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IMPLEMENTATION OF THE BIGGERT–WATERS FLOOD INSURANCE ACT OF 2012: ONE YEAR AFTER ENACTMENT

HEARING

BEFORE THE

SUBCOMMITTEE ON
ECONOMIC POLICY

OF THE

COMMITTEE ON
BANKING, HOUSING, AND URBAN AFFAIRS
UNITED STATES SENATE

ONE HUNDRED THIRTEENTH CONGRESS

FIRST SESSION

ON

EXAMINING THE CURRENT STATUS OF IMPLEMENTING THE FLOOD INSURANCE ACT REFORMS AND THE POSSIBLE EFFECTS ON POLICYHOLDERS

SEPTEMBER 18, 2013

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C O N T E N T S

WEDNESDAY, SEPTEMBER 18, 2013

WITNESSES

ADDITIONAL MATERIAL SUPPLIED FOR THE RECORD

IMPLEMENTATION OF THE BIGGERT–WATERS FLOOD INSURANCE ACT OF 2012: ONE YEAR AFTER ENACTMENT

WEDNESDAY, SEPTEMBER 18, 2013

U.S. SENATE,
SUBCOMMITTEE ON ECONOMIC POLICY,
COMMITTEE ON BANKING, HOUSING, AND URBAN AFFAIRS,
Washington, DC.

The Subcommittee met at 2:43 p.m., in room SD–538, Dirksen Senate Office Building, Hon. Jeff Merkley, Chairman of the Subcommittee, presiding.

OPENING STATEMENT OF CHAIRMAN JEFF MERKLEY

Chairman MERKLEY. Good afternoon. I call to order this hearing of the Economic Policy Subcommittee of the Senate Committee on Banking and Housing. Welcome, everyone. We will have opening statements, limited to 5 minutes or less, and then we will proceed with our first panel, and we are so delighted to have both Senator Vitter and Senator Landrieu here to share their insights on the challenges that are occurring in the State of Louisiana.

As a Nation, we are constantly reminded about the loss and damage caused by flooding, and the recent events in Colorado highlight the flooding and how it is affecting communities all across our Nation. And my thoughts are with the families and the communities in Colorado at this moment.

Historically, flooding has been the most common and costly natural disaster. We see and hear the stories of flooding along river banks and along coastlines in all parts of America. We have seen flooding events become more severe as storms intensify and storm surges increase, leaving untold destruction in their wake.

Currently, about 50 percent of the Nation's population lives along the coast or in floodplains, and this number is expected to grow. Thus, the impact of storms on our communities is also likely to grow.

In 1968, Congress enacted the National Flood Insurance Act, which established the National Flood Insurance Program. NFIP provides property owners in floodplains with an opportunity to purchase insurance, and over the years, the program has expanded. There are now 22,000 participating communities with 5.5 million policyholders, including $1.3 trillion in property and contents. However, NFIP has also suffered many years of catastrophic losses and is $24 billion in debt.

Last year, Congress enacted sweeping reforms to NFIP, commonly referred to as the "Biggert-Waters Flood Insurance Act." Folks may remember that this was added in conference to the MAP–21 transportation bill.

In order to make the program financially sound, insurance rates were restructured by establishing a schedule to phase out subsidies for certain homeowners. Moreover, the flood maps are being redrawn in many communities, resulting in mortgage companies requiring many families to buy flood insurance for the first time.

These two factors working together are really the reason that we are here today. We are holding this hearing for Senators to better understand the challenges of how these two circumstances are impacting ordinary families. Here are a few of the concerns.

First, unaffordable flood insurance. Many insurance policies that were previously $300 to $500 a year are now going up to several thousand dollars a year. And there are a whole bunch of folks who are buying homes between July 6th of last year and October 1st of this year who are getting a subsidized rate, and it is my understanding when they renew that they are going to have a big surprise because they will get an unsubsidized rate that may be a manifold increase.

A second significant problem is forced placement insurance. Many Oregonians who have been previously told by their lenders that they are not required to have flood insurance are now being told that they need to have that insurance, either because mapping has placed them into a floodplain or because mortgage companies that were not enforcing this standard are now enforcing it, in part because the bill that was adopted last year has higher penalties for not enforcing.

Carol from Cornelius, Oregon, purchased her home in 2005, reassured by a realtor that she would not need flood insurance. She received a letter from her mortgage company earlier this year informing her that if she did not buy insurance, they would place a $1,200 policy on the property. She is in the process of challenging this, but is forced to pay during the process of appealing the situation.

And one of the things we have to look at on force-placed insurance is whether or not there are abuses in that category in terms of very high rate policies with subsidies paid back to the mortgage servicers.

A third issue is the inability to sell a home. Take Carl Hay of Eagle Creek. Mr. Hay and his wife have been unable to sell their home and have had potential buyers withdraw their offer after learning that flood insurance will increase tenfold to $5,000 annually upon the sale of their home. Buyers are not protected by the same 20-percent cap that exists for homeowners.

Fourth, the challenge to the homeowner of obtaining accurate flood risk data. If a homeowner is challenging the fact that they have been described as being in a floodplain and the mortgage company thinks otherwise, the homeowner carries the burden of proof, and this can be expensive, costing between $500 and $2,000 to get a survey. And while such proof is being provided and acceptance of it is being sought, the homeowner must continue to pay.

Now, in addition to these problems facing the homeowners, many communities are having great difficulty with the challenge of securing accurate information for flood maps, which raises another set of issues. The 2012 NFIP bill has a number of features designed to address this challenge, and hopefully today we will hear a little bit about the progress in this regard. Some of those include a requirement for the agency to establish a technical mapping advisory council and an independent scientific resolution panel.

There is also a feature in Biggert-Waters to establish a flood protection structure accreditation task force. We would like to hear if this is set up and what value it is bringing to the process.

FEMA and the U.S. Army Corps are required to form a task force to better align the data the Corps is collecting during levy inspections with the data required under FEMA's accreditation program.

Also, Biggert-Waters requires FEMA to provide flood insurance to people living behind a levee that is undergoing construction or improvements at the same rate or the same premium price as those who reside behind a completed levee. Again, it will be interesting to know if this has gone into effect and is helping.

I look forward to all of the insights that our witnesses have, both on the challenges faced by the homeowners and the challenges faced by communities in obtaining and using accurate maps.

And I am so delighted that Cochair Heller is here today, and it is now your turn to give some comments.

STATEMENT OF SENATOR DEAN HELLER

Senator HELLER. Chairman, thank you. Like the Chairman, I want to start off by saying that my thoughts and prayers are with the citizens of Colorado who are dealing with the devastating flooding within their communities, and I wish to thank all the first responders and rescuers involved and hope that all those who are affected can recover as soon as possible.

Unfortunately, the flooding in Colorado demonstrates the importance of this hearing. I think almost everyone here would say that when they think of Nevada, flooding is not usually something that comes to mind. While wildfires are often our most dangerous natural disaster, in several parts of Nevada flooding is a very serious concern, especially when heavy rains or snow melts occur.

Just to give you an example, in Reno, Nevada, the Truckee River has continually flooded its banks, causing tremendous damage to residents, businesses, and infrastructure. None of the citizens of northern Nevada will forget the 1997 flood that put downtown Reno under several feet of water, with damages exceeding $1 billion over six counties.

In response to this flood, local communities and stakeholders, in partnership with the U.S. Corps of Engineers, have been working on measures to reduce future flood damages, restore miles of river wildlife habitat, and provide safe open-space amenities in the region.

Now, as we have seen from flooding in the Midwest to Hurricanes Katrina, Rita, and Sandy, flooding is the most costly and prevalent natural disaster risk in the United States. Many communities remain at serious risk of flooding, which threatens lives, property, and the economy.

I have always said that one of the most important roles the Federal Government plays is providing responsible safety nets for those who fall on hard times, and flood insurance is a critical safety net for many Americans who are victims of flooding disasters.

As we all know, for years Congress struggled to strengthen the financial solvency of the National Flood Insurance Program, which is billions of dollars in debt. With the passage of Biggert-Waters last Congress, new key reforms were enacted to try to avert the need for a taxpayer bailout. Today many communities and individuals are experiencing these new reforms for the first time. Now is the time that Federal agencies like FEMA must be open and transparent with accurate information for the American public about the implementation of these reforms.

I appreciate Administrator Fugate's willingness to address some of the concerns that many Americans have been voicing, and I want to thank all of our witnesses for being here today, including Senators Vitter and Landrieu, to share their experiences and to offer their thoughts on how to provide the best flood insurance policies for the American public.

Mr. Chairman, thank you, and I look forward to hearing all the testimonies from our witnesses.

Chairman MERKLEY. Thank you.

Senator Tester.

STATEMENT OF SENATOR JON TESTER

Senator TESTER. Well, thank you, Chairman Merkley. I, first of all, want to thank Senators Landrieu and Vitter for being here, and I look forward to your testimony and that of Mr. Fugate later on.

I would just like to say that, you know, we have been here before. Last year, Senator Vitter and I worked on a flood insurance bill with some certain parameters around it. Those parameters were to make sure that the Flood Insurance Program was actuarially sound. It was in the hole. It continues to be in the hole. And hopefully this bill, if implemented as intended, will help get the flood insurance back on sound ground without having to be bailed out with taxpayer dollars and increasing the liability on taxpayers.

That comes about with a price, and that price, especially with the regularity of major disasters in this country, is who pays the bill. Is it the Federal Government? Is it the taxpayer? Is it the property owner? And we tried to find the sweet spot in that, and we tried to level out the premium increases so that they did not hit all at once.

But the bottom line is that, as a body, we have to make a determination at what level are we going to subsidize flood insurance. And if we are not going to subsidize it at all, with the regularity of disasters, it is going to cost the premium payer a lot of dough. And if we are going to subsidize a little, it will help reduce that. If we subsidize a little more, it will reduce it some more.

So the bottom line is I think we all want something that is going to work and does not break the bank on folks who live in areas that are susceptible to flood, and work on this issue together as we move forth.

On the other hand, we have got to figure out what role the Federal Government is going to play in this, too.

Thank you, Mr. Chairman.

Chairman MERKLEY. Thank you.

Senator Warren, do you have an opening statement?

STATEMENT OF SENATOR ELIZABETH WARREN

Senator WARREN. I will just be brief. Thank you. Thank you, Mr. Chairman.

You know, I understand why it is important for flood insurance rates to reflect the real risks and the costs of flood damage. I get this. And I understand why we want our flood maps to represent the best scientific data available, including the latest evidence of climate change. And over time, I agree that it makes sense for us to move to a market-based system for setting flood insurance rates, provided we adequately take into account affordability concerns for low-income families. I get this.

I have more trouble understanding, though, why it has made sense for FEMA to implement various new rules at the same time that they are updating the flood insurance maps. When FEMA put out the new flood maps this year and last year, they placed hundreds of thousands of homeowners into a flood zone for the very first time, and so now there are thousands of people in Massachusetts, thousands of homeowners, who are suddenly being asked to pay thousands of dollars in premiums that they had never been asked to pay before. And many of these homeowners are dealing with new and unexpected costs. Many have no good options available to them.

One Massachusetts resident wrote to me and said, "I am 70 years old. I live on a fixed income, and I am unable to pay the proposed flood insurance."

That constituent and many others have said they do not know what to do.

So I am here today. I am very glad to have the opportunity to hear from Senator Landrieu, to hear from Senator Vitter, to hear from my colleagues and others who will be here to testify. I think we all know where we are trying to get, but I think there is a question about the path getting there. So thank you very much for being here.

Thank you, Mr. Chairman.

Chairman MERKLEY. Thank you, Senator.

I am particularly delighted that our first panel involves two of our colleagues who have been very engaged in this topic. Senator Vitter, thank you for your conversations that we have had that were very encouraging in terms of holding this hearing, and I look forward to your testimony.

And, Senator Landrieu, you have been passionately engaged on this, including getting David Miller, the head of NFIP, down to understand directly what is going on with Louisiana communities. I was there on the Senate Appropriations Committee when you laid out your proposal to grandfather properties and certainly the introduction of the Strengthen, Modernize, and Reform the NFIP Act that I hope you will be able to say a word or two about.

And so thank you both. I know this is certainly a huge issue in Louisiana, and so much to look forward to, to your thoughts and insights. Senator Vitter.

STATEMENT OF DAVID VITTER, U.S. SENATOR FROM LOUISIANA

Senator VITTER. Thank you, Mr. Chairman and Ranking Member Heller, for agreeing to this hearing, and thanks to all the Members here. Senator Landrieu and I really, really appreciate it.

I also want to recognize and thank several elected officials and community leaders here from Louisiana. But in doing so, I know we both want to emphasize that this is not some parochial Louisiana issue. This is a national issue, be assured. We might be feeling it first. More of our people might be experiencing first. But this movie is coming to a theater near you, and it "ain't" a good ending right now. And so we need to really get ahead of that curve and discuss and fix this problem.

I also want to thank Administrator Fugate for being the key witness of this hearing, and I am hopeful that with his presence this can be a truly substantive discussion that actually advances the ball down the field and is not just a lot of talk.

You know, we all knew what the discussion was when we were debating Biggert-Waters, and Senator Tester is right. We all expected some premium increases. We know that is necessary to make the system fiscally sound. But, quite frankly, what we have been told to expect since then is a completely different planet in some cases.

Before the fact and before the debate and the vote, we had several studies—and I have the citations here from Senate committees, GAO reports—that basically suggested that properties that were subsidized under the Flood Insurance Program might be subsidized up to 50 percent or 40 percent or 55 percent, those that were subsidized, and that was a minority. You know, to deal with some modest premium increases over time, to deal with that situation, and make the program fiscally sound is one thing.

Since Biggert-Waters has started to be implemented, we are hearing something dramatically different. We are hearing that—and my constituents and Mary's constituents are specifically hearing that they could face a premium increase from $633 a year to $28,544 a year for a policy worth $250,000.

Now, that is not just made-up numbers. That is Bill Bubrig, a resident of Plaquemines Parish. He lives in a home that was constructed at or above the elevation he was told he needed at the time. He followed all the rules at the time. He followed those rules, and that is what he is now being told that he might expect.

Now, one thing I hope this hearing gets to is exactly what he can expect because, quite frankly, in Administrator Fugate's written testimony, I think he is again downplaying the possible impacts. He is talking about some rates in Louisiana reaching as high as $10,000. Well, his FEMA employees have told many of our constituents to expect something way beyond that. So I hope we can clarify that.

Several weeks ago, on August 8, we did have a productive visit from David Miller and others at FEMA to south Louisiana to talk about just this, and it was productive. I asked David three questions then, and I told him they would be my three main and first questions to Administrator Fugate. And I think they are the three questions we need to start to get answers on, and so the Administrator has had well over a month's notice, and I want to lay those questions out.

Number one, the President has delayed major parts of Obamacare because they are not ready for prime time for implementation. So will the Administration and FEMA delay Biggert-Waters or at least major portions of Biggert-Waters for at least a year? Because it is clearly not ready for implementation.

Number two, will FEMA agree to halt releasing new flood insurance rate maps until issues involving their accuracy, properly taking into account all flood features, are completely worked out?

And, number three, will FEMA join Members of Congress, including everyone in the Louisiana delegation, and proactively promote solutions to the affordability issue? That is key, and we need help and leadership from FEMA. We are doing that. Many members are doing that. We need FEMA to do the same.

I will stop here and certainly look forward to expanding on those thoughts in our discussion.

Chairman MERKLEY. Thank you.

Senator Landrieu.

STATEMENT OF MARY LANDRIEU, U.S. SENATOR FROM LOUISIANA

Senator LANDRIEU. Thank you, Mr. Chairman. I have a long, detailed statement I am going to submit, and I am going to try to summarize the highlighted points in addition to what Senator Vitter has highlighted.

First, let me thank you for agreeing to have this hearing to begin the discussion to fix Biggert-Waters, to either repeal it, radically amend it, delay it, because we need help—not only in Louisiana but in many, many, many places in this country, not only along the coasts but as we all marked this morning the tragedy that is unfolding right now in Colorado and what happened most recently in Massachusetts, New York, and New Jersey.

Twelve days from now, FEMA will begin the process of increasing insurance rates on hundreds of thousands of homeowners and small businesses across the United States as a result of legislation that Congress passed without, in my view, full consideration of the potential impact that skyrocketing rates might have on families, small businesses, home sales, property values, local economies, or continued participation in the program. Good intentions to make the program self-sufficient, wholly inadequate data about the loss of affordability to the program, which is hitting us hard, hitting us right away, and devastating to our communities.

Both Biggert-Waters and the companion Flood Insurance Reform and Modernization Act that cleared this Committee 2 years ago in my view were built backwards and upside down. They authorized immediate rate increases on homeowners and businesses that played by the rules, did everything asked of them, before they even began to study the impacts these rate increases would have on affordability.

Let me mention two things about affordability. One, when this bill was debated in the House last year, there was an amendment offered by a Member of the House that was voted down by voice vote that would have required at least some vouchers for low-income and middle-income families that are going to be affected not only in Louisiana but Massachusetts. But let me say for the record, middle-income families, even some at the high end of the middle class, are going to have a hard time accepting the new rules and regulations coming from this bill.

There are 17.4 million households that live in Special Flood Hazard Areas where flood insurance is mandatory, but the question is: How many are going to, Senator Tester, be living in areas that are not special flood hazard but will flood, have flooded, can flood, and flood insurance is not mandatory, but they are going to be facing some rate increases as well?

Let me talk about the home trigger sale, which is very important, and this was in both bills. One of the most problematic provisions in Biggert-Waters, in both bills, is a requirement that under Section 205 any property purchased after July 6th of last year will immediately lose its entire subsidy on the active sale, penalizing homeowners who are buying these homes that had no way of knowing it; but, more importantly, in my view, penalizing the homeowners themselves who are without the ability to sell their homes now after July 6th without losing a substantial amount of their entire life equity.

I want to get us beyond premium increases into the fact that when you lose your subsidy on your home, which is your largest asset, you basically lose the majority of your wealth accumulated over a lifetime because of this bill. It was premature. It was not well thought out. It must be fixed.

Two of my constituents, Penny and David Boquia, bought a home in Baton Rouge on August 23rd. They were told they would maintain the seller's flood insurance at $650 a year. One week later, on August 30th, they received a letter notifying them it would go up 400 percent $2,500. That is an example of what happens to homeowners. But basically many of our folks are just saying they cannot put their homes for sale; they have no value.

All right. The catastrophic flood losses that occurred—and I want to submit this for the detail, and thank Michel Claudet, who is the president of Terrebonne, for bringing this to my attention. I kept hearing and hearing the program is underwater, underwater, underwater by $20 billion. I just assumed. I should have looked. The truth of the matter is that, before Katrina, this program was fairly actuarially sound, and you can look at the numbers yourself. What sticks out is, at Katrina, it was a $16 billion hit to this program. Katrina was the biggest natural disaster ever to hit the United States in the history of our country. It rocked everything. So what we did was we took this outlier year, $16 billion, and then reflected that loss, you know, I think prematurely forward, and created a program that is now not self-sustainable, not affordable to even middle-class families, businesses, and we have got to fix it.

Now, in closing, maybe FEMA can do some things to delay it. I hope they can find a way. I am very frustrated with them, as Senator Vitter is, for not finishing their affordability study. They say you all did not give them enough money, $750,000; they needed more time, they needed more money. I do not buy that excuse. But, anyway, there was no affordability study done.

I am going to put the rest of my comments into the record, but we have got to, you know, push back, reform, repeal, this flood insurance, get a better approach that works not just for Louisiana, the gulf coast, and coastal, but for everyone in the country. You know, whoever was to blame, let us forget about that, but let us move on together to try to fix it. And I know this Committee had good intentions, believe me. I have been here long enough to know the Members on this Committee on both sides. But we made a mistake, and we have got to fix it. And I wish it could be fixed administratively. Maybe it can. But I think it may need some action by this Committee. And, Chairman Merkley and Senator Tester, I am so grateful, and Senator Heller, for your at least openness to consider some of the testimony you are going to hear today.

Thank you so much.

Chairman MERKLEY. Thank you both very much for your testimony, and you are both invited to join us here on the panel.

With that, we will ask Administrator Fugate to join us up front.

Mr. FUGATE. Mr. Chairman, Senator Heller——

Chairman MERKLEY. Thank you very much for joining us, Administrator, and I will just do a brief introduction and then ask you to jump in, and we particularly appreciate your attendance today given the disaster in Colorado. I know you have worked very hard to try to make sure that everything was attended to so that you could be here with us for this conversation.

William Craig Fugate was confirmed by the U.S. Senate and began his service as Administrator of FEMA in May 2009. At FEMA, he has promulgated the whole-community approach to emergency management, emphasizing and improving collaboration with all levels of Government and external partners, including voluntary agencies, faith-based organizations, the private sector, and citizens. Prior to coming to FEMA, he has served as Director of the Florida Division of Emergency Management.

We very much look forward to your testimony, and, again, thank you so much for coming.

STATEMENT OF W. CRAIG FUGATE, ADMINISTRATOR, FEDERAL EMERGENCY MANAGEMENT AGENCY, DEPARTMENT OF HOMELAND SECURITY

Mr. FUGATE. Well, thank you, Mr. Chairman, Senator Heller, Senators.

I think Senator Tester started out with—I want to take a step back. Why we are in flood insurance in the first place? What is the purpose of it? And how did we get here?

Flooding in the 1940s and 1950s was so significant that ultimately the private sector insurance companies no longer provided coverage, and that created huge exposure for the financial market for mortgages.

In the 1960s, Congress determined to form a capability to provide that insurance to ensure those mortgages were protected against this risk, this singular risk that the private sector no longer would provide coverage to.

Until about 1979, the program actually was operated by a consortium of companies that they managed the program, and at a point where losses were greater than their ability to cover, appropriations were made by Congress to pay the difference.

In the 1970s, the decision was made for the Federal Government to take over the entire program and provide those coverages and provide the maps and other tools to implement the program in one National Flood Insurance Program. At that point the Federal Government was now not only providing the catastrophic coverage but the day-to-day coverage. And the history of the program was that in catastrophic losses, the program was not determined to be able to cover those. Appropriations would be made, but the actuarial rates that were charged and the primary tool here was actually land use and growth management. So as new homes were built, they were built to reduce future risk. That was the real importance of the maps, to establish a base flood elevation that, if you built above that, would significantly reduce the risk to the communities in the future.

So one element of this is, to participate in the programs, communities have to adopt land use ordinances and building codes for new and future construction based upon best available data.

Now, as this program came about, obviously there were very little areas that were mapped, and so in order to provide the opportunity to get people insured—and these are oftentimes referred to as "pre-FIRM," "pre-map," "pre-flood" insurance rate maps—many people were brought in at rates that, as new data came up, decisions were made to grandfather them and hold them at their pre-FIRM rates.

So as map changes would occur, if you maintained your current policy, there was no change to those rates. That led to some interesting outcomes that we have started seeing repetitive loss properties that would literally be paid out every couple years. But there was no incentive for people to make any changes because their rates were so low. So one of the things in Biggert-Waters was to address should we continue to subsidize the repetitive loss properties.

Another concern was there was a lot of secondary homes that we were providing very good insurance rates to. The question then became, which Biggert-Waters addressed: Should we subsidize somebody's vacation home? And the answer was no, and starting January 1st of this year, as you renew your policy, if you have a secondary property, you are going to a full actuarial rate.

But then it gets into how do you cover these catastrophic disasters. I think we have seen the program grow, but so has the exposure. Right now our exposure, total policies, is $1.28 trillion. Now, there are no disasters that are ever going to get to that point, but there are some areas along our coast—Florida in particular, Houston, New York, New Jersey—that have exposures that in a Category 2 or Category 3 storm would be even greater than Katrina, Senator Landrieu, potentially, and some of those again hitting those $16 to $20 billion exposures.

So in trying to move to a more actuarially based rate, we also have this other issue, which I think the Senators are well versed in. Is it public policy, is it the intention to fully charge the rate for a primary homeowner to the point where they cannot afford their home? Or should it be the public policy that we have determine an ability to pay on affordability? And recognizing some people who live and choose to live in areas may be able to afford those actuarial rates that can be very expensive. But should people who have lived their all their lives, who are middle class, be priced out of their homes? And I do not agree.

But to get to Senator Vitter's first question, I have found very little leeway, as much as I have tried, in how we can address affordability under the current provisions of the law as enacted. And so I look forward to the questions, Mr. Chairman. I fully believe we should stop subsidizing risk as we go forward for new construction, for secondary homes, and for businesses. But I think we need to look at affordability for people who live there, look at how we can mitigate the risk in the future, and not grow our risk at the same time, not putting people out of their homes because flood insurance is prohibitively expensive.

Thank you, Mr. Chairman.

Chairman MERKLEY. Thank you very much for your testimony, and we are now going to have a period of 5 minutes. And just to let folks know, according to how the staff has documented arrivals, after I ask questions and Senator Heller asks questions, it is Senator Warren, Senator Vitter, Senator Tester, Senator Schumer, and then Senator Heitkamp. And Senator Landrieu, whom we do not have on the list yet. Thank you.

Could you address first this issue of the affordability report that was required? FEMA was directed, I believe, in the legislation to advise Congress on the affordability of flood insurance and problems that might arise in that regard within 270 days, which would have been April 6th of this year. I understand FEMA has now said that it will take 2 more years, until 2015, to do this affordability report. Clearly, you can see from the many comments and concerns and questions, affordability is at the heart of many of our concerns. So if you could explain why the 270 days was not achievable and whether something in the nearer future rather than 2015 might be possible.

Mr. FUGATE. Mr. Chairman, we approached the National Academy of Science to conduct a study. Their initial response back to us was that, given the amount of money and the time, they could not do a complete report. And I guess this is as most succinctly as I can. The challenge is on those homes that are what we call pre-FIRM, there was never any elevation established. There was never any elevation required. So we do not know what the costs are. And one of the examples given of how they calculated this actuarially, as our team has built those tables, if you are at base flood elevation and you have maximum contents in a $250,000 home, it is about $1,600. If you are 4 feet above that, it drops to 400—about $500, I am sorry. If you drop to 4 feet below that, you get $10,000. And for every 4 feet you go down below base level elevation, it basically doubles.

So as Senator Vitter points out, you can very easily get to these very high numbers if you are in an area of significant risk that you were built part of that. But without that data, without those elevation certificates—and that is, we are finding out as one of the things. You cannot really get the calculation on a per house basis of what this number looks like. And so part of this is getting that kind of data and resolution to make those calculations is what we are getting as one of the reasons it is going to take longer and more money.

The other parts of the economic stuff, we have already started the process to give us at least what does the framework of this look like and what are the elements that they would need to calculate the affordability. But as we understand it, knowing base flood elevations, since those do not exist for the most of the pre-FIRM homes, makes it extremely difficult to just calculate what that looks like.

Chairman MERKLEY. So I would toss out the idea that I will be happy to follow up with subsequent to this hearing that perhaps there is a lot of work that could be done in the near term just by understanding the case stories that we are hearing back from folks about the challenges. For example, a family in which a corner of their property is in the flood zone and so a mortgage company concerned about the fees that would be charged to them is insisting on flood insurance even though the house is not in the flood zone itself, that is certainly one example. And there are many others that I have been hearing from different corners of Oregon. Certainly perhaps even a compilation of the categories of concerns that are flowing in would be very useful for our consideration of changes that we might need to make in the law, and kind of in this regard, the sooner the better.

Let me turn to FEMA has outlined new procedures to produce flood insurance rate maps while incorporating partially accredited levees, and I do not want to ask you to spend a lot of time on this, but is there any progress in that pilot program?

Mr. FUGATE. Yes, sir. We are in the pilot phase right now. We are working with several communities across the country, several in Louisiana, working on now taking the tool that we built to update the maps, working with the local community, and calculate the value. Senator Vitter, Senator Landrieu, and others have pointed out that our previous policy was, even if you had a levee, if it was not accredited, we basically took it out and said there was no structure there. We now have the tools to build it back in. We are working with the local communities as we use that tool, and we update their maps and show them what this looks like, because part of this will also be, as these results come back, in doing mapping there is a lot of the interaction with the local officials as they look at that data and go but have you looked at this, and there is other data so we get the best outcome of looking at the structure.

So we are in that process in the pilot phase, and from that that would be the point that would generate the formal rulemaking once we see that we have the ability to do this tool and get the results that local communities and others are looking for.

Chairman MERKLEY. Thank you. I have many more questions, but I am going to be fairly strict about the time so that everybody can get their thoughts in. So we will turn to Senator Heller.

Senator HELLER. Chairman, thank you. Mr. Fugate, thank you for being here today.

I have heard the word "mitigation" several times already in testimony. Besides elevation, what is another form of mitigation that a homeowner can use or provide to reduce insurance costs?

Mr. FUGATE. Well, this is not mitigation, and there is a cost to the homeowner because the program does not have the ability to provide it. But that is getting an elevation certificate, and that will be one of the challenges, because it does cost, and it can run anywhere from a couple hundred dollars to several thousand dollars, depending upon what you have to do to get that survey done.

But that will then be the point at which if you are at or above base flood elevation, you would see discounts in what these proposed rates would be. The elevation, again, something that we have seen and used quite a bit post disaster, but also you gave us additional tools within the National Flood Insurance Reform Act to do two things: elevations but also buyouts, offer some homeowners, particularly after a devastating flood—it may be the option that they do not want to rebuild there, yet they cannot really sell their property and it is destroyed, the opportunity to buy out. This is being used rather successfully in parts of the country, including in the Northeast after Sandy, to take some of the most vulnerable areas and buy those properties out, turn it into greenspace, and give people the resources to move elsewhere and reestablish their homes.

Senator HELLER. With the discussions that we had on the first panel and Members of both the Senate and the House, and the number of calls they get—and, again, even Nevada, I receive phone calls on this particular issue—it seems to me that there are so many numbers bouncing around. When a homeowner testified earlier, when numbers are thrown out like $28,000 a year, it just seems like there is a big communications gap between what your administration is doing and being able to educate and spend time with the citizens and letting them know what their options are.

What are we doing to enhance the communications?

Mr. FUGATE. Well, since the primary point of information of determining your rate is going to be the Write-Your-Own insurance agent, we have been working to get all of that training done and get them up to speed. I think right now we are over 8,000 that have been trained, because Senator Vitter, rightly so, said, you know, we are putting a lot of information out there prematurely, and until you get the actual actuarial tables done which have been completed, the Write-Your-Own agents then have to get the elevation of the home and knowing what that elevation is, where the map is, then they have the ability to then calculate the rate. And it is, as has been pointed out, can be substantial if your home was built below the current base flood elevation, either because you have new map data or when you were brought in pre-FIRM, there was never any requirement to have an elevation certificate.

But those are the two pieces that actually calculate an individual homeowner's rate: an elevation and the tables that have been generated.

And so part of this has been to communicate that part to the agents, work with the communities and States, but now as we go through this process, making sure that that information is out there both to local officials as well as to the public, that that will be the process.

Now, for people that have secondary homes, they are already getting those rates adjusted. Again, that started in January, and you will continue to hear from constituents because it will be when they renew that they get their increases. So we started in January, but it will probably be for the full year before everybody has seen that on a secondary home.

Senator HELLER. Thank you.

Mr. Chairman, I have additional questions, but I will wait until the second round.

Chairman MERKLEY. Senator Warren.

Senator WARREN. Thank you, Mr. Chairman.

Mr. Fugate, I just want to go back and make sure I understand this. What kind of outreach did FEMA do before it released the new maps or as it was releasing the new maps to tell homeowners who had never before been in flood zones that now they were going to end up in flood zones.

Mr. FUGATE. Well, community by community, when we go into update maps—and there is usually either we have a map that is old that we have new data, we have been requested by the community, or we have had a disasters, and disasters have been prioritizing a lot of that. We start our conversations with the community itself, the Government that is responsible for that jurisdiction. This process is actually a several-year process, that we start with them, we get the best available——

Senator WARREN. So you talk to the mayors? I just want to make sure I am following. You talk to the mayors, you talk to the county officials.

Mr. FUGATE. Yes, ma'am. We send a notification. Oftentimes the people we are working with are the public works, utilities, or whoever the land use management agency is. And then we work with them in developing the scoping of the maps, the areas we are going to look at to update any additional concerns they have. If they have data or newer data, FEMA contracts with engineering firms that then update those maps.

We do a series of preliminary maps. You may hear the term "pre-FIRM," a pre-Flood Insurance Rate Map, that we then go back to the community. They do notices. Oftentimes, though, this process, even though there is a public notices and there is outreach, most people do not pay too much attention to it until they see that their status has changed.

That is why we do the hearings. We provide that opportunity. At that point, if new information is given, we are able to take a look at that. We have had several where we have issued pre-FIRMs. Members of the communities have questioned the data. We got new data.

This process can take 2, 3 years, and then the community has to—the local officials, to make the maps official—FEMA cannot make the maps official, but to make them enforceable, the local government has to vote to adopt the maps as part of their ordinance.

Senator WARREN. So let me follow up to make sure that I am tracking on this. So when someone discovers that, because of the map, they are now in a flood zone, they had not been in a flood zone before, I understand that there is an appeals process for that.

Mr. FUGATE. Yes, ma'am.

Senator WARREN. Can you tell me how many people have appealed their status in a flood zone? Do we know yet? Do we have any idea?

Mr. FUGATE. I would have to respond for the record to that. I know it is in the hundreds, if not thousands. But I would have to go back, because we do so many maps across the country, and they are in all phases of production. Some are preliminary, some have already been in the pre-FIRM. But pre-FIRM is usually when the public first gets their look at the maps, and one of the things that we used to do was—it was always on paper, so you had to go somewhere to see it.

Senator WARREN. Yes.

Mr. FUGATE. So we have been working to get these out online as digital so people can go look up and get information easier to see that information and then make determinations about is there anything that they need to do or want to do about that information.

Senator WARREN. So maybe I should have asked this the other way to get the base rate. How many homeowners have been affected by moving from not in a flood zone to in a flood zone? Do you have some sense? Or have had their status changed because they are——

Mr. FUGATE. It is substantial, and it goes both ways.

Senator WARREN. Substantial as in——

Mr. FUGATE. Thousands. And I would have to—it depends upon maps. Some maps had good data, so you do not see big changes. Others are more substantial. We know—I can show you that in New York and New Jersey post Sandy that—we had already been doing maps prior to Sandy, and so in using that data, it has increased the flood risk in those areas. The maps display the risk, and so as we went through, we were actually mapping those areas and updating maps prior to Sandy. But there were substantial changes. So it is impacting how and where people rebuild. It is also affecting decisions local officials are making about where they want to buy out or apply mitigation dollars.

Senator WARREN. That surprises me, though, that you would say it is thousands. I would think it would be far more homeowners than that. But let me ask, in the appeals process, for someone to take an appeal—I had heard from someone in Massachusetts about this, someone in Brockton who was told that if she wanted to take an appeal, the only way she could do it was to pay more than $1,000 to an engineer to come in and do an elevation study of a nearby brook, even though the city of Brockton and the Army Corps of Engineers have no record of the brook ever overflowing at any time in history.

So the question I have is: For a homeowner to take an appeal, if they have to take on a cost like this, does that really give them an effective tool if they think that they should not be rated as in a flood zone?

Mr. FUGATE. Well, there are two parts to that.

The first piece is, unfortunately, the program does not have the money to pay for the elevation certificates, and that is what determines.

The second piece is I have been all over the country, and no disrespect, Senator, I have been in many places that have never flooded before until it is declared a disaster.

So we look at the basins, we look at the topography, we look at the risk, and we are dealing with risk of 100-year and 500-year and calculating these flood tables. So it is not uncommon to go into areas that have not had recent flooding because, quite fortunately, that is not the case in many places. But if you do have that rainfall event or that storm event, their risk would fall greater than 1 percent, which is the special flood risk area. But if we can get the elevation and say you are 1 foot above that, then that would move you back into a much better category of risk and would make the insurance much more affordable.

Senator WARREN. Good. Well, I have some more questions about the process. I want to say thank you, Mr. Chairman. I am sorry we ran over.

Chairman MERKLEY. Senator Vitter.

Senator VITTER. Thank you, Mr. Chairman. And thank you again, Mr. Administrator.

My first question was: Is FEMA willing to delay Biggert-Waters or significant parts of it for at least a year? And basically the answer I heard was no. I am not going to encourage that answer, but that is what I heard.

Mr. FUGATE. Senator——

Senator VITTER. Let me just finish the question. Part of Biggert-Waters was the affordability study. That was due April 6th of this year. In the same paragraph, you said that is nowhere in sight; that will be 2, 2½ years. So you can delay that or cannot complete that on time, or for whatever reason, and yet you cannot delay the axe which will in some cases yield unaffordable rates.

Doesn't that seem a little ironic, to put it politely?

Mr. FUGATE. Senator, I have read the legislation. I have had attorneys read the legislation. Our staff has looked at it. If I had a way to do it based upon anything other than the technical implementation of the program, I do not see it. And so, again, I am not trying to be obstructive here.

Senator VITTER. Aren't there all sorts——

Mr. FUGATE. I need help.

Senator VITTER. Aren't there all sorts of questions about technical implementation that are problems that make this not ready for prime time, questions you highlighted in your reason for not being near completing an affordability study?

Mr. FUGATE. Senator Vitter, let me put my cards on the table. I need your help. I have not, my attorneys have not found a way—and, again——

Senator VITTER. Well, let me use——

Mr. FUGATE. I understand the question, sir. I do not have—again, from our attorneys and everybody looking at this, I do not have the answer you are looking for. I need your help.

Senator VITTER. OK. Let me——

Mr. FUGATE. Without some additional legislative support, I am getting bound and boxed into—I cannot address—there is no provision for affordability in this bill. It is delayed and phased in, but there is no way to build affordability in. It is clear the bill wanted to go to an actuarial rate, and the affordability study was not coupled to a delay.

Senator VITTER. OK.

Mr. FUGATE. If it had been written so that until the study is done you would not raise rates—it was not written that way.

Senator VITTER. Let me be clear. I am not asking you to make up an affordability section out of thin air. I am asking you to properly recognize a lot of true implementation problems that make a lot of the implementation not ready for prime time.

That goes to my third issue. You say you need help. We all need to come together and participate in this. So my third question is pretty simple. I have put forward specific legislative and administrative proposals. So have others. When will FEMA make any specific legislative and/or administrative proposals to address affordability?

Mr. FUGATE. I have no answer for that, sir, because we continue to look at what the possible options are. And part of this is coming back to what is it that, as we go through the process of doing the implementation, we are identifying as we need more guidance or authorities or there are issues coming up that we cannot address. So we have not drafted——

Senator VITTER. Mr. Administrator, you say you need our help.

Mr. FUGATE. Yes, sir.

Senator VITTER. Many of us are willing to offer that help. We need your help as some of the experts involved. So when will we get your help? When will we get any specific proposals—legislative proposals, administrative proposals—regarding affordability?

Mr. FUGATE. Without the study, the affordability piece of this, I would not be able to give you a specific date, plus this will require, as anything in the Administrator position, a lot of input to provide you a very specific piece of legislative recommendations. So I do not have a date——

Senator VITTER. So no time soon?

Mr. FUGATE. No, sir.

Senator VITTER. OK. I will submit my second question that I highlighted and ask you to answer it for the record.

