Testimony of
Guy Williams
on behalf of the
American **Bankers** Association

before the
Subcommittee on Housing and Community Opportunity
of the
Committee on Financial Services
United States House of Representatives

Regarding Issues Related to Catastrophe Insurance Availability
and the Housing Markets

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Chairman Ney, Ranking Member Waters, and members of the Subcommittee, my name is Guy Williams. I am the President of Gulf Coast Bank and Trust Company in New Orleans, Louisiana. I am here to testify today on behalf of the American Bankers Association regarding issues related to catastrophe insurance availability and the housing market, including legislative proposals that have called for a national catastrophe insurance program.

The American Bankers Association, on behalf of the more than two million men and women who work in the nation's banks, brings together all categories of banking institutions to best represent the interests of our industry. Its membership - which includes community, regional and money center banks and holding companies, as well as savings associations, trust companies and savings banks - makes ABA the largest banking trade association in the country.

Last year, hurricanes Katrina, Rita and Wilma caused unprecedented devastation to the gulf coast region of our country. Lives, homes, businesses and neighborhoods were lost. Tens of thousands were displaced, and the rebuilding has only begun. I am proud to say that the banking industry was one of the first on the scene to address the damage caused, to begin the rebuilding and to restore our communities. We, our partners, our customers and our regulators have learned many valuable and often painful lessons which will help us and others face catastrophes in the future. I served on a task force of the American Bankers Association on Emergency Preparedness which prepared a Tool Kit for ABA's members that will help them prepare for, and deal with, emergency situations. Similarly, the banking regulators have published "Hurricane Katrina: Lessons Learned" which will also help us to prepare for and recover from disasters.

I would like to make three points here today:

1. The banking industry is accustomed to responding to customer needs during and after natural disasters.
2. The banking industry is strongly committed to our local communities.
3. We need additional tools and improved programs to help ensure recovery and rebuilding after future disasters.

The banking industry is accustomed to responding to customer needs during disasters.

When a disaster strikes, every consumer should know that their bank is prepared, their deposits are safe, and that they will have continued access to their funds. Banks are required by law to have extensive disaster recovery plans in place to protect customer accounts, and state and federal regulators routinely examine each bank on their preparations. Banks have an admirable record and a proven history of restoring service as soon as possible after any unexpected event and working with our customers to address their needs and concerns. Post 9/11 procedures and extensive preparations for Y2K strengthened the banking industry's ability to deal with a broad range of disruptions, and our experiences after last year's hurricanes have broadened those abilities. In even some of the hardest hit areas of the Gulf Coast, banks were up and running the day after Hurricane Katrina hit. Institutions resumed operations using generators and limited communications, often in temporary facilities. After Hurricane Katrina our bank could not return to any of its offices or our operations center or our main office. Nonetheless we reopened the Monday after the storm in rented facilities, our internet banking product continued to operate 24/7, and we made $18,000,000 in reconstruction loans in the 30 days after the storm.

<u>The banking industry is strongly committed to our local communities.</u>

Banks are a key player in the short and long term recovery after any disaster. From ensuring that cash is available immediately after a disaster to making bridge loans to help in short term recovery of individuals and businesses, to providing long-term financing for reconstruction, banks are on the scene and integral to disaster recovery. In the aftermath of last year's storms our industry has not treated the recovery as a competitive matter. Bankers from across the country immediately began providing assistance to banks in the most affected areas. We began working with our customers to help them deal with the aftermath of the disaster and plan for recovery. We extended forbearance on loans. We pushed the Small Business Administration to work more effectively to make disaster loans available. And we began making new loans to help customers rebuild. Almost immediately we faced challenges. Which brings me to my third and most extensive point:

<u>We need additional tools and program improvements to help ensure recovery and rebuilding after a catastrophe.</u>

A strong residential mortgage market requires a reliable secondary market for liquidity. After a disaster the need for liquidity is only enhanced. One of the first problems we faced in making new loans after the hurricanes was finding post-Katrina comparable appraisals that were acceptable to the secondary market. There simply were no comparables in the sense traditionally required by Fannie Mae and Freddie Mac. Initially we were unable to sell home mortgages to the agencies because of appraisal regulations. As a result of work by the Louisiana Bankers Association and the ABA we were able to work out an interim solution that allows loans to be purchased that are 80% of the hard cost or 70% of the pre-Katrina value. While this is helpful it clearly excludes borrowers that do not have the wherewithal to make 20% to 30% down payments. We are continuing to work with the agencies and hope to improve on these ratios as we go forward.

More problematic than the appraisal issue has been that of the availability and affordability of property and casualty insurance after a disaster. Currently, insurers have suspended writing new homeowners coverage in coastal areas around the Gulf, and many insurers, including the market leaders, are declining to renew some policies already in place. Insurers cannot find re-insurance at rates sufficiently affordable to continue offering homeowners policies at a rate state governments consider appropriate. As you are aware, homeowners insurance is subject to strict rate regulation in most states. As a result, Gulf state residents are seeing their homeowner's coverage, previously purchased through an insurance company, replaced by a policy written by the state's insurer of last resort.

The state insurers are themselves in a particularly precarious financial position. Not only are the state-run companies gaining market share - many are the second or third largest insurer in their state - but they are also in such a poor financial position that some believe that if these state-run insurers were private companies many would have been placed in receivership.

The loss of willing private insurers and the expansion of state-run insurers of last resort has increased premium costs for consumers, decreased the available supply of private homeowner's coverage as the government displaces private industry, and depressed, sometimes dramatically, the value of homes.

The state of Louisiana, like a number of other states, has a state sponsored "backstop" insurance program to provide insurance of last resort to those residents who are unable to obtain it from the private market. The Louisiana Fair plan will provide homeowners insurance when it is commercially unavailable. Unfortunately, the Louisiana plan is actuarially bankrupt and only the full faith and credit of the state of Louisiana is keeping it afloat. In order to cover last year's losses, all insurance policies issued in Louisiana will be subject to an 18% surcharge this year. Because of its low limits and precarious financial condition, the Fair plan is not the answer, nor will other state's similar plans suffice in the face of future disasters. Just this week our community bank approved two commercial loans that may not close because the borrowers cannot secure windstorm damage at any price. Without affordable insurance, our continued recovery is in doubt.

Due to these limitations faced by both the private insurance market and state sponsored "backstop" programs, the American Bankers Association believes that the creation of a federal disaster insurance program is necessary. Legislation to create such a program has been introduced in the last several congresses. The latest proposal has been introduced in this congress by Rep. Ginny Brown-Waite (R-FL). The approach taken in these proposals would create a national re-insurance program to be funded through regional auctions of re-insurance contracts to be purchased by eligible state catastrophe funds. These state funds would be financed through mandatory contributions by insurance companies in each of those states in an amount that reflects the catastrophe risk of the policies that they write in each state.

Each state fund would be required to set aside a minimum of $10 million and a maximum of 35% of investment income for mitigation programs. Rates for this coverage would be actuarially based and self-sufficient and would only be available to state programs that have established prevention and mitigation programs.

Absent this or a similar program, all taxpayers cover the costs of uninsured and underinsured properties when a catastrophe strikes. Providing a "backstop" ensures that risk-based insurance remains available and affordable, increasing the ability to cover those who need it and reducing the cost borne by taxpayers when a catastrophe strikes.

Mr. Chairman, I want to thank you again for inviting me to testify here today. I will be pleased to answer any questions you or other members of the subcommittee may have. Thank you.