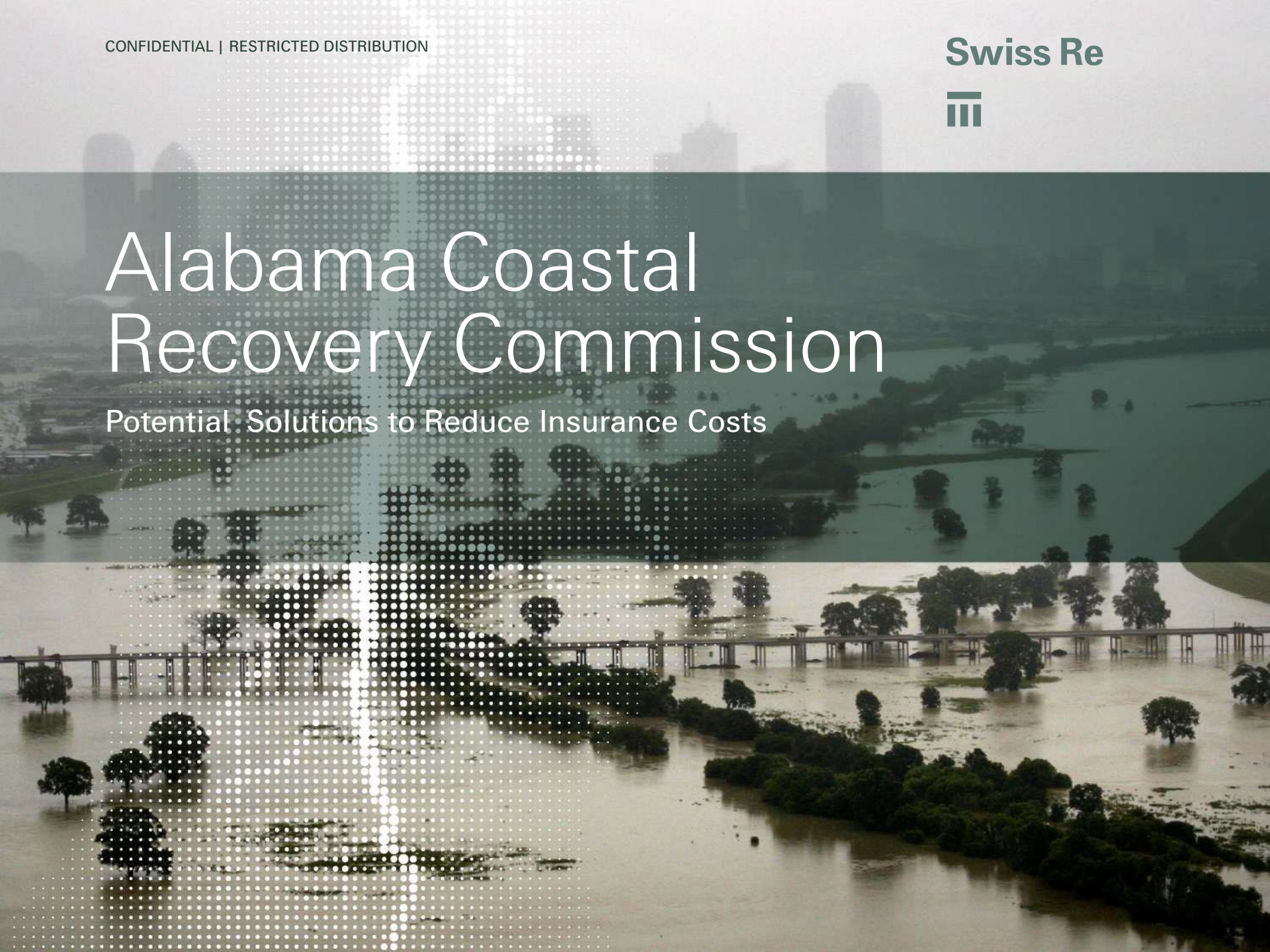




# Alabama Coastal Recovery Commission

Potential Solutions to Reduce Insurance Costs





# Understanding the *Exposure*



## Introduction

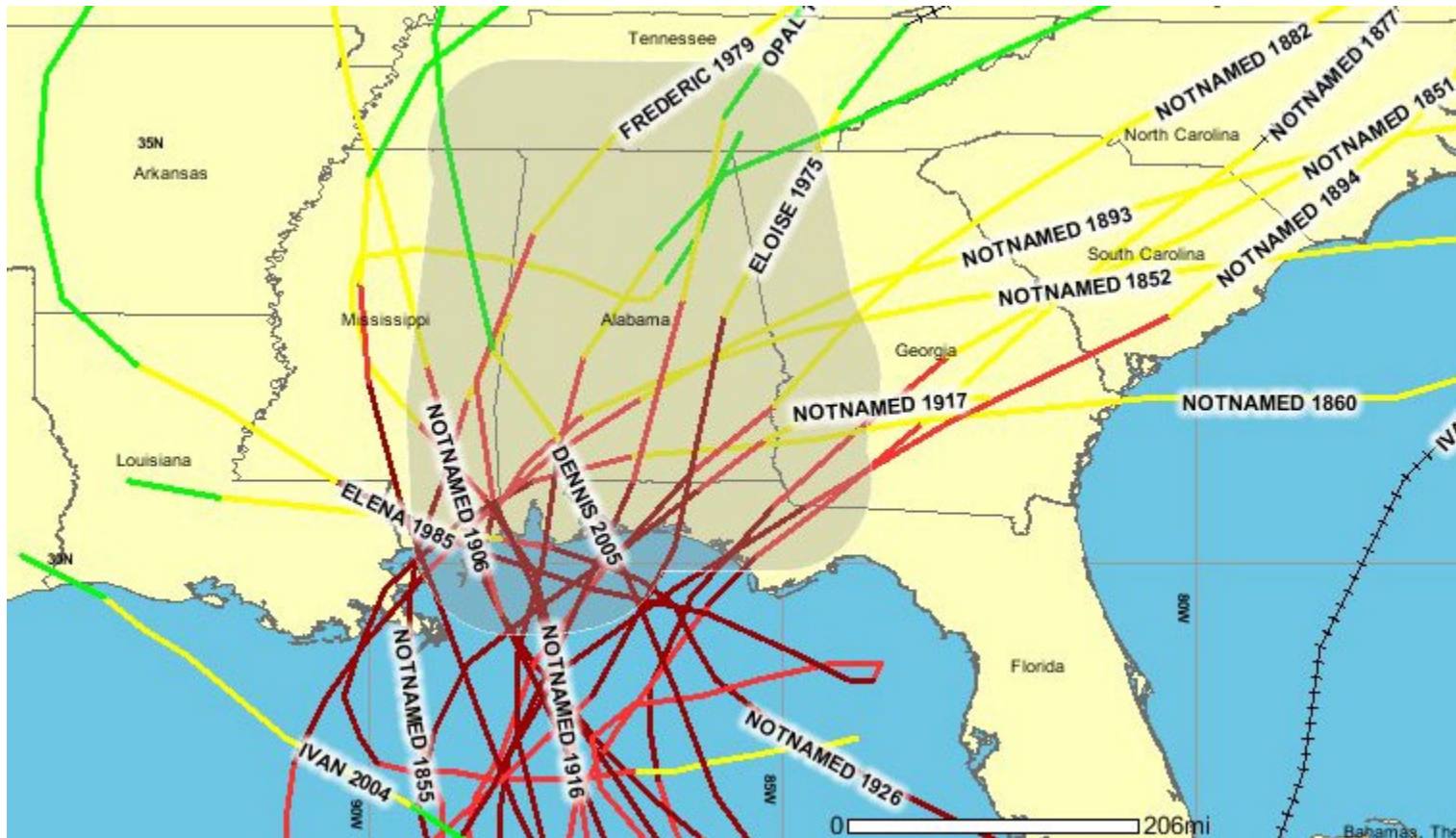
- The state of Alabama is facing increased economic and life safety risks, exacerbated by the current cycle of increased hurricane activity.
  - These risks are factored into all insurance premiums paid throughout the state
  - Though Alabama residents pay the 9<sup>th</sup> highest premiums nationally, they are insuring homes valued at 10% below the national norm
- In the aftermath of the Katrina and Ivan, coastal tourism, an engine for Alabama's growth and an employer to many, was particularly impacted
  - Lessons learned from Hurricanes Ivan and Katrina led to many insurers to raise premiums and cut wind coverage
  - Rising premium levels state-wide compounded normal financial challenges and are a long-term obstacle to economic development