I do in my time want to highlight a few other factors that go to solvency and, therefore, rate levels.

The best figure I have, number one, is that 40 percent of properties that are supposed to participate in the program do not, and there is little to no enforcement action to make them get in the program.

Now, that can clearly yield huge revenue into the program. It will mean some additional risk, but my guess is those folks do not think they are much at risk. So I would guess it yields a whole lot more revenue than risk. That can make a huge difference in terms of solvency and what premiums need to be. That is number one.

Number two, the best figure I have regarding the private side of the program, private participation, is that those private companies get basically a 30-percent markup, a 30-percent commission and servicing cost for paperwork not taking on any risk. To this pro-business conservative Republican, that seems absurd.

What am I missing?

Mr. FUGATE. On the first piece, because of the penalties of $2,000 if you do not as a financial institution ensure that you have identified those people in the special risk, you are getting a lot of folks now that are finding that their mortgage companies are notifying them that they have to buy that insurance now, and because they were not grandfathered in, they are going to the full rate; and if they fail to, they will buy it for them and put it in their account. So that is happening, Senator, and that tool of penalizing the financial institutions for not ensuring that if they write a mortgage for somebody in a special risk area and they do not have flood insurance is exactly what the Chairman was talking about; he heard from constituents that they were being told that they had to get it, and it was now at a very high rate that they had not expected.

And the second piece, the private sector does more than just write. This is not an easy policy to write for the private sector, particularly for the insurance agent. They have to have elevation certificates. There is a lot of reporting. We do very specific training that they have to have. They have to be certified to do flood insurance. You cannot just be an insurance agent. You have to be certified to do flood insurance. And then there is the servicing of that. And even with those dollars, some companies have chosen not to continue to write your own, rather large companies who shed significantly their exposure to this, because they did not see it in the interest of their shareholders.

So it is something we were looking at. You have asked us in this law to study that and also make recommendations, and as the rates increase, I think when you are talking smaller policies, 30 percent probably makes sense in some of those. But as you start getting to higher rates, is it proportional? Should it be at 30 percent fixed across the board? Or as it escalates, would you see that increase like you would a lot of other situations?

But that is something that we are working on and working with the insurance industry and the Write-Your-Own companies.

Chairman MERKLEY. Senator Tester.

Senator TESTER. Thank you for being here, Administrator Fugate. In your tenure as the head of FEMA, you have seen some pretty amazing disasters, maybe the largest in American history. I will start out by saying I appreciate your cooperation with Montana on the flood and fire seasons that we have had the last few years, and I want to thank FEMA for their fast response for the fire management grants this summer. When we had fires that were lapping at communities' doors, you guys stepped up, and I want you to know I very much appreciate that.

We worked pretty hard on Biggert-Waters to include a provision that got FEMA and the Army Corps to share information when it comes to flood protection structure, accreditation requirements. You are familiar with it. It established an accreditation task force to carry this out. It was supposed to be done and back to Congress by July 2013. Where is it at? And why is there a delay?

Mr. FUGATE. It is in concurrence in the Administration. We expect to have that report out in the next month. I am always cautiously optimistic in the concurrence process, knowing how that can sometimes take longer than I anticipate. But it took us that much time to get everything together, to get the report written, to get it into concurrence, and to get the product ready. And our hope is that we will be able to provide that to you I would say in the next month.

Senator TESTER. Thank you.

Mr. FUGATE. I know of nothing that is holding it up. It is just going through that final concurrence process to get it released, sir.

Senator TESTER. This is not an indication of the cooperation level between FEMA and the Army Corps?

Mr. FUGATE. No, sir. General Bostick and I have been working side by side, both through disasters but also in our responsibilities, in ensuring that we have the best cooperation working on our levees, maps, and other technical efforts to look at flood.

Senator TESTER. OK. You talked about needing our help, and I will say that there has been some talk about delay. You talked about the fact you do not want to price middle-class families out of their homes, and I appreciate all of that. I do not think there is an insurance company on the panel today, but what impact—I mean, you were talking about notices being sent out. What impact would a delay have on all that? And would that have an impact on—we are always being accused of not a lot of predictability around here. Would that have an impact on the overall program as far as people's comfort with it?

Mr. FUGATE. The one impact that would be most immediate would be those that either had a lapsed policy, a map change, or for some other reason would see the rates begin increasing now.

My real question is: Is—I do not believe—and I have not—I know there are concerns, but we have already done secondary homes, vacation homes, secondary properties. I do not know of any reason why we would want to delay that. That is already in effect. Those notices are out, and those properties are moving to these rates. Again, it is based upon secondary homes.

Repetitive loss properties, you had a provision in there, and this is something we run into. People refuse to be bought out or elevated, and we continue to subsidize their rates and pay them. And that ends as part of that.

Of the two sections, 205 I feel most strongly about implementing those now because they are the private sector businesses, they are the secondary homes, they are the repetitive loss that have not done things to mitigate. Section 207 gets into those areas that we are now talking about previously, either pre-FIRM'd or were grandfathered in rates that you cannot sell your home unless it jumps, you lose that, it is going to go up. If the map changes as we update maps, you now have a very short period of time, over several years, to move to those higher rates. And we have no basis to adjust those rates based upon affordability and what that affordability means.

Quite honestly, Senator, I am not sure we should be not slowing this down for new construction. If you are building condos in my home State of Florida, should we be giving you a discount rate?

Senator TESTER. Right. So from my perspective as a policy maker, those are the kind of recommendations I would like to hear from you, and I would hope that you would work with both Senators from Louisiana, and all of us, quite frankly, the leadership on this Committee, to try to figure out what we can do to not price the middle-class folks out of their home, OK?

Could you give me an idea—because Senator Vitter brought this up in his opening statement—what kind of a $250,000 property would have a $28,000 premium?

Mr. FUGATE. Based upon the actuarial tables that we produced—and we did this using the insurance models and everything—if you are at base flood elevation, that is considered about the medium risk, a $250,000 home with $100,000 contents, about $1,600. If you go 4 feet above that, it would drop to a little over $500. But if you drop below that in increments of 4 feet, it goes from about $1,600 to $10,000 and continues to almost double for every 4 feet.

So you can see very quickly how, if you had a community that was not mapped, you are in that Special Flood Hazard Area and you may be as low as 10 to 12 feet below that, particularly in coastal areas where you have got storm surge risk and those type of factors, as you look at that, you could see dramatic increases for a home that is worth $250,000 but now may have insurance rates potentially of almost 10 percent or more of the actual value of the home.

Senator TESTER. Thank you.

Chairman MERKLEY. Senator Heitkamp.

Senator HEITKAMP. Thank you so much, Mr. Chairman, and thank you for your testimony. Bet you do not know what I am going to ask.

As you know, more than 50 communities across the country, including 14 in my home State of North Dakota, have a so-called basement exemption. And I just want to make this point because I think for a lot of folks they wonder why that is. But a basement in a State like North Dakota and in a State that is plagued with tornadoes and bad weather can be a significant mitigation factor itself. And so I think there is good public policy to encourage the availability. And as we all know, those of us who have dealt with flood work in the past, you do not replace a finished basement if the basement is destroyed. You look at things that traditionally would be down there, like freezers and furnaces and maybe an electrical panel. And so a basement exemption is not—you know, recovering from a flooded basement is not full recovery. It is simply limited to those things that you would expect would be in a basement.

As part of this exemption, the city of Fargo, which has experienced its share of floods, has developed and adopted pretty rigorous flood-proofing construction requirements that meet or exceed the technical manuals. For example, the city requires that all residential structures be flood-proofed if they are located in the Special Flood Hazard Area or within 50 feet of it. The top of the basement walls must be elevated 2.5 feet above the base flood elevation, and fill adjacent to the structure must be 2 feet above the base flood elevation. Additionally, the foundations are subject to annual inspections. For new developments in the Special Flood Hazard Areas, the properties must be elevated with fill to at least the base flood elevation.

Now, overall the flood-proofing requirements have been a very effective flood mitigation tool in the region. In spite of some pretty heavy water pressures, not just floods but obviously high groundwater tables, more than the 600 flood-proofed foundations installed over the past 40 years, none have failed. But it is a great concern that I am going to raise with you, which is the elimination of the basement exemption.

What we are hearing from the officials in the city of Fargo is that that exemption—the elimination of that exemption could result in a $10,000-a-year increase for very modest homes, homes that are middle-class homes. And we have been discussing, I think quite accurately, the affordability issues.

And so I have two questions. Do you have an estimate on what those premiums would be in communities if the basement exemption is eliminated? And will you be maintaining this exemption? Have you made any decisions? I know that Senator Hoeven and I have been on this since I first got here, and we are curious about what your thinking is.

Mr. FUGATE. As far as the cost, I would have to go back and ask the question of staff: Does base flood elevation start at the base floor or would it be the basement? Because if a basement is 8 foot below and that is where they look at, you would see those numbers. But I do not know how you calculate, and I would have to ask staff. Do we calculate at the floor level, at grade, or do we calculate from the basement? So I would not know that, but we can get that for the record.

Mr. FUGATE. As far as the second part, I do not know that either. I will have to ask staff, because we saw so much of the language that allowed us to do exemptions exempted out that most of the affordability pieces, which this may be how it was looked at, were being exempted. I would have to ask staff is that what that is or is that still able to stand on its own. But because the way that Biggert-Waters is written, there were so many exemptions previously for affordability grandfathering that were taken out that I do not know if we even have that flexibility. But we will get back to you on that, Senator.

Senator HEITKAMP. That would be terrific, and if I can just indulge just one follow-up, I think it is important that, you know, as people think about it, maybe in areas where there are not tornadoes and areas where they do not need the basement for additional protection, that it is not just about affordability. It is about making sure that my people are safe when bad weather comes. And so I really encourage you to take a look at this, understand what that means not only for a State like mine but a State like Missouri and a number of States that are very dependent on a basement as an opportunity for shelter.

Mr. FUGATE. I understand. Senator, we will get back to you on those two points.

Senator HEITKAMP. Thank you very much.

Chairman MERKLEY. Senator Schumer.

Senator SCHUMER. I defer to Senator Landrieu.

Senator LANDRIEU. Thank you so much, Senator Schumer. I really appreciate that special opportunity. I am not a Member of the Banking Committee, and I really appreciate, Mr. Chairman, you allowing me to be here. This is such an important issue for Louisiana and for the gulf coast, but more importantly than that, this is an important issue for the whole Nation. And I really appreciate Senator Heitkamp's questioning because what I have tried to impress upon the Members of this Committee and the Senate in both parties, this is not a Louisiana issue. This is not a gulf coast issue. This is not a coastal issue. This is a national issue. And for the record, to impress upon that, I want to submit for the record of this Committee the 15 States that have more than—that have substantial policies: California, 256,000; Florida, 2 million; Louisiana, 486,000; Mississippi, 75,000; North Carolina, 138,000; New Jersey, 238,000; New York, 173,000; Pennsylvania, 73,000; South Carolina, 204,000; Texas, 645,000 homes and businesses; Virginia, 115. I am going to submit this to the record. It is 5 million homes in Louisiana—I mean in the Nation, including Louisiana, and businesses.

Now, one of my questions—and I do not want an answer, but I am going to ask you to submit in writing—are we going to see this total 5 million go up to 10 or 15 when new maps come out? What is the scale? That is rhetorical.

It is important, Mr. Chairman, to understand the scale of this. We have been talking about the details of the affordability study, the technical aspects. But the scale of this is important. This is a major bill that passed without the data necessary to use either compassion or common sense. OK? Compassion and common sense is what we are asking for. And it affects millions of homeowners and businesses. And it is not just homeowners and businesses. It is banks, real estate companies. It could have a devastating economic impact. It must be delayed, fixed, or modified.

Now, I do have a specific question. GAO's testimony cites five, Mr. Fugate, just five current gaps—there may be more, but five. I am going to do them quickly.

Second homes. Data on primary versus second home residence is outdated. You might have it. It is not dated correctly. FEMA classified properties as residential or nonresidential, but does not know which of these properties are schools and churches, still eligible for a subsidy, as opposed to businesses, which are not.

In substantial-damage properties, GAO says the law eliminates subsidies for properties with damage over 50 percent of their fair market value, but you do not even have data about people's fair market value of their home and no way to get it.

Substantially improved properties. The law also eliminates subsidies for properties whose renovations exceed 30 percent of their fair market value. You cannot calculate that ratio anyway.

Finally, multifamily SRL. FEMA does not define severe repetitive loss for multifamily properties either, so you would be unable to eliminate subsidies on these. You do not have the data to implement this law.

Now, there has got to be some overriding law in the Constitution of the United States that says you cannot implement a law if you cannot implement it. You know what I am saying? Like you have to implement it, but you cannot implement it if you do not have the data.

Now, this is maybe how we do business in Louisiana. I do not know. I can hear Chuck Schumer saying that. But there has got to be a way. If you do not have the data, how can you implement it? That is number one.

Number two, there are 3,000 counties in this country. We have 64 in Louisiana—parishes. What I would like to know is what FEMA is doing to reach out to NACo and to the mayors and to the national counties? Because this poor woman that Senator Warren spoke about never flooded in her life, creek never overflowed, never came out of the creek, now she has got to have $1,000. Maybe the county could organize a program to help homeowners like this.

So what are you doing county-wide? And will you include the levees that we build at our own experience into our rates?

Mr. FUGATE. We are reaching out through all the associations. We have been working through associations, floodplain managers and other associations, associations of Government, and we continue to do that.

As far as levee data, yes, ma'am, we will build whatever information, whatever protective measures—in fact, you gave us some tools in Biggert-Waters. There is not all bad here. One of the things you did do, which was really important, was remember——

Senator LANDRIEU. Mostly bad.

Mr. FUGATE. ——that we had a community that was getting and had funding to build a levee, and even though we would know it was being built, we would charge the higher rates and then we would have to adjust them when the levee got built? You gave us the provision that if we know it is being built within a certain time frame, that we do not have to raise the rates, knowing that the funding is obligated and there would not be new construction.

So, yes, we worked those in and built those in the maps, and we also factor in if it is under construction or will be under construction with funding, we can actually use that to do the map.

Senator LANDRIEU. OK. Mr. Chairman, beg me—just for 45 more seconds for two points.

One, if Biggert-Waters and the bill was prospective, I think the country could deal with this in a better way. The fact that it is so retrospective and catching people that have been in their homes for decades on slabs in places like Louisiana, we live below sea level, but we have been living below sea level for 300 years. We did not move there yesterday. And may I say just for the big picture of it, half the population of the Netherlands, which is 16 million people—I have been there five times. I think Mr. Fugate has been there—live below sea level. But, you know, they do not flood. They do not price their people out of the market.

You can live safely below sea level. People have been doing it for hundreds of years. But we have to have a policy that acknowledges that, supports that, not subsidizes at the great generosity of taxpayers, but is smart to recognize these economic coastal communities, like New York, New Jersey. People are not sunbathing there. We are operating the biggest port systems in the country.

So thank you, Mr. Chairman.

Chairman MERKLEY. Thank you very much, Senator.

Senator Schumer.

Senator SCHUMER. Thank you, Mr. Chairman. Thank you for holding this hearing. I thank Administrator Fugate.

Unfortunately, we have been dealing a lot with each other in the last few years. I say "unfortunately" not because I do not like dealing with you—you are an outstanding administrator, you are very responsive; I think the world of the job you are doing—but because we have had so many natural disasters in the New York area over the last few years. Between Irene and Lee and Sandy, just about every part of my State has been hit in addition to other issues.

So, first, I just want to add my voice. People have made the point well that we do not have an affordability study, and yet we are making people pay unaffordable rates, and they are just unaffordable. As Mary said, as Senator Landrieu said, this is not for rich people. We have got lots of middle-class and even poorer people living on the shore in Staten Island, in Brooklyn, in Queens, and Long Island. They cannot afford $9,000. And they are going to have to either leave their homes—and this is many people who were ravaged by Sandy. They are just beginning to rebuild their homes, and then they get their flood insurance go way up. And they do not have any money.

So I would ask you this: You say the law DOES NOT allow you to change it. What if all these people just drop out of the program? Which they will and make the program much less viable. Doesn't that give you the ability to delay things? You have delayed the affordability study. Why shouldn't you be delaying imposing these huge, huge fees on people? That is question one. I am going to ask my question seriatim.

Second, we are building——

Senator MENENDEZ. Does that mean in a row?

Senator SCHUMER. And that means in a row.

Mr. FUGATE. Yes, sir.

[Laughter.]

Senator SCHUMER. Thank you, Bob. In Hudson County, they have never heard the word "seriatim," but in Brooklyn we have. Anyway, Brooklyn and Hudson County, we can say that our kindred spirits in many ways.

Senator MENENDEZ. Does it mean something different in Hudson County?

Senator SCHUMER. It means something different in Hudson County.

[Laughter.]

Senator SCHUMER. I will not try to figure out what that is.

Second, in New York, we are building all kinds of dunes to protect our coastal areas, heavily populated, like never before, 12-foot dunes in the Rockaways and in Long Beach, maybe higher in parts of Suffolk County. But these people have just gotten their flood insurance rates, and they are based not on building a dune. So Mary asked, Senator Landrieu asked about what if they are building something—what if they are in the process of building with the levees? But what about us? We have already labeled—you have raised the rates, and now in 2 years it will be much more protected. I know how it is to get FEMA to redo a map because an area of half a million people has very strong, good protective dunes. We will never get you to do it. I hope we can look at that as well, because even on an actuarial basis, once these dunes are built, the likelihood of flooded is less.

So if you could answer both those questions seriatim, I would appreciate it.

Mr. FUGATE. I will start, first go backwards. Doing the dunes, it does offer significant protection against storm surge, and I would have to look at the data, but I also know that the back bay flooding the dunes do not address. So, again, looking at the protection and building that into the map updates we will continue to work on. And maps are not as final—I know this is—and I have been there a lot. When we publish maps and they get adopted, that is not the end of it. We always have the opportunity to come back and put new data in there, and since those maps, as you know, Senator, were already pretty well through the system before Sandy hit, we can still build in the improvements and run——

Senator SCHUMER. But, sir, in reality, I have tried to get—they used the wrong map for Nassau County, an egregious mistake. They used Suffolk County's map for Nassau County. Do you know how much effort and years it took to get a change? So to say you will redo it does not give us much comfort, because any of us who have dealt with FEMA, it is like pushing a big boulder uphill to get them to redo a map. We need some kind of ruling prospectively that when new—and, by the way, for the back bay areas, we are doing things for mitigation there, too. It may not be a dune, but we are doing other things there in terms of sewage systems, in terms of barriers, in terms of jetties, things like that. And is there any way to implement a system when that—they have to come out with a new assessment 6 months after something is built? We need something that you cannot just say, well, call your Senator, call your Congressman. Boy, oh, boy, that is frustrating for them and frustrating for us dealing with FEMA to change the maps. And then everyone's view is FEMA is doing this because they are in deep trouble and they want to collect as much money, correctly or incorrectly, as possible.

Mr. FUGATE. Well, Senator, the answer to that one is—and I am honest about this, and I realize there are always doubts. No, sir. But what I also believe is we should give people the best possible data. Much of the data for the areas impacted is what was called pre-FIRM. It was in the process of going through the adoption process. But we knew a lot of people had to make decisions about how they were going to rebuild, and they did not want them building back the way they were if you knew that if they built higher and elevated, they would get a preferred rate.

So there is the challenge of Sandy hit with the data we had trying to start that process, and we made decisions, working with State and local officials, to use that data to plan the future. But those maps are still going through the adoption process.

Senator SCHUMER. OK. Well, I wish you would consider some kind of—because we are going to be building our shoreline—I am sure Bob is in New Jersey—for a long time. And you did not answer—my time has run out, but you did not answer my first question. If you can delay the affordability study, why can't you delay—because on the basis that so many people are going to quit if you keep this in place, that it will affect the viability of the program?

Mr. FUGATE. The answer is, Senator, if there was those tools there, we would be looking at it. Staff has advised me, attorneys have advised me internally at FEMA that I do not have that authority. And it is not as easy to drop out as that, Senator. You have to maintain that as part of your mortgage if you have a federally backed mortgage. And if you were to voluntarily drop it, your mortgage company would purchase it and bill you for it anyway. So it does——

Senator SCHUMER. Well, that is of great consolation. Thanks for that.

Mr. FUGATE. I am just trying to be factual, Senator, that——

Senator SCHUMER. I know you are.

Mr. FUGATE. ——in a special flood risk area, it is tied—the requirement to have it—there is no requirement to buy flood insurance out of the special risk area. There is no requirement to buy flood insurance if you are in a special risk area unless you have a federally insured or backed mortgage, and then that is the requirement to purchase. So that is one of the ties that has been pointed out, looking at affordability, many of these people in the middle class have mortgages. They are also required to have the flood insurance to cover the exposure.

Senator SCHUMER. But they cannot afford it. They do not have $9,000, when they were paying $1,000 before. And you can say what you want—excuse me. You can say what you want, that, oh, they have to, because everyone has a federally insured mortgage in middle-class areas, so it is not saying, oh, all the people who do not have federally insured mortgages are not covered by this. But you are not giving them—it is not a satisfying answer to you or to us. We need a better one.

Mr. FUGATE. Absolutely, Senator.

Chairman MERKLEY. With that, we are going to have to continue, because we do have a second panel. Senator Menendez.

Senator MENENDEZ. Thank you, Mr. Chairman, and to the Ranking Member, for holding this hearing. And while I am not a Member of the Subcommittee, I appreciate the opportunity to be here as a member of the full Committee.

Administrator, first of all, I want to say that I think the incredible challenges that we have had in the region—Irene, Sandy—your overall responses and those of your agency have been extraordinary. And let me preface my remarks by saying that. I do not think that in the midst of this hearing we should lose sight about, from my perspective at least from the region, the tremendous work that you have done.

But this particular issue falls also in your bailiwick, and I have to be honest with you. Part of it is that telling my colleagues, some of my colleagues here, that you reap what you sow, I was very much one of those voices who said we should have some degree of subsidies. And I had an amendment to try to pursue that in the Committee. When it became clear that that was going to be a nonstarter because some of our colleagues on the Committee would not hear of it and would not move forward, then it was I who was pursuing the affordability study that ultimately got included in the legislation, which was supposed to be achieved 270 days after the enactment.

Now, I have read your testimony, and while I was not here physically, I have heard the answers. And I have a problem that we do not have the income levels, we do not know what the rates are. I do not know what you need to get the study done, but, you know, I would like to have the specifics of what you need to get the study done, number one.

Having said that, while we work to get the study done, I do not believe that FEMA should be allowed to phase out subsidies or end grandfathering until it presents a plan to make flood insurance more affordable.

Now, I hear that you say you do not have the wherewithal legislatively to do that, and I would invite you to submit to my office what is the language that you need, because I would like to put my colleagues to the test. Everybody who is complaining about flood insurance and the consequences to middle-class families, let us see if you are willing to put your vote to the opportunity to amend through some vehicle that I am sure will move to the floor the opportunity to create the affordability mechanism, or at least to delay while we determine what is the consequences, because these consequences are for real people. It is not just about property. It is not the property I am worried about. It is the people, the families, the people who call this their home, the people who are not going to be able to afford it as a result of this, the people who have put a lifetime of work and sacrifice to own the single piece of property that is their single economic asset that they have overwhelmingly for most American families. We are going to take that rug out right from underneath them. This is the triple whammy.

You have the storm that came in and destroyed people's lives. Then you had the flood maps and, you know, with all due respect, some of those flood maps in our New Jersey experience from where we went from to where we were, thank God that we had a push on the refinement of them because 80-percent reductions in V zones that would have dramatically—even beyond what we are talking about, would have made it impossible for people to afford flood insurance. So we will have to look at that process in the future.

And then, any, now a human-made disaster, which is the consequences of the insurance premiums that are unaffordable for families to keep.

And then, in addition the consequences to families, look at what is going to happen to this economy. The ripple effect of real estate that you cannot sell because the premium is unaffordable, that no one is going to buy because the premium is unaffordable, the consequences of falling ratables—and as a former mayor, I know the consequences of the challenges of falling ratables—and instead of getting behind this final nascent growth for the housing market, we are going to really pull the rug right out from underneath it, and that is going to have effects upon our economy as a whole, not just those people who find themselves in flood zones.

So I would like to get language from you to deal with the specificity that you think you need, and I expect the Department to give us that so that we know, and I am going to find a way to challenge my colleagues. I know Senator Landrieu had an amendment, which I supported, on the floor. Unfortunately, it was held up by one of our colleagues, would not let us even have a vote on it. I want to see who is really willing to help these property owners.

Finally, there are two other issues that I think are incredibly challenging. I mentioned the flood maps, and I do not think we should put out information when it ends up with 80-percent inaccuracy. I know there was the drive to get information and prepare people, but 6 months of preparation in which you are trying to think about what is the cost is enormous.

The last thing I would like to ask you—this is seriatim—how many claims for foundation repair have been denied due to earth movement? I have heard from a ton of constituents who had their flood insurance claim denied or reduced because the damage to their foundation was caused by earth movement, and the only reason the earth moved was because of the flooding. And most homeowners had no idea their policy did not protect them from this type of damage and are understandably—they have said they are being denied after responsibly paying flood insurance for years and years and years.

So how many claims for foundation repair have been denied due to earth movement? And what outreach is done when terms are changed, not the fine line, you know, that most people never read, but when terms are changed and certain types of damage are excluded from coverage, how do they know?

Thank you, Mr. Chairman. Can I get those answers before moving to the next——

Chairman MERKLEY. Yes.

Mr. FUGATE. First one, yes, we will work with your office on technical directing assistance, and we will continue to work with all members on that.

On the foundations, I will get those numbers to you, Senator. One thing, again, as Senator Landrieu points out, in Biggert-Waters one of the things they did do, which I think is helpful in the Write-Your-Own policies, it requires in big bold print what your policies cover and do not cover. I think that was to address the concerns when this comes up. But we will also get back to your office, Senator, those things we are doing about earth movement and how that appeal process works and the information on that.

Senator MENENDEZ. Thank you.

Chairman MERKLEY. Thank you very much.

Senator VITTER. May I have 10 seconds?

Chairman MERKLEY. Yes, 10 seconds.

Senator VITTER. Just as a brief follow-up to the first question, I do not think Senator Menendez was asking for technical drafting assistance. I think he was asking for the same thing I was asking for, which is leadership. And we would really like that as partners in fixing this issue.

Chairman MERKLEY. Senator Heller, did you want to jump in for a second?

Senator HELLER. Because of time restraints, I will submit additional questions. I have some mapping questions that I would certainly like you to address, and I will leave them with the Chair here and hear back from you, if that is OK.

Chairman MERKLEY. Thank you very much.

Administrator Fugate, I know given the number of emergencies around the country, we really appreciate you showing up to address this. I think it is very clear from this set of questions that there is a lot of concern about fundamental issues of fairness, families who have never needed flood insurance are suddenly being told they need it, but for every $1,000 they pay in flood insurance, the value of their house goes down by $20,000. And all sorts of challenges result if new buyers have to get flood insurance at a rate that essentially means that the house is now worthless.

And so we have conflicting issues that we are trying to get our hands around. I really will follow up and ask for aggressive help in translating all the stories you are hearing from around the country into a clear set of affordability challenges, and if there are other ways we can accelerate the affordability study as required, perhaps the goal is too expansive that you have set for yourself, and maybe there is information that would be very helpful. But I think you are going to see a lot of continued conversation from all of us because there are issues here that just demand our attention and our action.

Thank you again for appearing today, and we will be getting questions to you that are submitted. We will hold the record open for 7 days for any additional questions, and if you and your team could be responsive to those, we will then make sure they are circulated thoroughly. Thank you.

Mr. FUGATE. Thank you, Mr. Chairman. Thank you, Senators.

Chairman MERKLEY. We will now have our third panel come forward, please.

[Pause.]

Chairman MERKLEY. We are deeply appreciative that the four of you have come to testify, and indeed we are fortunate to be joined by top-notch experts. I would like to especially thank Christine Shirley, who has come from my home State of Oregon, and we look forward to hearing all of your testimony.

I am going to give an introduction for each and every one of you now, and so we can just proceed from one testimony to the next.

Alicia Cackley is Director in the Financial Markets and Community Investment Team at the U.S. Government Accountability Office. She oversees policy research and program evaluation on a broad range of insurance, consumer protection, housing, and finance issues, including the National Flood Insurance Program, consumer product safety and consumer financial protection, bankruptcy, financial literacy, and homelessness. Ms. Cackley received her Ph.D. in economics from the University of Michigan and has been with the Government Accountability Office since 1990.

Christine Shirley is the NFIP coordinator and natural hazards program planner for the State of Oregon, a position she has held since 2007. Ms. Shirley offers technical assistance to Oregon's 260 communities that participate in NFIP. She interacts daily, in addition, with State agencies, surveyors, building officials, real estate agents, building owners, and others who have questions or concerns about implementation of the act. Ms. Shirley studied at the energy and resources group at UC–Berkeley prior to earning a master of science degree in geographic information science from Birkbeck College, University of London, in 2004. She became a certified floodplain manager in 2005.

Steve Ellis joined Taxpayers for Common Sense in 1999 and serves as vice president, overseeing programs and serving as a leading media and legislative spokesperson. His expertise ranged from earmarks to flood insurance and a lot of spending issues in between. Mr. Ellis received his B.S. in Government from the U.S. Coast Guard Academy. He has earned both the Coast Guard Commendation Medal and the Coast Guard Achievement Medal.

Mr. Birny Birnbaum is a consulting economist and former insurance regulator whose work focuses on insurance regulatory issues. He serves as an economic adviser to and executive director for the Center for Economic Justice, a Texas nonprofit organization whose mission is to advocate on behalf of low-income consumers on issues of availability, affordability, accessibility of basic goods and services, such as utilities, credit, and insurance. He holds two master degrees from MIT in management and in urban planning, with concentrations in finance and applied economics.

Thank you all four for coming and bringing your expertise and frontline experience from across the Nation. Ms. Cackley.

STATEMENT OF ALICIA P. CACKLEY, DIRECTOR, FINANCIAL MARKETS AND COMMUNITY INVESTMENT, GOVERNMENT ACCOUNTABILITY OFFICE

Ms. CACKLEY. Chairman Merkley, Ranking Member Heller, I am pleased to be here today to testify on an NFIP, the National Flood Insurance Program.

As you know, the Flood Insurance Program is a key component of the Federal Government's efforts to minimize the damage and financial impact of floods. As of the end of fiscal year 2012, the program had more than 5.5 million policies with an insured value of about $1.3 trillion and collected about $3.5 billion in annual premiums.

My statement today will discuss the reasons that NFIP is considered high risk, changes to subsidized policies and implications of potential additional program changes, and additional challenges for FEMA to address. The testimony is based on two reports we recently issued in July of 2013 in NFIP coverage limits and subsidized properties, as well as other prior GAO reports on various issues related to NFIP.

The NFIP was added to GAO's high-risk list in 2006 and remains high risk due to losses incurred from the 2005 hurricanes and subsequent losses, the financial exposure the program represents for the Federal Government, and ongoing management and operational challenges. As of July 31st of this year, the program owed approximately $24 billion to the U.S. Treasury.

NFIP's financial condition highlights structural weaknesses in how the program has been funded, primarily its rate structure. NFIP offers two types of flood insurance premiums to property owners who live in participating communities, subsidized and full risk. The annual amount that NFIP collects in both subsidized and full-risk premiums is generally not enough to cover its operating costs, claim payments, and principal and interest payments for the debt owed to Treasury, especially in years of catastrophic flooding, such as 2005. Thus, much of the financial risk of flooding is transferred to the Federal Government and ultimately the taxpayer. Furthermore, the weaknesses we identified in NFIP management and operations, including financial reporting progresses and internal controls, strategic and human capital planning, and oversight of contractors, also put the program at risk.

The Biggert-Waters Flood Insurance Reform Act of 2012 mandated that GAO conduct a number of studies related to actual and potential changes to NFIP, including analyses of remaining subsidies and the effect of increasing coverage limits or adding coverage options. In our study of remaining subsidies, we estimated that, as of enactment of the Biggert-Waters Act, approximately 438,000 policies no longer would be eligible for subsidies, while subsidies on most of the approximately 715,000 remaining subsidies policies are expected to be eliminated over time as properties are sold or coverage lapses, as are previous exemptions from rate increases after flood zone revisions.

Reducing the financial impact of remaining subsidized policies on NFIP generally could involve accelerating elimination of subsidies, targeting assistance for subsidies, expanding mitigation efforts, or some combination of these three. Each approach has advantages and disadvantages that would need to be carefully considered, and action would be required from both Congress and FEMA.

Similarly, in our mandated report on raising coverage limits or adding optional coverage types, we found there were advantages and disadvantages to making more changes to the program, which would need to be carefully weighed. We estimated that the financial impact on the program of raising coverage limits or adding business interruption or additional living expenses coverage would depend on the adequacy of the rates charged.

Looking forward, FEMA will require several years to fully implement the Biggert-Waters Act, and FEMA officials have acknowledged that they have challenges to resolve. These include updating and correcting information on whether a policy is for a primary or a secondary residence, determining the fair market value of insured properties, and developing a definition of "severe repetitive loss" for multifamily properties. Further, FEMA must establish full-risk rates that reflect flood risk for active policies that are no longer eligible for subsidies. However, at this point in time, it does not have a plan to do so.

In conclusion, when we placed NFIP on the high-risk list in 2006, we noted that comprehensive reform likely would be needed to address the financial challenges facing the program. Since passage of the Biggert-Waters Act, FEMA has taken some important first steps toward implementing the reforms the act requires, but the extent to which the changes included in the act and FEMA's implementation of these changes will reduce the financial exposure created by the program is not clear, and the program's long-term financial condition is not yet assured. Getting NFIP on a sound footing, both financially and operationally, is important in achieving its goals, and at the same time reducing its burden on the taxpayer.

Mr. Chairman, this concludes my prepared statement. I would be happy to respond to questions.

Chairman MERKLEY. Thank you very much. We are going to hold questions until the end.

Ms. Shirley.

STATEMENT OF CHRISTINE SHIRLEY, NATIONAL FLOOD INSURANCE PROGRAM COORDINATOR, PLANNING SERVICES DIVISION, OREGON DEPARTMENT OF LAND CONSERVATION AND DEVELOPMENT

Ms. SHIRLEY. Thank you for having me. I am very grateful to be here, Chairman Merkley and Ranking Member Heller and the rest of the panel.

For the last 5 months, I have been making the rounds to our local floodplain managers, surveyors, real estate agents, and so on, and some appraisers, to talk about the Flood Reform Act, and I can say there is a lot of confusion out there, and this confusion is causing a lot of fear and causing FEMA to lose some credibility out there in the community. And the real estate market is responding, as we heard earlier. Darby from the State of Florida actually contacted me yesterday and summed up the situation there as saying, "The reality of the situation is that this crisis has immediately stopped all real estate sales in my area. Overnight, once word got out, no homes in any flood areas are selling."

Appraisers who were crazy busy before the market was booming are now going 3 or 4 days without seeing an appraisal, and banks are refusing refinancing because they cannot determine fair market values. I am seeing exactly the same thing, especially on the coast areas of Oregon, but also in other flood-prone areas in Oregon.

The main thing is it is very important to note that markets do not like uncertainty, and the uncertainties caused by this rollout of the program are having an effect.

I want to stress that Oregon supports the intent of the NFIP, and the NFIP is woven into our statewide land use plan, and we really are trying hard to make Oregon a flood-resilient State. In order to do that, we need an NFIP that is based on accurate flood maps, that is understandable, and that goes beyond insurance and encourages mitigation. The reform act, as we see it, focuses too heavily on insurance and not enough on mitigation.

As you know, the flood maps provide the basis for cities and counties to identify and manage their floodplains, and we have generally found the FIRMs to be accurate, in some areas better than others, but they do help us manage our floodplain.

And I want to also point out that there is a difference between having an accurate flood map and being able to read the flood maps, and most of the problems that we see are a result of flood zone determination companies and lenders not reading the maps accurately and determining whether a building is in or out of the flood zone.

Map improvements can be made, and those require funding. We are very happy that the reform act authorized $400 million a year for mapping, but we need that to be translated into appropriations. In 2010, $220 million was appropriated for flood mapping. Now we are down to $95 million, and we really need to get those numbers up to the previous—even the $400 million would be great.

So as I said, our problem is not so much with the quality of FIRMs. Our real problem is with risk communication, and this has increased with the reform act. It has always been a challenge.

The reform act implementation has been very poor in terms of communicating what is happening out there to the professionals and the public that need to hear about it. First of all, the training for the Write-Your-Own agents is terrible. There is not enough of it. It is too short. And many of the agents that I have talked to do not have sufficient information to translate to their customers what the reform act means.

Also, there is a large population of buildings in the Special Flood Hazard Areas that do not have flood insurance, and they have not for a long time. They do not have an agent that they can talk to. So reliance on flood insurance agents is not a good way to get the word out.

Also, important professional groups like surveyors and real estate agents have not been informed properly, and those should be our partners. We need to talk to them, NFIP needs to talk to them, and likewise local government officials.

And, finally, NFIP has not provided sufficient information to the public in a form that they can understand and digest. It has too much jargon. It assumes too much knowledge about the flood program. So in response, we need NFIP to do a much better job communicating with these groups of people that I just pointed out.

I want to say that I applaud NFIP's recent release of the specific rating guidelines. Those were formerly in a black box, a secret document that talked about how FEMA rated below base flood elevation policies. That is public now. It will help me a great deal in communicating risk to my public.

But the reform act problems go well beyond those associated with education and outreach. We have talked about affordability. I am very concerned that the unaffordability of flood insurance will cause people to drop their flood insurance, and they drop it by paying all cash. And what is happening in Oregon is that all-cash buyers are buying buildings at fire-sale reduced prices, and they are not insuring those buildings, which does not make Oregon resilient against flood.

I am going to skip some things here, but I do want to point out that mitigation is extremely important, and I think we need to think creatively about it. We need to encourage partial mitigation, which involves installing flood vents, perhaps filling in below-grade crawl spaces, and removing mechanicals from basements to help reduce costs, even if those actions do not result in a lowest floor that is above the base flood elevation.

And then I want to talk briefly about those people who bought policies after July 6th and before October 1, 2013—July 6, 2012, and October 1st. They are seeing renewals at full-risk rates. They need to get an elevation certificate, and they cannot afford it, and I have already received many tearful phone calls. And if there is anything I want to get out of this hearing, it is that policy has to be reversed. Those people need to be extended—have the subsidized rates extended to them for a longer period of time.

And then my last point is I would like to see NFIP institute an ombudsman program so that policyholders can have a venue to go to when they have rating issues. And because the insurance agents are not well informed, they cannot get through to their underwriters, they cannot get through to the FEMA insurance specialists, they do not know they exist, I get the phone calls, and I really think that FEMA needs to have an ombudsman function.

Thank you.

Chairman MERKLEY. Thank you very much.

Mr. Ellis.

STATEMENT OF STEVE ELLIS, VICE PRESIDENT, TAXPAYERS FOR COMMON SENSE

Mr. ELLIS. Thank you. Good afternoon, Chairman Merkley, Ranking Member Heller. I am Steve Ellis, vice president of Taxpayers for Common Sense, a national nonpartisan budget watchdog. Thank you for inviting me here today to testify on the National Flood Insurance Program, something I have worked on pretty much my whole professional career.

