New Orleans area deserves better insurance options, prices as hurricane season begins, officials say

http://www.nola.com/hurricane/index.ssf/2011/05/new_orleans_area_deserves_bett.h...

Clad in hard hats and sturdy shoes, about 20 insurance executives from around the country tromped through the new state-of-the art concrete flood defenses fortifying the New Orleans area to decide for themselves whether the region is safer — and more insurable — than it was six years ago.

Their impressions could have a big effect on how easy it is for homes and businesses in the New Orleans area to find property insurance coverage and what they pay for it.

A local insurance broker, Anderson Baker, organized the tour earlier this month out of frustration that insurers in faraway places like New York and Connecticut don't understand the geography of the New Orleans area and the scope of the $14.6 billion of flood protection improvement work that the Army Corps of Engineers has substantially completed.

"They think we're sitting down here ready to float off into the Gulf of Mexico any day now," said Baker, president of the commercial insurance agency Gillis, Ellis & Baker.

This year, the New Orleans area is in a very different place as it heads into hurricane season because the city will have reliable levees and true surge protection against a 100-year storm event. Public officials and insurance agents believe it's the best chance yet to demonstrate that the region deserves better insurance options and prices, but they're finding it's an uphill battle to displace images and perceptions from Hurricane Katrina.

"That's a huge investment in making us safe. We could have handled Katrina without flooding, I am certain, if it happened again," Insurance Commissioner Jim Donelon said. "I think they're generally aware it's going on, but I don't think they know the $15 billion, or what the condition of the levees was before."

Donelon has hosted web broadcasts with the corps each year on the anniversary of Katrina to keep insurers updated on progress, but has not yet been out on a flood protection tour. He said he plans to

start taking insurers out to see the work.

But at the very moment when the region has real protection against rising water, the insurance industry is throwing a new curveball at the city. A new crop of hurricane computer models that the insurance industry will use to assess risk in the New Orleans area either don't take the $14.6 billion in flood defenses into account, or in Donelon's estimation, don't give the engineering work enough credit. At the same time, one of the three major computer models shows increased potential for storm surge in coastal areas. "It's a huge negative for us," Donelon said.

Models drive decisions

Hurricane models are computer simulations that hurtle tens of thousands of storms at the coast to assess how the damage might look. Models change all the time because of breakthroughs in atmospheric research about how storms behave, advances in computing power and increasingly detailed data points about how different types of buildings fared in recent hurricanes.

Models have tremendous sway in what consumers and businesses pay for property insurance and how much coverage is available. Companies that insure a home or business use them to justify rates. Reinsurers, the unregulated global companies that sell extra coverage to regular insurance companies to shield them from the most extreme events, use them to decide what rates and how much coverage they'll sell. And financial rating agencies use them to decide whether companies have enough capital on hand to cover claims. If a company's portfolio shows a bigger risk of damage, the insurer needs to drop policies, raise rates, or a combination of the two, as happened after Hurricane Katrina, to maintain a healthy rating. Even if the company insuring a home or business doesn't use one of the models with the most dire predictions, chances are that company's reinsurer or rating agency does, so it still affects the consumer at the end of the line.

Proponents say that computer models bring science and a big picture view to insurance. Critics say that the models can change so much from one version to another — and estimates vary so much from one company to another — that the prognostications are junk. "It gives me cause for questioning their numbers and their motives," Donelon said. "They are paid by the companies that hire them. The insurers then use those numbers to justify rate increases."

The model that has insurance commissioners and consumer advocates reeling is a new model released in February by California company Risk Management Solutions.

The RMS 11 model will be most consequential for inland parts of Louisiana, because it shows much greater potential than in the past for hurricane wind losses far from the coast, but it's a mixed bag for

New Orleans. Scientists reviewed the corps' flood defense plans while they were devising the model and took those plans into account, but the model drastically increases the potential for hurricane storm surge damage in coastal areas, and leaves open the possibility that levees around New Orleans could fail. "This model was largely built before all the defenses were completed, but the plans were known," said Ryan Ogaard, senior vice president of natural catastrophe modeling and portfolio solutions at RMS.

RMS presented its model to the National Association of Insurance Commissioners and to the Louisiana Department of Insurance this year, and Donelon doesn't believe it gives enough credit to the corps' levee work, or to the statewide building code enacted after Katrina. He has not decided whether he will allow companies to use it in rate filings in Louisiana. The state generally follows Florida's decision, because it's the only state in the country that has built its own hurricane model to assess the performance of others. The Florida Commission on Hurricane Loss Projection Methodology meets June 2 to consider the RMS 11 model.