**Affordable and available insurance is an absolute must for South Alabama due to its exposure to hurricanes**



# Category 3+ Hurricanes within 120 kilometers of Alabama (1851-2008)

Frequency of Category 3+ hurricanes within 120 kms: 1 every 10 years



Tracks courtesy of NOAA/CSC; Colors represent severity of event (i.e., Green = tropical cyclone; dark red = Category 4)



## Potential Exposure of Alabama

Return Period	Avg. Estimated Insurance Loss	Insurance Loss as % GSP <sup>1</sup>	Estimated Economic Loss <sup>2</sup>	Economic Loss as % of GSP
5	50	0.0%	100	0.1%
10	715	0.4%	1,431	0.8%
15	1,691	1.0%	3,383	2.0%
20	2,591	1.5%	5,182	3.0%
25	3,369	2.0%	6,737	4.0%
30	4,064	2.4%	8,128	4.8%
35	4,705	2.8%	9,410	5.5%
40	5,308	3.1%	10,616	6.2%
45	5,883	3.5%	11,765	6.9%
50	6,433	3.8%	12,867	7.6%
100	10,743	6.3%	21,485	12.6%
250	16,480	9.7%	32,961	19.4%
500	21,296	12.5%	42,593	25.1%

1. Based on Gross State Product of USD 170 billion

2. Assuming standard ratio of Insured vs. Economic loss of 1:2



# Understanding the *Solution*

## Mitigation and Inspection

- The long term goal is to reduce insurance premiums in a sustainable manner. **To accomplish this mitigation is key:**
  - Clear benchmark should be to bring coastal homes in AL to IBHS standards
- Mitigation of homes is a two-step process:
  1. Homeowners have home inspected to detail what modifications would be required to bring home to IBHS code
  2. Homeowner hires a contractor to complete the specified improvements
- Finally, in order to receive full credit for home improvement in insurance premium, homeowner provides insurance company proof (certification) of mitigation
- Key to success is providing the right incentives to allow homeowners to do all of the above
  - One solution may be by establishing an Coastal Mitigation Trust ("CMT")

## Coastal Mitigation Trust Concept

- CMT is funded by public money and offers Alabama residents a grant or loan to complete mitigation home improvements
  - Grant or loan is provided through local banks, not by Trust directly
- To qualify, for a grant or loan, a detailed inspection must be completed and submitted to the Bank
  - Through Bank, Trust will provide certified inspector list and pay for inspections
- Once inspection is complete, homeowner submits loan request to Bank
  - Bank loan is provided and guaranteed by CMT allowing for low interest rates
  - Repayment of loans will refresh Trust allowing for on-going grants and loans
- Interest on loans may be state tax-deductible, creating more incentive
- Once improvement is certified, insurance premiums will immediately decrease based on DoI rate filings (reductions in 20% - 30%)



# Coastal Mitigation Trust

**Homeowner**

Homeowner applies to Bank for inspection grant and loan/grant for mitigation. Following mitigation, Homeowner gets benefit of reduced premiums and receives state tax credit for interest payments on mitigation loan.