TCS works on this issue with SmarterSafer.org, a broad coalition of taxpayer, environmental, and insurance interests, in favor of promoting public safety through fiscally sound, environmentally responsible approaches to natural catastrophe policy. We applaud the work this Committee did last Congress to address the long-term sustainability of the NFIP by enacting the Biggert-Waters Flood Insurance Reform Act. Even with flaws, this legislation eliminates wasteful subsidies and moves flood insurance premiums to more closely match rates that are charged in the private market. It is critical that these reforms proceed without delay.

When the NFIP was established in 1968, Congress was warned by the task force reviewing the issue that subsidies could "invite economic waste of great magnitude." Well, $25 billion later, we know how that story unfolded. Although the subsidies were largely envisioned to be limited and short term, they were not. As of July 2013, out of 5.5 million policies, an estimated 1.15 million subsidized policies remain. And even after the reforms of Biggert-Waters, 62 percent of the subsidized policies will remain until rate maps are updated.

The availability of taxpayer-subsidized Federal flood insurance over the last several decades made it financially attractive to develop in high-risk areas and helped fuel the coastal development boom that increased the program's risk exposure and losses. Even worse, the program's benefits have flowed disproportionately toward repeatedly devastated properties and to the wealthy. Repetitive loss properties represent only 1 percent of all policies, yet have accounted for 25 to 30 percent of the cost of claims. And the Government Accountability Office study has found that, even after reform, subsidized NFIP policies are skewed toward counties in the top deciles of median home value and income.

As a consequence of the Biggert-Waters reforms, several types of properties that had previously received subsidies would gradually—25 percent a year—have their rates increased until they meet full risk-based rate, most notably second homes, businesses, and severe repetitive loss properties. In addition, properties in newly mapped or remapped areas would not have a subsidized grandfathered rate. Instead, the new rate would also be gradually implemented 20 percent per year.

While this may be financially painful in some cases, the new rates incentivize practices that reduce risk and in the long run will be good for the individual and for taxpayers. Not surprisingly, this effort has been met with some backlash, a lot of which we saw here. In some cases, homeowners are facing steep increases in premiums after years, even decades, of paying the same subsidies rates. As a result, there has been a series of efforts in Congress to delay flood map modernization or delay rate increases.

There have been charges of exorbitant rate increases to as much as $30,000 a year. It is worse, considering the underlying data that would lead to such a rate. Considering the maximum amount of flood insurance a homeowner can obtain under NFIP is $250,000 and an additional $100,000 for contents, that would basically mean that FEMA expects this property to be a total loss every decade. Either this individual and their property are at incredible risk, in which case delaying the rate increase sends absolutely the wrong signal; or the possible rate increase is overstated, as seems to have been the case when more recent information came to light, knocking the price down by half as much or more in some cases. Also, it appears it is a relatively small number of total properties involves. If there is a mapping error, Biggert-Waters set up a process to deal with it. Communities have to accept the map. Congress should develop solutions to help deal with affordability, not try to delay reality.

It may be politically expedient or popular locally to delay reforms, but what may make good local politics generally makes bad insurance and public policy. People deserve to know the costs and risks of where they live, and taxpayers deserve to have those who choose to live in harm's way pick up their share of the tab. Furthermore, delaying map implementation reduces rates for some, but policy owners remapped with reduced flood risk will keep higher premiums.

Delay also does not change the total amount of premium revenue the program must generate as a whole, meaning everyone will have to pay more. If Congress wants to deal with the issue of affordability, there are responsible ways to accomplish this goal. Any responsible approach to affordability should be temporary, targeted to those who need it, account for existing protection of homes, and independent of the NFIP rate structure.

FEMA's updated flood maps, which are crucial to the program's success or failure, must be up to date, accurate, and based on the best available science to be effective.

There is an increasing fatigue around the country with the cost of the NFIP program among taxpayers. To delay or derail the reforms enacted a year ago would put this program on perilous footing, fiscally, politically, and existentially. The reforms must be enacted as planned. Affordability should be addressed.

Thank you very much for the opportunity to testify, and I look forward to answering any questions you might have.

Chairman MERKLEY. Mr. Birnbaum.

STATEMENT OF BIRNY BIRNBAUM, EXECUTIVE DIRECTOR, CENTER FOR ECONOMIC JUSTICE

Mr. BIRNBAUM. Thank you, Chairman Merkley, Ranking Member Heller. Thank you for the opportunity to speak about the impact of the Biggert-Waters Act on the availability and affordability of flood insurance. My name is Birny Birnbaum. I am executive director of the Center for Economic Justice. I have been asked to talk about force-placed flood insurance, a topic on which I have worked for many years as an insurance regulator, a consumer advocate, and consulting economist. My comments today are presented on behalf of CEJ, the Consumer Federation of America, United Policyholders, the Center for Insurance Research, the National Fair Housing Alliance, and the National Consumer Law Center.

So what is force-placed insurance? Well, federally regulated lending institutions may not make a loan secured by improved real estate in a Special Flood Hazard Area unless the improved property serving as collateral for the loan is covered by a minimum amount of flood insurance. If a borrower fails to maintain the required voluntary flood insurance, the mortgage servicer will force-place insurance and charge the borrower. Consequently, a borrower cannot simply opt out of the NFIP to escape high flood premiums. In fact, force-placed flood is likely to cost the borrower much more than an NFIP policy.

Federal law also provides for forced placement of flood insurance in the event the borrower fails to maintain the required amount, and this law places the responsibility on the lender or servicer to determine if a lapse in required coverage has occurred and to notify the borrower of such a lapse prior to force-placing.

So the way these force-placed policies work is a mortgage servicer purchases a master or group policy from an insurance company, and it provides automatic coverage for any property in the servicer's portfolio if the coverage, the voluntary coverage, lapses. When coverage lapses and coverage is issued, force-placed coverage is issued, then the insurance company charges the mortgage servicer, who in turn charges the borrower. So this is a group policy that provides automatic coverage, and that is the key to force-placed insurance.

In terms of the force-placed market, data are not available for force-placed flood alone, but they are available for all of force-placed insurance, including force-placed hazard, which is like fire insurance.

The overall data show that force-placed insurance premiums quadrupled from 2004 to 2011, and during this period, loss ratios were very low. And by "loss ratio," I am talking about the claims that were paid under these force-placed policies compared to the premiums that were collected. The loss ratios over the period were 25 percent. That compares to over 60 percent for homeowners. What that means is these very low loss ratios suggest that force-placed rates were significantly excessive. However, force-places rates are inflated because of reverse competition, and what that means is the insurance companies market to the mortgage servicers, not to the consumers. And by marketing to the mortgage servicers, they actually pay kickbacks, and they build the cost of those kickbacks into the force-placed insurance premiums. So what happens is that consumers pay inflated amounts for this force-placed insurance.

Investigations by the New York Department of Financial Services and Fannie Mae have shown that FPI rates are significantly inflated by kickbacks in the form of commissions, captive reinsurance agreements, and free or below-cost services.

So there is going to be an explosion in the amount of force-placed flood insurance in the coming years, for three reasons:

First, more borrowers will now be required to purchase flood because of new flood maps. With more borrows required to purchase, there is going to be more force-placed flood.

Second, the rate hikes are going to make it unaffordable for consumers who are not going to be able to purchase the NFIP, but they are still going to have to pay for somehow force-placed flood.

And then, third, as lenders and servicers face greater penalties from Biggert-Waters for failure to ensure required flood insurance is placed, servicers are more likely to err on the side of too many force-placed placements. And, in fact, testimony in hearings before the New York department indicated that something on the order of 10 to 20 percent of force-placed insurance was wrongly placed.

So there is little consumer protection for excessive and unreasonable force-placed rates. There are only a few States that have looked at this issue. New York has led the pack. But even their efforts have focused largely on hazard force-placed insurance. Other States have not taken any action to force cuts in these inflated force-placed insurance rates. Federal agencies have addressed some of the issue with force-placed, but nothing to address the excessive costs or the affordability issues.

There is one opportunity, and that is with the Federal Housing Finance Authority. In March of this year, Fannie Mae was about to embark on a direct purchase program of force-placed insurance and insurance tracking, and by purchasing it directly, Fannie was able to use its market power to actually reduce the cost of force-placed insurance they estimated by hundreds of millions of dollars a year. Just as they were about to award that and implement that program, their conservator, FHFA, directed them not to go ahead with that. Instead, FHFA kept the status quo in place of Fannie reimbursing mortgage servicers for the inflated premiums and has embarked on a program of looking at ways to stop some of the kickbacks. But to date, FHFA has not taken any action on that.

So, consequently, FHFA is in a singular position to address problems with FPI flood by allowing Fannie and Freddie to implement this direct purchase program and also to stop some of the other abuses that are going on.

Thank you.

Chairman MERKLEY. I thank all of you for your testimony, and we will go 5 minutes and go back and forth as long as everyone would like to continue.

Senator HELLER. Sure.

Chairman MERKLEY. I want to start with the last testimony on force-placed insurance. Was there any indication by the Director of FHFA as to why he was blocking Fannie from providing this much more economical solution to homeowners?

Mr. BIRNBAUM. Well, the public information about why FHFA did not want Fannie to go ahead with that was that they said that Fannie did not have enough data. Basically the reasons were, in the view of the consumer groups, fairly weak. We thought that Fannie had studied the issue for over a year. They had gone through a request for proposal process. They had provided a very detailed set of requirements that clearly indicated they understood what was going on. So we and other consumer groups were dismayed when FHFA pulled the plug on that.

Chairman MERKLEY. And is there anything at all in Biggert-Waters that would provide authority to fend off this sort of predatory forced-placement insurance?

Mr. BIRNBAUM. There is one provision that will come into effect in mid-2014. In its mortgage servicing rules, at the beginning of this year, the Consumer Financial Protection agency basically made a requirement for mortgage servicers to pay the premium on voluntary insurance to keep that insurance in place if the borrower had an escrow account and if the payment of the premium would keep the policy in place. In other words, if the policy was canceled for some other reason other than nonpayment of premium, the rule would not apply. So keep the policy, voluntary policy, in place if it is a loan with an escrow account.

Biggert-Waters requires that all loans that have flood insurance have an escrow account for flood. So when you combine those two, the requirement in Biggert-Waters and the rule under the Consumer Financial Protection agency, it will ensure that voluntary NFIP policies remain in place. However, that does nothing to address the affordability issues of the NFIP, and it also does not address excessive retroactive billing. It is a small step, but it is not addressing what the concerns of this Committee are.

Chairman MERKLEY. Absolutely. I really appreciate your testimony on that topic when you talked about the 25-percent loss ratio. I just want to be absolutely clear what we are talking about is that for every $4 in premiums you bring in, you are paying out $1 in damages, and that is a pretty extraordinary situation.

Mr. BIRNBAUM. Yes. And just to be clear, that is for all force-placed insurance, so that would include force-placed flood and force-placed hazard. But, yes, there is no question that force-placed insurance, because of the noncompetitive market and the kickbacks to mortgage servicers, the prices have been highly inflated.

Chairman MERKLEY. Thank you very much, and I wanted to ask you one question that is related to your expertise, and that is the discussion that many of us have had up here about the affordability study that was required under the law to be done within 270 days. Is there any real reason that FEMA could not have completed that in 270 days?

Mr. BIRNBAUM. Well, I have done a number of insurance availability and affordability studies. I was chief economist at the Texas Department of Insurance. Before that I was chief economist at a Texas agency dedicated to representing consumers on insurance issues. So I have done many studies on insurance availability and affordability. And when I heard that FEMA needed to do such a study, I outlined what was needed for that, and it did not approach 3 years and $750,000.

There are data that are available today from the NFIP, from lender-placed insurers, from voluntary insurers, from the Census Bureau, that you could do an order-of-magnitude analysis of availability and affordability of flood insurance. So I think that can be done in a far shorter time frame.

Chairman MERKLEY. Thank you very much.

Senator HELLER. Mr. Chairman, thank you, and I want to thank the panelists for taking time today to be with us. I really do appreciate your testimony, what you have to say, and all those that have sat through the last couple of hours and listened to some of these comments and questions that we have raised.

Mr. Ellis, I have a couple of questions for you, if you do not mind, having specifically to do with private flood insurance. Obviously, we want to make sure that everybody has proper and affordability flood insurance, but the concern is obviously the viability and the fiscal solvency of NFIP. What is the viability today of private flood insurance?

Mr. ELLIS. There is some private flood insurance available. A lot of it is supplemental since it only—under NFIP you can only insure $250,000 for your property, so somebody who has more valuable property can get the supplemental onto that.

There is also some private insurers—there are certain parts of the country that are not eligible for flood insurance—the coastal barriers that are designated that way since 1982—and so they are serviced as well by a private market. I mean, it is more expensive than what you can get through NFIP, which is why generally it has not really developed. But one of the things—there are other countries that actually—many other countries that actually insure privately that do not have a national or a Government program. And so part of our hope would be that eventually when we move toward more actuarial rates that we will actually develop a real insurance system. We are not in 1968 anymore. We can actually map and price risk much more effectively than we could before, and so these are actually underwriteable events that in the 1960s we just did not have the modeling and the technology.

Senator HELLER. Ms. Landrieu brought up the Netherlands; half the population lives below sea level. Do they have a national flood insurance program or is it mostly done through private entities?

Mr. ELLIS. I would have to get back to you on that for the record, but I often hear about the Netherlands in the whole context of flood protection, and I would say that the ocean presents an existential threat to the existence of the Netherlands. And so they devote a significant amount of GDP to maintaining their flood protection structures.

And the other thing I would point out is that under the Flood Insurance Program—and I do not necessarily agree with this, but this is the rule—if you have 100-year protection, if you have protection from the 1-percent event, you do not have to buy it. So, I mean, really in a lot of places where—so in the case of the Netherlands, there probably are parts where under our rules they would not even have to buy flood insurance because they have that adequate—or that level of protection that we have deemed to be adequate.

Senator HELLER. Let me change for a little bit over here to some means testing. What are your thoughts on means testing the NFIP policies?

Mr. ELLIS. I think that is going to be one of the ways to go forward on affordability, and the fact is that, you know, you have millionaire homeowners that would be—that under the approaches that legislators have put forward about delaying the maps or delaying the rate increases, it kind of repeats the same problem that we had initially in the Flood Insurance Program in that everybody gets subsidized whether they really need the subsidies or they do not. And so any issue dealing with affordability we really believe—one is people should still know their real rates; we should not do it within the rate structure. It should be money that comes in on the side of that.

Two is that it should be done potentially through a surcharge on everybody's flood insurance policy so that we keep it within the program, we are not burdening the taxpayer anymore.

And it needs to be means-tested so that we are really only helping those that need the help and not a lot of these second-home owners that have been getting these subsidies for decades.

Senator HELLER. Thank you.

Chairman MERKLEY. Thank you. I want to turn first, Ms. Shirley, to a note that you put in your testimony about those folks who are buying homes between July 2012 and October 2013, and they are getting a subsidized rate. I understand upon renewal—and I want you to clarify this. Is it upon a 1-year renewal, they get a 1-year policy, then upon renewal of that policy, their rates will go to the unsubsidized?

Ms. SHIRLEY. Yes, as soon as—the first renewal after October 1st they will lose their subsidy and go to an unsubsidized rate. So some of those folks that bought very early may get one more year out of it, but most people who purchased after September would renew at full-risk rates after 1 year.

Chairman MERKLEY. After 1 year.

Ms. SHIRLEY. Right.

Chairman MERKLEY. And so when folks bought homes with this subsidized flood insurance, was there kind of a big red page in the closing package that says when you renew in a year, your—and, by the way, if you can give us a few examples of what kind of rate increases we are talking about, I think I have heard tenfold, and I do not know if that is legitimate or not. But, anyway, a big red warning that says, hey, your $500-a-year flood insurance will go to $5,000 and so forth? Is there a warning system? And what kind of rate increases are we talking about?

Ms. SHIRLEY. There was absolutely no way that a buyer could have known that those rates would increase until March 29, 2013, when FEMA announced how they were going to implement the program. So between July 2012 and March 2013, nobody knew that this was going to happen. After March 29th, I suppose you could make the argument that you should have known, but most people did not because there was no outreach.

Chairman MERKLEY. So basically a 9-month period, no way of knowing, and then an additional 7-month period, virtually no notification about these rules. So there was no big red sheet in the closing package saying this is going to happen.

Ms. SHIRLEY. Correct.

Chairman MERKLEY. So are you basically saying we are going to have perhaps hundreds of thousands of new homeowners who are going to have deep shock when they receive a notice saying that their insurance is going to go up? And if we talk about a family that has a $250,000 house in a 100-year flood zone, what type of increase are we talking about?

Ms. SHIRLEY. Well, it depends on the nature of the house. You need an elevation certificate to ascertain that. But it could easily be three times and could be as much as 10 times more expensive. And in the coastal zones, it could exceed that.

Chairman MERKLEY. So it is not unreasonable to say a house could go from $500 to $2,500 or $500 to $5,000?

Ms. SHIRLEY. That is correct. Not unreasonable.

Chairman MERKLEY. Am I correct in believing that if a family has to pay $1,000 more a year in flood insurance, one of the costs, if you will, that is essentially equivalent to dropping the value of the home $20,000 since $1,000 at 5 percent pays for a $20,000 mortgage?

Ms. SHIRLEY. I do not know the exact ratio, but I can tell you that homes are not selling in some particularly flood-prone areas. The market is frozen, partly because of uncertainty and partly because of affordability.

Chairman MERKLEY. Now, I think you spoke to basically all-cash buyers coming in to basically take advantage of the fact that the seller has suddenly lost the value in their home because the new buyer has to buy this really expensive policy.

Ms. SHIRLEY. Correct.

Chairman MERKLEY. And so we are creating something where homeowners who have built up equity over their lifetimes, maybe they have owned the home 30 years, are seeing that equity devastated and essentially given away to the advantage of those who are well off enough to pay full cash for the house.

Ms. SHIRLEY. That is right. And those well-off buyers do not buy flood insurance, making us more vulnerable and less resilient as a State.

Chairman MERKLEY. Which brings me to a different question, but I am going to come back to it.

Senator HELLER. Let me, Ms. Shirley, continue with you on disputes. Based on your testimony that you gave earlier, you mentioned that NFIP policyholders with rating issues have limited access to the dispute resolution process?

Ms. SHIRLEY. Correct.

Senator HELLER. You also mentioned that these FEMA regional offices do have insurance specialists that are on staff, but at times are not easily accessible. Can you expand on that? And what do you mean by that? Are they not returning phone calls, emails? What is the concern that you have there? And is it a publicity issue? I mean, do they not publicize to citizens how they can get access?

Ms. SHIRLEY. OK. So the general way that FEMA wants homeowners to dispute their policy is to go through the insurance writers who go through their underwriters, and generally—well, often that does not work. They cannot resolve it. And when the insured get to that point, it is not well known who they should call. So they end up calling their Senators or their Congress people, and they end up calling me, and then we refer them to an insurance specialist up at FEMA Region 10. So the insurance specialists—the existence of the insurance specialist is not well publicized, and by the time they call me, they are very, very frustrated because they have been everywhere else first.

So I want to have it more visible where people should call when they have gone through their insurance companies and they cannot resolve their problem.

Senator HELLER. I mentioned early on in my discussions with the Administrator about my concerns about this communication, and you heard his answer. And I think you raised the same concerns about their communications with real estate agents, Government officials, frankly, the public at large, about the changes in the Biggert-Waters bill.

After hearing what the Administrator said and answering my question on this frenzy that we have out there right now, did the Administrator answer any of your concerns?

Ms. SHIRLEY. No. There is not enough information out there. And it is so full of jargon and it is difficult to understand. Unless you understand flood insurance, it is just not useful information. And FEMA does have a Web site that has two or three brochures on it, but it is not sufficient information, and it does not talk about—it does not address those who are not insured now and who will be asked to purchase flood insurance in the future. And it really does not talk about the renewals of these policies purchased after July 6, 2012.

Senator HELLER. Very good. Thank you, Mr. Chairman. I am done.

Chairman MERKLEY. Mr. Ellis, I hear your argument for policies that are based on a full and fair assessment of the risk, but I want to ask you about a couple of anomalies that we have heard about. For example, you buy a house, you are not in a flood zone. You are 10 years into the mortgage, and then you get a notice saying, well, we have remapped—we, the community or the FEMA officials or whomever, have remapped, and you know what? We had it wrong. You have never seen a flood. Nobody in 50 years has seen a flood, but by our calculations, by our modeling, you are in a 100-year flood zone, and now you are going to be required to buy this unsubsidized insurance that may be several multiples of your mortgage.

Is there a fundamental unfairness to that? And if there is—I say "unfairness" in the sense that you made a deal based on the public information you were given at the time of purchase. And the public has turned around and changed that information in a way that has huge financial consequences for you. If there is a fundamental unfairness, how should we address it?

Mr. ELLIS. Well, I certainly think that the individual will feel that it is very unfair to them, and I do not necessarily disagree in that respect, although geography changes and, you know, to some extent, the idea that everything is static from the day you bought your home to the end of your 30-year mortgage kind of loses perspective when you think about this. And I think that when people keep talking about the rates, they forget to think about the fact that we are telling these people they are at risk, they should purchase flood insurance, because they are in the 1-percent chance of flooding every year if they are in the 100-year floodplain. And so we are doing them a disservice if we say, "You do not need to purchase flood insurance because you were not in the floodplain before and we will just keep ignoring that," and you are going to end up being flooded, and you are going to get five grand, ten grand from FEMA in a Small Business Administration loan, which is not what people need when they are flooded.

And so I think there has to be—there is a balancing that needs to be done here, Mr. Chairman, and so it is something where we need to address, if it is an affordability issue. If it is not an affordability issue, then I think that people need to be paying the full freight. We are doing the rest of the country a disservice if we are not doing this. And we are doing this person a disservice because they can do things to mitigate their risk, to actually make them less vulnerable in the future. And so that way, when the flood does come, because, as Administrator Fugate mentioned, you know—I think I wrote down he has been to too many places that have never flooded before until there was a disaster. And so these are places that are at risk or we have determined to be at risk, and so I would hope that they would purchase their flood insurance, and if it is an affordability issue, then we need to deal with it.

Chairman MERKLEY. So a family says to you, you know, this policy which is going to cost $5,000, that was never anticipated because I was not in a flood zone when I bought the house, this was the difference between whether or not my son or daughter attends, can afford to attend college; it is a difference on whether my kids in grade school can pay the activity fees to be involved in sports or my children in high school can join the debate team or whatever fees, says, you know, this is America, I should be able to decide for myself whether I want to spend that $5,000. If I want to bear that risk, shouldn't I be able to bear that risk? This was not part of the contract when I bought this house. Shouldn't it be up to me whether I want to buy flood insurance? Now being fully informed that I am being told there is a higher risk than anybody thought, shouldn't it be up to me to decide whether or not to buy that insurance or to buy other valuable things for the success of my family?

Mr. ELLIS. Certainly I am sympathetic to the individual. I mean, this is the way the program has been structured. But, you know, the problem is that, as Americans, we are often—we are very bighearted, and so instead of—you know, part of the reason why the Flood Insurance Program was created was because there was so much ad hoc disaster assistance going out there to help people out after disasters, and so they wanted to create a program like this.

My concern would be that when that property does eventually flood, and my sympathy would go to that family, then they would be trying to get more disaster assistance because we are a bighearted country, and we are kind of soft-headed when it comes to that sort of thing. We are not tough on it.

So I think that there is a challenge, and I am concerned in this debate, Mr. Chairman, in that we are seeing a lot of the tail wagging the dog. We are seeing a lot of these extreme circumstances that are trying to dictate the overall policy. You have people talking about, lawmakers talking about $30,000 policies or $28,000 policies, and so then they want to delay all the maps across the country. That does not—you know, that is the exception making the rule to me, Mr. Chairman, and I am concerned about that, especially because some people will benefit from their new maps, at least as far as in 2010—and I think that Administrator Fugate was addressing this to Senator Warren. He said it goes both ways, and he did not get to finish his comment, but I know in 2010 he said that they were mapping as many properties out of the floodplain as they were mapping in. I do not know if that is still the case, but I do know he said that then. And so some of these are broad solutions trying to deal with a very narrow instance.

Chairman MERKLEY. Mr. Birnbaum.

Mr. BIRNBAUM. Yes, a couple of comments. First, it is patently unfair. Yes, it is really important that consumers see the true price of protection. Risk-based pricing is important so consumers can make investment decisions that are rational. You do not want to do a bait-and-switch where you come in, you think that it is a $500-a-year cost to protect yourself from flood, and it turns out to be a $6,000-a-year thing. But that is exactly what happened.

You know, if that had happened with a mortgage, if a mortgage company gave you a mortgage that was $1,000 a month and then all of a sudden said now it is going to be $1,800 a month or $1,600 a month, with barely notice, the Consumer Financial Protection Bureau would be all over that.

You know, there are millions of people in California who are at risk of earthquake damage, and yet they have the ability to sort of opt out of buying earthquake insurance.

So, you know, the issues that you raise are important; however, you know, the things that Steve says are also valid. It is vitally important that consumers see what the cost is of protection, because without that you cannot make a rational, long-term decision about whether that is a good investment for you, whether you can afford it.

More importantly, if you do not have the risk-based price, you do not have the proper incentives for loss mitigation. That is just critical. If there should be one overriding goal of Federal policy, it should be—for natural disaster policy, it should be to promote sustainable and resilient communities. And what that means is that when the Government makes money, it should not be subsidies. If somebody is having a problem with affordability, then that money should go in as an investment in loss mitigation to enable that consumer to pay the affordable amount of insurance. But continuing to do subsidies is the Government sort of spending money without any return. Making those investments in loss mitigation is the Government making investments that have a very positive return for that consumer and for society at large.

Chairman MERKLEY. I have one more question to throw out to you all, and it really stems from what Senator Landrieu said. She said up until we had—and I am not sure which storm it was.

Mr. ELLIS. Katrina.

Chairman MERKLEY. It was Katrina. Up until we had this big natural disaster, Katrina, essentially the rates were sufficient to keep the fund solvent, and she waived that sheet in the air. And it made me start thinking about what it is we are insuring against. Are we insuring about garden variety flooding or the really big exceptional hurricanes? And are we in the course—and should there be a difference between those two things? And if, in fact, what we are insuring against is the hurricanes, then are the costs of the insurance as distributed around the country actually fair to those who do not live in hurricane zones? In other words, are we essentially charging the entire country on these policies more than should be there to cover the river coming up and so forth to cover these great national disasters?

And so I will just throw those two thoughts out to all of you. Do we really have two different kinds of things embedded in these insurance policies? And are the costs of the insurance policies actually fair to folks who are in different parts of the country in terms of the risk being reflected accurately by the premium? Does anyone want to take on those questions? Mr. Ellis.

Mr. ELLIS. Yes, Mr. Chairman. Well, one, it is instructive to look at how the total—the way the system is set up is that they have the average historical loss year, and that is before Biggert-Waters was—every year except for what FEMA decided were extraordinary years, so they left out 2005, which had three of the largest storms, natural disasters, three of the top 10 in our country's history as far as loss, and then 2011, because of the Midwest flooding, and so they basically threw those out or discounted them very, very heavily. And then that set the total amount of premium that the program was supposed to achieve to then basically offset a year, and then that trickles down to everybody's individual premiums to aggregate. You know, it is like algebra, basically.

After Biggert-Waters, everything had to be included, including the 2005 loss year and the 2011 loss year. I think there is an argument to be made that that should be discounted at least somewhat, but clearly, if Sandy has any lesson, it is that 2005 is not as big of an anomaly as we all wish it was. And so that has to be priced into there somewhere.

And then, also, Mr. Chairman, where I think you are absolutely on the merit is that obviously now that is being dispersed to everybody, and that is part of the reason why I say if you delay the rate increases for one group of properties, everybody else's rates are going to go up because the total amount that they are trying to achieve is exactly the same. So that side of the equation, that side of the equals sign, is not changing. And so that is going to end up increasing everybody's flood insurance premiums in other places, and I would argue that is not fair.

And then, last, where it is a little bit different, though, is obviously people are paying the risk of their particular property. So if you live in a hurricane zone, if you live in a storm surge area, you are going to pay a lot more, even at a base flood elevation, than somebody who lives in Bend, Oregon. You know, and so there is that issue as well, so there is a bit more concentrating on the risk associated with a particular property.

Chairman MERKLEY. So, in short, the folks who live on a stream in Oregon are not subsidizing a hurricane zone on the Atlantic coat.

Mr. ELLIS. Probably to some extent there is. There is cross-subsidies in the program. There are less cross-subsidies post Biggert-Waters than there were before.

Chairman MERKLEY. Does anyone else want to jump into this conversation? Ms. Cackley.

Ms. CACKLEY. Well, I think Mr. Ellis is correct in terms of the changes in Biggert-Waters did change the cross-subsidies. But there still are some because of the way the premium is set. It is not exactly—and especially because FEMA does not have the information they need for elevation certificates for every property, you cannot—you do not have a true risk, true actuarial fair rate for each property that needs one.

Chairman MERKLEY. Thank you.

Mr. Birnbaum.

Mr. BIRNBAUM. I guess what I would add to this is that if you want to make sure that rates are truly accurate, then what you want to do is privatize the Flood Insurance Program. You want to sort of utilize the ability of the insurance industry to do the risk modeling and to do the pricing that they do for other types of perils. And there would be some real advantages to privatizing the Flood Insurance Program. It would provide flood coverage at a much more efficient and cost-effective level. You would not have a second administrative layer. You would not have that 30 percent Write-Your-Own commission. You would not have all of the stuff going on between whether it is a wind loss or a flood loss and all of the costs associated with trying to figure out whether it is covered by the wind policy or the flood policy.

So there are some real advantages to sort of looking at privatizing the Flood Insurance Program, both in terms of accuracy of pricing but also in getting the insurance industry more involved in loss mitigation. They do not have any skin in the game. If they are on the hook, then all of a sudden you will see them doing what European insurers are doing, which is getting extremely active in all sorts of flood loss mitigation and entering into partnerships with policyholders to invest in loss mitigation. So I just throw that out as something to consider.

Mr. ELLIS. We support that.

Chairman MERKLEY. Yes, Ms. Cackley.

Ms. CACKLEY. I just wanted to point out that GAO is in the process of doing a study on the possibilities of privatizing the system. It was one of our mandates under Biggert-Waters. FEMA was also mandated to do a similar study. So you will be getting that information by the end of the year.

Chairman MERKLEY. Great. Well, I am going to wrap this up. Everyone has been very patient in staying here a long time, and thank you very much. I am struck by the fact that we started the hearing, hearing about how essentially a private system broke down because the policies were too high and people were not buying them. And now we essentially are trying to create risk-based policies that kind of reflect what the market should do, and the prices are so high that it is breaking down. And we started to hear some of the stories about that today, and then the recommendation here at the close that maybe we should go back to the private side.

So we have got a lot to wrestle with. I thank very much my Vice Chair, Senator Heller, for being very supportive of holding this hearing and all the colleagues who came to weigh in today. I think we are going to hear a tremendous amount from our constituents. As Ms. Shirley pointed out, we are going to hear a lot of constituents screaming when they go to renew and find out that the deal that they thought they made when they bought that new property during that 9-month period turns out to be a deal that is very different than they anticipated with no warning. And so I think we have got a lot to address.

With that, I adjourn the hearing. Thank you.

[Whereupon, at 5:05 p.m., the hearing was adjourned.]

[Prepared statements, responses to written questions, and additional material supplied for the record follow:]

PREPARED STATEMENT OF W. CRAIG FUGATE

ADMINISTRATOR, FEDERAL EMERGENCY MANAGEMENT AGENCY, DEPARTMENT OF HOMELAND SECURITY

SEPTEMBER 18, 2013

Introduction

Good afternoon Chairman Merkley, Ranking Member Heller and distinguished Members of the Subcommittee. My name is Craig Fugate, and I am the Administrator at the U.S. Department of Homeland Security's (DHS) Federal Emergency Management Agency (FEMA). It is an honor to appear before you today on behalf of FEMA to discuss the National Flood Insurance Program (NFIP) and our efforts to implement the Biggert-Waters Flood Insurance Reform Act of 2012.

In my testimony today, I will discuss the NFIP; the changes FEMA is making as a result of the Act; the role of flood maps and levees; and steps property owners can take to mitigate against flood damage.

Flooding and the Need for a National Program

Flooding has been, and continues to be, a serious risk in the United States. Most insurance companies have historically excluded flood damage from homeowners insurance because of adverse selection—only those most susceptible to flooding will purchase coverage. To address this need, Congress established the NFIP in 1968 to make flood insurance available, identify flood risks and encourage sound local flood risk management. The NFIP is administered by FEMA.

The NFIP was broadened and modified with the passage of the Flood Disaster Protection Act of 1973 and other legislative measures. It was further modified by the National Flood Insurance Reform Act of 1994 and the Flood Insurance Reform Act of 2004. The most recent reforms have come after numerous short-term reauthorizations and lapses in Program authority over the past several years.

About 40 percent of the U.S. population lives in counties that border the ocean or Great Lakes and are directly or indirectly affected by flood risk, and most U.S. counties contain rivers and streams that present flood hazards. Moreover 5.6 percent of the U.S. population lives in the highest risk coastal and riverine flood hazard areas, making flooding the most costly and prevalent natural risk in the United States. Additionally, sea level rise, climate change, urbanization, and other factors may lead to even more Americans living in high flood risk areas in coming years.

The NFIP serves as the foundation for national efforts to reduce the loss of life and property from flood disasters that may occur. The Program is designed to insure against, as well as minimize or mitigate, the long-term risks to people and property from the effects of flooding, and to reduce the escalating cost of flooding to taxpayers. The NFIP works closely in partnership with Write Your Own (WYO) insurance companies to market, sell, administer, and adjust claims for policyholders. By encouraging and supporting mitigation and floodplain management efforts, the NFIP is estimated to save the Nation $1.6 billion annually in avoided flood losses.

Today, almost 22,000 communities in all States and territories participate in the NFIP, with 5.6 million NFIP policies providing over $1.2 trillion in coverage.

The NFIP was, by statute and design, not actuarially sound. Specifically, 20 percent of policyholders, including many of the NFIP's highest risk structures, paid premiums that were less than actuarially sound and the Government was subsidizing on average 60 percent of the loss. The debt resulting from Hurricanes Katrina and Sandy, the two costliest storms in NFIP history, illustrate the financial challenges for the NFIP that the Biggert-Waters Flood Insurance Reform Act of 2012 aimed to address. Significant concentrated losses in high policy coverage areas could set the program up for future losses beyond the authorized borrowing authority. In addition, the financial challenges are heightened due to subsidies and grandfathering that were established to encourage older structures to participate in the Program and make premiums affordable for these policyholders in high risk areas.

Pursuant to the statute before the Biggert-Waters Flood Insurance Reform Act of 2012, FEMA established subsidies for owners of existing homes and businesses built prior to the initial Flood Insurance Rate Map (FIRM) and made them eligible to purchase insurance at subsidized rates. In other words, a building built before flood risk was known, and at an elevation below the 1-percent annual chance flood, could be insured at a rate substantially less than their real risk rate.

The NFIP collects more than $3.5 billion in annual premium revenue, and FEMA estimates that an additional $1.5 billion annually is needed from subsidized policyholders.

FEMA also established grandfathered rates to address rates for structures built in compliance with existing FIRMs that experienced subsequent increases in flood risk. FEMA allowed those structures to grandfather according to the risk identified on the earlier FIRM, and did not adjust premiums to reflect the current risk. Grandfathered properties are not subsidized by the Program, and FEMA establishes cross subsidies within classes of structures to maintain the actuarial integrity of the rate structure.

This annual premium shortfall during catastrophic flooding events, such as Hurricanes Katrina and Sandy, required FEMA to use its statutory authority to borrow funds from the U.S. Department of Treasury. These funds were used to pay covered flood damage claims to policyholders. Although payments have been made to reduce this obligation, $24 billion in debt remains.

Biggert-Waters Flood Insurance Reform Act of 2012

Congress determined that further reforms were needed to make sure the NFIP was financially sustainable.

To execute these reforms, Congress passed the Biggert-Waters Act. The law required changes to all of the major components of the program, including flood insurance, flood hazard mapping, grants, and the management of floodplains. Many of the changes are designed to strengthen the fiscal soundness of the NFIP by ensuring that flood insurance rates more accurately reflect the real risk of flooding. The changes are being phased in over time, beginning this year. Biggert-Waters also reauthorized the NFIP for 5 years, which injected confidence and stability into the real estate and mortgage markets.

Removal of Subsidies and Grandfathered Rates

Biggert-Waters ushered in changes that will lead to premium rate increases for some—but not all—policyholders over time.

Today, I would like to focus on the sections of the Act that remove subsidies and grandfathered rates.

Currently, approximately 20 percent of policyholders, representing approximately 1.1 million of the 5.6 million NFIP policies, now pay subsidized rates. As FEMA implements the changes stipulated in the Biggert-Waters legislation, these policyholders will eventually pay rates that reflect actual risk to their properties. The remaining 80 percent of policyholders will not see increases as a result of this change, although it is possible that their rates will increase if, in the future, new maps reveal higher risk under the phase-out of grandfathered rates required by the legislation.

Specifically, the following changes for subsidized policyholders will be or have already been implemented due to the legislation:

- Beginning January 1, 2013, owners of properties previously eligible for subsidized rates on nonprimary/secondary residences in a Special Flood Hazard Area (SFHA), saw a 25 percent increase annually in their rates, as required by the law, which will continue until rates reflect true risk.
- We anticipate that under a final rulemaking, owners of substantially damaged or improved properties previously eligible for subsidized rates will see a 25 percent rate increase annually, as required by the law, until rates reflect true risk.
- Beginning October 1, 2013, owners of subsidized policies on business/nonresidential properties and severe or repetitive loss properties in a Special Flood Hazard Area will see a 25 percent rate increase annually, as required by the law, until rates reflect true flood risk.

All subsidized properties, including primary residences, will move immediately to actuarial rates if:

- The policy lapses;
- The property suffers severe, repeated, flood losses; or
- The property is purchased.

Each property's risk is different. Some policyholders may reach their true risk rate after less than 5 years of increases, while other policyholder increases may go beyond 5 years to get to the full risk rate required by the new law.

With regard to grandfathered rates, additional changes to premium rates may also occur upon remapping. We are evaluating when it is administratively feasible to implement these rate changes.

When a map is revised or updated, grandfathering will no longer be available. Grandfathering is applied in two situations: to allow policyholders in a Special Flood Hazard Area built in accordance with flood maps to keep rates that reflected that compliance even if a later map would increase their premium; and to enable structures built outside of the Special Flood Hazard Area and later remapped into the

Area to purchase insurance based on an average cross-subsidized rate. The Act replaces the policy of offering grandfathered rates with a 5 year phase-in to rates that reflect the current risk when a FIRM is revised or updated.