Another California company, Eqecat, will release a new model in July that's expected to be kinder to Louisiana, but the company's current model is banned for use in Louisiana because Donelon believes it overstates risk.

David Smith, senior vice president of model development at Eqecat, said the company's new model will show small to moderate decreases in risk for the New Orleans area, and that it does take the region's state-of-the-art flood defenses into account. The previous version only showed the levees as they were before Katrina. "It is clear that the defenses are much superior to what they were pre-Katrina," Smith said.

Boston-based AIR Worldwide released a major update to its hurricane model last summer that doesn't credit New Orleans for its new flood defenses.

Jayanta Guin, senior vice president of research and modeling, said that Louisiana's risk level is unchanged in AIR's latest model, but storm surge risk in coastal areas actually decreases slightly because AIR has changed the way it shows wind striking land. The new model takes into account the statewide building code that Louisiana enacted after Hurricane Katrina, but not the flood protection improvement work. "When we deem that we fully understand what the flood defense work from the Army Corps means, we will see if it can be factored into the model explicitly," Guin said.

Do rates reflect risks?

The levee improvement work won't have an effect on flood insurance until after the Federal Emergency Management Agency certifies the protection as bona fide 100-year defenses and revises its maps. An

application to begin that process probably won't go in until at least next year.
Meanwhile, the private insurance industry has been cool to news of improved flood defenses in New Orleans.
"The completion of this levee project is an important milestone. But we need to understand that the levees don't stop wind damage," said Bob Hartwig, president of the Insurance Information Institute, speaking on behalf of the property insurance industry. "Because most homes that are insured for flood are insured through the National Flood Insurance Program, there's not a great deal of impact on the risk profile of New Orleans homes."
Hartwig further said that insurers will need to decide for themselves if the work is any good. "Without the levees being tested in a Katrina-like situation, it's hard to say. Has there really been a difference, or is there some weakness in the system?"
The notion that property insurers won't benefit from the levee improvement work contrasts sharply with rhetoric after Katrina, when commercial and homeowners insurers alike told Donelon and then-Gov. Kathleen Blanco that they were concerned about doing business in Louisiana because of the condition of the levees.
Large commercial policies often cover flood damage, while small-business policies and homeowners policies let the federal flood insurance program cover flood risks. But companies of all types told Donelon and Blanco that flooding matters because if a hurricane generates both flood and wind damage, litigation increases as everyone tries to sort out the cause of damage. Meanwhile, in a place like New Orleans, where water can sit for weeks rather than roll out with the tide, a flood can increase an insurer's costs because business interruption policies are triggered and consumers are displaced from their homes for a longer period of time.
Amy Bach, executive director of United Policyholders, a California advocacy group that worked in New Orleans after Hurricane Katrina, said that insurers should be ashamed of themselves if they don't give the state credit for the flood defense work.
"It speaks volumes to what really goes into insurance rates. They claim to be so scientific and risk-based in their pricing, but the truth is, it's an elaborate justification for charging what they think the market is going to bear. I don't think their rates reflect the actual risks," Bach said. "I think that should really anger the property owners in the state. What more do they want?"
Levees get detailed scrutiny
On Baker's flood defense tour, insurance executives asked detailed questions of corps officials as they

checked out the giant blockade and pump house of the West Closure Complex on the West Bank, and later, at the storm surge barrier blocking water from Lake Borgne as they tried to overcome their doubts lingering from Katrina. What is the subsidence rate at the new levees? Who will operate and maintain the new flood protection equipment, locals or the feds? Can pumps be operated remotely? How much fuel is available to run the pumps if the power goes out? What is the wind rating of the safe houses where the pump operators will work?

At the end of the tour, which was deemed off-the-record so that companies could process what they saw without risk of being quoted, one executive said he was impressed with the scale of the improvements and that the corps was blocking water long before it got to populated areas. Another was wowed by the quality of the construction and engineering. But another said he was disappointed a state agency would operate the controls rather than federal officials.

After the tour and a private dinner where companies could digest what they saw, Baker said many of his guests remarked on the competence of the corps and the confidence officials displayed in their engineering work. Baker even said he thought it was beneficial that the insurers visited when the Mississippi River was rising, because it gave companies a chance to see that the corps really did have the situation under control.

“While I hope that the corps tour helps, we’re fighting an uphill battle. But, we’re fighting it,” Baker said.