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Paying \$224 Million for an Omaha Stake Won't Protect Florida from Fiscal Disaster

By Eli Lehrer

On July 29 Florida's State Board of Administration voted to spend \$224 million in return for a billionaire's pledge. Warren Buffett, the "Oracle of Omaha," guaranteed that his Berkshire Hathaway firm would buy \$4 billion in state bonds if a storm caused more damage than Florida's catastrophe fund could cover.

The 2-1 vote, with Attorney General Bill McCollum dissenting, gave Floridians the clearest signal yet of the state government's precarious fiscal condition.

Quite simply, Governor Crist and the Legislature have bet the state's fiscal future on remaining storm-free. And, even with this deal, the state still faces enormous risks. The agreement simply reduces the state's total Hurricane Catastrophe Fund liability after a major storm to \$28 billion from \$32 billion.

Yet given that no state has ever issued more than \$11 billion in bonds all at one time, even \$28 billion is more than Florida taxpayers could handle. With or without Buffett's funding -- which won't even kick in until the state spends a lot of its own money -- the state would still face an unprecedented fiscal crisis if a major storm hit.

Nonetheless, the deal arguably could be marginally worth the investment

under the right set of circumstances: a major storm, but not too major. The Cat Fund has \$5 billion in reserves of its own, so the deal to provide \$4 billion more does almost double its capacity. That does slightly reduce the risk that a major storm would bankrupt the state.

Of course, simply reducing the size of the Cat Fund, a measure State CFO Alex Sink has advocated, would have had just about the same fiscal impact and cost the state nothing. (The Legislature rejected it because insurance premiums might have gone up a bit, especially for affluent homeowners living in vulnerable coastal areas.)

Still, it's worth respecting Attorney General McCollum's vote against the proposal. The money going to Buffett's firm, for example, could have funded other priorities in Florida's state budget -- a 40 percent increase in programs for the elderly, for instance, or health insurance coverage for more than 200,000 children.

Some optimists evidently believe that the federal government would approve a bailout for Florida if a major storm exceeded the combined resources of the state's Cat Fund and Mr. Buffett's bond purchase.

Although a plan has passed the U.S. House of Representatives in two different forms --once as federal “wind insurance,” the other as a federally-backed version of the Cat Fund that’s supposedly private -- the plan couldn’t even get 30 votes in the Senate, where any proposal needs 60 votes out of 100 to pass against a determined filibuster.

In the long term, Florida needs to follow Ms. Sink’s suggestion and phase out the Cat Fund. Florida Citizens Property Insurance Corporation, the state agency that serves as Florida’s largest provider of homeowners’ insurance, also needs to go.

While doing these things, the state also needs to let free-market competition - rather than state bureaucrats -- set the rates that private insurance companies may charge. Unfortunately, in recent hearings on insurers’ proposed rate hikes, the state has not done so. However, a bigger test of the regulatory climate will come in the weeks ahead when two of the largest companies – State Farm and Allstate -- face rate-related hearings.

For coastal homeowners, the transition would not be easy: Premiums would go up. But many of the homeowners facing higher insurance premiums are comparatively well off. In fact, Dan Sutter of the University of Texas-Pan American has shown that Florida’s coastal counties are actually wealthier than its inland areas.

Nonetheless, some residents of modest means may have a difficult time affording higher premiums. There are several ways in which the state can help them. First, the “My Safe Florida Home” program -- intended to make homes safer

and more storm resistant -- ought to be renewed and expanded. Lowering the risk of damage can make property insurance more affordable. In connection with this, the state should set a goal of conducting a safety inspection of every storm-vulnerable home by the end of 2009.

Second, through tax credits and low-interest loans, the state and Federal government should help people pay for improving the storm resistance of their homes. Studies conducted after Hurricane Andrew devastated a wide swath of South Florida in 1992 revealed that many structures failed because the region’s strict building code was not strictly enforced by local governments.

In short, when it comes to property insurance, government ought to fix the mess that government made by helping homeowners to weather storms while also sparing the state a financial storm.

What Florida cannot do is rely on bond deals with billionaires to save its fiscal future. Instead, the state needs to buckle down and help its own citizens secure their property against hurricanes.

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