The Role of Flood Maps and Levees

Mapping and identifying flood hazards enables informed, smart development and encourages communities to adopt and enforce minimum floodplain management regulations. These efforts minimize the financial impact of flooding on individuals and businesses, and mitigate the effects of flooding on new and improved structures.

FEMA consistently releases new flood maps and data, giving communities across America access to helpful, authoritative data that they can use to make decisions about flood risk, enabling safer development and rebuilding following disasters. FEMA is required to review community flood maps every 5 years and assess whether to revise or update them based on current conditions.

Flood hazard conditions are more accurately captured now as a result of FEMA's Risk Mapping, Assessment, and Planning (Risk MAP) program.

FEMA began implementing the Risk MAP program at the start of Fiscal Year (FY) 2009. Risk MAP not only addresses gaps in flood hazard data, but uses that updated data to form a solid foundation for risk assessment and floodplain management, and to provide local, State, and tribal governments with information needed to mitigate flood-related risks. Risk MAP is introducing new products and services extending beyond the traditional digital flood maps produced in Flood Map Modernization, including visual illustration of flood risk, analysis of the probability of flooding, economic consequences of flooding, and greater public engagement tools. FEMA is increasing its work with officials to help use flood risk data and tools to effectively communicate risk to citizens, and enable communities to enhance their mitigation plans.

FEMA has initiated 600 Risk MAP projects affecting 3,800 communities and addressed their highest priority engineering data needs, including coastal and levee areas.

Regarding levees, FEMA has also reviewed its approach to mapping flood hazards with respect to nonaccredited levees. FEMA recognizes that levee systems that do not fully meet the requirements for accreditation may still provide some measure of flood risk reduction.

As a result, FEMA is introducing a new approach of targeted modeling procedures to replace the previous "without levee" approach, that did not recognize a nonaccredited levee as providing any level of protection to communities behind the levees during the base (1-percent-annual-chance) flood. These procedures better characterize actual conditions that a community may encounter when addressing nonaccredited levees or levee systems.

FEMA devised this new approach by leading a multidisciplinary project team comprised of representatives from FEMA, the U.S. Army Corps of Engineers, and experts from the academic and engineering communities to evaluate technical options for nonaccredited levees. The FEMA-led team explored a broad spectrum of levee analysis and mapping procedures. Based on the results of the development, testing, review and public comment efforts, FEMA created and is implementing a levee analysis and mapping approach that is flexible and will produce more precise flood hazard maps and supporting data where levee systems are involved.

FEMA will use these new procedures to produce Flood Insurance Rate Maps (FIRMs), Flood Insurance Study reports, and related products for communities and Tribes impacted by nonaccredited levee systems. A core goal of the new procedures includes identifying more precisely the flood hazard associated with levee systems and reflecting the results in the mapping. An important outcome of the effort is also increasing the credibility of FIRMs where nonaccredited levee systems exist.

The new approach, accompanied by operating guidance, will be applied to a limited number of projects during FY2013, and other future mapping projects will be prioritized as additional funding is available.

FEMA Regional Offices will be in contact with communities to identify participants for a discussion about their local levee system and to facilitate a Local Levee Partnership Team as needed.

This team will be comprised of FEMA and community representatives to provide input and guide the implementation of the approach.

Educating Stakeholders and Implementing the Provisions of Biggert-Waters

FEMA has undertaken significant steps to inform its policyholders and stakeholders about these changes to the NFIP, including educating:

- Insurance agents selling flood insurance;

- Realtors, the banking community, floodplain managers, insurance executives, and others;
- Political leadership at local, State, tribal, and Federal levels;
- Disaster survivors so they can be informed should they choose to rebuild; and
- Affected policyholders, who will receive notification from their insurance company in their bills explaining changes.

The Act has also necessitated programmatic changes to the NFIP itself, including its processes and regulations. Areas specifically impacted by Biggert-Waters include actuarial sciences, insurance underwriting, floodplain management, and floodplain mapping.

FEMA is actively meeting with affected communities throughout the country to discuss these changes. This summer, Associate Administrator for Federal Insurance and Mitigation David Miller traveled to Louisiana and Mississippi to see and hear first-hand the potential impacts of the law on policyholders. Additionally, many FEMA staff participated in outreach meetings with national and regional associations and communities to provide information on the new law. While in the Gulf Coast region, it was very clear that there are challenges to implementing the law when premiums may exceed $10,000 or in more high risk areas where homes are not easily elevated or bought out. In the Gulf Coast, many policyholders are required to have insurance and live near the industry jobs that support our national economy. In States with recent disasters like New Jersey and New York, communities are going through the process of adopting new maps as a result of increased risks found in mapping completed both pre- and post-disaster.

The Role of Mitigation in Affordability

As the NFIP transitions toward full risk rates, there will be significant increases in premiums for some subsidized and grandfathered structures. Individuals whose properties are at risk of flooding may lack the resources to make prudent risk management and mitigation decisions, including the decision to relocate, mitigate, or purchase adequate insurance.

Pursuant to the provisions in Biggert-Waters, FEMA is charged with completing a study with the National Academy of Sciences to explore ways to: encourage/maintain participation in the NFIP, methods to educate consumers about the NFIP and flood risk, and methods for establishing an affordability framework for the NFIP, including implications of affordability programs for the NFIP and the Federal budget. The Academy estimates that it will likely take at least 2 years to complete the study due to the need to obtain data on policyholders and their incomes.

There are steps the public can take to minimize their risk of damage should a flood occur, as well as to reduce premiums. FEMA's Hazard Mitigation Assistance (HMA) programs provide funds for projects that reduce the risk to individuals and property from natural hazards. These programs enable mitigation measures to be implemented before, during and after disaster recovery. Local jurisdictions develop projects that reduce property damage from future disasters and submit grant applications to the State. The States submit applications to FEMA based on State criteria and available funding. The HMA programs include:

- *Hazard Mitigation Grant Program (HMGP)*—The Hazard Mitigation Grant Program provides grants to implement long-term hazard mitigation measures after a major disaster declaration. The purpose of HMGP is to reduce the loss of life and property due to natural disasters and to enable mitigation measures to be implemented during recovery from a disaster.
- *Mitigation Assistance Grants*—The Mitigation Assistance Grants program provides funds from the National Flood Insurance Fund on an annual basis so that measures can be taken to reduce or eliminate risk of flood damage to buildings insured under the NFIP.

FEMA encourages property and business owners concerned about potential rate increases as a result of Biggert-Waters to contact their local community planning, emergency management, or State Hazard Mitigation Officer to learn more about implementing these mitigation efforts.

Conclusion

FEMA administers the NFIP to help communities increase their resilience to disaster through risk analysis, risk reduction, and risk insurance. The NFIP helps individual citizens recover from the economic impacts of flood events, while providing a mechanism to reduce exposure to flooding through compliance with building standards and encouraging sound land-use decisions.

FEMA looks forward to working with the Congress as Biggert-Waters is implemented.

Thank you again for the opportunity to appear before you today. I am happy to answer any questions you may have.

PREPARED STATEMENT OF ALICIA P. CACKLEY

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Testimony

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NATIONAL FLOOD INSURANCE PROGRAM

Continued Attention Needed to Address Challenges

Statement of Alicia Puente Cackley, Director
Financial Markets and Community Investment Team

GAO-13-858T

GAO Highlights

Highlights of GAO-13-858T, a testimony before the Subcommittee on Economic Policy, Committee on Banking, Housing, and Urban Affairs, U.S. Senate

Why GAO Did This Study

NFIP, established in 1968, provides policyholders with insurance coverage for flood damage. FEMA, within the Department of Homeland Security, is responsible for managing the program. NFIP offers two types of flood insurance premiums to property owners: subsidized and full-risk. The subsidized rates are not based on flood risk and, according to FEMA, represent only about 40-45 percent of the full flood risk. GAO placed NFIP on its high-risk list in 2006 because of concerns about its long-term solvency and related operational issues.

GAO was asked to testify about NFIP issues and its recent work on NFIP. This statement discusses (1) the reasons that NFIP is considered high-risk, (2) changes to subsidized policies and implications of potential additional program changes, and (3) additional challenges for FEMA to address. In preparing this statement, GAO relied on its past work on NFIP, including GAO-13-607, GAO-13-568, and GAO-13-283.

What GAO Recommends

GAO continues to support its previous recommendations made to FEMA that focus on the need to address management and operational challenges, ensure that the methods and data used to set NFIP rates accurately reflect the risk of losses from flooding, and that oversight of NFIP and insurance companies responsible for selling and servicing flood policies is strengthened. FEMA agreed with these recommendations and is taking steps to address them.

View GAO-13-858T. For more information, contact Alicia Puente Cackley at (202) 512-8678 or cackleya@gao.gov.

September 2013

NATIONAL FLOOD INSURANCE PROGRAM

Continued Attention Needed to Address Challenges

What GAO Found

The National Flood Insurance Program (NFIP) was added to GAO's high-risk list in 2006 and remains high risk due to losses incurred from the 2005 hurricanes and subsequent losses, the financial exposure the program represents for the federal government, and ongoing management and operational challenges. As of July 31, 2013, the program owed approximately $24 billion to the U.S. Treasury (Treasury). NFIP's financial condition highlights structural weaknesses in how the program has been funded—primarily its rate structure. The annual amount that NFIP collects in both full-risk and subsidized premiums is generally not enough to cover its operating costs, claim payments, and principal and interest payments for the debt owed to Treasury, especially in years of catastrophic flooding, such as 2005. This arrangement results in much of the financial risk of flooding being transferred to the federal government and ultimately the taxpayer. Furthermore, weaknesses in NFIP management and operations, including financial reporting processes and internal controls, strategic and human capital planning, and oversight of contractors have placed the program at risk.

The Biggert-Waters Flood Insurance Reform Act of 2012 (Biggert-Waters Act) mandated that GAO conduct a number of studies related to actual and potential changes to NFIP, including analyses of remaining subsidies and the effect of increasing coverage limits or adding coverage options. In a study of remaining subsidies, GAO estimated that with the changes in the Biggert-Waters Act approximately 438,000 policies no longer are eligible for subsidies, including about 345,000 policies for nonprimary residences, about 87,000 business policies, and about 9,000 policies for single-family properties that had severe-repetitive losses. Subsidies on most of the approximately 715,000 remaining subsidized policies are expected to be eliminated over time as properties are sold or coverage lapses, as are previous exemptions from rate increases after flood zone map revisions. Reducing the financial impact of remaining subsidized policies on NFIP generally could involve accelerating elimination of subsidies, targeting assistance for subsidies, or expanding mitigation efforts, or some combination. Each approach has advantages and disadvantages. In GAO's 2008 study about rate-setting, GAO noted that the losses generated by NFIP have created substantial financial exposure for the federal government and U.S. taxpayers—due in part to its rate-setting process. Partly because of these rate-setting issues, GAO concluded in a July 2013 report that the advantages and disadvantages to additional changes to the program, such as raising coverage limits or adding optional coverage types, would need to be carefully weighed.

The Federal Emergency Management Agency (FEMA) will require several years to fully implement the Biggert-Waters Act. FEMA officials acknowledged that they have challenges to resolve. These include updating and correcting information on whether a policy is for a primary or secondary residence, determining the fair market value of insured properties, and developing a definition of severe repetitive loss for multifamily properties. Further, FEMA must establish full-risk rates that reflect flood risk for active policies that no longer are eligible for subsidies; but it does not have a plan to do so. In an effort to update payment formulas to insurance companies, as GAO recommended, FEMA has begun receiving actual flood-related information from some insurance companies but all companies are not reporting the information consistently.

Chairman Merkley, Ranking Member Heller, and Members of the Subcommittee:

I am pleased to be here today to testify on the National Flood Insurance Program (NFIP). As you know, the flood insurance program is a key component of the federal government's efforts to minimize the damage and financial impact of floods. Created in 1968, it is administered by the Federal Emergency Management Agency (FEMA) within the Department of Homeland Security. As of the end of fiscal year 2012, the program had more than 5.5 million policies with an insured value of about $1.3 trillion and collected about $3.5 billion in annual premiums.

My statement today will discuss (1) the reasons that NFIP is considered high risk, (2) changes to subsidized policies and implications of potential additional program changes, and (3) additional challenges for FEMA to address. This testimony is based on two reports we recently issued in July 2013 on NFIP coverage limits and subsidized properties and other prior GAO reports on various issues related to NFIP.[1] In conducting work for our July 2013 reports, we analyzed FEMA data on flood insurance policies, claims, and repetitive losses, as well as historic data on claims and premiums for policies with subsidized and full-risk rates. We also interviewed industry experts, including representatives from FEMA, insurance industry organizations, brokers, insurance companies, and consumer advocacy organizations. Finally, we reviewed prior GAO reports and testimonies and relevant studies conducted by RAND, the Wharton Risk Management and Decision Processes Center, Deloitte Consulting LLP, the Congressional Research Service, and academics.

We conducted the work on which this statement is largely based in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that

[1]GAO, *Flood Insurance: More Information Needed on Subsidized Properties*, GAO-13-607 (Washington, D.C.: July 3, 2013); *Flood Insurance: Implications of Changing Coverage Limits and Expanding Coverage*, GAO-13-568 (Washington, D.C.: July 3, 2013); *High-Risk Series: An Update*, GAO-13-283 (Washington, D.C.: February 2013); *Flood Insurance: Options for Addressing the Financial Impact of Subsidized Premium Rates on the National Flood Insurance Program*, GAO-09-20 (Washington, D.C.: Nov. 14, 2008); and *Flood Insurance: FEMA's Rate-Setting Process Warrants Attention*, GAO-09-12 (Washington, D.C.: Oct. 31, 2008).

the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Background

The National Flood Insurance Act of 1968 established NFIP as an alternative to providing direct disaster relief after floods.[2] NFIP, which makes federally backed flood insurance available to residential property owners and businesses, was intended to reduce the government's escalating costs for repairing flood damage. Floods are the most common and destructive natural disaster in the United States; however, homeowners' insurance generally excludes flooding. Because of the catastrophic nature of flooding and the inability to adequately predict flood risks, private insurance companies historically have been largely unwilling to underwrite and bear the risk resulting from providing primary flood insurance coverage. Under NFIP, the federal government assumes the liability for the insurance coverage and sets rates and coverage limitations, while the private insurance industry sells the policies and administers the claims.

NFIP offers two types of flood insurance premiums to property owners who live in participating communities: subsidized and full-risk. The National Flood Insurance Act of 1968 authorized NFIP to offer subsidized premiums to owners of certain properties. These subsidized rates are not based on flood risk and, according to FEMA, represent only about 40-45 percent of the full flood risk. Congress originally mandated the use of subsidized premiums to encourage communities to join the program and mitigate concerns that charging rates that fully and accurately reflected flood risk would be burdensome to some property owners. Even with highly discounted rates, subsidized premiums are, on average, higher than full-risk premiums. The premiums are higher because subsidized structures built before Flood Insurance Rate Maps (FIRM) became available generally are more prone to flooding (that is, riskier) than other structures. In general, pre-FIRM properties were not constructed according to the program's building standards or were built without regard to base flood elevation—the level relative to mean sea level at which there is a 1 percent or greater chance of flooding in a given year.

[2] Pub. L. No. 90-448, Title XIII, § 1302, 82 Stat. 476, 572 (1968).

Potential policyholders can purchase flood insurance to cover both buildings and contents for residential and commercial properties. NFIP's maximum coverage for residential policyholders is $250,000 for building property and $100,000 for contents. This coverage includes replacement value of the building and its foundation, electrical and plumbing systems, central air and heating, furnaces and water heater, and equipment considered part of the overall structure of the building. Personal property coverage includes clothing, furniture, and portable electronic equipment. For commercial policyholders, the maximum coverage is $500,000 per unit for buildings and $500,000 for contents (for items similar to those covered under residential policies).

NFIP largely has relied on the private insurance industry to sell and service policies. In 1983, FEMA established the Write-Your-Own (WYO) program.[3] Private insurers become WYOs by entering into an arrangement with FEMA to issue flood policies in their own name. WYOs adjust flood claims and settle, pay, and defend claims but assume no flood risk. Insurance agents from these companies are the main point of contact for most policyholders. WYOs issue policies, collect premiums, deduct an allowance for commission and operating expenses from the premiums, and remit the balance to NFIP. In most cases, insurance companies hire subcontractors—flood insurance vendors—to conduct some or all of the day-to-day processing and management of flood insurance policies. When flood losses occur, policyholders report them to their insurance agents, who notify the WYOs. The companies review the claims and process approved claims for payment. FEMA reimburses the WYOs for the amount of the claims plus expenses for adjusting and processing the claims, using rates that FEMA establishes. As of September 2012, about 85 WYOs accounted for about 85 percent of the more than 5.5 million policies in force.[4]

[3]From 1969 through 1977, the Department of Housing and Urban Development (HUD), which administered NFIP at the time, had an agreement with a consortium of private insurers known as the National Flood Insurers Association. Under this agreement, HUD reimbursed the association for operating costs and provided an annual operating allowance equal to 5 percent of policyholders' premiums. From 1978 through 1983, a federal contractor (not an insurance company) sold and serviced policies.

[4]Although WYOs handle most flood policies, FEMA still contracts with a company that serves as the insurer of last resort when an eligible customer cannot purchase insurance from a WYO.

NFIP Remains on GAO's High-Risk List Due to Financial Instability and Other Challenges

NFIP was added to GAO's High-Risk List in 2006 due to losses from the 2005 hurricanes and the financial exposure the program created for the federal government.[5] Until 2004, NFIP was able to cover most of its claims with premiums it collected and occasional loans from the U.S. Treasury (Treasury) that it repaid. However, after the 2005 hurricanes—primarily Hurricane Katrina—the program borrowed $16.8 billion from Treasury to cover the unprecedented number of claims. In prior work we found that NFIP, as it was then structured, was not likely to generate sufficient revenues to repay this amount.[6] NFIP since has received additional borrowing authority in the amount of $9.7 billion to cover claims for Superstorm Sandy. As of July 31, 2013, the program owed Treasury approximately $24 billion.

NFIP's financial condition highlights structural weaknesses in program funding—primarily its rate structure. By design, NFIP does not operate for profit. Instead, the program must meet a public policy goal—to provide flood insurance in flood-prone areas to property owners who otherwise would not be able to obtain it. NFIP generally is expected to cover its claim payments and operating expenses with the premiums it collects. However, subsidized policies have been a financial burden on the program because of their relatively high losses and premium rates that are not actuarially based. As discussed previously, subsidized policies are associated with structures more prone to flood damage (either because of the way they were built or their location). As a result, the annual amount that NFIP collects in both full-risk and subsidized premiums is generally not enough to cover its operating costs, claim payments, and principal and interest payments to Treasury, especially in years of catastrophic flooding. This arrangement results in much of the financial risk of flooding being transferred to the federal government and ultimately the taxpayer.

The Biggert-Waters Flood Insurance Reform Act of 2012 (Biggert-Waters Act) addressed some of the structural challenges that have contributed to the program's financial instability.[7] For example, new flood insurance policies will not receive subsidized premium rates, subsidies on existing

[5]GAO, *GAO's High-Risk Program*, GAO-06-497T (Washington, D.C.: Mar. 15, 2006).

[6]GAO-13-283.

[7]Biggert-Waters Flood Insurance Reform Act of 2012, Pub. L. No. 112-141, 126 Stat. 405, 916 (2012).

policies for many other properties will be phased out, and policies for properties that are remapped to a higher risk level will be subject to higher premium rates. In addition the Biggert-Waters Act requires FEMA to implement other changes to its rate-setting process, including building a reserve fund and updating maps used to set rates to reflect relevant information on topography, long-term erosion of shorelines, future changes in sea levels, and the intensity of hurricanes.[8] While these changes may help increase NFIP's long-term financial stability, the program still faces challenges in implementing the changes and their ultimate effect is not yet known.

Furthermore, weaknesses in NFIP management and operations, including financial reporting processes and internal controls, strategic and human capital planning, and oversight of contractors, also have placed the program at risk. For example, in 2011 we found that FEMA had not developed goals, objectives, or performance measures for NFIP. In addition, FEMA faces challenges modernizing NFIP's insurance policy and claims management system. As a result, we made recommendations to improve the effectiveness of FEMA's planning and oversight efforts for NFIP; improve FEMA's policies and procedures for achieving NFIP's goals; and increase the usefulness and reliability of NFIP's flood insurance policy and claims processing system. While FEMA agreed with our recommendations and has taken some steps to address them, continued attention to these issues is vital and additional steps are needed to address the concerns we have identified in the past.[9]

Change to Subsidized Policies and Implications of Additional Program Changes

The Biggert-Waters Act mandates that GAO conduct a number of studies related to actual and potential changes to NFIP, including analyses of remaining subsidized properties, and the effect of increasing coverage limits or adding coverage options. In one of our studies responding to these mandates, of remaining subsidized properties, we estimated that with the changes in the Biggert-Waters Act approximately 438,000 policies are no longer eligible for subsidies, including about 345,000 nonprimary residential policies, about 87,000 business policies, and about

[8]Pub. L. No. 112-141, §§ 100212, 100216, 126 Stat. 405,922,927 (2012).

[9]GAO, *FEMA: Action Needed to Improve Administration of the National Flood Insurance Program*, GAO-11-297 (Washington, D.C.: June 9, 2011).

9,000 single-family, severe-repetitive-loss policies.[10] Subsidies on most of the approximately 715,000 remaining subsidized policies are expected to be eliminated over time. Under the act, most remaining subsidized policies no longer would be eligible for subsidies if NFIP coverage lapsed or the properties were sold or substantially damaged. We estimated that with implementation of the provisions addressing sales and coverage lapses, the number of subsidized policies could decline by almost 14 percent per year. At that rate, the number of subsidized policies would be reduced by 50 percent in approximately 5 years. After about 14 years, fewer than 100,000 subsidized policies would remain. However, the actual outcomes and time required for subsidies to be reduced could vary depending on the behavior of policyholders and the actual rate of sales and coverage lapses. In terms of characteristics, we found that the geographic distribution of remaining subsidized policies was similar to the distribution of all NFIP policies. Other characteristics we analyzed—indicators of home value and owner income—were different for the policies that continue to be eligible for subsidized premium rates compared to those with full-risk rates. In particular, counties with higher home values and income levels tended to have larger percentages of remaining subsidized policies than policies with full-risk rates.

In our July 2013 report on subsidized policies, we identified three broad options that could help address the financial impact of remaining subsidized policies on the program, but the advantages and disadvantages of each would need to be considered and action would be required from both Congress and FEMA. These options are not mutually exclusive and may be used together to reduce the financial impact of subsidized policies on NFIP. The way in which an option is implemented (such as more aggressively or gradually) also can produce different effects in terms of policy goals and thus change the advantages and disadvantages.

- *Adjust the pace of eliminating subsidies.* Accelerating the elimination of subsidies could improve NFIP's financial stability by more quickly increasing the number of policies with premium rates that more accurately reflect the full risk of flooding, but could exacerbate the difficulty some policyholders may have in adjusting to new rates. In contrast, delaying the elimination of subsidized policies or lengthening

[10] GAO-13-607.

the phase-in period would continue to expose the federal government to increased financial risk over a longer time. Moreover, delaying the elimination of subsidies would not represent a long-term fix for those policyholders who could not afford the new premium rates, whenever they came into effect.

- *Target assistance for remaining subsidies*. Assistance or a subsidy could be based on the financial need of the property owners, which could help ensure that only those policyholders needing the subsidy would have access to it and retain their coverage, with the rest paying full-risk rates. Targeting subsidies based on need—through a means test, for example—is an approach other federal programs use. However, NFIP does not currently collect the policyholder data required to assess need and determine eligibility and it could be difficult for FEMA to develop and administer such an assistance program in the midst of ongoing management challenges. Moreover, unlike other agencies that provide—and are allocated funds for—traditional subsidies, NFIP does not receive an appropriation to pay for shortfalls in collected premiums caused by its subsidized rates. One approach to maintain subsidies but improve NFIP's financial stability would be to rate all policies at the full-risk rate and appropriate subsidies for eligible policyholders.
- *Expand mitigation efforts such as elevation, relocation, and demolition of properties*. This would include making mitigation mandatory to ensure that more homes were better protected. Mitigation efforts could be used to help reduce or eliminate the long-term risk of flood damage; especially if FEMA targeted the properties that were most costly to the program, such as those with repetitive losses. However, mitigation is expensive for NFIP, taxpayers, and communities.

In our October 2008 study of NFIP's rate-setting, we found that the losses generated by NFIP have created substantial financial exposure for the federal government and U.S. taxpayers—due in part to the program's rate-setting process.[11] We also found that FEMA's rate-setting methods, even for full-risk rates, do not result in rates that accurately reflect flood risks. For example, FEMA's rate-setting process does not fully take into account ongoing and planned development, long-term trends in erosion, or the effects of global climate change.[12] Furthermore, FEMA sets rates

[11] GAO-09-12.

[12] The Biggert-Waters Act requires FEMA to include, among other things, relevant information on topography, coastal erosion areas, changing lake levels, future changes in sea levels, and intensity of hurricanes.

on a nationwide basis, combining and averaging many topographic factors that are relevant to flood risks, and does not specifically account for these factors when setting rates for individual properties.

Partly because of the rate-setting issues, in our July 2013 report on raising coverage limits or adding optional coverage types, we found that the advantages and disadvantages to making more changes to the program, such as these, would need to be carefully weighed.[13] To determine the financial impact on NFIP of increasing coverage limits, we estimated the potential financial effect on NFIP if coverage limits had been raised in 2002–2011. Higher coverage limits would have been associated with increased net revenue in all fiscal years from 2002 through 2011, except for fiscal years 2004 and 2005 when the program experienced catastrophic losses. The overall results were the same when we conducted the analyses using variations in our assumptions to (1) decrease the premiums by 20 percent below the baseline estimate; (2) decrease the claims by 20 percent below the baseline estimate; and (3) estimate that only 25 percent, 50 percent, or 75 percent of all policyholders increased their coverage. Overall, the financial impact on the program of raising coverage limits would depend on the adequacy of the rates charged for the additional coverage. We also found that adding business interruption coverage to NFIP could be particularly challenging. For example, properly pricing risk, underwriting, and claim processing can be complex. Similarly, offering optional coverage for additional living expenses would have many of the same potential effects on NFIP, although this coverage generally is less complex to administer.

Additional Challenges for FEMA to Address

In July 2013, we reported that FEMA will require several years to fully implement the Biggert-Waters Act and FEMA officials acknowledged that they have data limitations and other challenges to resolve before eliminating some subsidies as required in the act. The following points highlight some of the challenges we identified:

- The act eliminated subsidies for residential policies that covered nonprimary residences and business policies. FEMA has data on whether a policy covers a primary residence, but officials stated that the data may be outdated or incorrect. In addition, FEMA categorizes

[13] GAO-13-568.

policies as residential and nonresidential rather than residential and business. As a result, FEMA does not have the information to identify nonresidential properties such as schools or churches that are not businesses and continue to be eligible for a subsidy. Beginning in October 2013, FEMA will require applicants for new policies and renewals to provide property status (residential or business).

- The act states that subsidies will be eliminated for policies that have received cumulative payment amounts for flood-related damage that equaled or exceeded the fair market value of the properties, and for policies that experience damage exceeding 50 percent of the fair market value of properties after enactment. Currently, FEMA is unable to make this determination as it does not maintain data on the fair market value of properties insured by subsidized policies. FEMA officials said that they have been in the process of identifying a data source.
- The act eliminates subsidies for severe repetitive loss policies and provides a definition of severe repetitive loss for single-family homes. However, it requires FEMA to define severe repetitive loss for multifamily properties and FEMA has not yet developed this definition.

The act also requires FEMA to phase in full-risk rates on active policies that no longer are eligible for subsidies, but we found that FEMA generally lacks information needed to establish full-risk rates that reflect flood risk for the properties involved and also lacks a plan for proactively obtaining such information. Federal internal control standards state that agencies should identify and analyze risks associated with achieving program objectives, and use this information as a basis for developing a plan for mitigating the risks. In addition, these standards state that agencies should identify and obtain relevant and needed data to be able to meet program goals. However, in July 2013 we reported that FEMA does not have key information used in determining full-risk rates from all policyholders. According to FEMA officials, not all policyholders have elevation certificates, which document their property's risk of flooding. Information about elevation is a key element in establishing premium rates on certain properties. Elevation certificates are required for some properties, but optional for others. According to FEMA officials, consistent with the act they are phasing in rate increases (of 25 percent per year) for policyholders who no longer are eligible for subsidies. The increase will continue until the rates reach a specific level or until policyholders supply an elevation certificate that indicates the property's risk, allowing FEMA to determine the full-risk rate.

Although subsidized policies have been identified as a risk to the program because of the financial drain they represent, FEMA does not have a plan to expeditiously and proactively obtain the information needed to set full-risk rates for all of them. Instead, FEMA will rely on certain policyholders to voluntarily obtain elevation certificates, which can be expensive for the property owner. Those at lower risk levels have an incentive to do so because they may then be eligible for lower rates. However, policyholders may not know their risk level, and policyholders with higher risk levels have a disincentive to voluntarily obtain an elevation certificate because they then could pay a higher premium. In our July 2013 report, we concluded that without a plan to expeditiously obtain property-level elevation information, FEMA will continue to lack basic information needed to accurately determine flood risk and continue to base full-risk rate increases for previously subsidized policies on limited estimates. As a result, FEMA's phased-in rates for previously subsidized policies still may not reflect a property's full risk of flooding; with some policyholders paying premiums that are below and others paying premiums that exceed full-risk rates. We recommended that FEMA develop and implement a plan, including a timeline, to obtain needed elevation information as soon as practicable.[14] FEMA agreed with this recommendation and plans to evaluate the appropriate approach to obtain or require the submittal of this information.

The Biggert-Waters Act also requires a number of other changes that the agency has been starting to implement. For example FEMA must adjust rates to accurately reflect the current risk of flood to properties when an area's flood map is changed, subject to any other statutory provision in chapter 50 of Title 42 of the Unites States Code.[15] As we reported in July 2013, FEMA has been determining how this provision would affect properties exempted from rate increases when they were remapped.[16] The act also requires FEMA to develop a plan for repaying the current debt owed to Treasury and establish a catastrophic loss reserve fund. FEMA officials told us that Superstorm Sandy delayed development of the repayment plan, but they are scheduled to submit a plan to Congress on September 30, 2013. They also noted that they planned to create a reserve fund by increasing each premium by a certain percentage (as the

[14] GAO-13-607.

[15] 42 U.S.C. § 4015(e).

[16] Pub. L. No. 112-141, § 100205, 126 Stat. 405, 919 (2012).

agency deems appropriate) over a number of years beginning October 1, 2013.[17]

We continue to monitor the status of FEMA's actions related to recommendations we have made in prior reports. In 2008, we recommended that FEMA develop a rate-setting methodology that uses data that results in full-risk premiums that accurately reflect the risk of losses from flooding.[18] Data used to develop rates should take into account the effects of long-term planned and ongoing development, including climate change. In response to our continued support of this recommendation as well as requirements in the Biggert-Waters Act, FEMA officials stated that they have made progress. For example, FEMA stated they already have revised damage calculations for flooding events that only reach the foundation of the structure, and performed a study to assess the long-term impacts of climate change. FEMA's ongoing efforts include analyzing water-depth probability curves for the various zones and piloting studies to determine structure elevation and flood depths for various return periods.

In 2009, we also recommended that FEMA consider the actual flood-related expenses and profits of WYOs when setting payment rates, while also taking other actions to ensure the accuracy of this financial information.[19] Consistent with our recommendations, the Biggert-Waters Act requires FEMA to develop a methodology for determining the appropriate amounts that property and casualty insurance companies participating in the WYO program should be reimbursed for selling, writing, and servicing flood insurance policies and adjusting flood insurance claims.[20] The act also requires that FEMA publish a rule revising expense reimbursements and that such reimbursements be structured to track actual flood-related expenses "as closely as practically possible." FEMA officials told us that the agency has begun to obtain actual flood-related financial information and has been working with the

[17]Effective on or after October 1, 2013, a reserve fund ratio of 5 percent of the total premium will be applied to each NFIP policy, with certain exceptions.

[18]GAO-09-12.

[19]GAO, *Flood Insurance: Opportunities Exist to Improve Oversight of the WYO Program*, GAO-09-455 (Washington, D.C.: Aug. 21, 2009).

[20]Pub. L. No. 112-141, § 100224, 126 Stat. 405,936 (2012).

National Association of Insurance Commissioners (NAIC) and conducting other analyses to ensure that WYOs accurately report this information. However, FEMA officials stated that the agency cannot take action that completely addresses our recommendations until the WYOs reliably report to NAIC and that it might take several years before all companies consistently report such information. The agency also has been considering how to best introduce the WYOs' actual flood-related expenses into payment formulas over the next several years, when FEMA expects to have more reliable financial information and less variation in reported expense ratios.

In 2011, we recommended that FEMA improve strategic planning, performance management, and program oversight within and related to NFIP.[21] FEMA agreed with our recommendations and has addressed some of them, such as strategic planning, but it still needs to continue to address the management and operational weaknesses we identified, including human capital planning, acquisition management, policy and claims management systems, financial management, collaboration, and records management. Unless these management issues are addressed, FEMA risks ongoing challenges in effectively and efficiently managing NFIP, including its management and use of data and technology.

In conclusion, when we placed NFIP on the high-risk list in 2006, we noted that comprehensive reform likely would be needed to address the financial challenges facing the program. Since passage of the Biggert-Waters Act, FEMA is taking some important first steps toward implementing the reforms the act requires, but the extent to which the changes included in the act and FEMA's implementation will reduce the financial exposure created by the program is not clear and the program's long-term financial condition is not yet assured. In addition, our previous work has identified many of the necessary actions that FEMA should take to address a number of ongoing challenges in managing and administering the program. Getting NFIP on a sound footing, both financially and operationally, is important to achieving its goals and at the same time reducing its burden on the taxpayer.

[21] GAO-11-297.

Chairman Merkley, Ranking Member Heller, and Members of the Subcommittee, this concludes my prepared statement. I would be happy to answer any questions that you may have at this time.

Contact and Staff Acknowledgments

If you or your staff have any questions about this testimony, please contact me at (202) 512-8678 or cackleya@gao.gov. Contact points for our Offices of Congressional Relations and Public Affairs may be found on the last page of this statement. Other staff who made key contributions to this testimony include Jill Naamane and Patrick Ward (Assistant Directors); Isidro Gomez; Karen Jarzynka-Hernandez; Barbara Roesmann; Rhonda Rose; and Jessica Sandler.

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PREPARED STATEMENT OF CHRISTINE SHIRLEY

NATIONAL FLOOD INSURANCE PROGRAM COORDINATOR, PLANNING SERVICES DIVISION, OREGON DEPARTMENT OF LAND CONSERVATION AND DEVELOPMENT

SEPTEMBER 18, 2013

Good morning Chairman Johnson, Ranking Member Crapo, and Members of the Committee. I am Christine Shirley, National Flood Insurance Program Coordinator for the State of Oregon. I am pleased to offer testimony on behalf of Oregon's 34,700 NFIP policyholders, and the estimated additional 150,000 buildings owners in Oregon who do not have flood insurance, but probably should because their buildings are located in the Special Flood Hazard Area.

Since April 2, 2013, soon after the National Flood Insurance Program (NFIP) announced implementation of section 100205 of the Biggert-Waters Flood Insurance Act of 2012 (Reform Act), we have made over two dozen presentations to land use planners, real estate agents, surveyors, and the public about NFIP premium rate and rule changes brought about by the Reform Act. I am here today to give you a field report. I will touch on outreach, affordability and mitigation. Let me say right away fear and confusion about the reforms are prevalent among professionals and the public alike. I will speak more about that later. First I want to explain a little about how Oregon implements the National Flood Insurance Program.

The NFIP Supports Oregon's Planning Principles and Goals

The Department of Land Conservation and Development (DLCD), the State's land use planning agency, is also Oregon's NFIP coordinating agency. DLCD's guiding principles are to:

- Provide a healthy environment;
- Sustain a prosperous economy;
- Ensure a desirable quality of life; and
- Provide fairness and equity to all Oregonians.

Since the mid 1970s the National Flood Insurance Program has played an important role in support of these principles. For those unfamiliar Oregon's statewide land use planning program, it originated in 1973 to provide protection of farm and forest lands, conservation of natural resources, orderly and efficient development, coordination among local governments, and citizen involvement. This is accomplished by requiring city and county governments to adopt comprehensive plans that address each of 19 statewide planning goals. Goal 7 directs counties and cities to adopt comprehensive plans that reduce risk to people and property from natural hazards. Participation in the NFIP satisfies Goal 7's requirement to address flood hazards. As a result, virtually all of Oregon's residents have access to NFIP flood insurance (only 2 very small cities newly mapped and with minimal flood risk have yet to participate in the NFIP).

Development of Accurate Flood Insurance Rate Maps Requires Sufficient Funding

The NFIP's Flood Insurance Rate Maps (FIRMs) provide the basis for Oregon cities and counties to identify and manager development in flood prone areas. By and large, over the years, we have found the FIRMs to reasonably depict where flooding is most likely to occur. We are confident that refined modeling, cartographic, and analysis techniques implemented through the RiskMAP program, and by Oregon's own Department of Geology and Mineral Industries as a Cooperating Technical Partner with FEMA, will result in even more accurate and informative FIRMs and derivative risk analysis products.

Such map accuracy requires sufficient funding. Appropriations for mapping have been reduced by more than half from the 2010 level of $220 million. The Administration's budget request for FY2014 was $84 million. The Homeland Security Appropriations bills (one passed by the House; the other reported out of committee in the Senate) both provide $95 million. While this reflects Congressional recognition of the importance of accurate flood maps, it is, nevertheless, still a major reduction. We urge Congress to increase appropriations for flood mapping back to 2010 levels as soon as possible.

Poor Risk Communication and Outreach Undermines Trust

Our problem is not so much with the quality of FIRMs, but rather with risk communication. Many people who reside in Special Flood Hazard Areas have never experienced flooding at their location and they simply don't believe it's possible, so they question the veracity of the FIRMs. Sometimes they're right. DLCD regularly counsels landowners on how to use FEMA's Letter of Map Change process to refine Special Flood Hazard Area boundaries on their properties.

One year after enactment of the Reform Act of 2012 our risk communication challenge has increased, not only because of changes brought about by the Act, but also by how the NFIP has explained and implemented section 100205: Reform of Premium Rate Structure. It appears to us that NFIP intends to rely on flood insurance agents to disseminate information about changes brought about by the Reform Act. We find this communication model flawed for several reasons:

- Training for NFIP Write-Your-Own flood insurance agents is woefully inadequate;
- Too many Oregonians with buildings located in Special Flood Hazard Areas are not insured by the NFIP and therefore lack a means to obtain information about the consequences of the Reform Act;
- Important professional groups, particularly surveyors and real estate agents, have not been informed by the NFIP of impending changes;
- Likewise, local Government officials and staff have not been provided with digestible and sufficient information to address their citizens' concerns or assess their own vulnerabilities;
- NFIP has not provided information to the public that allows building owners to make informed decisions about their individual situations.

