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The Homeowners Defense Act: Bad Policy and a Dangerous Precedent

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The Homeowners Defense Act (H.R. 3355) is a dangerous step toward a federal government subsidy of property insurance coverage for natural disasters. The bill would also make it easier for individual states to create unrealistic disaster insurance programs, with underpriced policies, by creating a federal loan fund to cover losses suffered by those programs. Congress should reject attempts to place the risk of property losses due to natural disasters on the federal government.

The bill would establish a consortium of state-sponsored natural disaster insurance funds that would be able to issue bonds to jointly finance these programs. Though there is nothing wrong with this and states are already empowered to create such consortiums, H.R. 3355 would grant this consortium a federal charter that would make it appear that the bonds issued by the group have a federal guarantee, when in fact, no such guarantee would exist. This false federal imprimatur could increase pressure for a federal bailout following any disaster.

What is worse, the legislation would also create a direct federal loan program to provide federal "bridge loans" to cover losses to state reinsurance programs when natural disaster claims exceed the state funds' assets. As experience with the federal flood insurance program shows, once those federal loans reach a significant level, there will be an immediate attempt to get the government to forgive them. In essence, then, the bridge loan program is nothing les than a back-door approach to having the federal government assume much of the risk for property losses caused by hurricanes and similar disasters.

A number of states, Florida being among the worst, have reacted to increasing property insurance rates by setting up state property insurance and reinsurance systems. In many cases, these state systems provide coverage at artificially low rates that are more influenced by short-term political considerations than actuarial estimates of risk. The Homeowners Defense Act would make it easier for states with the most unrealistic insurance rates to pool their risks with more responsible states and issue bonds that reflect the overall pool risk level rather than their own higher risk. This would allow them to issue bonds at lower interest rates than they would be able to otherwise.

State governments are free to develop irresponsible property insurance programs as long as they and their citizens understand that they must bear the consequences. H.R. 3355, however, creates a way for those states to make taxpayers in other states share in those inevitable losses. This bad policy should be avoided.

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