**Coastal Mitigation Trust**

Government-funded Coastal Mitigation Trust provides capital and loan guarantees to local banks to facilitate mitigation loans; CMT also reimburses individuals for inspection costs through banks or directly to inspectors

**Bank**

Bank provides Mitigation Loan as well as pays for inspection, with reimbursement from Trust. Bank receives funds from CMT but earns a spread on the loan, and has direct recourse to CMF if the homeowner defaults (no credit risk)

**Inspector**

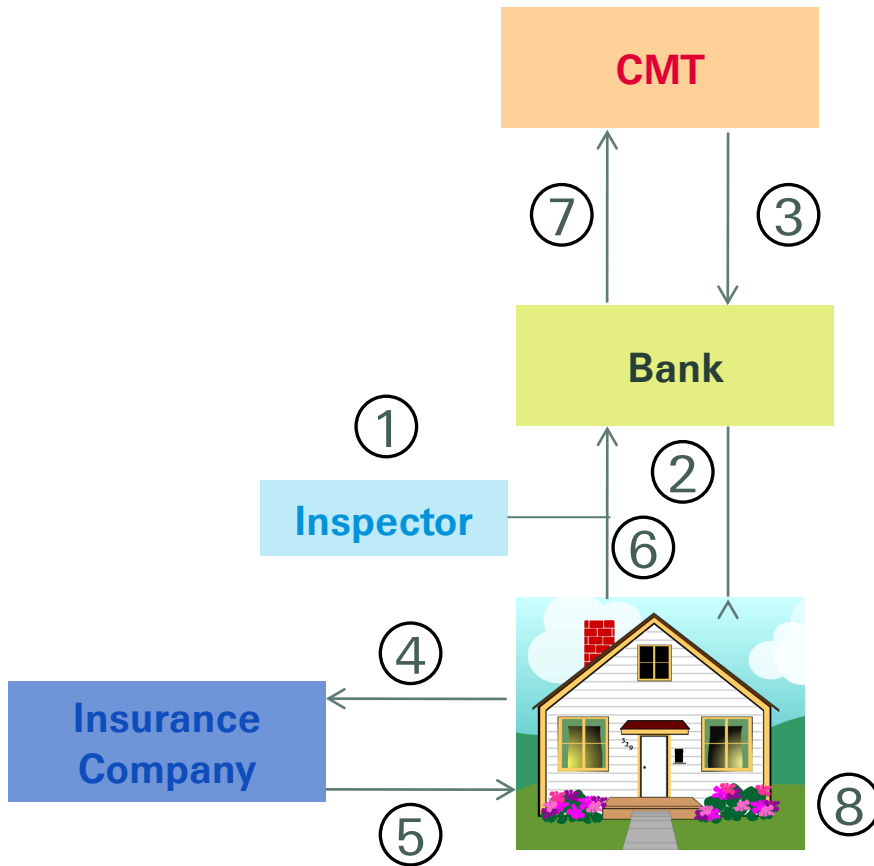
Licensed inspectors examine homes before mitigation and provide assessment of required improvements to achieve IBHS code levels. Charges fixed inspection cost.

**Insurance Company**

Insurance company provides immediate fixed premium discounts upon receiving Certification of Mitigation, based on DoI filings.

\* Loan may be made directly to contractor to ensure loan is used for mitigation

# Coastal Mitigation Trust



Step 1: Homeowner receives grant from CMT (via Bank) to complete inspection\*

Step 2: Post inspection, Homeowner requests from Bank low-interest loan or grant for home improvement

Step 3: Bank receives funds for loan from CMT, provides them to Homeowner

Step 4: Homeowner takes mitigation certification to Insurance Company

Step 5: Homeowner receives a mitigation credit that lowers his premium (based on DoI rates)

Step 6: Over length of loan, Homeowner pays back low-interest loan to Bank (no payback with grant)

Step 7: Bank returns capital back to CMT (including inflation, but without interest)

Step 8: Homeowner may receive state tax credit for interest on loan

\* Grant may be made directly to contractor to ensure loan is used for mitigation

## Conclusion

- The Coastal Mitigation Trust is designed to provide concrete incentives to homeowners to improve the mitigation qualities of their homes
  - Most critically this will directly lower their insurance premiums and could also provide tax credits
- However, the concept has additional benefits:
  - Increase in **employment** for small business (contractors and inspectors)
  - Good socially oriented but profitable **lending** for banks (no credit risk)
  - Better mitigation means more insurance **competition** (further reducing rates)
  - Sustainability of loan pool to ensure **long term mitigation** efforts are funded
- The CMT offers a public-private solution that provides the foundation for long term economic development of South Alabama



Thank you



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