As a result, building owners and the general public are receiving contradictory and confusing information, which has had the effect of undermining the credibility of the NFIP. This unfortunate side effect has made it even more difficult for NFIP Coordinators like myself to communicate the benefits of carrying flood insurance. Let me address each of these bullet points in turn:

NFIP Agent Training

Training for agents that sell NFIP flood insurance is woefully inadequate. Many agents are not able to explain to their customers how the NFIP works and most are not able to advise clients on how to reduce flood insurance premiums by making simple building modifications.

NFIP sponsored exactly one instructor-led flood insurance agent training in Oregon in 2013. Unfortunately I heard from insurance agents who attended the class that this general training did not address Reform Act section 100205 changes in sufficient detail to allow them to effectively advise clients on its consequences.

Outreach about availability of instructor-led classes and webinars also is lacking. DLCD learned just days before that the above mentioned training was about to be canceled due to lack of participation. Fortunately, we convinced our Insurance Division to announce the class to their mailing list, filling the class. Likewise, H2O Partners, NFIP's flood insurance training contractor, has offered webinars that cover section 100205 changes but these have not attracted enough agent participation in Oregon.

NFIP must be provided with sufficient resources to develop a comprehensive outreach and training program; one that does not passively rely on Web sites to notify Write-Your-Own agents of training opportunities. More training opportunities must be provided because well trained agents bolster the credibility of the NFIP.

Reliance on Agents To Inform Their Clients

It is an unfortunate truth that flood insurance take-up rates in Oregon, and nationwide, are too low. Relying on insurance agents to get the word out about changes brought about by the Reform Act ignores a large segment of the affected population. NFIP needs to develop public service announcements and printed material suitable for wide distribution to traditional and nontraditional media outlets.

Outreach to Surveyors, Real Estate Agents, and Other Professionals

Real estate agents and surveyors are on the front line of implementing Reform Act changes. These professionals speak directly with building owners, often before an insurance agent does. DLCD has found these professionals to be interested and receptive to information about the Reform Act. So much so that our technical support to NFIP communities has suffered as a result of numerous requests to speak at their professional gatherings. Word of mouth has kept us busy since April 2, 2013, during which time we have addressed 15 real estate associations and 3 surveyor chapter meetings. We have started coordinating with statewide professional organizations to take over this training function so that we can get back to our regular NFIP job duties. NFIP needs to reach out to professional groups with literature suitable for distribution to their clients as well as with training materials and opportunities.

Outreach to Government Officials and Staff

While it might not be obvious why Government officials and staff need to know about flood insurance reform, in fact, because they manage floodplain development per the NFIP, they are often the first people building owners call to explain why flood insurance costs are increasing and what can be done to reduce them. In addition, any loss of property values brought about by the Reform Act will be felt directly via decreased property tax revenue, and even increased foreclosure rates. Oregon's assessors offices have expressed interest in learning more about the NFIP reforms, as have city and county land use and planning offices. NFIP Coordinators are the best conduit to local government, however, we have had to spend an inordinate amount of time deciphering the Write-Your-Own Bulletins intended for insurance agents to explain the consequences of the Reform Act to local government. While these Bulletins are the most reliable source of information they are also full of jargon. Read out of context they can be confusing and misleading. NFIP needs to develop easy to understand educational material specifically targeted to local government officials and staff.

Public Outreach

Much of the specific material NFIP has prepared for the public about consequences of the Reform Act has been directed to those affected by Superstorm Sandy. This and other material produced by NFIP has taken a worst-case-scenario approach to explaining the consequences of not elevating flood-damaged buildings. For example, in a widely circulated fact sheet NFIP estimated future flood insurance costs using the maximum amount of building plus contents insurance available for residential structures, even though most building owners will not purchase this much insurance. We find this material to be unnecessarily alarming. People stop reading as soon as they see that flood insurance costs could exceed $10,000 per year. Until recently, with public release of NFIP's Specific Rating Guidelines on September 5, it was virtually impossible for even an experienced flood insurance agent to provide more realistic information about potential flood insurance costs under the Reform Act when a building owner's lowest floor was 2 or more feet below base flood elevation. We applaud release of these Guidelines as this information will help us develop realistic cost ranges for the types of flood risks and building values typical for Oregon. The Guidelines also help us better understand what drives costs up and what building owners might do to reduce these costs. DLCD understands how difficult it is to present information about costs in the absence of specific information about a building's characteristics and how easy it is to create false expectations. Nonetheless, we recommend that NFIP develop public outreach material that more accurately reflects the range of costs typical of certain classes of buildings—or at least work with States to help us develop such material tailored to our demographics and building values.

Flood Resilient Oregon

Problems with the Reform Act go beyond those associated with education and outreach. The Reform Act does not sufficiently address affordability or mitigation of flood risk. We fear that, together, these deficiencies will cause Oregon to be less resilient to flooding than before the Reform Act was passed.

Oregon is committed to being a flood resilient State; a strong National Flood Insurance Program helps us achieve our resiliency goal because insured residents don't require Federal disaster declarations to begin recovery. Even in the event of a Federally declared disaster, we've learned that well insured communities recover faster. As such we support efforts to move the NFIP to sound financial footing. We are concerned, however, that the rate increases required by section 100205 will not help Oregon become more flood resilient unless they are accompanied by programs to assist low- and moderate-income families afford adequate coverage and more attention is paid to mitigation.

New Construction in the Special Flood Hazard Area Does Not Support Resiliency

Oregon's mitigation strategy emphasizes acquisition. Acquired buildings are demolished and the land maintained as permanent open space, eliminating the potential for future flood damage and displaced families. It is discouraging to find a couple years later a new building being constructed in the Special Flood Hazard Area only a few hundred feet away from an acquired property. We urge Congress to pass legislation that limits the availability of flood insurance to existing buildings. NFIP flood insurance should not be offered to new development in the Special Flood Hazard Area.

Unaffordable Flood Insurance Does Not Support Resiliency

Architects of the Reform Act picked what looked like low-hanging fruit—phasing out and removing subsidies to increase revenue on a class of properties that suffer disproportionate losses. This strategy alone may not result in anticipated revenue growth because phasing out subsidies for pre-FIRM buildings could actually discourage purchase of NFIP flood insurance. We've already had inquiries from buyers about where to buy private insurance. At least one jurisdiction in Oregon is contemplating offering a private community-based flood insurance program.

Furthermore, in some areas of Oregon, those characterized by a high concentration of older buildings located in the Special Flood Hazard Area, the resale real estate market is frozen. Buildings are not selling until asking prices are dramatically lowered, attracting all-cash buyers who purchase flood prone property at fire-sale prices and then don't purchase flood insurance. Sadly, not all of these cash buyers have the resources to self-insure against potential losses, leaving Oregon less flood resilient.

Affordability is not only a problem for approximately 2,500 insured nonprimary residences, commercial buildings, and severe repetitive loss buildings in Oregon. Nor is it only an issue at the approximate 5,700 insured pre-FIRM buildings expected to be sold in the near future. An estimated 35,000 pre-FIRM buildings in Oregon located in the Special Flood Hazard Area do not carry NFIP flood insurance. Owners of these buildings are already receiving notices from their lenders demanding that they purchase flood insurance within 45 days at full risk rates. Elevation Certificates also are needed from licensed surveyors at a cost of $500 to $1,000 each to properly rate the flood insurance policy. Many of these pre-FIRM buildings' lowest floors will be below base flood elevation resulting in expensive flood insurance. These unexpected costs have the potential to force families from their homes and businesses to close. This scenario is the result of the Reform Act's increased penalties for lender noncompliance with mandatory purchase requirements, but without sufficient attention paid to the consequences of unaffordability.

As these examples illustrate, the complex issues surrounding affordability were not taken into account by the Reform Act. Section 100236 only requires a study on affordability. We urge the NFIP and National Academy of Sciences to complete the affordability study mandated by the Reform Act as quickly as possible. In the meantime we urge Congress and the NFIP to consider implementation of a temporary means-tested voucher program for low- and moderate-income households such as that described in the recent Wharton School, University of Pennsylvania report "Addressing Affordability in the National Flood Insurance Program: Means-Tested Vouchers Coupled with Mitigation Loans". Congress also should consider acting on House passed bill providing for study of the feasibility of community based group flood insurance policies (H.R. 1135).

Mitigation Reduces Flood Losses and Increases Resiliency

As important as affordability is, the ability to purchase flood insurance does not reduce flood losses. An insurance settlement to repair flood damage only ensures future losses. NFIP and FEMA must focus attention on mitigation.

Oregon's experience suggests that it takes too long and consumes inordinate staff time to complete mitigation projects using FEMA grant programs. We recognize that this is not exclusively an NFIP issue, however, NFIP needs to think creatively about how to encourage mitigation before floods occur. For example: NFIP could encourage building owner to undertake building elevation projects on their own by refunding premiums back 5 years upon completion of the project. Without such incentives it could be difficult for building owners to both pay for flood insurance and mitigation. Loan or grant programs to provide up-front costs could be provided to low- and moderate-income families in lieu of premium refunds. NFIP would benefit by reducing risk exposure.

Flood mitigation grants offered by the NFIP have traditionally focused on 100 percent solutions: elevate the lowest floor above the base flood elevation, or acquire and demolish flood-damaged buildings. Oregon has completed hundreds of such projects over the years. They work, but elevations and acquisitions are expensive, time consuming, and are difficult for States and local government to administer. We can only accomplish a handful of such projects each year.

NFIP should promote innovations such as partial mitigation. Flood vent retrofits, moving utilities out of basements, or filling below grade crawlspaces can save the insured hundreds if not thousands of dollars per year and also reduce NFIP risk exposure. Oregon has calculated that partial mitigation is cost effective for many pre-FIRM buildings, even if these mitigation projects do not result in the lowest floor being elevated above the base flood elevation. Partial mitigation is inexpensive and is cost effective even if a building is fully mitigated later on. NFIP should develop a means-tested grant program to facilitate such partial mitigations, perhaps tied to a voucher program that assists with annual flood insurance costs.

Unfair Renewals at Full-Risk Rates on Policies Purchased Between July 6, 2012, and September 30, 2013

It's bad enough not being able to sell a building because of buyer's fear of high flood insurance costs. What's worse is having purchased a pre-FIRM building between the time the Reform Act was signed on July 6, 2012, and when new rates go into effect on October 1, 2013. According to NFIP Write-Your-Own Bulletin W-13016, published March 29, 2013, purchasers of pre-FIRM buildings located in the Special Flood Hazard Area were able to buy (and will continue to be able to buy until October 1) subsidized flood insurance policies, *but these will renew at full risk rates,* with premium increases amounting to possibly thousands of dollars per year. This implementation strategy denied those who purchased pre-FIRM buildings in the Special Flood Hazard Area between July 6, 2012, and March 29, 2013, any ability to make an informed decision about the long-term financial consequences of their purchase. No party in the deal could have known that these subsidized policies would renew at possibly very expensive full-risk rates. Even those who purchased pre-FIRM buildings after publication of NFIP's March 29, 2013, Bulletin can make the case that they were denied the ability to make an informed decision because of the NFIP's limited outreach to insurance agents and real estate professionals.

DLCD has already received tearful phone calls from buyers who purchase pre-FIRM buildings last summer and are now facing unaffordable flood insurance renewal costs. The Palmer family in Eugene summed it up like this, "It's one thing to buy a home knowing what you are in for. It's another to have an act of god cause a change that no one could have anticipated. But it's simply wrong to change the terms of an insurance contract at renewal in a manner that could force us out of our home when no flood event has taken place." We are generally not in favor of delaying implementation of section 100205 the Reform Act, except for on renewals of new policies purchased as a result of a real estate transaction made on or after July 6, 2012, and before October 1, 2013. These policyholders should, as a matter of fairness, be allowed to keep their subsidy unless and until they suffer a flood loss.

Aggrieved NFIP Customers Lack a Venue To Resolve Problems

NFIP policyholders with rating issues have limited access to a dispute resolution process. Although each FEMA regional office has an insurance specialist on staff, this person is not easily accessible to the insured. We urge NFIP to establish a visible ombudsman office to field rating disputes. Congress should fund FEMA to create such an office if NFIP lacks the authority or resources.

Thank you for this opportunity testify.

PREPARED STATEMENT OF STEVE ELLIS

VICE PRESIDENT, TAXPAYERS FOR COMMON SENSE

SEPTEMBER 18, 2013

Good afternoon, Chairman Merkley, Ranking Member Heller, Members of the Subcommittee. I am Steve Ellis, Vice President of Taxpayers for Common Sense, a national nonpartisan budget watchdog. Thank you for inviting me here today to testify on the National Flood Insurance Program (NFIP).

Taxpayers for Common Sense has advocated for reform of the National Flood Insurance Program since our inception 18 years ago. The need to remove the subsidies, shift toward risk-based rates, and develop a reserve fund became even clearer after the devastating hurricane season of 2005 left the program nearly $18 billion in debt to the taxpayer. The point became moot after Superstorm Sandy upped the debt load to roughly $25 billion and counting.

Taxpayers for Common Sense appreciates the hard work done by this Committee to pass the flood insurance reform bill last summer. While we would have argued for even stiffer medicine, the bill represented a good step forward to make the program more responsible for all Americans. It is important that the reforms proceed as enacted and that any efforts to deal with affordability and map modernization be supplemental and not impede the effort to put the flood insurance program on sounder financial footing. There is an increasing fatigue with the cost of the program among taxpayers.

TCS is allied with SmarterSafer.org, a coalition in favor of promoting public safety through fiscally sound, environmentally responsible approaches to natural catastrophe policy. The groups involved represent a broad set of interests, from free market and taxpayer groups to environmental and insurance industry groups.[1] The depth and breadth of the coalition underscores the importance of making NFIP responsible.

Unintended Consequences

It is important to understand how we came to this place: a Federal flood insurance program of 5.5 million policies that takes in $3.6 billion in premiums and owes the Treasury roughly $25 billion.

After years of ad hoc disaster aid being meted out by Congress, the National Flood Insurance Program was established in 1968 to create "a reasonable method of sharing the risk of flood losses through a program of flood insurance which can complement and encourage preventative and protective measures."[2] The program was to make up for a perceived lack of available private flood insurance. But even at the time Congress was warned that it was playing with fire. The Presidential Task Force on Federal Flood Control Policy wrote in 1966:

> A flood insurance program is a tool that should be used expertly or not at all. Correctly applied it could promote wise use of flood plains. Incorrectly applied, it could exacerbate the whole problem of flood losses. For the Federal Government to subsidize low premium disaster insurance or provide insurance in which premiums are not proportionate to risk would be to invite economic waste of great magnitude.[3]

Well, we know which way that story unfolded. Although subsidies were largely envisioned to be limited and short-term, they weren't. And while the program has encouraged standards and construction that help reduce flood risks for participating communities, the availability of taxpayer-subsidized Federal flood insurance over the last several decades made it financially attractive to develop in high risk areas. Along with other factors, NFIP helped fuel the coastal development boom that increased the program's risk exposure and losses.

To foster increased participation, the NFIP did not charge truly actuarially sound rates, or increase rates based on previous loss experience. The program's goal of fiscal solvency is defined as charging premiums that will generate enough revenue to cover a historical average loss year.[4] FEMA's average largely discounted catastrophic loss years in the equation, something a private insurer would have to take into account. The program covers any fiscal shortfalls by borrowing from the U.S. Treasury, which is a significant subsidy in itself, especially since the loans are virtually interest-free.

NFIP's fiscal solvency was further challenged because properties that pre-date a community's involvement in the NFIP or the applicable flood insurance rate map (whichever is later) charitably enjoyed significantly subsidized rates, paying only 35–45 percent of their actual full-risk level premium, depending on certain assumptions.[5] While the initial thought may be that because of their vulnerability these pre-FIRM (Flood Insurance Rate Map) properties would diminish over time, the Government Accountability Office estimates that 1,153,193 subsidized policies remain.[6] In 2011, FEMA put the percentage of properties in the NFIP that were receiving explicitly subsidized rates at more than 20 percent.[7]

Furthermore, properties that experienced repetitive losses have made up a demonstrable and disproportionate amount of the program costs. A repetitive loss property is one that has had two or more claims of $1,000 over 10 years. These properties represent only 1 percent of the total number of policies, yet account for 25 to 30 percent of the cost of claims.[8] Properties like one in Wilkinson, MS, that has flooded

[1] Full list is available at *www.smartersafer.org.*

[2] P.L. 90-448.

[3] U.S. Task Force on Federal Flood Control Policy, "A Unified National Program for Managing Flood Losses", August 1966. P. 17. Available at: *http://www.loc.gov/law/find/hearings/floods/floods89-465.pdf.*

[4] Hayes, Thomas L., and Neal, D. Andrew, "Actuarial Rate Review", Federal Emergency Management Agency. October 1, 2011. P. 5. Available at: *http://www.fema.gov/media-library-data/20130726-1809-25045-6893/actuarial__rate__review2011.pdf.*

[5] Congressional Budget Office, "Factors Affecting Actuarial Soundness", November 2009. P. 6. Available at: *http://www.cbo.gov/sites/default/files/cbofiles/ftpdocs/106xx/doc10620/11-04-floodinsurance.pdf.*

[6] Government Accountability Office, "Flood Insurance: More Information Needed on Subsidized Policies", July 2013. P. 14. Available at: *http://www.gao.gov/products/GAO-13-607.*

[7] Hayes and Neal. Supra Note 4 at 22.

[8] Statement of Orice Williams Brown, Director Financial Markets and Community Investment, Government Accountability Office before the Senate Committee on Banking, Housing, and Urban Affairs. P. 7. *http://www.gao.gov/new.items/d11670t.pdf*

34 times since 1978 and received payments worth nearly 10 times the home's $70,000 value. Or another property owner in Houston, TX, that has received $1.6 million worth of claims for a house worth $116,000.[9] We need to help these people out—out of harm's way—and at the same time help the taxpayer who is stuck with the tab.

Biggert-Waters and Beyond

The Biggert-Waters Flood Insurance Reform Act of 2012 made many significant changes to the NFIP to help it become less fiscally reckless and to better inform policyholders of their flood risk.

In Biggert-Waters, Congress helped address the long-term sustainability of the NFIP. As a consequence, several types of properties that had received pre-FIRM subsidies would have their rates increased by 25 percent a year until they met the full risk based rate. While this may be financially painful in some cases, the subsidies had served to disincentivize behavior and practices that would reduce risk and in the long-run be good for the individual and good for the country. The properties included:

- Nonprimary residences
- Severe repetitive loss property (four or more claims exceeding $5,000)
- Properties that have received flood payments that in aggregate exceed the fair market value of the property
- Business properties
- Property that since July 6, 2012, has sustained damage exceeding 50 percent of the fair market value; or had substantial improvements that exceed 30 percent of the fair market value of the property
- New or lapsed policies
- Policies where the insured refuses mitigation assistance (including relocation)

It is important to recognize that policyholders are not being denied the ability to purchase flood insurance. This provision of the law simply eliminates the subsidized rates. Furthermore, while it may sound like a lot of affected properties, because pre-FIRM primary residences that maintain coverage are not included, 62 percent of policyholders (715,259 policies) with subsidized premiums would be unaffected by these changes. In reality, the biggest shift will be that second homes and businesses that used to claim 38 percent of the subsidized policies will now represent only 1.5 percent of the total.[10]

In addition, when flood maps are updated with any changes that increase rates, all properties will be subject to the new rates that will be phased in at 20 percent a year for 5 years. This effectively ends the previous grandfathering process where some properties retained the highly subsidized premiums for decades.

Biggert-Waters also included several other reform provisions, including:

- Increased lender penalties from $350 to $2,000 per violation, for failing to enforce mandatory purchase requirements for properties in the Special Flood Hazard Areas (SFHA—the 100 year, or 1 percent chance or more, floodplain).
- Dictates that FEMA set premium rates in aggregate that would generate enough revenue to offset the true average historical loss year (not discounting catastrophic years like 2005).
- Charge premiums that would generate revenue to create a reserve fund to reduce borrowing from the Treasury. FEMA has adopted a 5 percent surcharge on all premiums to develop the fund.

Other notable provisions regarded mapping: Biggert-Waters established a Technical Mapping Advisory Council to help FEMA improve accuracy, develop standards, and make recommendations on future conditions mapping to more accurately estimate risk. FEMA must incorporate any recommendations from this Council. There is also a Scientific Resolution Panel to arbitrate community appeals of maps using technical or scientific data.

Accurate Maps Are Critical

The NFIP is driven by maps because geography ultimately determines flood risk. They determine the veritable alphabet soup of what flood zone your structure is in:

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[9] Frank, Thomas, "Huge Losses Put Federal Flood Insurance Program in the Red", *USA Today*. August 26, 2010. Available at: *http://usatoday30.usatoday.com/news/nation/2010-08-25-flood-insurance__N.htm.*

[10] Government Accountability Office. Supra Note 6 at 14.

A, V, X, or variants within each category. Your property could be in the 100-year floodplain or the 500-year floodplain; high-risk storm surge zone or special flood hazard areas. The maps are key to the program's success or failure because they define the Nation's flood risk and the policyholder responsibility. They must be up to date, accurate, and based on the best available science to be effective. This is why FEMA's map modernization program is critical to the appropriateness of Federal Government participation in the program and should not be delayed or side-tracked in any way.

The Nation's floodplains are dynamic and fundamentally risky. Not just from natural forces, but also the impacts of development, weather patterns, and topographical changes. Areas that were previously less likely to flood could now be more likely. Levees that were adequate to provide 100-year protection a decade ago may provide far less due to poor maintenance or increased flood elevations due to increased runoff or new development.

Not surprisingly, the map modernization effort has been met with some controversy. In some cases, homeowners are facing steep increases in premiums after years, even decades, of paying the same grandfathered pre-FIRM subsidized rate. While the uproar is understandable, it doesn't change the underlying circumstances or the risk or the need to manage the program responsibly. In some cases property owners that didn't have to purchase flood insurance under existing law now find themselves required to do so; others have been mapped out of the floodplain.

Help Those Who Need It

It may be politically expedient and popular locally to delay map modernization or delay rate increases. But what may make good local politics generally makes bad insurance policy—and by extension with Federal flood insurance—bad public policy. People deserve to know the cost and risks of where they live. And taxpayers deserve to have those who choose to live in harm's way pick up their share of the tab.

In communities affected by possible rate increases there have been a lot of rumors about enormous rate increases. One insurance agent in Plaquemines Parish, LA, estimated that under new maps, his flood insurance rate would go from $633 to $28,000.[11] That would certainly give anyone sticker shock, but it is hard to square that rate with what the data to justify it would mean. The median home sales price in Plaquemines Parish fluctuated in 2012 but it is roughly between $200,000 and $250,000.[12] Considering the maximum amount of flood insurance a homeowner can obtain under NFIP is $250,000 (and an additional $100,000 for contents) that would basically mean that FEMA expects this property to be a total loss every decade. If true, this individual and his property are at incredible risk, in which case delaying the rate increase sends absolutely the wrong signal. Or the possible rate increase is inflated, which seems to be the case in St. Charles Parish, where homeowners had been concerned about new $30,000 rates. However as a recent newspaper story noted, the maximum rate was down to $15,000, although the only actual instances cited in the story are of $2,000 and $7,300.[13] These rates are the result of new maps and the ending of grandfathering. The parish has indicated their interest in appealing the maps, which is their right and is an import part of the reformed program. Some technical changes may need to be made to the maps, which is something for FEMA and the Scientific Resolution Panel established by Biggert-Waters to consider. Defining the actuarially accurate rates and associated maps are critical to the long-term viability of a Federal flood insurance program. That is, the concern is not a matter of local frustration, but of the long term existence of a fiscally fragile program.

In Congress, there has been a series of efforts to delay map implementation and rate increases. In both the House and Senate reported versions of the Fiscal Year 2014 Department of Homeland Security Appropriations bills there are provisions to deny funds "to implement, carry out, administer, or enforce section 1308(h) of the National Flood Insurance Act." That section deals with premium adjustments that would result from updated maps. Depending on how it is interpreted, this provision could lead to at least a 1 year delay. Or even worse, by allowing new maps to be finalized but not allowing rates to be adjusted on the implementation dates—subsidized rates being grandfathered again until the next map update years from now.

[11] Hughes, Siobahn, "Flood Insurance Prices Surge", *Wall Street Journal.* August 12, 2013. P. A3. Available at: *http://online.wsj.com/article/SB10001424127887323446404579008922222799170.html.*

[12] *http://www.city-data.com/county/Plaquemines__Parish-LA.html*

[13] Barnett, Kyle, "FEMA Insurance Rates Not as High as Projected, But Still Unaffordable", *St. Charles Herald Guide.* September 12, 2013. Available at *http://www.heraldguide.com/details.php?id=13049.*

Conversely, this would deny any policyholder who would see their rate decrease in new maps from enjoying that rate reduction.

There is other legislation that would delay map implementation or rate increases through a variety of means.

None of these delay proposals deal with affordability or efficiency issues or recognize the very real challenges facing Government participation and continued national support for the National Flood Insurance Program. Furthermore the broad nature of the proposals means that millionaire homeowners get the same break that is being championed on the backs of those less well off. It also means that policyholders who were going to see their rates decrease with the new maps will be forced to continue to pay more. And lastly, because the total premium target, which is set by the average historical loss year, is unchanged by these individual delay proposals, every policyholder will have to pay more premium than they would otherwise to make up for continuing decades old subsidies. This is about fundamental fairness within the flood insurance program and eliminating the cross subsidies that have a few properties paying full freight while picking up the tab for properties that have enjoyed subsidized premiums for decades.

While the argument to derail reforms centers on the issue of affordability, the data reveals the flood insurance program subsidies substantially benefit the well off. A GAO analysis found that the NFIP program is particularly generous to those in the top deciles of median household income and home value. The GAO reviewed the distribution of subsidized premiums by median home value and median income. It targeted 351 counties[14] that represented more than 70 percent of the remaining subsidized policies and 41 percent of total primary residence policies.

Its analysis found that more than a quarter of the remaining subsidized policies were in counties in the top decile for both median home value and median home income. Only 7 percent of the nonsubsidized policies were in those same counties. Furthermore, 43 percent of subsidized policies were in counties in the top decile of median home value and 69 percent were in the top two deciles. Overall, 76 percent of the subsidized and nonsubsidized policies were in counties in the top two deciles. The counties in the bottom two deciles had 0.4 percent of the subsidized policies and 0.2 percent of the total policies.

A Responsible Approach

A critical role of a Federal flood insurance program is to inform people of their flood risk so they can take steps to financially protect their own investments. Rates provide an important price signal of risk.

If Congress wants to deal with the issue of affordability, there are responsible and well-understood ways to accomplish this. The Wharton Risk Management and Decision Processes Center outlines one strategy. The Association of State Floodplain Managers details another. For Taxpayers for Common Sense, any responsible approach to affordability would be:

- *Self-contained*—the taxpayer should not be asked to take on a further burden to support this program. If an affordability policy is undertaken, a small surcharge should be placed on all flood insurance policies to prefund the account.
- *Targeted*—One of the underlying problems of subsidized flood insurance is that the subsidies flow to wealthy vacation beach house owners as well as those of modest means. The affordability measures must be available only on a means-tested basis.
- *Temporary*—This should be a short term program to help policyholders deal with sticker shock. A long-term program will undercut the important risk information provided by the price signals.
- *Independent*—The aid should be vouchers or some other assistance that is outside the NFIP rate structure so that it doesn't undercut the price signals of risk.
- *Helpful*—Obviously aid is helpful, but the funding should allow the policyholder to use it for mitigation as well as rate relief.
- *Logical*—Properties should get premium credit for the level of protection that they currently have, even if the flood protection isn't greater than 100-year protection. Last minute maneuvering stripped a provision from Biggert-Waters that would have allowed this.

[14] GAO selected 351 counties nationwide, this included every county with more than 500 subsidized single unit primary residence policies and five counties in every State with the most remaining subsidized policies for single-unit primary residences.

Conclusion

The National Flood Insurance Program is a narrow program. There are 5.5 million policies, 3.6 million of which are for primary residences and another 1.7 million for second homes. But there are 132.3 million housing units in the United States.[15] This means that while only 4 percent of housing units nationwide have flood insurance, those policyholders are roughly $25 billion in debt to American taxpayers.

It took extraordinary amount of effort in Congress to increase the NFIP borrowing authority by $9.7 billion after Superstorm Sandy, and that was to enable the program to pay off claims to policyholders. This demonstrates there is fatigue and impatience with this program that is $25 billion in debt. To delay or derail the reforms enacted a year ago would put this program on perilous footing, fiscally, politically, and existentially.

[15] *http://quickfacts.census.gov/qfd/states/00000.html*

PREPARED STATEMENT OF BIRNY BIRNBAUM

EXECUTIVE DIRECTOR, CENTER FOR ECONOMIC JUSTICE

SEPTEMBER 18, 2013

Statement of Birny Birnbaum

on behalf of

The Center for Economic Justice, The Consumer Federation of America, United Policyholders, The Center for Insurance Research, The National Fair Housing Alliance and The National Consumer Law Center (on behalf of its low-income clients)

Before the Senate Committee on Banking, Housing and Urban Affairs Subcommittee on Economic Policy

"Implementation of the Biggert-Waters Flood Insurance Act of 2012: One Year After Enactment."

September 18, 2013

Chairman Merkley, Ranking Member Heller and Members of the Subcommittee, thank you for the opportunity to speak about impact of the Biggert-Waters Act on the availability and affordability of flood insurance. My name is Birny Birnbaum and I am Executive Director of the Center for Economic Justice (CEJ). CEJ is a non-profit organization advocating on behalf of consumers on insurance, credit and utility issues. I have been asked to talk about force-placed flood insurance, a topic on which I have worked for many years as an insurance regulator, consumer advocate and consulting economist. My comments are presented on behalf of the Center for Economic Justice[1], the Consumer Federation of America[2] United Policyholders,[3] the Center for Insurance Research[4], the National Fair Housing Alliance[5] and the National Consumer Law Center (on behalf of its low-income clients)[6].

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[1] The **Center for Economic Justice** is non-profit consumer organization advocating on behalf of consumers on insurance, credit and utility issues. www.cej-online.org

[2] **Consumer Federation of America** is an association of nearly 300 nonprofit consumer organizations established in 1968 to advance the consumer interest through research, advocacy and education. www.consumerfed.org

[3] **United Policyholders** is a non-profit 501(c) (3) organization whose mission is to be a trustworthy and useful information resource and an effective voice for consumers of all types of insurance in all 50 states. www.uphelp.org

[4] **The Center for Insurance Research** is a non-profit consumer organization providing an independent voice for reform in debates about insurance, banks, financial services companies and related public policy issues around the nation. www.centerforinsuranceresearch.org

[5] Founded in 1988, **The National Fair Housing Alliance** works to eliminate housing discrimination and to ensure equal housing opportunity for all people through leadership, education and outreach, membership services, public policy initiatives, advocacy and enforcement. www.nationalfairhousing.org

[6] Since 1969, the nonprofit **National Consumer Law Center®** (NCLC®) has worked for consumer justice and economic security for low-income and other disadvantaged people through its expertise in policy analysis and advocacy, publications, litigation, expert witness services, and training. **www.nclc.org**

1. What is Force-Placed Insurance?

Federally-regulated lending institutions may not make, increase, extend, or renew any loan secured by improved real estate in a Special Flood Hazard Area (SFHA), as determined by the Federal Emergency Management Agency (FEMA), unless the improved property serving as collateral for the loan is covered by a minimum amount of flood insurance.[7]

Federal law also provides for force-placement of flood insurance in the event the borrower fails to maintain the required amount of flood insurance coverage.[8] The law places the responsibility on the lender / servicer to determine if a lapse in required flood insurance has occurred and to notify the borrower of such lapse in coverage prior to force-placing flood insurance.[9]

Among other responsibilities, a mortgage servicer is also required, through its servicing agreement with the owners of the mortgage loan, to ensure that required flood insurance coverage on the properties serving as collateral for the loan is in-force. This requirement involves two distinct activities – tracking insurance on loans being serviced and placing insurance when the borrower fails to maintain the required insurance coverage. The insurance placed by the servicer under these circumstances is called lender-placed flood insurance or force-placed flood insurance (FPIF). FPIF protects the lender's collateral in the event the borrower fails to maintain insurance protecting the collateral and enables the servicer to comply with federal requirements.

This division of responsibilities – insurance tracking for the servicer, provision of FPIF coverage under the master policy by the insurer – is well recognized in regulatory requirements and industry practice. For example, in the cover letter to an FPI rate filing in Florida earlier this year from the largest writer of force-placed insurance (FPI), American Security Insurance Company (ASIC) wrote:[10]

> Any type of real estate loan involving a commercial or residential structure requires the borrower to keep sufficient insurance coverage in force to satisfy the lender's interest should the structure (collateral) be destroyed or damaged. In order to make sure this requirement is met, most lenders have a department which keeps track of all the insurance policies covering properties for outstanding loans. If borrower provided coverage is cancelled or expired, the lender begins sending a series of follow-up letters to the borrower reminding the borrower of his obligation to keep insurance in force. If the borrower fails to comply, the lender will request issuance of the policy.

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[7] 42 USC § 4012a(b)
[8] 42 USC § 4012a(e)
[9] 42 USC § 4012a(e)
[10] Filing No. 13-04125 with Florida Office of Insurance Regulation

1.1 Ensuring Continuous Insurance Coverage

Mortgage lenders and servicers are required to ensure that borrowers in SFHAs have continuous flood insurance coverage. To ensure there is no lapse in flood coverage, servicers purchase FPIF policies from insurers. The FPIF insurance policy sold to the servicer is a group insurance master policy. Group insurance means that the policy covers a group of properties and not just a single property like the homeowners insurance policy purchased by a borrower. A master policy means that the policy covers all eligible properties and, as a property becomes eligible for coverage, a certificate of coverage for the individual property is issued under the master policy.

The FPIF policy provides that coverage begins on any property in the servicer's covered mortgage loan portfolio at the instant that the borrower's voluntary policy ceases to provide the required coverage. This provision is called automatic coverage. The FPIF policy provides coverage, for example, if the borrower's voluntary flood insurance policy is canceled by the borrower or the NFIP, or lapses because of non-payment of premium. The FPIF policy provides coverage whenever the borrower's required insurance fails to remain in-force – even if the servicer or its vendor do not discover this failure of insurance coverage for days or weeks after the borrower's policy coverage has ended. The FPIF group policy covers all properties in the servicer's loan portfolio and provides coverage as needed.

When a lapse in coverage is discovered on a property in the mortgage loan portfolio, the FPIF insurer is instructed to issue a certificate of coverage retroactive to the date and time the borrower's coverage ceased to be in-force along with correspondence to the borrower on behalf of the servicer that such insurance has been issued and the charges for the FPIF has been added to the borrower's escrow account. The correspondence informs the borrower that the FPIF coverage will be canceled if the borrower provides the required evidence of insurance coverage. This process is largely automated and conducted by a single vendor providing insurance tracking services and FPIF insurance.

The FPIF insurance company bills the servicer on a periodic basis for all the insurance provided. In most instances, the servicer, in turn, assesses FPIF charges to individual borrowers, removes funds from the borrower's escrow to pay for the FPIF premium, debits the borrower's escrow if there are insufficient funds to pay the premium, or establishes an escrow account if one does not exist and debits the new escrow account for the amount of the FPIF premium. Again, while this is a servicer responsibility, some or all of these activities are performed by the FPIF insurance company or vendor on behalf of the loan servicer under a contract with the servicer.

If the borrower provides evidence that there was no lapse in required insurance coverage, the FPIF insurance company will refund the premium paid by the servicer and the servicer will refund the FPIF amounts charged to the borrower's loan.

1.2 FPIF GAP

Because almost all voluntary flood insurance is provided by the NFIP and because NFIP coverage is capped at a maximum amount of $250,000 for a residential structure, FPIF coverage is force-placed not only when a borrower is required to maintain flood insurance and has no flood coverage, but is also force-placed when the borrower has insufficient voluntary flood coverage in place. When a borrower has purchased a voluntary flood insurance policy, but the coverage provided by that policy is less than the amount of coverage required by the servicer, the servicer will force-place FPIF in the amount of the difference between the required amount of flood coverage and the amount of voluntary flood coverage. This excess FPIF is sometimes referred to as FPIF GAP.

1.3 Servicer Recovers FPIF Premiums Even In Event of Foreclosure

The mortgage servicer recovers the FPIF premium it has paid to the FPIF insurer, even in the event that a borrower defaults and there is a foreclosure or short sale because the FPIF premiums are paid by the owner of the loan (the investor) to the servicer out of the proceeds from the foreclosure or short sale.

1.4 Blanket FPIF Policies – No Servicer Charges to Individual Borrowers

In the most common type of FPIF program the servicer pays a premium to the FPIF insurance company and then assesses FPIF charges on individual borrowers. However, there is no statute or regulation requiring a servicer to charge a borrower for FPIF. In fact, there are FPIF products for which the servicer does not assess a separate charge to borrowers.

Under a typical FPIF program, the premium charges to the servicer are based on coverage issued under the FPIF master policy as directed by the servicer to the FPIF insurer. If all borrowers maintained required insurance, no coverage would be issued under the FPIF master policy and the servicer would not be charged a premium by the FPIF insurer. Under a blanket FPIF program, the FPIF coverage is based on the amount of outstanding loan balance at the end of the month, regardless of how many borrowers, if any, have a lapse in required voluntary insurance. With a blanket FPIF program, the servicer does not assess a separate FPIF charge to specific borrowers, but spreads the cost of the blanket FPIF coverage over the entire loan portfolio.

1.5 The NFIP's FPI Flood Product is Not Used

The NFIP offers a force-placed insurance product, called the Mortgage Portfolio Protection Program (MPPP).[11] The NFIP Manual states,

> When a mortgagee or a mortgage-servicing company discovers, at any time following loan origination, that there is no evidence of flood insurance on a property in a Special Flood Hazard Area (SFHA), then the MPPP may be used by such lender/servicer to obtain (force-place) the required flood insurance coverage. The MPPP process can be accomplished with limited underwriting information and with special flood insurance rates.[12]

MPPP rates are far higher than voluntary NFIP flood insurance rates. The chart below, with NFIP voluntary insurance rates and MPPP rates by rate category, shows MPPP rates are six times greater than voluntary NFIP rates for some rate categories.[13]

The MPPP is not used by mortgage servicers because the MPPP does not provide the automatic coverage of FPIF that servicers require in order to ensure continuous coverage.

Comparison of NFIP Single Family Rates to MPPP Rates

Rate Category	*NFIP Single Family*	*MPPP*
Emergency Program Building	$0.76	$4.32
Emergency Program Contents	$0.96	$4.36
A Zones Building to $60,000	$0.76 to $0.81	$4.32
A Zones Building, 60,000 to $250,000	$0.77 to $0.37	$2.19
A Zones Contents to $25,000	$0.96	$4.36
A Zones Contents, $25,000 to $100,000	$1.16 to $1.38	$2.10
V Zones Building to $60,000	$0.99 to $1.08	$6.43
V Zones Building, 60,000 to $250,000	$1.94 to $6.11	$6.43
V Zones Contents to $25,000	$1.23	$6.04
V Zones Contents, $25,000 to $100,000	$2.81 to $3.31	$6.04
A99 Zones Building to $60,000	$0.96 to $1.08	$1.12
A99 Zones Building, 60,000 to $250,000	$0.25 to $0.41	$0.67
A99 Zones Contents to $25,000	$1.46 to $1.65	$1.49
A99 Zones Contents, $25,000 to $100,000	$0.45 to $0.60	$0.60

[11] http://www.fema.gov/media-library-data/20130726-1912-25045-6307/10_mppp_may2013.pdf

[12] NFIP Manual, May 1, 2013, at pages MPPP 1-2.

