offer homeowners' coverage if they seek to offer auto insurance in the state, mandating below-market rates, and expanding the state insurance company. In 2002, Florida created Citizens Property Insurance Corporation as the state's "insurer of last resort" for property owners unable to secure wind coverage through the private market because of high hurricane risk. According to one report, at its founding, Citizens had 600,000 policies and an exposure of $148 billion. It is now Florida's largest property insurer, with more than 1.3 million policies and an exposure of around $440 billion.

Within 3 years of its creation, Citizens was billions of dollars in debt. According to the Georgetown report, the Florida legislature was forced to bail out Citizens by appropriating $715 million from

the state treasury, as well as assessing insurers and policyholders. In addition to Citizens, the state maintains the Florida Hurricane Catastrophe Fund (FHCF), which sells subsidized reinsurance to insurers to encourage them to write business in the state. The FHCF currently provides $27.85 billion in coverage despite having only $2.2 billion in non-debt cash assets.

MARKUP OF H.R. 3355, THE HOMEOWNERS' DEFENSE ACT OF 2007

On September 25, 2007, the Financial Services Committee approved H.R. 3355 by a mostly party-line vote of 36–27. Several fiscally-responsible Republican amendments were rejected at markup. Representative Shays offered an amendment to replace the convoluted text of H.R. 3355 with a bipartisan, blue-ribbon commission to report specific recommendations to Congress to increase the availability and affordability of natural catastrophe insurance. This amendment is similar to both H.R. 3644, a natural catastrophe commission bill sponsored by Representatives Shays and Blumenauer, and a bill approved by the Senate Banking Committee earlier this year. Representative Shays' amendment would have required the Commission to specifically examine the impact of H.R. 3355 and other proposals currently before Congress, including Representative Taylor's expansion of the NFIP to include wind insurance, Representative Brown-Waite's natural catastrophe reinsurance backstop, and tax reserving proposals by Representatives Feeney and Jindal.

Representative Price offered three amendments to reduce the burden this bill imposes on taxpayers. One amendment would have allowed the Treasury Secretary to increase the event size trigger before subsidized Federal loans would be provided to limit further displacement of the private market. A higher trigger would also encourage state reinsurance funds to build additional surplus capital before an event. His second amendment would have required Treasury to issue a loan only if it would not displace or reduce private sector competitiveness. His third amendment would have limited subsidized loans to natural disaster events that Treasury determined exceeded the capacity of the insurance industry for a particular region, or that are greater than a one in one-hundred year nationwide event for the homeowners' insurance marketplace.

REPUBLICAN CONCERNS REGARDING H.R. 3355

Treasury and various consumer, environmental, and industry groups have voiced concerns that H.R. 3355 would expose taxpayers to massive liabilities and encourage further development along hurricane-prone coastlines. A critical Wall Street Journal editorial dated October 10, 2007 quoted Assistant Treasury Secretary Phillip Swagel, who testified at a September 6, 2007 Financial Services Committee legislative hearing on the bill, as saying "taxpayers nationwide would subsidize insurance rates in high-risk areas, which would be both costly and unfair." On September 24, 2007, the National Wildlife Federation transmitted a letter to Chairman Frank and Ranking Member Bachus, opposing H.R. 3355 on grounds that the bill does not contain adequate mitigation provisions, could lead to increased building in vulnerable areas, and would unnecessarily burden taxpayers.

It is unclear whether Title I of H.R. 3355, which would create a voluntary Federal consortium to pool state catastrophe risk, securitize that risk, and broker reinsurance contracts for states, would offer any additional value other than providing an implicit Federal guarantee or backing. States already can and do purchase reinsurance and sell catastrophe bonds through their risk pools and funds. In fact, Florida raised money for the FHCF this way for the past two years. It is dubious whether regional pooling facilitated by a consortium would have any benefit in reducing costs over pooling through the global reinsurance markets. Florida and other states with catastrophe risks have already met and discussed on numerous occasions pooling their risks, but without generating any new synergies.

The ability of the consortium to dump billions of dollars into the catastrophe bond marketplace is also highly questionable. Catastrophe bonds are high-risk, but potentially high-yield, financial instruments that generally appeal to institutional investors wanting to hedge against other risks. Large, sophisticated investors find these securities attractive because the risk natural catastrophes pose differs, and is not correlated with, financial risks in the capital markets. The Committee has requested numerous Government Accountability Office (GAO) studies in the past on catastrophe bonds that have suggested the appetite for further cat bond issuance beyond its current slow annual growth is significantly limited by the sophistication required to analyze the offerings, the riskiness of the issues, and its cost disadvantages versus traditional reinsurance. At the legislative hearing on H.R. 3355, one witness, a hedge fund manager specializing in risk-linked securities, expressed doubts that the consortium would increase demand for catastrophe bonds.

Even more troubling is Title II of H.R. 3355, which mandates that Treasury offer below-market subsidized loans to state reinsurance funds. Two types of long-term loans would be available to states with a fund, although the FHCF is currently the only pure reinsurance fund and, thus, the only “qualified reinsurance fund” as described by the bill. Liquidity loans would be offered in amounts up to the ceiling coverage limit of state reinsurance funds that have a capital liquidity shortage and are not able to access capital more cheaply. Catastrophic loans would be available to state reinsurance funds after the state experiences a natural catastrophe resulting in insured losses of at least 150% of direct earned premium from the previous year for all lines of property and casualty insurance written in the state. While Title II has been criticized as a subsidized Federal loan, a recent GAO report on natural catastrophes questions whether Congressional disaster loans would ever be repaid. Although the event size trigger for the catastrophic loan was increased at Committee markup of the bill, minimizing the chance that taxpayers will be on the hook for relatively minor events, Republicans are concerned that this increased trigger does not apply to liquidity loans. State reinsurance funds would be eligible for liquidity loans upon suffering “insured losses,” with no prescribed loss amount or event size.

Despite receiving testimony from witnesses that H.R. 3355 lacks any real mitigation mechanism, little improvement has been made

in this area since the bill's introduction. The lack of any additional mitigation mandates furthers the potential exposure for taxpayers. As reported, H.R. 3355 requires adherence to state building codes in order to be eligible for liquidity and catastrophic loans, but this fails to recognize that some states and localities lack effective building codes. Substandard codes would not bar the receipt of these Federal loans. Republicans also remain concerned that recipient states would not be required to retain any losses before becoming eligible for the loans. Without a retained loss requirement, state reinsurance funds will have little incentive to adequately capitalize prior to an event, relying instead on post-event debt financing from the Federal government and taxpayers. Instead of propping up bankrupt state programs that undermine the private market, some Republicans have suggested as a more efficient use of taxpayer dollars, encouraging "reverse" loans for "equity rich, cash poor" homeowners meeting a set of criteria, to help defray the escalating costs of private homeowners' insurance in the aftermath of a large catastrophe. The rising cost of homeowners' insurance in Florida has become a stultifying burden on many coastal homeowners. Congress needs to be responsive to this crisis by enacting thoughtful bipartisan reform that addresses the marketplace and regulatory dysfunction. Unfortunately, H.R. 3355 falls far short of these goals.

SPENCER BACHUS.
SHELLEY MOORE CAPITO.

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