[13] NFIP Manual, May 1, 2013 at pages Rate 1-2 and pages MPPP 1. Voluntary rates are from Table 2A Regular Coverage – Pre FIRM Construction Rates. Rates are expressed as annual cost per $100 of coverage.

2. FPI Premium Have Quadrupled Since 2007

Mortgage servicers place FPI not only for flood coverage, but also for hazard coverage, when a borrower's voluntary homeowners insurance lapses. Insurers selling FPI report their experience to state insurance regulators annually in the Credit Insurance Experience Exhibit supplement to Statutory Annual Financial Statements. The data are not broken out separately for FPI flood versus FPI hazard. While the data reflect the experience of the largest writers of the market, some insurers writing FPI have failed to submit required CIEE reports. I estimate the CIEE data reflect about 90% to 95% of the total FPI market.

The CIEE data show huge increases in gross written premium (GWP), net written premium (NWP) and earned premium (EP)[14] from 2004 through 2011 and continued high premium levels in 2012. The data also show that the ratio of claims paid to premiums collected by FPI insurers has been very low – averaging about 25%.[15]

[14] Gross written premium is the total amount of premium charged to servicer policyholders on coverage issued in a particular year before any refunds. Net written premium is the total amount of premium charged to servicer policyholders on coverage issued in a particular year after refunds for cancellations. Earned premium is the premium associated with exposures during a particular year. For example, if coverage was issued on July 1 with an annual premium charge of $5,000 and assuming the coverage was not canceled and refunded, the gross and net written premium would be $5,000. The earned premium would be six months of the annual policy – from July through December of the year – for a total of $2,500 in the year the coverage was issued and $2,500 in the following year.

[15] Paid loss ratio equals dollars of claims paid in a particular year divided by net written premiums in that year. Earned loss ratio equals incurred losses in a particular year divided by earned premiums in that year. Incurred losses are the insurer's estimate of the ultimate amount of claim dollars that will be paid on coverages issued – exposures – in that year. Paid loss ratio is a cash flow measure, while incurred loss ratio is generally a better measure to evaluate the reasonableness of rates.

FPI Nationwide Experience, 2004-2012

Year	GWP	NWP	EP	Paid LR	Incurred LR
2004	$1,485	$796	$807	33.5%	33.1%
2005	$1,832	$919	$850	40.4%	53.5%
2006	$2,163	$1,074	$988	29.5%	29.0%
2007	$3,058	$1,647	$1,402	16.0%	20.5%
2008	$4,000	$2,209	$1,999	20.1%	23.3%
2009	$5,181	$3,049	$2,641	16.0%	20.7%
2010	$5,915	$3,223	$3,248	15.7%	17.3%
2011	$5,692	$3,450	$3,256	22.5%	24.7%
2012	$5,115	$2,870	$3,187	30.5%	30.8%
2004-12	$34,442	$19,238	$18,378	22.4%	25.3%

2.1 FPI Market Dominated by Two Insurer Groups

At least 90% of the FPI premium is written by just two insurers – Assurant and QBE. Assurant and QBE provide FPI and insurance tracking services to the largest mortgage servicers. Assurant alone provides tracking and FPI for about 70% of all outstanding mortgages.[16] The remaining FPI premium is written primarily through managing general agents who administer FPI and insurance tracking to the remaining thousands of community banks, credit unions and small lender/servicers.

[16] Assurant Earnings Call Transcript, 2013 Q2 in which Assurant reports tracking 35 million loans – about 70% of the roughly 50 million mortgage loans outstanding. http://seekingalpha.com/article/1573552-assurant-inc-aiz-management-discusses-q2-2013-results-earnings-call-transcript

2.2 FPI Premiums are Far Greater Than Those for Voluntary Insurance, but Loss Ratios Are Lower

FPI premium charges are significantly higher than voluntary insurance premium charges for the same property. Assurant has testified that FPI premiums average about twice those of voluntary premiums,[17] but there are numerous examples of FPI premiums being three, four or more times greater than voluntary insurance premiums. Insurers selling FPI argue that the higher premium charges are justified:

- Lack of individual underwriting, take-all-comers means FPI is much riskier than homeowners insurance for which the voluntary insurer can underwrite and reject individual properties.
- FPI exposures are concentrated in catastrophe-prone areas and, consequently, more susceptible to catastrophe losses.
- FPI expenses are greater than expenses for homeowners insurance because of the special activities associated with administering an FPI policy.
- FPI expenses are greater than expenses for homeowners because many or most FPI coverages are canceled before the full term of coverage.

If these arguments are true, we would expect to see higher loss ratios for FPI than voluntary homeowners insurance. With average FPI premiums twice that of average homeowners insurance, the same percentage for expenses produces twice as many expense dollars. We would not expect twice as many expense dollars for FPI than for homeowners since there is no individual property underwriting – which means no expenses for property inspection, obtaining credit histories, CLUE (claims history reports), obtaining information from the policyholder about the amount and types of coverages as well as other acquisition expenses not found with FPI.

If we assume FPI poses greater risk and, consequently, produces greater claims and the expense percentage of FPI is less than the expense percentage of homeowners – even with the lower FPI expense percentage producing more expense dollars per covered property – we would expect that claim payments for FPI would be a greater percentage of premium than they are for homeowners insurance. Stated differently, based on the industry explanation for higher FPI rates, we would expect higher FPI loss ratios than homeowners loss ratios. And we would also expect greater volatility in FPI loss ratios than homeowners loss ratios if FPI is more susceptibility to catastrophe events.

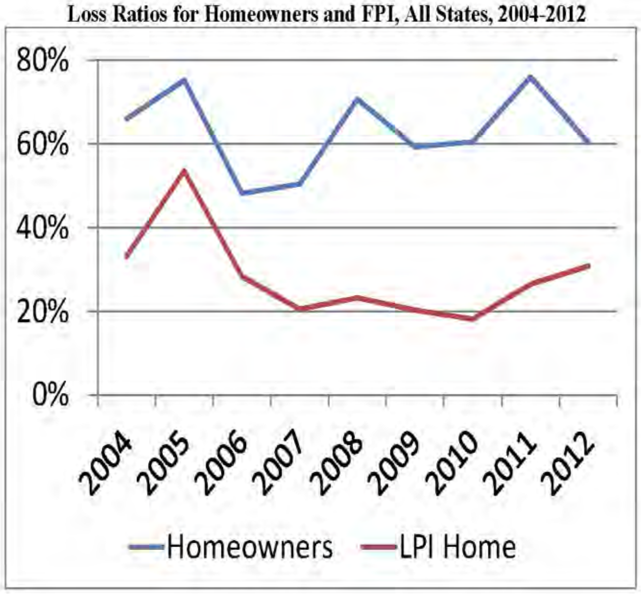
[17] See presentation of John Frobose of Assurant at http://www.naic.org/documents/committees_c_120809_public_hearing_lender_placed_insurance_presentation_frobose.pdf

The loss ratio results from 2004 through 2012 show FPI loss ratios have been far less than homeowners loss ratios.[18]

Loss Ratios for Homeowners and FPI, All States, 2004-2012

Year	Homeowners	FPI Home
2004	66.0%	33.1%
2005	75.2%	53.5%
2006	48.2%	29.0%
2007	50.4%	20.5%
2008	70.7%	23.3%
2009	59.3%	20.7%
2010	60.5%	17.3%
2011	75.4%	24.7%
2012	60.4%	30.8%
2004-2012	63.0%	25.3%

Loss Ratios for Homeowners and FPI, All States, 2004-2012



[18] Data Sources: LPI Home, NAIC Credit Insurance Experience Exhibit data compiled by Birnbaum. Homeowners 2004-2011, *NAIC Report on Profitability by State by Line in 2011*; Homeowners 2012, compilation by Birnbaum of State Page data provided by NAIC. The NAIC does not endorse any calculations performed on data it provides.

The table below shows that in Florida – the state with the greatest catastrophe risk and the largest amount of FPI premium – FPI loss ratios were far less than homeowners loss ratios in years with and without catastrophe events. The table also shows homeowners and FPI loss ratios for all states except Florida. Again, the FPI loss ratios are far below the homeowners loss ratios. Of particular note are the years 2011 and 2012. While the homeowners loss ratio jumped in 2011 because of major catastrophe events, the FPI loss ratio remained low in 2011. And in 2012, the year of Superstorm Sandy, despite flood being covered by FPI but not by homeowners insurance, the FPI loss ratio remained far below the homeowners loss ratio.

Homeowners and FPI Loss Ratios, Florida Only and All States Ex Florida, 2004-12

	FL HO	FL FPI	All State Ex FL HO	All States EX FL FPI
2004	303.0%	75.2%	52.2%	28.0%
2005	153.6%	102.5%	60.2%	47.9%
2006	32.6%	29.6%	58.7%	28.9%
2007	25.6%	11.4%	63.0%	22.2%
2008	33.9%	10.6%	86.6%	26.7%
2009	38.4%	11.7%	72.5%	24.7%
2010	38.1%	7.2%	72.5%	23.1%
2011	35.9%	9.9%	90.8%	32.6%
2012	31.6%	13.3%	72.2%	40.3%
2004-2012	61.4%	13.6%	70.9%	30.0%

3. Reverse Competition in FPI Markets Leads to Excessive Charges to Borrowers

Reverse competition describes a market structure in which consumers/borrowers exert little or no market power over prices. Instead of competing for individual consumers, insurers compete for the entities with the market power to steer the ultimate consumer to the insurer. Insurers compete for the servicer's business by providing considerations to the servicer, with the cost of such considerations passed on to the borrower. Greater competition for the lender's business leads to higher prices of credit-related insurance, including FPI, to the borrower. This form of competition, which results in *higher* prices to consumers, is called reverse competition.

3.1 Consumers Are Especially Vulnerable to Excessive FPI Charges

The incentives and potential for excessive FPI charges are great. Consumers do not request the insurance, but are forced to pay for it. The cost of FPI is much higher than a policy the borrower would purchase on his or her own. Servicers have financial incentive to force-place the insurance because the premium includes commission and other consideration for the servicer.

Borrowers are vulnerable to excessive charges for FPI because the borrowers / consumers exert no market power in the setting of these rates. In addition, there is no downward market pressure on rates; the vendors/insurers offering FPI do not compete on the basis of price, but on the basis of services provided to the lender and compensation and other considerations provided to the lender or its affiliates.

Fannie Mae is a government-sponsored enterprise that purchases mortgages originated by others. Fannie Mae is the largest single owner of mortgages in the United States and contracts with mortgage servicers to service the tens of millions of mortgage loans Fannie owns. Fannie pays a fee to mortgage servicers for each mortgage loan serviced. In addition, when a mortgage owned by Fannie goes into default and the mortgaged property is foreclosed, Fannie pays any outstanding FPI premium due on the defaulted loan to the servicer. In a 2012 request for proposal for insurance tracking and FPI, Fannie Mae also describes the problem with unreasonable expenses included in FPI premium charges.

> After extensive internal review, Fannie Mae believes that current Lender Placed Insurance costs are not market competitive and can be improved through unit price reductions and fee transparency to the benefit of both the taxpayers and homeowners.
>
> Current Situation
> Fannie Mae's current Lender Placed Insurance situation is as follows:
>
> 1. Homeowners are required to maintain voluntary hazard insurance on Fannie Mae insured properties.

2. Lender Placed Insurance must be acquired by mortgage Servicers when a property is no longer eligible for Voluntary Insurance, or when the Servicer cannot obtain proof of adequate Voluntary Insurance from the homeowner, irrespective of whether or not that homeowner is current or delinquent on the loan.

3. The cost of Lender Placed Insurance is higher than the cost of voluntary hazard insurance. Homeowners are billed for the Lender Placed Insurance premiums. However, if the homeowner does not pay the premium (for example, if the property has already been vacated), then Servicers pass on the premium costs to Fannie Mae.

4. Servicers are responsible for providing tracking services, per Fannie Mae Guidelines. Many large Servicers have chosen to outsource the Insurance Tracking and associated administrative process to third parties, the largest of which are affiliated with Lender Placed Insurers.

5. Lender Placed Insurers often pay commissions/fees to Servicers for placing business with them. The cost of such commissions/fees is recovered in part or in whole by the Lender Placed Insurer from the premiums, which the Servicers pass on to Fannie Mae.

6. The existing system may encourage Servicers to purchase Lender Placed Insurance from Providers that pay high commissions/fees to the Servicers and provide tracking, rather than those that offer the best pricing and terms to Fannie Mae. Thus, the Lender Placed Insurers and Servicers have little incentive to hold premium costs down. In addition, Fannie Mae is often paying twice for Insurance Tracking services; once via the servicing fee that Fannie Mae pays to Servicers, and again via the Lender Placed Insurance premiums, since those premiums may include or subsidize the costs of tracking services (to the extent that insurers are providing such services).

In appropriate Circumstances, Lender Placed Insurance is necessary and important to the preservation of Fannie Mae assets. However, much of the current Lender Placed Insurance cost borne by Fannie Mae results from an incentive arrangement between Lender Placed Insurers and Servicers that disadvantages Fannie Mae and the homeowner.

3.2 Unreasonable Expenses

Because of reverse competition, borrowers are charged excessive FPI amounts because of unreasonable expenses included in the FPI premiums paid by the mortgage servicer to the FPI insurer. To compete for servicer business, FPI insurers must provide considerations to the lender. This cost of these considerations – payments by the FPI insurer to the servicer or expenditures by the FPI insurer to subsidize the servicer's cost for non-FPI activities – inflate the FPI premium beyond the reasonable costs of providing the insurance. Unreasonable expenses included in FPI rates include:

- Tracking/Servicing Activities Unrelated to the Provision of FPI
- FPI Commissions
- Captive Reinsurance Administrative Costs
- Affiliate Transactions at Above-Market Prices

3.2.1 Tracking and other Servicer Activities

Table 1 provides a list of FPI-related activities and identifies the activities as associated with servicing a portfolio of loans versus the issuance and administration of the FPI master policies and individual property coverages.

Although most of the activities in Table 7 are servicing activities, most or all of these activities are typically performed by the FPI vendor for the servicer. Some of these services may be billed separately from the FPI premium, but some portion of the FPI insurer's expenses are for performing servicer activities not a part of the provision of FPI. Such expenses are unreasonable to include in FPI premium charges to borrowers.

Table 1
FPI-Related Servicing and Insurance Activities

Activity	Servicing vs. Insurance
Tracking Insurance	
Loading Insurance Information into Database	Servicing
Contacting Borrowers, Problems with Insurance	Servicing
Customer Service Borrowers Insurance Evidence	Servicing
Contacting Insurers/Agents Insurance Evidence	Servicing
Placing Insurance	
Notifying Insurer to Issue Binder or Policy	Servicing
Issuing Temporary Binder	Insurance
Determining Coverage Amount	Servicing
Servicer Payment to Insurer	Insurance
Billing Borrower for FPI Premium	Servicing
Setting up Escrow when necessary for FPI	Servicing
Refunds to Servicer	Insurance
Refunds to Borrower	Servicing
Issuing Permanent Policy	Insurance
Customer Service about Insurance Placement	Servicing
Customer Service about Borrower Refunds	Servicing
Customer Service about FPI Coverage	Servicing
Customer Service about FPI Claims	Insurance

3.2.2 Commissions to Servicer-Affiliated Producers

Testimony at the 2012 New York Department of Financial Services hearing on FPI revealed that "commissions" paid to servicer-affiliated producers are not justified by any service provided by these producers and represent a kickback to the servicer for placing the FPI. When asked what activities the servicer-affiliated producers perform to justify the commissions, the responses included:

- Soliciting FPI providers
- Reviewing FPI form letters and other documents
- Third-party broker commissions are commonplace
- Broker commissions are an accepted and approved practice
- FPI broker commissions are similar to those in other lines of insurance
- Manage the FPI rating program
- Manage the FPI vendor relationship
- Quality review of the FPI vendor
- Commissions are a cost of doing business

The classic role of the insurance producer is to help the policyholder determine her insurance needs and shop the market for the insurance product that meets the policyholder's needs while seeking the most competitive price for the product. Such activities simply do not exist in FPI because there are only two national providers of the necessary package of insurance and related services and there is no price competition among the insurers. Soliciting new business consists of asking typically two vendors for proposals – and such activity is a rare event for most servicers.

Reviewing FPI form letters and other communication templates is the servicer's responsibility. A servicer-affiliated producer performing such review is performing servicer activity which should not be compensated for through FPI insurance premiums.

The fact that third-party broker commissions are commonplace or a standard industry practice in FPI or other lines of insurance is no justification for such commissions in the FPI market. There have been a variety of standard industry practices by servicers and insurers that were unfair and abusive to consumers – and which were not justified by virtue of many servicers or insurers engaging in the same practice. In the servicing realm, recent settlements between states and servicers have identified a number of unfair industry practices, such as robosigning foreclosure documents. In the insurance realm, steering of business based on contingent commissions, unfair use of retained asset account and abusive sales of financed single premium credit insurance, were industry standard practices, to name a few.

Other justifications cited by industry witnesses –managing the FPI vendor relationship and quality review of the FPI vendor – are responsibilities of the servicer and, to the extent the servicer-affiliated producer is performing these activities, the commissions to these producers represent a kickback of the FPI premiums to subsidize servicer activities.

In summary, industry witnesses have provided no justification for any FPI commissions to servicer-affiliated producers. Fannie Mae's new policy – to not reimburse servicers for any portion of FPI premiums paid as commission to servicer-affiliated producers – provides further evidence that no commissions to servicer-affiliated producers are warranted.

3.2.3 Captive Reinsurance

Captive reinsurance arrangements – in which the FPI insurer reinsures a portion of FPI business with a reinsurance company owned or affiliated with the servicer – are simply profit-sharing mechanisms designed to provide additional considerations to the servicer. These arrangements serve no substantive risk management purpose and, consequently, serve no purpose for the consumers/borrowers of FPI.

The arrangements should be prohibited because they create a conflict of interest between the servicer and the borrower. By having a financial interest in the price and placement of FPI through a captive reinsurance program, the servicer has a glaring conflict with the interest of the borrower for lower-cost FPI. Testimony of industry witnesses – "we can see that there might be a perception of a conflict, but it does not affect our practice" – does not address or eliminate the actual conflict of interest. The person who has a conflict of interest does not eliminate the conflict simply by saying, "I'm not affected by these financial incentives."

Regardless of whether the captive reinsurance arrangements are prohibited, the expenses associated with administering the arrangements should be excluded from FPI rates because these expenses provide no benefit for the borrower. The administrative expenses for captive reinsurance arrangements are likely substantial; the 2011 American Security Insurance Company statutory annual statement shows dozens of such arrangements.

3.2.4 New York DFS Settlement with Assurant, Balboa and QBE

In October 2011, the New York Department of Financial Services (NYDFS) launched an investigation into the force-placed insurance industry and conducted public hearings in May 2012. The NYDFS investigation revealed[19]:

- The premiums charged to homeowners for force-placed insurance are two to ten times higher than premiums for voluntary insurance, even though the scope of the coverage is more limited.

[19] April 5, 2013 letter from Superintendent Benjamin Lawsky to other state insurance regulators at http://www.dfs.ny.gov/about/press2013/Force-Placed_Letter.pdf

- The loss ratios for force-placed insurance seldom exceed 25 percent. Nevertheless, rate filings made by insurers with DFS reflected loss ratio estimates of 55 to 58 percent.

- Insurers and banks have built a network of relationships and financial arrangements that have driven premium rates to inappropriately high levels ultimately paid for by consumers and investors.

- Force-placed insurers have competed for business from banks and mortgage servicers through "reverse competition": i.e., rather than competing for business by offering lower prices, insurers have created incentives for banks and mortgage servicers to buy force-placed insurance with high premiums by enabling banks and mortgage services, through complex arrangements, to share in the profits associated with the higher prices.

The Consent Orders with Assurant, QBE and Balboa included requirements for minimum loss ratio standards and for rate filings to ensure those standards are met. The Consent Orders also contained specific prohibitions, including:

- The FPI insurer shall not issue FPI on mortgaged property serviced by a servicer affiliated with the FPI insurer.
- The FPI insurer shall not pay FPI commission to a servicer or entity affiliated with the servicer.
- The FPI insurer shall not engage in captive FPI reinsurance agreements with affiliates of the servicer.
- The FPI insurer shall not pay contingent commissions based on underwriting profitability or loss ratios.
- The FPI insurer shall not provide free- or below-cost outsourced services to servicers, lenders or their affiliates.
- The FPI insurer shall not make any payments to servicers, lenders or their affiliates in connection with securing business.

On April 5, 2013 New York Superintendent of Financial Services Benjamin Lawsky wrote to other state insurance regulators describing the New York DFS investigation and settlements and urging the other state regulators to utilize the settlement provisions as a template for the states to use "to help root out the kickback culture that has pervaded the force-placed insurance industry and lower rates for hard-working homeowners."[20]

[20] http://www.dfs.ny.gov/about/press2013/Force-Placed_Letter.pdf

4. Other Problems with FPI Flood: Excessive Retroactive Billing and Unnecessary Placement

4.1 Excessive Retroactive Billing

Mortgage servicers are responsible for tracking insurance coverage on the loans they service. When there is a lapse in a homeowner's insurance coverage, the servicer, typically through an insurance tracking vendor, notifies the force-placed insurer. It is the servicer's responsibility to identify lapses in insurance and notify homeowners of these lapses in a timely fashion.

Regulatory requirements and industry practice make clear that that insurance tracking is a responsibility of the mortgage servicer. Among other things:

a. Federal law requires federally regulated or insured lenders / servicers to monitor loans for the continuous presence of required flood insurance on properties located in a Special Flood Hazard Area[21] and federal regulation requires mortgage servicers to provide notices in specified time frames before charges for hazard FPI and prohibits placing FPI if a borrower has an escrow account on her loan and payment of premium will keep the voluntary policy in force.[22]

b. Notices to borrowers regarding required hazard or flood insurance are sent on mortgage servicers' letterhead; and

c. Fannie Mae has determined that insurance tracking is a servicer responsibility whose costs should not be included in FPI charges to borrowers.

Mortgage servicers purchase FPI coverage from insurers through a master policy covering all properties serving as collateral for serviced loans. The master policy provides automatic coverage if and when the borrower's voluntary hazard or flood insurance coverage lapses and that coverage comes into force the instant the voluntary insurance coverage lapses.

Once a lapse in voluntary coverage is discovered by the servicer and FPI coverage is issued under a FPI master policy, the FPI insurer charges a premium to the servicer. The servicer, after sending required notices to affected borrower and failing to receive evidence of voluntary insurance, charges the borrower for FPI. Servicers charge borrowers for FPI at some point after the lapse in coverage, but charge for coverage beginnings at the date of the lapse. Consequently, servicers retroactively charge borrowers for the coverage that was automatically in-force the instant the borrower's voluntary hazard or flood insurance coverage lapsed.

[21] 42 U.S.C. § 4012a (e)
[22] Regulation X (12 C.F.R.) §§ 1024.34, 1024.37.

It is not unreasonable that the servicer (or insurance tracking vendor) may not instantly discover a lapse in coverage, resulting in retroactive charges for a short period of time--perhaps up to 60 days from the lapse. ***It is unreasonable, however, for a servicer to fail to discover a lapse in coverage for an extended period of time, fail to notify the borrower in a timely fashion, and to then retroactively charge for lengthy periods of time.*** A 60-day period gives the servicer or vendor sufficient time to discover a lapse in coverage and notify the before imposing any FPI charges. If the servicer fails to identify the lapse in coverage within this reasonable period of time, the servicer – not the borrower – should bear the responsibility for the cost of the FPI.

4.1.1 An Example of Excessive Retroactive Billing for FPI Flood

On January 30, 2012, Mr. and Mrs. Leghorn[23] were notified by their servicer that temporary FPI flood coverage had been placed for a 90-day period beginning on December 12, 2009. This notice arrived ***more than two years*** after the alleged lapse in coverage. On March 6, 2012, the servicer charged the Leghorns for FPI flood coverage for the full year from December 12, 2009 to December 12, 2010 – almost 27 months after the lapse in coverage and almost 15 months after the coverage had expired, but only 36 days after the notice of problems with evidence of required insurance.

The servicer then sent a notice the next day, March 7, 2012, to the Leghorns stating that it required evidence of flood insurance for the period from December 12, 2010 through December 12, 2011. Thirty days later, on April 6, 2012, the servicer charged the Leghorns for FPI flood for the period December 12, 2010 through December 12, 2011 – almost 16 months after the lapse in coverage and almost four months after the coverage had expired. Both of these charges were unreasonable because the charges were made long after 60 days from the date of lapse of the voluntary flood policies and long after the Leghorns could make use of the information in the required notices

Retroactive charges for extended periods of coverage are unfair to borrowers for at least two reasons. First, the lengthy retroactive charges render the notice requirements for FPI meaningless. The purpose of the notice requirements is to empower the borrower to take action to avoid FPI charges. When a borrower receives the FPI notices long after she can take any action to avoid the FPI charge, the notice is meaningless. Second, a lengthy retroactive charge means that the servicer has failed to do a reasonable job of tracking voluntary insurance coverage. Since tracking is the servicer's responsibility, it is unfair for the servicer to charge the borrower for the servicer's failure.

[23] See complaint in *Leghorn, et al v. Wells Fargo Bank, N.A.*, Case No. 4:13-CV-00708-JCS (N.D. Cal.).

4.2 Unnecessary FPI Flood Placement

Servicers have unnecessarily placed FPI Flood on borrowers because of errors in tracking the need for flood insurance and errors in tracking the presence of voluntary flood insurance. Hundreds of Oregonians have been wrongly charged for FPI Flood because of servicer's false determination that the borrower requires flood insurance. Borrowers are forced to challenge the flood determination and have paid hundreds of dollars to hire surveyors and otherwise provide evidence refuting the servicer's flood determination. The number of such challenges in Oregon has more than doubled over the past several years.[24]

A concern raised by Oregonians is that penalty increases in the Biggert-Waters Act for lenders who fail to ensure that homes in SFHAs have flood insurance has caused lenders and servicers to place FPIF in more situations when flood insurance is not actually required.

Another cause of unnecessary FPIF placements is servicers placing FPIF when the servicer could maintain the voluntary flood policy simply by advancing the premium for the borrower who has not had an escrow account or for borrowers with escrow accounts but without sufficient funds to in the escrow account to pay the voluntary flood insurance premium due. When a servicer force-places FPIF, the servicer debits an existing escrow account for the amount of the FPI premium or, in the case of a borrower without an escrow account, creates an escrow account and then debits that new escrow account for the amount of the FPIF premium. Consequently, instead of simply advancing funds to keep the voluntary policy in place, the servicer advances – and charges the borrower – a far greater amount for the FPIF coverage. As discussed below, some help is on the way in 2014 to address this problem

5. The Coming Explosion in FPI Flood

The number of FPIF placements has surely increased this year and will increase even more as the Biggert-Waters Act is implemented. The increase in FPIF placements will be driven by at least three factors. First, many more borrowers will now be required to purchase flood insurance due to new flood maps from FEMA. With more borrows required to purchase flood insurance will come more FPIF placements. Second, the Biggert-Waters-required NFIP rate hikes will raise NFIP premiums for borrowers in a range from significant to massive. As NFIP premiums become unaffordable and borrowers are unable to maintain NFIP coverage, servicers will force-place FPIF. Of course, this is no solution for borrowers since FPIF rates are also very high. Third, as lenders / servicers face greater penalties from Biggert-Waters for failing to ensure required flood insurance is in place, servicers will be likely err on the side of too many FPIF placements.

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[24] "FEMA, lenders wrongly charge Oregon homeowners flood insurance," April 5, 2013, *The Oregonian* at http://www.oregonlive.com/forest-grove/index.ssf/2013/04/fema_lenders_wrongly_charge_or.html

Borrowers faced with massive flood insurance premium increases are harmed not only because of the added costs to maintain their mortgage loans, but because the value of their property – and their ability to sell their home – is hugely diminished. I estimate, based on a borrower seeing an increase in NFIP premium from $600 to $6,000 annually will lose over $80,000 in home value.[25]

5.1 *Important Consumer Protections Not in Force until Mid-2014*

In January of this year, the Consumer Financial Protection Bureau promulgated a mortgage servicing rule which requires mortgage servicers to advance the funds for a voluntary insurance policy – instead of force-placed FPI – if the borrower has an escrow account in place and if payment of the voluntary insurance premium will keep the voluntary policy in force. This important provision does not, however, protect those borrowers who pay their insurance premiums directly to the insurer and who do not have an escrow account. This provision comes into force in January 2014.

The Biggert-Waters Act includes a provision requiring all lenders to create an escrow account for flood insurance, if flood insurance is required. That provision does not come into force until mid-2014. Together with the CFPB rule, this requirement for creating an escrow for flood insurance should greatly reduce the placements of FPIF. However, these consumer protections do not address the affordability issues associated with increased NFIP rates.

5.2 *Little Consumer Protection for Excessive and Unreasonable FPIF Rates*

For many years, the state insurance departments with responsibility to ensure FPIF rates are reasonable and not excessive failed to protect consumers from excessive rates and kickback arrangements between FPIF insurers and mortgage servicers. In recent years, the New York Department of Financial Services has been the leader in identifying and addressing FPI abuses and excessive rates. But, even the NY DFS's fine efforts are focused more on FPI hazard than FPI flood. The settlements between NY DFS and FPI insurers – which include rate filing and minimum loss ratio requirements – do not cover FPI flood. California and Florida are two other states which have taken action to address excessive FPI rates with California obtaining rate cuts of about 30% from FPI insurers. Other states have not taken action to force FPI rate cuts. And the majority of states have approved a new filing by Assurant which allows the servicer to choose the "commission" it wants to receive and increases the rates charged as the "commission" increases. Most state insurance regulators have approved this "pick-your-kickback" filing.

While the CFPB mortgage servicing rule addressed one aspect of unnecessary FPI placements, the rule does nothing to address unreasonable and excessive rates.

[25] The calculation is based on a 30-year mortgage at 5%. With a $600 annual premium, the borrower is paying $50 per month, which supports a loan amount of about $9,300. With a $6,000 annual premium, the borrower is paying $500 per month which supports a loan amount of about $93,000. With the $6,000 annual NFIP premium, a home buyer would be able pay about $84,000 less for the home and still have the same monthly payment as a home purchase with a $600 NFIP annual premium.

5.3 Fannie Mae Direct Purchase of FPI Best Option for Quick Consumer Relief

Earlier this year, Fannie Mae – after issuing a request for proposal in March 2012 – was about to purchase FPI and insurance tracking directly from FPI providers instead of reimbursing servicers. By purchasing the FPI and insurance tracking directly, Fannie would be able to create price competition for its business – and end the reverse competition that drives up FPI rates. Fannie estimated millions of dollars in annual savings to borrowers and taxpayers as a result of the direct FPI purchase program.

Just as Fannie was awarding the contract for the direct purchase FPI and insurance tracking, the Federal Housing Finance Agency (FHFA) – the agency that is the conservator for Fannie Mae and Freddie Mac – directed Fannie ***not*** to go forward. Instead, the FHFA left the existing reimbursement system in place. In March of this year, FHFA issued for comment a proposal that Fannie and Freddie would continue to reimburse servicers for FPI, but would not reimburse certain expenses, including commissions to servicer-affiliated insurance agents and proceeds from servicer-affiliated captive reinsurance agreements. FHFA has not taken action to date to finalize or implement those proposals and the status quo remains in place for FPI and Fannie Mae and Freddie Mac.

Because Fannie and Freddie own or guaranty over half of the mortgages outstanding today, action by Fannie and Freddie to address FPI flood can impact millions of borrowers. Consequently, FHFA is the singular position to address problems with FPI flood by:

1. Allowing Fannie (and Freddie) to implement the direct purchase FPI and insurance tracking program that was ready to go at the beginning of the year;
2. Addressing excessive retroactive billing by refusing to reimburse a servicer (or insurance tracking vendor) for any ***retroactive*** FPI charges for more than 60 days of coverage and for any period of time after 60 days from the lapse in coverage; and
3. Requiring servicers to advance payment for voluntary insurance policies that are at risk of cancellation for non-payment of premium instead of placing FPI, regardless of whether the borrower has an existing escrow account.

RESPONSES TO WRITTEN QUESTIONS OF SENATOR HELLER FROM W. CRAIG FUGATE

Q.1. We are trying to ensure that everyone has proper and affordable flood insurance coverage while also ensuring the fiscal solvency of the overall National Flood Insurance Program. The further development of the private flood insurance market could be a reasonable option for some Americans. Biggert-Waters specifically requires lenders to accept private flood insurance.

With the National Flood Insurance Program in such debt; would it be beneficial to have more private flood insurance policy options available to take some of the burden off of the NFIP?

With some NFIP rates increasing do you view private flood insurance as a viable tool for some consumers to find lower cost options?

How has FEMA been encouraging other regulators such as the Federal Reserve, FDIC, and OCC to issue guidance to industry lenders to accept private flood insurance policies as proper flood insurance coverage?

A.1. In regard to the current NFIP debt of $24 billion, private flood insurance could be both a benefit and a detriment. It could be a benefit in that private flood insurance could take on much of the current NFIP policyholder base and thus greatly lessen the amount of additional future debt that the Program might incur from future flood catastrophes. However, it could also be a detriment to the NFIP's ability to ever payoff its current $24 billion debt—fewer policyholders would reduce the amount of free cash flow the Program would experience during light loss years—it could be that in light loss years, the Program still wouldn't have enough cash remaining after paying claims and operating expenses to service the interest on the debt.

Private flood insurance would create competition. It is possible some homeowners could find lower cost options for flood insurance as a result of private market competition. Some homeowners may also find that private market rates are higher than the rates currently offered by the NFIP. At this point, we cannot anticipate how many could see lower rates due to private market competition.

FEMA has been meeting regularly with regulators discussing the implementation of the Biggert-Waters Flood Insurance Act of 2012 and other topics. On October 11, the Federal Reserve and other regulators released a proposed rule requiring the acceptance of private flood insurance policies. However, it is important to note that FEMA does not regulate mortgage companies and is not responsible for enforcing mandatory purchase guidelines for the NFIP. FEMA does not influence the actions that other Federal agencies are required to implement in the law.

Q.2. Starting in 2008, Douglas County in Nevada raised questions about FEMA's revised flood study and maps used in the Carson Valley after discovering improper hydrology methods were used. Douglas County tried to work with FEMA Region 9 during the formal appeal period, before any final decisions were made. FEMA's unwillingness to form a partnership with the County throughout the appeal process to address the inaccuracies left the County with no choice but to restudy the watersheds in question, with their own funds. Now for over the past 3 years, the County has undertaken a new substantial effort to collect more detailed and advanced scientific analysis. Due to the lengthy review process many property owners may be paying flood insurance premiums that are not based on accurate information.

If FEMA should find an entity like Douglas County was correct in their appeal—Can FEMA develop a formal protocol and set aside funds and provide financial reimbursement to affected property owners who unnecessarily paid higher rates and reimburse entities that individually funded restudying data?

If so—when will FEMA implement the program to make reimbursements?

How can FEMA improve and develop a more fair and unbiased technical appeal process where FEMA partners with communities toward the mutual goal of accurate floodplain mapping?

A.2. Section 100246 of the Flood Insurance Reform Act of 2012 authorizes FEMA to reimburse appellants (as defined under 42 U.S.C. §4104 (b) or (c)) in certain circumstances, but the law does not allow implementation of Section 100246 to occur until regulations are established. FEMA is prioritizing rulemaking activities in response to the Flood Insurance Reform Act of 2012 and other Congressional direction, but FEMA cannot begin reimbursing under this provision until regulations are completed. Therefore, there are no specific procedures applicable to Section 100246 and reimbursements currently in place.

FEMA's flood hazard mapping mission is to identify flood hazards, assesses flood risks, and partner with States and communities to provide accurate flood hazard and risk data to guide them to mitigation actions. FEMA strives to achieve these objectives via the Risk MAP program. For Risk MAP projects, an emphasis is placed on collaboration with local communities to leverage locally available data and identify the areas of greatest need for improved and updated floodplain mapping. Community and stakeholder involvement is an important component of the flood hazard mapping process. FEMA involves community officials and other stakeholders, including Federal agencies, in the planning stages of the mapping process and offers stakeholders and the public the opportunity to review and provide comments on mapping products. Also, in an effort to obtain all relevant information and ensure accurate study results, FEMA routinely holds public meetings for community officials and interested parties. The appeals process is available to communities who are not satisfied with the results of the subsequent mapping effort and who have scientific or technical data to support changes to the proposed map. FEMA has taken two critical steps in recent years to improve and enhance this appeal process.

First, FEMA expanded the appeals process to include appeals based on new or modified flood hazard information shown on a Flood Insurance Rate Map (FIRM). The appealable flood hazard information now includes additions or modifications of any floodplain boundary, flood zone designation, or regulatory floodway. Thus, more communities and individuals now have access to the appeal process.

Also, the use of a Scientific Resolution Panel (SRP) has been made available to communities in support of the appeal resolution process when conflicting scientific or technical data is submitted during the appeal process, and a mutual resolution has not been achieved. SRPs are panels composed of independent and unbiased panels of experts in hydrology, hydraulics, and other pertinent sciences established to review conflicting scientific and technical data and provide recommendations for resolution.

Q.3. Recently FEMA has been changing flood zones on U.S. Forest Service property or near foothill areas to Zone D. Zone D is used where flood hazards are "undetermined." Zone D can lead to the worst rate for homeowners who may want to purchase flood insurance.

How can FEMA improve its work with the U.S. Forest Service in understanding and evaluating U.S. Forest Service property areas around cities before Zone D is used?

A.3. Community and stakeholder involvement is an important component of the flood hazard mapping process. FEMA involves community officials and other stakeholders, including Federal agencies, in the planning stages of the mapping process and offers stakeholders and the public the opportunity to review and provide comments on mapping products. Also, in an effort to obtain all relevant information and ensure accurate study results, FEMA routinely holds public meetings for community officials and interested parties.

The initial coordination activities for a mapping study include an evaluation and prioritization of the community's mapping needs and the available funding, to establish the level of study undertaken in each area and options for mapping the areas. After these discussions, study efforts may need to focus on certain high-risk or high-population locations and delay the analysis of areas deemed less critical. This may result in areas of the FIRM being designated Zone D. A Zone D designation is used for areas where there are possible but undetermined flood hazards, as no analysis of flood hazards has been conducted. Flood insurance is not federally required by lenders for structures in Zone D because it is not a Special Flood Hazard Area. Although these areas are often undeveloped and sparsely populated at the time they are designated as Zone D, lenders may subsequently become aware that new development has increased the possibility of property damage from flooding and may require coverage as a condition of their loans. Flood insurance rates for properties in Zone D are commensurate with the uncertainty of the flood risk.

At any time, community officials can submit scientific or technical data to FEMA to support a flood zone revision. All requests for map revisions should be submitted through the Chief Executive Officer of the community, because the community must adopt any changes to the FIRM. To help communities compile the data required to support map revision requests, FEMA has developed a package of step-by-step instructions and forms. These forms and cost information for map revisions are available on the FEMA Web site at *www.fema.gov/mt-2-application-forms-and-instructions.*

In addition, there is a statutory 90-day appeal period whenever new or modified flood hazard information is shown on a preliminary Flood Insurance Rate Map and Flood Insurance Study report. When conflicting scientific or technical data is submitted during the appeal process, and a mutual resolution has not been achieved, the use of a Scientific Resolution Panel (SRP) has been made available to communities in support of the appeal resolution process. SRPs are panels composed of independent and unbiased panels of experts in hydrology, hydraulics, and other pertinent sciences established to review conflicting scientific and technical data and provide recommendations for resolution.

RESPONSES TO WRITTEN QUESTIONS OF SENATOR SCHUMER FROM W. CRAIG FUGATE

Q.1. Please provide a detailed timeline for implementing Sections 100205 and 100207 of the Biggert-Waters Act.

A.1. Below is a timeline of FEMA's plans for implement Sections 100205 and 100207 of the Biggert-Waters Act.

Section 100205

January 1, 2013:

At the time of policy renewal, Pre-FIRM rates increase 25 percent above the rates in effect for nonprimary pre-FIRM subsidized residences. FEMA will continue phasing out the Pre-FIRM subsidies for Pre-FIRM nonprimary residences by 25 percent every year until the property reaches full risk rates.

October 1, 2013:

Premium Increases: Pre-FIRM rates increase (including the reserve fund assessment) 25 percent above the rates in effect when the Biggert-Waters Act was enacted for policies issued on:

- Severe Repetitive Loss (SRL) properties
- Properties that have incurred flood-related damages in which the cumulative amount of NFIP claim payments exceeded the fair market value of the property (as a subset of SRL properties)
- Business properties

No Extension of Subsidy to New Policies or Lapsed Policies for Pre-FIRM Subsidized Properties in SFHAs and Zone D (New Business): FEMA is prohibited from offering Pre-FIRM subsidized rates for certain properties. As such, NFIP will no longer provide any extension of Pre-FIRM subsidized rates to new or lapsed Pre-FIRM properties/policies, or Pre-FIRM properties purchased after the date BW was enacted. These properties will be charged the full-risk premium rate. Unless eligible for Post-FIRM rating grandfathering, to determine the full risk premium rates for these properties, the policyholder must submit to his agent an Elevation Certificate (EC) and photos showing the elevation of the lowest floor compared to the base flood elevation. For the first year of implementation only, FEMA will use tentative or provisional rates while the policyholder obtains an EC. New business Pre-FIRM application submissions will use Post-FIRM rating procedures. The following Pre-FIRM properties/policies are impacted:

- Properties not insured by the NFIP as of the date of enactment of BW12.
- Policies under the NFIP that have lapsed in coverage as a result of the deliberate choice of the policyholder.
- Properties purchased after the date of enactment of the Biggert-Waters Act.

June 1, 2014:

For purposes of determining pre-FIRM subsidized nonprimary residences subject to 25 percent increases, the NFIP will revise the threshold for determining nonprimary residence from living in the residence less than 80 percent to 50 percent or less of the 365 days following the policy effective date.

January 1, 2015:

Rulemaking for Installment Plans: FEMA currently does not have authority to cancel a policy if a payment is missed; this authority is required before FEMA can offer installment plans. FEMA will initiate Rulemaking to change the flood insurance policy to allow cancellations for nonpayment of premium under Section 100205(d).

Substantial Improvement: FEMA will initiate Rulemaking to deny subsidized premiums to any property which, since the date of enactment of the Biggert-Waters Act, has experienced or sustained substantial improvement exceeding 30 percent of the fair market value of the property.

Section 100207

FEMA plans to implement section 100207 on October 1, 2014. Guidance about the change will be released to stakeholders at least 6 months prior to October 1, 2014.

Q.2 What outreach efforts, if any, has FEMA taken to inform property owners and other stakeholders about the implementation timeframe referenced in Question 1, and the associated premium increases resulting from those reforms? What outreach efforts, if any, has FEMA taken to inform property owners and stakeholders about the phase-out of grandfathered rates?

A.2. FEMA has undertaken a broad strategy to educate consumers, stakeholders, elected and appointed officials, and the media.

Because of the multiple audiences and multiple channels through which policyholders receive information, FEMA launched a comprehensive and aggressive strategy to educate lenders, realtors, insurance agents, local officials, elected officials and the news media. While FEMA depends on Write-Your-Own (WYO) insurance companies and others to communicate to policyholders about changes to the NFIP, FEMA is also using several BW12 specific Web sites, partner social media sites, FEMA social media, and FloodSmart.gov educational tools to reach out directly to policyholders and the public.

FEMA has worked closely with:

- Partners in the Insurance Industry, including Write-Your-Own companies and others, ensure agents have the tools needed to have important discussions. In many, if not most cases, an individual's insurance agent is their only link with the NFIP and it is critical that agents are fully educated on the changes and impacts of BW12.
  - FEMA has worked through our agent training programs, through our WYO partners, through industry associations and directly to agents via in-person conferences and distance learning to ensure our partner agents have the information and tools they need to properly communicate with policyholders.
  - FEMA developed materials that each policyholder will get in their annual insurance renewal information package describing the rate changes and encouraging them to talk more with their insurance agents.
  - FEMA developed a new suite of materials designed for agents to have the BW12 conversation when appropriate with their customers and a specialized tool kit with input from former agents on the tools needed to talk with customers.
  - Since May 2013, FEMA has trained more than 6,400 agents and 11,500 total insurance professionals (lenders, adjusters, realtors, others) on BW12 changes. FEMA is very near the goal of training 19,100 insurance professionals including 8,000 agents by the end of the calendar year. FEMA has also developed a new series of six training videos for agents specifically on BW12 which will are available online.
- FEMA has held conference calls and webinar training for staffs of more than 40 State insurance commissioners.
- FEMA conducted more than 10 in-person briefings for the National Association of Realtors at the national and State levels, and plan to conduct more training with them in the future.
- In May 2013, FEMA dedicated most of the educational portions of the annual Flood Insurance Conference to the implementation of Section 205.
- FEMA has conducted more than 50 visits to Capitol Hill to educate Members of Congress and staffs on BW12.
- FEMA has worked—through the Association of State Floodplain Managers—to reach out to local officials to educate them on BW12.
- FEMA met with nearly 1,000 Local floodplain managers at the ASFPM National Conference this year, providing them tools and resources to communicate changes to their communities. FEMA is also developing a suite of BW12 materials specifically for use by local officials.
- FEMA has met with disaster survivors in Colorado, in Sandy-affected areas in the Northeast, and Isaac-affected areas on the Gulf Coast to ensure that as they rebuild, they have the information they need to make the best rebuilding decisions for them.

- FEMA has conducted scores of in-person briefings and webinars through our HQ and regional offices to inform the public about Section 205 changes.

Q.3. How does FEMA plan to assess the "current risk of flood" as required under Section 100207 of Biggert-Waters for properties where FEMA does not have risk information in the form of an elevation certificate? What additional measures, other than an elevation certificate, if any, has FEMA considered in using to determine risk? If none, why?

A.3. Properties that currently do not have an elevation certificate documenting the necessary risk information to determine the current risk of flood, primarily elevation of the structure and the Base Flood Elevation will be required to obtain an elevation certificate. WYO companies are required to give notice that an Elevation Certificate is needed a minimum of 45 days prior to policy expiration, and WYO companies typically give notice 60–90 days prior to expiration.

FEMA is exploring other remote sensing options for determining the elevation of structures and Base Flood Elevations, but so far no methods have been tested and proven to sufficiently replace an Elevation Certificate completed by a licensed surveyor or engineer.

Q.4. What plans, if any, does FEMA have to work with localities to address unique housing stocks, such as those in dense urban areas?

A.4. Following major declared disasters FEMA puts in place plans to work with State and local officials on their recovery needs. While hurricane and flood disasters in dense urban areas are not new, the impacts of Hurricane Sandy on New York and New Jersey were large and significant to a variety of housing stocks from detached single family homes to high rise apartments, condominiums, and mixed use buildings. In support of its mission to create safer communities, enable individuals to recover more rapidly, and lessen the financial impact of disasters on the Nation, the Federal Insurance and Mitigation Administration (FIMA) implemented plans to assess the performance of damaged buildings, produce Recovery Advisories of recommended mitigation solutions to common observed damage trends, and roll out comprehensive training, education, and outreach to stakeholders of various housing stocks.

From early on in the disaster, FEMA put up a Web site with available Building Science Resources *http://www.fema.gov/building-science/hurricane-sandy-building-science-activities-resources* and added new resources as they became available. There are Recovery Advisories and Fact Sheets on residential building design and construction, foundation requirements, mechanical, electrical and plumbing systems, designing for higher flood levels, reducing interruptions to mid- and high-rise buildings and protecting building fuel systems. There are links to the extensive library of relevant free Building Science publications such as Technical Bulletins on the minimum building performance requirements of the National Flood Insurance Program (NFIP), Coastal Construction guides and fact sheets, Flood Retrofit and Utility Protection guides, building code requirements in flood hazard areas, and many other resources.

FEMA also collaborated with State and local official for specific activities focused on stakeholders of various housing stocks that were impacted. Examples include the *Hurricane Sandy Road to Recovery: A New Jersey Homeowner's Guide* (March 2013) *http://184.72.33.183/Public/Public__Documents/New__York__Homeowner__Guide.pdf* and the Housing Recovery Forums conducted throughout New York City where the public had access to mitigation and insurance specialists from FEMA and other Government agencies.

For technical audiences of builders, designers, and local officials, FEMA delivered numerous training classes in New York, New Jersey, and online covering housing related topics such as mitigation best practices, coastal construction and foundation design, floodproofing, flood codes and standards, retrofitting flood-prone buildings, and others. Thousands of attendees were reached through these efforts.

FEMA has also delivered presentations at several State realtor association functions, legal bar associations, civic groups, town hall meetings and Governor Cabinet meetings educating and informing citizens, elected and appointed officials and real estate professionals on an overall comprehensive mitigation strategy. This includes awareness of Hazard Mitigation grants for elevations, acquisitions, flood proofing, etc., and sound floodplain management principles that emphasize planning, risk assessment, and mitigation actions. Those plans continue with aggressive and comprehensive outreach campaigns to assist State Partners and the local floodplain mangers with technical assistance.

FEMA continues collaboration with HUD, State and local elected and appointed officials with disaster grant assistance programs including CDBG, 404 and 406 Hazard Mitigation for vulnerable housing stocks.

Q.5. What alternative mitigation measures, if any, has FEMA considered, evaluated, or adopted for premium credits other than home elevation or filling-in of basements for urban areas? If none, why?

A.5. Under the NFIP, all new and substantially improved/damaged residential structures must have the lowest floor elevated to or above the Base Flood Elevation (BFE). Any space below the BFE may be used only for parking, access, and storage. We have consistently found in our post-disaster assessments and flood insurance experience, that properly elevated residential buildings successfully minimize flood damages. Structures built to NFIP floodplain management requirements experience 80 percent less damage through reduced frequency and severity of losses.

> FEMA is in the process of finalizing Post-Sandy Recovery Advisory No. 7 (Reducing Flood Risk and Flood Insurance Premiums for Existing Residential Buildings) to provide guidance for providing protection to single-family homes and for a row house and town house to the BFE by modifying and strengthening their foundation to an open foundation or with foundation walls and converting the ground floor living area to an enclosure used only for parking, assess, and storage. The living area would be moved above

the BFE. If the building meets other NFIP requirements, the building can qualify for reduced flood insurance rates.

Since the NFIP's inception, all residential structures are required to be elevated above the BFE. Allowing people to sleep, recreate, or otherwise occupy the space, and place utilities and mechanical equipment below the BFE of a residential building of any type, places not only the building, but also lives at significant risk. From time to time, we have been asked to allow residential structures to be dry floodproofed. FEMA has not allowed residential structures to be dry floodproofed because of the concern for people living below the BFE, and because of the technically complex methods that dry floodproof nonresidential structures require.

Dry Floodproofing: Dry floodproofing requires an architect or engineer to certify that the building design, specifications, and plans meet the NFIP requirements. Under the NFIP, a dry floodproofed nonresidential structure in A Zones must be designed so that below the BFE, the structure and associated utilities and sanitary facilities are watertight with walls substantially impermeable to the passage of water. Making the structures watertight requires sealing the walls with waterproof coatings, using impermeable membranes, and/or a supplemental layer of masonry or concrete. Dry floodproofed buildings must be capable of resisting hydrostatic, hydrodynamic, and debris impact loads. An emergency operation plan must be in place, and there must be an inspection and maintenance plan to ensure that all elements of the dry floodproofing measures are in good condition.

The International Building Code and the International Residential Code do not allow dry floodproofed residential structures of any type. The American Society of Civil Engineers national consensus standard for Flood Resistant Design and Construction (SEI/ASCE 24-5) does not allow dry floodproofing for residential structures, and for nonresidential structures it is only permitted outside of "high risk" flood hazard areas that are subject to high velocity flows and wave action. State adopted building codes are also consistent with the International Codes with respect to elevation of residential buildings. In addition, the elevation requirements for residential buildings of any type are consistent with the mandates of Executive Order 11988—Floodplain Management that Federal agencies must follow for actions in the floodplain.

- *Dry Floodproofing Mixed Use Buildings:* In A zones, professionally designed buildings that have both commercial (nonresidential) and residential uses may be designed with floodproofing measures. However, all residential-use areas of the building must be above the BFE and the nonresidential portion of the building below the BFE must be floodproofed. While the NFIP regulations state that dry floodproofing of below-grade parking garages is allowed only for nonresidential buildings, FEMA generally applies the mixed use guidance to situations where the parking garage is below grade on all four sides with the next higher floor dedicated to nonresidential uses.
- *Insuring Dry Floodproofed Buildings:* The minimum requirement for floodproofing a nonresidential structure is to the BFE;

however, when a floodproofed nonresidential structure is rated for flood insurance, one foot is subtracted from the floodproof elevation. Therefore, the floodproofed nonresidential structure has to be floodproofed to one foot above the BFE to receive the same favorable insurances rates as a nonresidential building elevated to the BFE.

Options for Protecting Existing Residential Structures That Are Not Substantially Improved or Have Been Substantially Damaged

There are a variety of simple low-cost measures that can be implemented to minimize the effects of flooding. Although these measures are designed to reduce flood damages, they may not eliminate flooding altogether, and would not result in reduced flood insurance premiums. Examples of mitigation measures include:

- Relocate contents to a safer location, preferably above the BFE.
- Protect mechanical and utility equipment. Elevate as much of the utilities and mechanical equipment as possible to protect them from flood damage.
- Remove modern finished materials from basements or other areas below the BFE. Replace the finished materials with flood resistant materials.
- Install "mini" floodwalls to protect openings, such as window wells.

FEMA Grant Programs

FEMA Flood Mitigation Assistance (FMA) grants and Hazard Mitigation Grant Program (HMGP) funds may be available to acquire high risk structures as an alternative to elevation or other mitigation actions. These grant programs may also be available for mitigation activities for existing buildings that were not substantially damaged or not being substantially improved.

Q.6. What outreach efforts, if any, has FEMA taken to educate property owners in floodplains about the need for flood insurance?

What outreach efforts, if any, has FEMA undertaken to inform property owners in floodplains about new flood map development and the effects of such new maps on insurance rates? What plans, if any, does FEMA have to work with localities, like New York City, in evaluating new flood maps and educating property owners about rate increases?

A.6. In response to your questions concerning FEMA's outreach efforts in response to the implementation of the Biggert-Waters Flood Insurance Reform Act of 2012, we offer the following information and examples of how FEMA has educated local officials and property owners in areas experiencing flood map revisions, as well as the effects of flood hazard changes on insurance costs. We also outline steps FEMA has taken, and will continue to take, to work with local officials to inform communities about the effects of flood map updates.

Promotion of Flood Insurance on a National Basis

- *Alerting homeowners of the need for flood insurance is a multi-pronged effort accomplished through a number of channels and touch points with property owners.* FEMA actively engages with property owners and insurance agents through its Floodsmart (floodsmart.gov) public awareness campaign. Through television spots, billboard advertisements, an active Internet presence, direct mail, and numerous other channels, FEMA encourages ALL property owners to consider protecting themselves against the financially devastating effects of flooding by purchasing a National Flood Insurance Program (NFIP) policy. Floodsmart's integrated marketing campaign includes:
  - *Web site*: On FloodSmart.gov, the public can access information about the NFIP and flood insurance, types of flood risk, preparation and recovery, and mapping activities. Various interactive tools also connect users to local insurance agents to learn more about the user's unique situation and to obtain a flood insurance quote.
  - *Direct Mail:* FloodSmart sends more than 10 million direct mail pieces per year to homeowners, renters, and business owners across the Nation to increase public awareness of flood risk and the availability of flood insurance. The audiences include consumers without policies, consumers with policies that are about to expire, consumers who did not renew their policies, and small business owners.
  - *Direct Response Television, Print, and Radio Ads:* FloodSmart uses these mediums to inform consumers about the risks of flooding and to encourage them to learn more about their flood risk.
  - *Online Digital Banners:* FloodSmart creates digital banners that engage consumers and direct them to interact with additional tools and information on FloodSmart.gov.
  - *Industry Outreach:* FloodSmart engages insurance agents, insurance companies, and insurance trade associations and provides informational and marketing materials to help them explain flood risk and flood insurance requirements to all residents.
  - *Stakeholder Outreach:* FloodSmart engages with various stakeholder groups to share materials that will help them educate their communities about flood risk and flood insurance.
- *Local officials in NFIP participating communities are often a primary source of information to residents about flood risk, flood insurance, and flood map changes.* Nearly 22,000 communities have joined the NFIP. Each one has made a commitment to maintain Flood Insurance Rate Maps (FIRMs) developed by FEMA for public inspection. These flood maps form the basis of locally adopted floodplain management ordinances and are a catalyst to promote flood insurance. The map is adopted by the community, and the community has a responsibility to alert residents of proposed and adopted changes. When a new map is prepared or an existing map is revised, FEMA, with the

assistance of the local community, conducts a series of meetings to share that information with the public. The new map's effect on flood insurance is among the primary topics discussed during these meetings.

Some communities have chosen to join the NFIP Community Rating System (CRS) and can receive flood insurance premium discount credits for promoting flood insurance. 1,273 communities have joined the CRS and implement floodplain management programs that exceed the Federal NFIP minimum standards. As a CRS participant, these communities commit to implementing specific practices which the NFIP recognizes by giving credit points. Ninety percent, or 1,143 CRS communities, receive specific credit for public outreach activities that include reference to the importance of flood insurance.

By offering CRS credit, the NFIP has created an incentive for communities to promote the importance of purchasing of flood insurance. New York City does not currently participate in the CRS, but since Hurricane Sandy, is actively researching the possibility of joining.

- *FEMA has worked closely with partners in the Insurance Industry, including Write-Your-Own companies and others, to ensure agents have the tools needed to have important discussion with property owners.* In many, if not most cases, an individual's insurance agent is their only link with the NFIP and it is critical that agents are fully educated on the changes and impacts of BW12.
  - FEMA has worked through our agent training programs, through our WYO partners, through industry associations and directly to agents via in-person conferences and distance learning to ensure our partner agents have the information and tools they need to properly communicate with policyholders.
  - FEMA developed materials that each policyholder will get in their annual insurance renewal information package describing the rate changes and encouraging them to talk more with their insurance agents.
  - FEMA developed a new suite of materials designed for agents to have the BW12 conversation when appropriate with their customers and a specialized tool kit with input from former agents on the tools needed to talk with customers.
  - Since May 2013, FEMA has trained more than 6,400 agents and 11,500 total insurance professionals (lenders, adjusters, realtors, others) on BW12 changes. FEMA is very near the goal of training 19,100 insurance professionals including 8,000 agents by the end of the calendar year.
  - FEMA has also developed a new series of six training videos for agents specifically on BW12 which will are available online.
- *Realtors and lenders are another key source of floodplain information for a property owner.* The Flood Disaster Protection Act of 1973 and the National Flood Insurance Reform Act of 1994

made the purchase of flood insurance mandatory for federally backed mortgages on buildings located in Special Flood Hazard Areas (SFHAs). It also affects all forms of Federal or federally related financial assistance for buildings located in SFHAs. Following Hurricane Sandy, FEMA representatives met with and presented information on the updated flood hazards in New York and New Jersey to area realtors.

- *The flood insurance requirement applies to secured mortgage loans from key financial institutions.* These include organizations such as commercial lenders, savings and loan associations, savings banks, and credit unions that are regulated, supervised, or insured by Federal agencies such as the Federal Deposit Insurance Corporation and the Office of Thrift Supervision. It also applies to all mortgage loans purchased by Fannie Mae or Freddie Mac in the secondary mortgage market. Federal financial assistance programs affected by the laws include loans and grants from agencies such as the Department of Veterans Affairs, Farmers Home Administration, Federal Housing Administration, and the Small Business Administration, as well as FEMA, in the case of some disaster assistance programs. Therefore, communicating the mandatory purchase requirement to property owners is the obligation of a number of agencies and businesses.
- *FEMA offers additional vehicles for communicating about flood insurance.* FEMA's Citizen Corps program promotes a holistic approach to preparedness, and recommends that individuals who live in areas of flood risk contact an insurance agent to learn more about flood insurance. The Government Delivery broadcast email subscriber service reaches more than 1,000,000 subscribers with information on flood insurance.

Promotion of Flood Insurance on a Regional Basis

- *Examples of FEMA's latest outreach efforts can be seen in those communities most affected by Hurricane Sandy in New York and New Jersey.* In the storm's aftermath, FEMA immediately began creating advisory mapping products to assist communities in the rebuilding process, and to ensure that new and repaired structures would be significantly stronger in the face of future storms. FEMA explained to officials and residents of the affected communities that building or repairing structures to be stronger and above flood levels will help minimize flood insurance costs. The advisory products, most recently the preliminary work maps, will be incorporated into new FIRMs for the communities. FEMA also attended numerous Housing Recovery Forums around New York City to provide residents with recovery information and give participants an opportunity for one-on-one discussions with experts on rebuilding and flood insurance.
- *FEMA presented the new flood hazard information through community meetings, Webex trainings, and the region2coastal.com Web site.* Along with explaining the science behind the advisory products, the region2coastal.com Web site also provides a searchable mapping tool that allows property

owners to determine how the revised maps will affect their property's flood hazard designation once the maps are finalized. The region2coastal Web site provides multiple ways for residents to ask additional questions. FEMA also established a flood insurance hotline for residents to call and speak directly with flood insurance experts about any questions or concerns they may have. Through each of these tools, FEMA shares information and recommendations on how to reduce flood insurance rates by incorporating safer building standards into new and repaired buildings.

- *As communities proceed from preliminary FIRM to final FIRM, FEMA will first host meetings with community officials to review the preliminary FIRMs, and then coordinate with community officials to conduct separate public open house meetings.* During these open house meetings, the general public and other interested parties may view the preliminary FIRMs and ask questions about the effects the flood maps will have on flood insurance rates, the flood hazard mapping process, and opportunities to mitigate flood risk.

FEMA's Outreach Efforts With New York City

New York City, as a participant in FEMA's Cooperating Technical Partner program, is pursuing a public information campaign on flood risk and flood insurance, and a consumer education program to assist residents with flood preparation/planning, mitigation, and insurance.

New York City and FEMA Region II representatives are working together to:

- improve targeted outreach strategies to those communities most affected by the new maps; and
- inform public decision makers of the importance of the maps for planning, emergency management, guiding development toward safer areas, ensuring compliance with building codes and floodplain management requirements, and helping residents and businesses make sound development decisions.

Q.7. What is the status of FEMA's mandated study on evaluating negatively elevated buildings?

A.7. FEMA has awarded two studies to the National Academy of Sciences to evaluate negatively elevated buildings.

The first is the affordability study mandated by the Biggert-Waters Flood Insurance Act of 2012 under section 100236. This study is being conducted in two phases. The first phase is to scope the study and determine the appropriate methodology given the lack of risk information referenced in your question 997198. This first phase has been awarded with a period of performance ending March 31, 2015.

The second study is a voluntary study by FEMA to determine what improvements can be made to the rating criteria and methods used for negatively elevated buildings. This study has also been awarded and has a period of performance ending February 28, 2015.

RESPONSES TO WRITTEN QUESTIONS OF SENATOR TESTER FROM W. CRAIG FUGATE

Q.1. There's been some concern at the State level over whether Montana will be able to compete with some of the larger States for mitigation grants, which is going to affect people making adjustments to their structures. How can we ensure that Montanans and other folks from less populated States are given their fair shake in this process?

A.1. Prior to the passage of the Biggert-Waters Flood Insurance Reform Act of 2012 (BW12), the Flood Mitigation Assistance (FMA) program allocated funds to each State or Territory based on the total number of National Flood Insurance Program (NFIP) insurance policies and the total number of repetitive loss properties within the State or Territory. With the exception of a $100,000 allocation per State or Territory for the Planning portion of a Hazard Mitigation Plan, BW12 removed this allocation process. Therefore, each State and Territory, regardless of size or population, has the ability to apply for a grant during an open Hazard Mitigation Assistance application cycle.

The FMA program will continue to fund discretionary mitigation activities in States and local communities. BW12 eliminates the Severe Repetitive Loss (SRL) and Repetitive Flood Claims (RFC) programs and adds funding for the mitigation of SRL properties to FMA. FEMA prioritizes FMA applications based on the percentage of SRL structures that are mitigated by the proposed project. Properties included in a FMA projects must be NFIP-insured at the time of the application submittal. Flood insurance must be maintained through completion of the mitigation activity and for the life of the structure.

States may also submit projects under the disaster Hazard Mitigation Grant Program that address flood risk or other all hazard risks.

RESPONSES TO WRITTEN QUESTIONS OF SENATOR TESTER FROM ALICIA P. CACKLEY

Q.1. I know you've done a lot of work analyzing this legislation and figuring out where there are still issues, as outlined in your testimony. FEMA has publicly shared its specific rating guidelines on how it calculates risk. In your testimony, you cited an October 2008 study conducted by GAO that concluded that FEMA's rate-setting process excluded ongoing and planned development, climate change, and long-term erosion trends. Do you think FEMA has actively worked to incorporate these changing conditions into its rate formulas, as mandated under Biggert-Waters? How can they stay on top of these highly unpredictable factors?

A.1. As of June 2013 the Federal Emergency Management Agency (FEMA) was making changes to its rate-setting process as a result of the Biggert-Waters Flood Insurance Reform Act of 2012 (Biggert-Waters Act). Among other things, the act requires FEMA to set premium rates that fully reflect the risk of losses from flooding and to include many of the elements we recommended in our October 2008 report (GAO-09-12). More specifically, we recommended that FEMA take steps to ensure that its rate-setting methods and data would result in full-risk premiums rates that accurately reflect the risk of losses from flooding. We noted that these steps should include verifying the accuracy of flood probabilities, damage estimates, and flood maps; ensuring that the effects of long-term planned and ongoing development and climate change were reflected in the flood probabilities used; and reevaluating the practice of aggregating risks across zones.

According to FEMA officials, the agency revised damage calculations for flooding events that only reach the foundation of a structure, reassessed and decided to continue the practice of nationwide average premiums, and performed a study to assess the long-term impacts of climate change. FEMA's ongoing efforts include analyzing water-depth probability curves for the various zones, analyzing the extent of zone grandfathering, and piloting studies to determine structure elevation and flood depths for various periods.

We have not conducted the work necessary to answer how or if FEMA plans to periodically reassess ongoing and planned development, climate change, and long-term erosion trends.

Q.2. Flood insurance has populated the GAO's High Risk List now for 7 years. Based on your research, do you think the reforms in Biggert-Waters will be enough to get the NFIP off that list? As currently drafted, how many years do you think that would take?

A.2. We placed the National Flood Insurance Program (NFIP) on our High-Risk list in 2006 due to the program's financial instability and FEMA's operating and management challenges. FEMA has begun implementing some of the changes included in the Biggert-Waters Act, such as the creation of a reserve fund for catastrophic losses and elimination of subsidies for some properties. These are important first steps for addressing NFIP's financial challenges. FEMA also has begun to address some of the management challenges we identified, such as strategic planning.

However, we do not yet know the extent to which the changes FEMA has been making in response to Biggert-Waters will improve the long-term financial stability of NFIP. As you know, many of the premium rate increases resulting from the act are set to be phased in over several years. We understand the financial challenges property owners can face, and note that delaying rate increases will add to the time it takes to reduce the financial exposure NFIP presents to the Federal Government.

In order for NFIP to be removed from the High-Risk List, it will be important to place the program on a sound footing, both financially and operationally. For example, FEMA will need to fully establish the reserve fund and implement the premium rate changes begun in response to Biggert-Waters and continue to address management challenges, such as updating NFIP policy and claims information systems and improving oversight of contractors.

Finally, we cannot estimate how long it will take FEMA to address the management and operational challenges that we have identified that also contribute to NFIP remaining on the high-risk list. However, we are in periodic contact with FEMA about the status of open GAO recommendations.

ADDITIONAL MATERIAL SUPPLIED FOR THE RECORD

STATEMENT OF THE INDEPENDENT COMMUNITY BANKERS OF AMERICA, SUBMITTED BY SENATOR MERKLEY

ICBA
INDEPENDENT COMMUNITY BANKERS of AMERICA®

September 18, 2013

NFIP Changes Pose a Serious Threat to Homeowners and the Housing Market

On behalf of the nearly 7,000 community banks represented by the Independent Community Bankers of America (ICBA), thank you for convening this hearing on "Implementation of The Biggert-Waters Flood Insurance Act of 2012: One Year After Enactment." ICBA is pleased to have this opportunity to submit a statement for the record. ICBA has serious concerns about the impact of drastic and unsustainable flood insurance premium increases on homeowners, local housing markets, mortgage lenders, and the broader economy. Pending premium increases are already depressing home values and freezing the housing market in certain communities, and the impact will only get worse as the law continues to be phased in. ICBA urges the Senate to expeditiously pass legislation to stop premium increases until the Federal Emergency Management Administration (FEMA) completes its study on affordability, as mandated by the Biggert-Waters Flood Insurance Act ("Biggert-Waters").

ICBA does not believe Congress intended the rapid dislocation that premium increases of such magnitude will bring. In some cases, premiums will increase by 500 percent or more and the phase-in schedule, though helpful, will do little to offset the impact. Premiums of $25,000 a year or more on modest single family homes are disproportionate to the risk and to the value of the home. Properties built to code under then-current flood maps ("grandfathered properties") as well as older properties that pre-date the NFIP ("subsidized properties") but have never experienced a flood will be subject to these premium increases. Moreover, new flood maps do not take into account a community's flood mitigation efforts, including levees and pump systems paid for by the community, and therefore mandate unnecessary elevations. If no action is taken, dramatic rate increases will:

- Price people out of their homes. New premiums will simply be unaffordable for many middleclass homeowners.
- Cause homeowners to drop coverage and thereby undermine the NFIP.
- Destroy home values. Home values are already dropping in certain communities in anticipation of the rate increases. For example, the St. Charles Parish, Louisiana Tax Assessor estimates new premiums will depress home values by 18 to 30 percent. In many communities, the housing market recovery could be abruptly reversed.
- Undermine the value of mortgage collateral, drive mortgages into delinquency, erode bank capital, and thereby depress new lending.
- Curtail property tax revenues local governments rely on to fund schools and other essential services.
- Depress consumer spending and economic growth.

The impact of rate increases will be seen not only in coastal communities but in any community located near a river. Broad swathes of the country will be impacted.

One Mission. Community Banks.

1615 L Street NW, Suite 900, Washington, DC 20036 ▪ 202-659-8111 ▪ Fax 202-659-9216 ▪ www.icba.org

We urge Congress to act expeditiously to amend the Biggert-Waters Flood Insurance Act. ICBA supports all viable solutions to provide immediate relief for policy holders. We are grateful to Senators Mary Landrieu (D-LA) and David Vitter (R-LA) for their leadership on this issue and support their legislative efforts. In particular:

- S. 996, sponsored by Senator Landrieu, would create an exemption from new risk-based premium rates for properties purchased before the enactment of the Flood Insurance Act of 2012.
- An amendment sponsored by Sens. Landrieu and Vitter would provide a three-year delay in changes to flood insurance rates for grandfathered properties and would accelerate the FEMA affordability study. Senator Landrieu subsequently amended the Senate Department of Homeland Security Appropriations Act to prohibit the use of funds by FEMA for one year to implement changes to flood insurance rates for grandfathered properties.
- The Responsible Implementation of Flood Insurance Reform Act (S. 1098), sponsored by Senator Vitter, would prohibit premium adjustments based on incomplete or inaccurate maps and require FEMA to recognize community-funded flood systems built without federal dollars, among other changes.

In addition, the House-passed Department of Homeland Security Appropriations Act contains an amendment, sponsored by Rep. Bill Cassidy (R-LA), that prohibits FEMA for one year from using funds to implement changes to flood insurance rates for grandfathered properties. That both the House and Senate versions of the Department of Homeland Security Appropriations Act contain premium increase-delay amendments is evidence of strong bipartisan and bicameral support for that policy.

ICBA urges this Committee and the Senate to act, without delay, as premium increases for additional properties go into effect this October 1 and in 2014. While ICBA supports reforms to strengthen the NFIP, the impending changes will only weaken the NFIP by driving down participation. Premium rate shock will endanger homeowners, mortgage lenders, local governments and the broader economy.

Thank you for your consideration.

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STATEMENT OF REPRESENTATIVE C.W. BILL YOUNG OF FLORIDA, SUBMITTED BY SENATOR HELLER

Statement for the Record
Committee on Banking, Housing, and Urban Affairs
Subcommittee on Economic Policy
U.S. Senate
Hearing on Implementation of the Biggert-Waters Flood Insurance Act of 2012: One Year After Enactment
September 18, 2013
Representative C. W. Bill Young, Florida 13th District

Chairman Merkley, Senator Heller, and distinguished Members of the Committee,

I want to thank you for the opportunity to submit this statement on the devastating impact that provisions in the Biggert-Waters Flood Insurance Reform Act of 2012 will have on many communities throughout the United States, including those in the 13th district of Florida, which I have the privilege to represent. While I support the goal of getting the National Flood Insurance Program (NFIP) back onto sound financial footing, the current reforms are being implemented in a way that could lead to even greater instability in the program and run counter to its original goals.

Flooding is the nation's number one disaster and affects every state, but most private insurance companies do not offer their own flood insurance and standard homeowner insurance policies do not cover flooding. Recognizing this problem, in 1968, Congress passed the National Flood Insurance Act to enable people to insure against the risk of flood and reduce the burden on the taxpayers of compensating victims after flood disasters. The purpose of the program was explicitly designed to "pool risks, minimize costs, and distribute burdens equitably among those who would be protected by flood insurance and the general public" (42 U.S.C. 4001). Since anyone buying a home or building in high-risk flood areas with mortgages from federally regulated or insured lenders are required to have a supplemental flood policy in order to receive approval for their mortgage, buyers and sellers became dependent on the NFIP and its affordability.

Until 2005, premium income and fees were enough to cover the NFIP's expenses, claims payments, and repayment of any amount that needed to be borrowed from the Treasury. However, following the devastation of Hurricanes Ike and Katrina, the program become mired in debt, which it has been unable to repay in the years since. The Congress struggled with how to resolve the solvency of the NFIP and from 2008-2013 the program operated on short-term extensions that caused great instability in housing markets across the country that relied on this coverage, especially during the four times that the program authority was allowed to lapse. In finally providing for a five-year reauthorization of the NFIP, one that promised to stabilize the program and enable it to repay the debt to the Treasury, we thought that we were helping those who need the program. We were wrong. Instead, over one year later, NFIP policyholder and Members of Congress are finally seeing how the changes to the program will be implemented and for many the picture is grim.

A great number of my constituents have been contacting me in the past few months expressing concern, outrage, and fear at the devastating affect that the premium increases, mandated in the

2012 authorization, will have on their homes and livelihood. I have included some of their letters with my statement. Many homes in Pinellas County and throughout the country were built prior to the creation of the NFIP and the adoption of current flood maps, and, as such, were built below current flood elevation standards. Prior to the 2012 changes, flood insurance was affordable for those who owned these homes and businesses because they were able to purchase flood insurance based on the risk of flood that was in effect when the structure was built. Now, these affordable rates are being eliminated and, for some, the new rates are absolutely astounding. I have been contacted by constituents who are being sent notices by their insurance agent of annual flood insurance rates increasing from $1,000-$2,000 to $10,000-$20,000 per year, with a few instances of policies in excess of $20,000. This is just for a flood insurance policy and does not include traditional homeowners insurance, which further drives up the annual cost for these owners. Even worse, a large number of the homeowners I represent are seniors who carefully planned and budgeted for their retirement and are now terrified that they will lose their homes and retirement savings. For them and all the rest of those that I represent, these rates are unrealistic and unsustainable and are already having a negative impact on home and property values.

In my district, which encompasses the majority of Pinellas County, Florida, there are more than 50,000 subsidized flood policies in place, which is 35 percent of the 142,000 total subsidized NFIP policies in the county. I have been told this is the largest number of subsidized policies in a single county in the United States. In total, subsidized policies account for 19 percent of all flood insurance policies. Of these 19 percent, there are five percent of policyholders with subsidized policies for non-primary residences, businesses, and severe repetitive loss properties who will begin to see a phased-in premium increase of about 25 percent per year, starting this year, until their policies reflect the true risk premium. Another 10 percent of these subsidized flood policies that cover primary residences will remain subsidized unless the property is sold or the policy is allowed to lapse, however, these homeowners will still see a 10-20 percent increase in their policy each year, until they reach actuarially sound rates. I can tell you that home sales of these properties have almost completely halted, with prospective buyers backing out of offers once they are quoted the price for flood insurance coverage. Those trying to sell their property are now considering just walking away from their now unsellable home, which risks destabilizing the fragile recovery of the nation's housing market.

Even worse, those who bought their home starting July 6, 2012, will see an immediate increase in their policy to the full risk rate the next time their policy is up for renewal. Many of these homebuyers were not told of this when they bought their policies and are now looking at dramatic increases that may lead to them dropping their policies rather than renewing. As these increases begin to take effect, more and more people may begin to drop flood insurance coverage, a problem that already plagues the NFIP as highlighted by Hurricane Sandy where the majority of homeowners did not have flood insurance coverage in place when the storm struck. Already, studies show that many individuals living in special flood hazard areas do not maintain their flood insurance policies but lack of coverage is widespread, with the Insurance Information Institute estimating that only 18 percent of Americans have flood insurance. The situation will only get worse as these new rates are implemented and dropped policies could increase the need for FEMA assistance after a disaster.

This change has caught policyholders unaware and unable to even consider steps to mitigate their risk prior to implementation of the higher rates. As FEMA continues with the planned adoption of new rate maps in many communities throughout the United States, the situation will only get worse as individual flood risk changes and new locations are mapped into special flood hazard zones. Homes built to current elevation standards may see changes to their flood risk, which will lead to increased cost of flood insurance coverage. Communities that invested in flood mitigation may be told that their efforts were not enough to meet the new FEMA standards.

These problems are not addressed through the Biggert-Waters reform bill and the lack of focus on continued affordability is disturbing. Section 100236 of the law requires a study on the affordability of flood insurance that was to be submitted to the Congress 270 days after the date of enactment. This deadline has passed and the affordability study has not been submitted. FEMA indicates that this study will not be completed until at least 2015, which will be too late to help owners facing unaffordable premiums and considering a short list of options for dealing with the increase.

Continued affordability must be a consideration when implementing new premiums for the NFIP. We must find a way for owners to maintain their flood insurance coverage and mitigate these massive premium increases. Several pieces of legislation have been introduced with a variety of proposals to address this issue and the Congress must decide the best path forward, however that will take time. Unfortunately, there is not enough time to fully consider these options prior to implementation of these new rates, which is why I support efforts to delay implementation of the law until we receive the affordability study and have time to consider options to sustain the NFIP, while still ensuring that homeowners are able to afford coverage.

Again, thank you for reviewing this statement and for seeking solutions to assist policyholders facing these dramatic increases. I stand ready to work with my colleagues in both the House and the Senate to ensure the continued affordability of coverage in the NFIP.

Insertions to be Included with Statement for the Record

Letter from the Pinellas County Board of County Commissioners:

> To the Committee on Banking, Housing and Urban Affairs Subcommittee on Economic Policy,
>
> As Pinellas County Florida will be the most impacted area in the country, with more than 50,000 properties with subsidized flood insurance policies, we strongly urge you to delay the implementation of the Biggert-Waters Flood Insurance Reform Act of 2012.
>
> If the Act is not immediately delayed or amended, the economic impact to our area and others would be devastating. Pinellas County property owners will face unreasonable and unaffordable rate increases with little or no time to prepare. The real estate market will collapse, economic growth will be stifled and reversed and our number one industry, tourism will be in turmoil.

We recognize that the current program is not sustainable; however, it is critical that adequate time be allotted to fully review the National Flood Insurance Program and consideration be given to slow the rate of increase, extend grandfathered provisions and fully assess the impacts of the Biggert-Waters Flood Insurance Reform Act of 2012.

Sincerely, the Pinellas County Board of County Commissioners

Letter from the Barrier Islands Governmental Council (BIG-C):

Dear Representative Young,

Please see the letter below which was sent to Florida's two United States Senators.

> The Barrier Islands Governmental Council, comprised of municipalities along the beaches of Pinellas County, is concerned over the impact full implementation of the Biggert-Waters Act of 2012 will have on its individual communities, as well as to other cities across Florida and the country.
>
> Among Florida's 67 counties, Pinellas County will be the hardest hit by the changes mandated by Biggert-Waters. There are now over 50,000 subsidized flood insurance policies in the county that could face substantial rate increases. The U.S. House of Representatives has passed a measure that would postpone for at least one year the act that, if not amended, will decrease property values, stop real estate sales, and cripple Florida's economy.
>
> Home affordability may soon become but a memory washed away by policy form and fiscal discipline in the name of Biggert-Waters. Consequently, it is respectfully requested that you take an active role in delaying Biggert-Waters. Please support immediate consideration of the House bill and any measure that would slow the rate of increase, extend grandfathered provisions, encourage mitigation programs, and assess better the full impact of Biggert-Waters. Otherwise, the housing market in our cities will collapse, and that consequence will affect our ability to operate programs and services at current levels.
>
> Thank you for your attention to this issue, and with warm, personal regards, I am
>
> Sincerely,
> George N. Cretekos
> President

Letter from a Pinellas County Realtor:

Dear Representative Young,

I would like to bring to your attention the repercussions of the upcoming implementation of the Biggert-Waters Act for the residents of Pinellas County. Using my own home as an example, as it is representative of 1,000's of homes in Pinellas County, this Act of Congress, if implemented as written, will make my home and 1000's of others in your constituency virtually un-salable. My home was built in 1962 so it is a home that is receiving "subsidized" rates more commonly referred to as "PRE-firm" rates. The Biggert-Waters Act would trigger "actual risk rates" if I were to sell my home. My home, built prior to there being any flood program, sits at approximately 6 feet above sea level. The current "base flood elevation" in Treasure Island is 12 feet, making my home 6 feet BELOW the base elevation.

Being an insurance agent, I asked my flood writer to give me an anecdotal quote for a new owner if I were to sell my home. My current flood rate is approximately $2,500 per year, the quote for a new buyer would be almost $24,000 per year. My home just became unsalable. Multiply this scenario by 1,000's of homes in Pinellas County AND 10's of thousands around Florida and the impact on our real estate market will be nothing short of devastating. I am hoping that further review will lead to amending the Act as to reduce the impact on our area. I understand the need to reduce the debt of the program, but do not believe that this Act will have ANY of the intended results. I thank you for this opportunity to express my concerns.

Anita

Letter from a Pinellas County Homeowner:

Dear Representative Young,

We bought our intra coastal home in December 2012 and just found out that our flood insurance rate will jump from $2,500.00 per year to about $12,000.00 per year. When we bought this home, we did not know that this flood insurance was subsidized through FEMA, nor were we told by anyone or any agency that our cost would be about $12,000.00 after the first year. We did due diligence when we bought this home so we would know our total costs and affordability. This never entered into our equation. We are retired and on a tight budget and cannot afford this. Unfortunately, we may not be able to sell this property either and are stuck. This is one of my worst life decisions I ever made. We feel so blindsided by all of this, as I am sure everyone else does. We need your help as our representative. Thank you

Cynthia

Letter from a Pinellas County Homeowner:

Dear Representative Young,

I am writing you about my concerns and opposition (in its current form) to the Flood Insurance Reform Act of 2012 (Biggert-Waters Act). As my representative, I would like you to take an active role in the repeal and/or modification of this legislation. Please take a bipartisan approach because the impact of this legislation affects all voters.

I purchased my home, which is my primary residence in North Redington Beach on June 19th, 2013. (1957 pre-FIRM in AE zone) Leading up to the purchase of my house, the flood insurance reform act of 2012 was not even on my radar screen. I never heard of it. It came up first when my Florida real estate agent mentioned to me that she recently learned of new legislation, which could possibly increase the cost of flood insurance. I talked with some insurance folks and got the typical answers ranging from the sky is falling, meaning polices are going up from $1,800 to between $10,000 and $25,000 to more practical answers like, fixes are in the works and you will see some reasonable rise (20%) in insurance costs but nothing catastrophic like some people were saying. This is the type of advice I was getting with one of the largest financial transactions most people every make buying a house. So how do you make a decision in that environment?

Well, I tried to gather as much information on my own as I could, mostly opinions on the internet. At one point, I actually considered breaking my real estate sales contact because I just could not clearly understand what the future would be regarding my flood insurance cost. Had I broken my contract and taken the ultra-conservative course, I would have lost my earnest money of $10,000, plus all the other complication that would have come with that course of action. I had to make a big decision with totally inadequate information. I was not happy with this because of all the paperwork the government and lender requires for mortgages (HUD statements, etc) nothing stated my government mandated flood insurance (because I have a mortgage) may reach $2,000 or more a month. There were plenty of warnings about my interest rate cost and lots of protections for the lender. It seems strange the government and my lender were so concerned I might not be able to pay my mortgage but it was taken for granted I can afford future mandated flood insurance.

I still cannot get an accurate estimate of what my flood insurance might be in the future. I am basing everything on what I can find out on my own. Because my home is a pre-FIRM home in an AE zone, I do not know if my rates will go up immediately or gradually. That is because I do not know what the cutoff date for recent purchases as described in the legislation was. (There was not a date specific from what I can tell) If my insurance increases from $1,800 to between $10,000 and $25,000 it will be a financial disaster. Between property taxes and insurances (property, wind, flood) my escrow account payment could be over $2,000 a month. If this were the case, I would have to put my house up for sale. I would not be able to afford this during retirement and it would certainly be a large financial burden. The most frightening part would be selling the house for less than I owe on its mortgage. A real possibility because housing prices in the flood zones will definitely go down under this legislation.

I have not studied enough, nor do I have the benefit of a sub-committee and staffers to advise me on how on to fix the problems associated with subsidized government flood insurance, but I will give you some ideas I think might be reasonable to start with.

1. The most important thing you can do now is to delay the enactment of this legislation until we all can understand its potential impact on individuals,

families, businesses and the economy at large. Sometimes trying to do the right thing can cause bad unintended consequences. I think that is the situation here. Congress did try to fix a big problem but in the process is going to cause more long-term harm than good. That is what I think about this piece of legislation.

2. Look at difference sources of revenue to maintain lower cost flood insurance besides just passing all the cost onto the homeowners. Many of the places impacted are tourist havens. What about a special tax on tourism in those areas or some other creative way.
3. The property I own has never been flooded, yet it is in the AE zone so I get terrible rates. Ask how the risk can be reasonably accessed. One price for all? I don't think so. If there have been no claims on the property, this must be reflected in the rates.
4. Look at why flood insurance is mandatory for housing that carries a government backed guarantee mortgage. (Why does government have to guarantee all mortgages anyways) Maybe the risk can be shared some other way. Most people today cannot pay cash for a mortgage therefore you are forced into buying flood insurance. What about working with lenders who give mortgages in high risk zones to charge a slightly higher interest rate and to fund the government subsidized insurance pool. The lenders need to have some risk in this also.
5. For individuals like myself and others who are facing unbelievable flood insurance increases because we have purchase pre-FIRM houses, provide direct grants for practical ways to protect against floods. Raising a structure is not always practical and cost effective. (i.e. a cement slab home) When it's not, how can homeowners be assisted.
6. Consider allowing people to self-insure some risk for flooding.

The above are just some of my current ideas. Making the required changes to the legislation will take some careful thought and serious consideration on the impact to real individuals. You need to realize how much of an impact this legislation is going to have on people like myself and others. For my current situation I am not sure what I am going to do next. Sit tight and see what happens or put my home up for sale and cut my losses. I hope congress can come up with a solution for all our interests. I am asking for your help to delay/modify/change this legislation.

Respectfully submitted,

David

Letter from a Pinellas County Homeowner:

Dear Representative Young,

Please try everything you can to save our homes from these crazy high insurance rates. I have lived in my waterfront property, which was built in 1962, I have never had any damage from floods or winds. I understand that some areas are more likely to have damage from flood and wind, but areas that have not should not suffer the consequences of higher insurance costs, to offset areas that are hit repeatedly. People that have lived n their houses for years and are on fixed income cannot afford to pay for these exorbitant insurance rates.

Donna

Letter from a Pinellas County Realtor:

Dear Congressman Young,

If this bill is allowed to go forward it will have devastating impact on the real estate market not only in Florida but around the country in coastal communities. Florida, as you know, has paid its fair share of premiums having paid in about 4 times more than claims collected in recent years. The increase for flood insurance rates would be cost prohibitive to home buyers and would immediately start a rapid decline in the real estate market and just at a time that we are seeing the recovery in real estate. Waterfront or near coastal properties will be impossible to sell. Another result of this bill will be the amount of properties that will go underwater with their mortgages as a result of the decline in property values from the implementation of this bill. This will cause another possible bank bailout with banks holding mortgages that no longer have an asset value that is more than the loan. We just went through a big bust in real estate over the last 7 years. We do not need another bust like that! The real estate market drives the economy and when the real estate market declines as a result of this bill it will cause a similar decline in the economy. We cannot afford to stop this recovery in the real estate market right now. We need to delay the implantation of this bill for at least 3 years as the legislators from Louisiana have proposed. Give our real estate market a chance to come back and to grow the economy and employment of more Americans!

One current example of a waterfront home for sale in a waterfront community on Treasure Island, Florida, where probably 90 percent of all properties were built before 1974 and before the enactment of Base Flood Elevation (BFE) by FEMA. Trying to sell this home to a buyer will be a very difficult task, because the house was built on the ground and as a result the lowest living area of the home is around 6 feet. This puts it at minus 5 since the BFE is 11 feet where this house is located. If you do the calculation the flood policy will be somewhere between $10,000-$15,000 annual premium, making it virtually impossible to sell to a new buyer. Buyer will need a wind policy and hazard policy as well! These sellers, like many homeowners, over the last few years have improved their property by over $122,000 in updates. If we implement the Biggert Waters Act as passed all of the improvements that the current owners invested in the home will be worthless since the property value will be determined by the value of the land only because the new Buyer would have to knock the house down and build a new home at or above the BFE in order to obtain affordable flood insurance for this home. There are thousands of properties throughout Florida and many more around the country who have done the same to their property over the last 10 years improving them by thousands of dollars. They are not millionaires!

Think of all of the homeowners throughout the country who bought in a flood zone in houses similar to this property which were built before the BFE was enacted by FEMA in the Mid 70's. Most are not aware of what is happening before their eyes. They will be very aware when they try to sell the house and will be forced to suffer enormous losses in value due to this act. This act will destroy the property values throughout the coastal zones across the country, resulting in lower revenue to taxing districts, many more foreclosures of existing homes. We cannot let this happen. Please do your best to postpone this devastating bill!

Best Regards,

Jim

NATIONAL FLOOD INSURANCE FUND OPERATING RESULTS SUMMARY SUBMITTED BY SENATOR LANDRIEU

National Flood Insurance Fund Operating Results Summary FY 1969 through FY 2012
Based on NFIP Financial Statements

	Income		Losses and Expenses					
Fiscal Year	Premium and Fees	Other Income	Loss & Loss Adjustment Expenses	WYO Expense Allowance	Interest	All Other expenses		Net Surplus/Deficit
1970	$373,000	$0	$0	$0	$0	$313,000		$60,000
1971	$6,347,000	$0	$336,000	$0	$39,000	$2,383,000		$3,589,000
1972	$6,964,000	$0	$9,451,000	$0	$105,000	$2,808,000		($5,400,000)
1973	$15,566,000	$0	$35,626,000	$0	$393,000	$7,048,000		($27,501,000)
1974	$25,777,000	$0	$37,666,000	$0	$2,790,000	$10,715,000		($25,394,000)
1975	$40,951,000	$0	$43,554,000	$0	$4,246,000	$10,812,000		($17,661,000)
1976	$79,500,000	$0	$89,190,000	$0	$8,920,000	$34,550,000		($53,160,000)
1977	$89,263,000	$0	$70,119,000	$0	$9,125,000	$37,488,000		($27,469,000)
1978	$105,801,000	$0	$146,994,000	$0	$11,755,000	$32,685,000		($85,633,000)
1979	$137,327,000	$0	$399,345,000	$0	$22,120,000	$39,090,000		($323,228,000)
1980	$153,985,000	$0	$292,865,000	$0	$63,652,000	$53,351,000		($255,883,000)
1981	$228,418,000	$561,085,000	$118,415,000	$0	$42,437,000	$59,128,000		$569,523,000
1982	$278,768,000	$328,240,000	$163,316,000	$0	$7,370,000	$67,160,000		$369,162,000
1983	$297,148,000	$43,081,000	$973,499,000	$0	$870,000	$71,248,000		($705,388,000)
1984	$365,574,000	$37,521,000	$356,163,000	$8,887,000	$12,694,000	$86,426,000		($61,075,000)
1985	$354,483,000	$206,860,000	$173,570,000	$32,308,000	$230,000	$81,616,000		$273,619,000
1986	$415,498,000	$40,711,000	$276,175,000	$71,611,000	$0	$78,669,000		$29,754,000
1987	$478,155,000	$3,901,000	$147,308,000	$48,452,000	$0	$114,561,000		$171,735,000
1988	$414,931,000	$37,696,000	$60,979,000	$105,282,000	$0	$103,161,000		$183,205,000
1989	$548,183,000	$61,490,000	$533,857,000	$112,540,000	$21,155,000	$88,333,000		($146,212,000)
1990	$597,761,000	$46,478,000	$320,075,000	$150,045,000	$1,586,000	$98,877,000		$73,656,000
1991	$619,412,000	$40,398,000	$226,537,000	$161,777,000	$0	$101,795,000		$169,701,000
1992	$675,588,000	$33,588,000	$474,691,000	$157,655,000	$0	$97,323,000		($20,493,000)
1993	$708,200,000	$23,653,000	$1,059,688,000	$177,276,000	$0	$96,859,000		($601,970,000)
1994	$765,443,000	$5,227,000	$208,574,000	$198,251,000	$0	$94,139,000		$269,706,000
1995	$875,614,000	$4,491,000	$1,121,559,000	$230,662,000	$0	$103,928,000		($576,044,000)
1996	$964,049,000	$8,878,000	$1,078,503,000	$275,249,000	$27,256,000	$128,337,000		($536,418,000)

National Flood Insurance Fund Operating Results Summary FY 1969 through FY 2012
Based on NFIP Financial Statements

	Income		Losses and Expenses				
Fiscal Year	Premium and Fees	Other Income	Loss & Loss Adjustment Expenses	WYO Expense Allowance	Interest	All Other expenses	Net Surplus/Deficit
1997	$1,084,398,000	$6,255,000	$735,017,000	$282,376,000	$44,686,000	$145,783,000	($117,209,000)
1998	$1,272,744,000	$6,206,000	$718,780,000	$367,080,000	$43,208,000	$150,481,000	($599,000)
1999	$1,409,557,000	$6,277,000	$714,210,000	$387,726,000	$29,794,000	$152,301,000	$131,803,000
2000	$1,468,985,000	$6,210,000	$317,487,000	$417,845,000	$26,603,000	$160,287,000	$552,973,000
2001	$1,597,182,000	$5,887,000	$1,519,088,000	$421,078,000	$8,199,000	$173,240,000	($518,536,000)
2002	$1,556,298,000	$6,533,000	$191,078,000	$434,832,000	$16,550,000	$189,674,000	$730,697,000
2003	$1,755,702,000	$8,850,000	$601,416,000	$519,017,000	$151,000	$196,372,000	$447,596,000
2004	$1,879,902,000	$12,074,000	$1,700,295,000	$521,635,000	$0	$166,860,000	($496,814,000)
2005	$2,047,826,000	$11,928,000	$2,280,794,000	$631,021,000	$2,799,000	$180,753,000	($1,035,613,000)
2006	$2,552,439,000	$15,839,000	$18,045,860,000	$683,465,000	$172,412,000	$237,557,000	($16,571,016,000)
2007	$2,722,335,000	$9,886,000	$1,219,944,000	$672,931,000	$717,482,000	$223,962,000	($102,098,000)
2008	$3,029,303,000	$9,558,000	$941,241,000	$754,259,000	$730,565,000	$267,327,000	$345,469,000
2009	$3,103,918,000	$8,576,000	$3,466,644,000	$850,207,000	$298,240,000	$335,083,000	($1,837,680,000)
2010	$3,319,195,000	$7,049,000	$1,143,258,000	$904,852,000	$117,215,000	$329,740,000	$831,179,000
2011	$3,308,010,000	$5,829,000	$243,183,000	$903,154,000	$71,714,000	$517,792,000	$1,577,996,000
2012 *	$3,485,948,000	$31,052,000	$2,445,000,000	$954,000,000	$88,696,000	$350,304,000	($321,000,000)
TOTAL	$44,842,821,000	$1,641,307,000	$44,701,350,000	$11,435,473,000	$2,605,057,000	$5,480,319,000	($17,738,071,000)

* 2012 Numbers are preliminary numbers. The numbers may change when final reconciliation is audited.

STATEMENT SUBMITTED BY THE NATIONAL ASSOCIATION OF REALTORS

NATIONAL ASSOCIATION of REALTORS®
REALTOR®

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STATEMENT OF

THE NATIONAL ASSOCIATION OF REALTORS®

TO THE

SENATE BANKING, HOUSING AND URBAN AFFAIRS
SUBCOMMITTEE ON ECONOMIC POLICY

HEARING TITLED

IMPLEMENTATION OF THE BIGGERT-WATERS FLOOD INSURANCE ACT OF 2012: ONE YEAR AFTER ENACTMENT

SEPTEMBER 18, 2013

On behalf of the 1-million members of the National Association of REALTORS® thank you for this opportunity to comment on the implementation of the Biggert-Waters Flood Insurance Reform Act. The Biggert-Waters Act provided a critical 5-year reauthorization without which the National Flood Insurance Program (NFIP) would have continued to operate month-to-month or may have shut down altogether, stalling 40,000 home sales each month. We applaud your leadership and thank you for holding this important hearing to ensure access to affordable flood insurance nationwide. Based on the first year of implementation, Biggert-Waters has already raised legitimate questions about the continued affordability of flood insurance that warrant further investigation. We urge Congress to delay the rest of the rate provisions until FEMA complies with Sec. 236 of the Act and reports to Congress on their impact on flood insurance affordability.

Flood Insurance Affordability is in Question

Included in the long-term reauthorization were provisions to phase-out rate subsidies for the less than 20 percent of flood insurance policy holders who paid less than the full actuarial rate. At the time, the NFIP owed approximately $20 billion (now closer to $30 billion) in outstanding loans and interest to the federal treasury. REALTORS® understood that for this program to continue long-term, all property owners would eventually have to pay actuarially responsible rates on their properties, as long as the flood risk was accurately identified and assessed on property owners fairly. We worked to ensure that existing pre-Flood Insurance Rate Map (FIRM) policy holders would not see the full actuarial rate until Biggert-Waters was fully implemented over time. The subsidy phase-outs were designed to be gradual and spread out over 4 or 5 years if not longer.

In addition to availability, affordability is also a key policy concern when dealing with flood insurance. The insurance product must be priced appropriately to encourage widespread uptake. If too few floodplain residents buy into the program, taxpayers could be forced to spend more on federal disaster relief for uninsured properties after the next major flood.

Yet today, REALTORS® are reporting insurance rate quotes of $20,000 or more for flood insurance in many parts of the country. Others have received varying rate quotes from different insurers for the same property based on the same FEMA rate tables. Homeowners are understandably confused and concerned about flood insurance affordability. They do not know if they have a subsidized policy or will be next to see their insurance rate climb to unaffordable levels. They also have no way to check the accuracy of these rate quotes or appeal the result as they could if there were a mapping dispute. Most assume that the increases are due to Biggert-Waters because it is the most proximate change, but it is not clear to what extent a) flood map updates (an on-going FEMA initiative that is separate from but could have a major impact on Biggert-Waters implementation) or b) confusion among insurers over FEMA implementation is contributing to the increases. We will know more once FEMA submits the congressionally mandated report to Congress on flood insurance affordability under Biggert-Waters reforms.

FEMA Implementation of Biggert-Waters is creating Market Uncertainty

- Retroactively applying immediate rate increases. FEMA waited nearly nine months after the enactment of the Biggert-Waters law to issue the required Write-Your-Own directive eliminating rate subsidies for properties purchased after July 2012. Then the Agency retroactively applied it. In doing so, FEMA has not only added another layer of complexity to an already complicated law, but in effect, it has changed the rules in the middle of the game for many who bought their home over the past year. Those purchasing a home between enactment of Biggert-Waters and the directive's effective date of October 1, 2013, have received the subsidized rate but will see their rate jump to the full actuarial cost at the first policy renewal a year following purchase. Those purchasing after October 1 will see the actuarial rate at point of sale. As a result, some insurers are issuing two rate quotes for a single property – one showing the rate if the property goes to closing before October 1 and the other showing the rate afterward. Other insurers are apparently not aware of the Biggert Waters Act at all or this directive, as they are providing only the first rate quote and not the second; it will not be until the renewal notice comes in the mail that some home owners will learn of devastating increases.

- Implementing some reforms but not others.
    - By delaying the phase-out of grandfathered rates (Sec. 207) until late 2014 or later, FEMA is not providing the certainty that real estate markets require in the 20,000 communities where flood insurance is required for a mortgage. (A "grandfathered" property is one in area where the flood risk map has been updated but the owner has been allowed to keep lower rate associated with the older rate map, because the property was built and maintained in compliance with previous standard.) According to the GAO,[1] FEMA does not have the information it needs to implement the rate increases for grandfathered properties.
    - While NAR appreciates the fact that FEMA is, in effect, delaying the elimination of grandfathering, we have many concerns regarding this provision once FEMA begins the implementation phase. We do not know if once implemented, FEMA intends to apply Sec. 207 retroactively to properties in areas remapped since Biggert-Waters or only looking forward once FEMA is able to implement the provision. We also do not know if FEMA intends to apply this provision to principal residences. Under Sec. 205, principal residences are exempt from the subsidy phase-out until the

[1] GAO, "Flood Insurance: More Information Needed on Subsidized Properties," Report #GAO-13-607, July 3, 2013.

property is sold, the policy lapses or is newly issued, but Sec. 207 applies to "any" property upon remapping.

- FEMA has yet to implement Sec. 205(d) (providing installment payments for flood insurance, which might help with affordability), Sec. 246 (providing reimbursement of expenses for successful flood map appeals), and Sec. 236 (requiring a report to Congress on the impact of Biggert-Waters reforms on flood insurance affordability).

Insurance Companies are adding to the Rate Confusion

We investigated a number of the +$20,000 rate quotes but often there was not enough information to replicate these estimates. None were found in available FEMA rate tables; apparently, all used "Submit-to-Rate" procedures that required individual judgment and advanced training for properties two or more feet below the base flood elevation. Their assumptions were not transparent. Our calculations did not match theirs. One "quote" was not even for a real property; an insurance agent had simply generated a rate table for a hypothetical one-story home if it were built on slab from 4 to 10 feet below base flood elevation in a "V" (coastal highest risk) zone. We do not have data on the distribution of these properties by elevation so we do not know how many of them actually exist.

There also appeared to be confusion among insurers over implementing the Biggert-Waters Act. One REALTOR® reported six separate quotes all estimating $21,000 for a single property but the insurers all made the same mistake on the construction date; they had incorrectly categorized it as pre-FIRM and subject to the Act. When the date was corrected, the true rate was closer to $500/year. Another REALTOR® provided three quotes ranging from $2,700 to $8,200 for that property but when the elevation certificate was used, the true rate was not in the quoted range. One insurer admitted to quoting the rate based on false assumptions about the property, rather than the actual facts from the elevation certificate. Another did not seem to be aware of Biggert-Waters.

To our knowledge, insurers do not routinely re-underwrite old policies or even verify the accuracy of basic facts about a property before applying rate increases. At least one insurer was correcting a rate because the original agent writing the policy 10 years before had missed a basement. Another listed a basement on the declaration page even though one does not exist for the property. There does not appear to be a single federal point-of-contact or process for homeowners to verify or appeal rate quotes. There is no continuing education requirement on write-your-own agents and it is not clear what QA/QC is provided for their training.

More Accurate Flood Maps Are Complicating the Situation

The vast majority of the REALTOR® reports were from areas that were recently remapped or in the process of remapping, an on-going FEMA initiative that would have occurred regardless of Biggert-Waters' enactment. Virtually none had appealed or were aware that they could appeal the flood map determination. One in particular was about the owner of a principal residence that had not been sold and who had not allowed the policy to lapse therefore the quote could not be caused by Sec. 205 (which exempts such residents) or Sec. 207 (which has not been implemented). Some property owners may be seeing dramatically higher rates because the property was originally categorized in an "A" (high risk inland) or "X" (low risk) zone when it should have been categorized in the higher risk coastal velocity or "V" zone.

Conclusion

Thank you for the opportunity to share the views of the National Association of REALTORS® on such an important topic. We stand ready to work with you to ensure that affordable flood insurance remains widely available to American homeowners who need it.

STATEMENT SUBMITTED BY THE NATIONAL ASSOCIATION OF HOME BUILDERS

NAHB®
National Association of Home Builders

Statement of the
National Association of Home Builders to the

Economic Policy Subcommittee of the Senate Committee on Banking, Housing and Urban Affairs
Hearing on

"Implementation of The Biggert-Waters Flood Insurance Act of 2012: One Year After Enactment"

September 18, 2013

Written Statement

On behalf of the more than 140,000 members of the National Association of Home Builders (NAHB), I thank you for holding a hearing on *"Implementation of The Biggert-Waters Flood Insurance Act of 2012: One Year After Enactment."* NAHB appreciates the opportunity to provide a written statement on this important issue.

NAHB is a Washington, D.C. based trade association representing over 140,000 member firms who design, construct, and supply single-family homes; build and manage apartments, condominiums, commercial, and industrial structures; develop land; and remodel homes. Collectively, NAHB's members employ over 1.26 million people and will construct about 80% of the new housing units projected for 2013. In addition, 57% of NAHB's builder members and many of its associate members are involved in the remodeling industry. As a leading advocate for the residential construction industry NAHB promotes policies that will keep housing a national priority.

Since 1968, the Federal Emergency Management Agency's (FEMA) National Flood Insurance Program (NFIP) has played a critical role in directing the use of flood-prone areas and managing the risk of flooding for residential properties. NAHB members depend upon the NFIP to be annually predictable, universally available, and fiscally viable. A strong NFIP enables the housing industry to continue to provide safe, decent, and affordable housing to consumers.

While NAHB strongly supported the passage of the Biggert–Waters Flood Insurance Reform Act of 2012 (BW-12) in order to secure a five-year reauthorization of the NFIP program, NAHB's members from across the country are extremely concerned about the dramatic rate increases and unaffordable NFIP insurance premiums as well as the impact BW-12 is having on the sales of older housing stock, properties in newly mapped areas, new homes, and on the remodeling market in affected communities

BACKGROUND

The NFIP provides flood insurance to over 5.6 million policyholders nationwide, enabling homeowners to protect their properties and investments against flood losses. The NFIP also creates a strong partnership between state and local governments by requiring them to enact and enforce floodplain management measures, including building requirements that are designed to ensure occupant safety and reduce future flood damage. This partnership, which depends upon the availability of comprehensive, up-to-date Flood Insurance Rate Maps (FIRMs) and a fiscally solvent federal program allows local communities to direct development where it best suits the needs of their constituents and consumers.

This arrangement has, in large part, worked well. Unfortunately, the losses suffered in the 2004 and 2005 hurricane seasons, including the devastation brought about by Hurricanes Katrina, Rita and Wilma, and most recently Superstorm Sandy, have severely threatened the solvency of the NFIP, which is currently in debt to the U.S. Treasury by $19 billion.

When BW-12 was signed into law, it was heralded as a solution to ensure the long-term fiscal stability and soundness of the NFIP by ending the federally subsidized and grandfathered insurance rates paid by owners of the the older properties. While NAHB supported many of the reforms as necessary for the viability of the overall NFIP program, NAHB raised concerns in its June 2011 testimony to the Banking Committee about insurance availability and affordability, noting that reforms aimed at reducing federal subsidies to primary residences must ensure that overall affordability is not adversely affected.

Now that specific provisions of BW-12 are being implemented, NAHB's concerns about the unintended economic consequences that could occur in specific housing markets have started to become a reality.

BW-12 RATE CHANGES

As part of the effort to ensure the fiscal soundness of the NFIP, BW-12 mandates that all policyholders will ultimately pay the full actuarial risk rate for their properties. While most properties insured by NFIP already pay full-risk rates, just over 20% of policyholders receive subsidized rates; generally paying between 40-45% of the actuarial premium. Those rates tend to belong to structures (known as pre-FIRM) that were built pre-1974, or before the first FIRMs were established for the respective community. FEMA has also allowed "grandfathered" properties to pay less than the actuarial rate. Grandfathered policyholders are those that are allowed to continue paying lower-risk premium rates despite a new flood map locating them in a higher-risk zone.

Under BW-12:

- Any pre-FIRM or grandfathered properties that are sold will immediately shift to a **full-risk rate**.
- All pre-FIRM policyholders will see their policies increased by 25% **of the full-risk rate** starting October 1, 2013 (for a total of four years). Owners of second homes were subject to this rate increase starting January 2013.
- Any pre-FIRM properties that undergo renovation resulting in "substantial improvement" of 30% or more of the market value of the structure will see a phase-in **of the full-risk** rate over four years (with premiums increasing 25% of the full-risk rate a year).
- All flood maps are to be redrawn using scientifically based data to show the true risk of flooding, and provide FEMA a clearer picture of where actuarial rates should be set. In 2014, the new maps should be completed and BW-12 requires that all grandfathered properties in new FIRMs be phased-in to **the full-risk rate** over five years (with premiums increasing by 20% of the full-risk rate each year).

AFFORDABILITY CONCERNS

NAHB believes a financially-stable NFIP is in the nation's best interest, yet we must also ensure that flood insurance remains available and affordable for those property owners that require it. Unfortunately, in its pursuit of financial stability for NFIP, the implementation of BW-12 has left members of NAHB across the country concerned about the sharply rising cost of flood insurance; with some members already seeing the rates on their own homes increased by several thousand dollars.

For example, a builder from Oregon has seen his pre-FIRM rate go from $600 to over $10,000. Builders from North Carolina are seeing their rates increase as much as 1,000% from current pre-FIRM rates. Another builder in Louisiana bought a new home for his young family and is now having to pay the full risk-rate of $10,000 a year, when the same property was previously only $600. These rate increases are not only affecting the coastal communities, they are also impacting areas across the country. Several of NAHB's North Dakota builders have reported rate increases that have priced prospective buyers out of their developments, and this sentiment is shared in many other regions of the country.

NAHB is alarmed by the potential adverse effects that will result from the immediate removal of subsidized rates (for both pre-FIRM and grandfathered properties) upon sale or property transfers. The immediate adjustment of flood insurance premium rates to actuarial rates at the time of purchase is already deterring prospective homebuyers from purchasing pre-FIRM properties. And the prospect of an actuarial rate may decrease the value of properties in floodplains, as prospective buyers will factor the immediate increase into the price of the property.

Because NFIP's mandatory purchase requirement requires all federally backed mortgages located within the Special Flood Hazard Areas (SFHAs) to be covered by flood insurance, NAHB is also concerned that many prospective homebuyers could be prevented from qualifying for a mortgage under normal mortgage underwriting standards. We estimate that up to 1.9 million households could be priced out of the market because they could no longer qualify for a traditional residential mortgage under the slated increase in insurance premiums for pre-FIRM properties.

Concerns about affordability also stem from the fact that over 17.4 million Americans live in the 100-year SFHA. According to a recent U.S. Department of Housing and Urban Development (HUD) study, 41.4% of these households were categorized as being Low to Median Income (LMI). Meaning these households are going to find any increase in NFIP rates as unaffordable, causing them to be priced out of the NFIP and possibly their homes.

Given the current state of tight credit conditions, which are preventing many prospective homebuyers from even qualifying for a mortgage, it is clear that requiring full-risk rates to be paid upon sale or transfer for historically subsidized and previously grandfathered properties will have a negative impact on many local housing markets at a time when the U.S. housing recovery remains fragile and uneven.

And those effects will not be limited to the sale of existing homes; it will also impede the sale of new homes in communities with pre-FIRM and grandfathered properties. Although the brunt of the effects will be experienced by those who hope to purchase these older properties, the trickle-down effects will touch states, municipalities, developers, builders, remodelers, real estate agents, neighbors and ultimately, property owners.

NAHB is also concerned with the remapping process under BW-12. We are hearing from builders across the country that the new FIRMs are not taking into account various local flood control structures, placing NAHB members, their clients and homeowners into higher rate zones unnecessarily. Further, the media has recently pointed out that many of the FIRMs are being drawn inaccurately, forcing homeowners and communities to fight FEMA for corrections or face much higher premiums.

REMODELING CONCERNS

NAHB also remains troubled by the effect of BW-12 on remodeling activity. The law lowers the threshold for what is considered a substantial improvement to a structure from the historic 50% to 30% of the structure's fair market value. Any renovation that reaches new, lower, substantial improvement threshold will trigger a phase in of the full-risk rate over four years (with premiums increasing 25% of the full-risk rate per year).

While the substantial improvement clause has long been a part of the NFIP, the threshold has historically been set at 50% of fair market value of the property, which was established by FEMA in recognition of a wide range of conditions, including recognized zoning standards. NAHB believes that the lowering of this threshold in BW-12 was done arbitrarily, without taking those conditions into consideration.

NAHB believes the implementation of this provision will adversely impact homeowners by forcing them to either forgo necessary and appropriate improvements or shoulder sharply increased flood insurance rates. NAHB estimates that the new lower substantial improvement threshold will place up to $8.5 billion in annual remodeling economic activity at risk. And if disincentives (or costs) are such that homeowners are unable or unwilling to repair or mitigate homes, there is a significant trail of impacts that will accrue to communities, lenders, and neighbors.

FEMA has indicated that a rulemaking will be necessary before the 30% threshold and its phasing in of full-risk rates are implemented, but the issue is appropriately a pressing concern for the home remodeling industry.

CONCLUSION

NAHB is committed to ensuring that the NFIP remains a viable and affordable program to its policyholders, while being mindful of the costs to the American taxpayer. We look forward to working with you to find legislative solutions that will:

- Delay the rate increases to provide immediate relief for policy holders;
- Grandfather all existing policies on transfer or sale;
- Return the "substantial improvement" threshold to the 50% limit;
- Require FEMA to complete the NFIP affordability study mandated by BW-12; and
- Prohibit premium increases based on incomplete or inaccurate maps.

NAHB would like to thank the Subcommittee for its leadership on the NFIP and wants to ensure its continued success. Thank you for this opportunity to provide this statement to the members of the Subcommittee.

LETTER SUBMITTED BY BRAD THALER, VICE PRESIDENT OF LEGISLATIVE AFFAIRS, NATIONAL ASSOCIATION OF FEDERAL CREDIT UNIONS

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September 18, 2013

The Honorable Jeff Merkley
Chairman
Subcommittee on Economic Policy
Committee on Banking, Housing,
and Urban Affairs
United States Senate
Washington, D.C. 20510

The Honorable Dean Heller
Ranking Member
Subcommittee on Economic Policy
Committee on Banking, Housing,
and Urban Affairs
United States Senate
Washington, D.C. 20510

Re: Today's hearing on the "Implementation of the Biggert-Waters Flood Insurance Act of 2012: One-year after enactment."

Dear Chairman Merkley and Ranking Member Heller:

On behalf of the National Association of Federal Credit Unions (NAFCU), the only trade association that exclusively represents the interests of our nation's federal credit unions, I write in conjunction with today's Economic Policy Subcommittee hearing "Implementation of the Biggert-Waters Flood Insurance Act of 2012: One-year after enactment."

As you examine the issue of flood insurance, NAFCU urges the Subcommittee to support efforts to delay the National Flood Insurance Program (NFIP) premium increases scheduled to take effect as early as October 1st until at least such time as the Federal Emergency Management Agency (FEMA) completes its affordability impact study and Congress is able to review the findings.

Failure to act in this regard could mean that premiums will skyrocket for some in just a matter of days, and various local housing markets could face drastic negative impacts. New premiums could be unaffordable to many, dropping home values in an already tenuous economy. We are already hearing reports from our member credit unions that these impacts are beginning to materialize, so any action on this matter must be timely.

Thank you for holding this important hearing today and for examining this issue. If NAFCU can be of assistance to you, or if you have any questions regarding this issue, please feel free to contact me or NAFCU's Director of Legislative Affairs, Jillian Pevo, at 703-963-7082.

Sincerely,

Brad Thaler
Vice President of Legislative Affairs

cc: Members of the Subcommittee on Economic Policy