OPPORTUNITIES AND CHALLENGES FACING THE NATIONAL FLOOD INSURANCE PROGRAM

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BEFORE THE

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HOUSING AND INSURANCE

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OPPORTUNITIES AND CHALLENGES FACING THE NATIONAL FLOOD INSURANCE PROGRAM

Tuesday, January 12, 2016

U.S. HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON HOUSING AND INSURANCE,
COMMITTEE ON FINANCIAL SERVICES,
Washington, D.C.

The subcommittee met, pursuant to notice, at 10 a.m., in room 2128, Rayburn House Office Building, Hon. Blaine Luetkemeyer [chairman of the subcommittee] presiding.

Members present: Representatives Luetkemeyer, Royce, Pearce, Posey, Stivers, Ross, Barr, Rothfus; Cleaver, Clay, Green, Moore, Beatty, and Kildee.

Ex officio present: Representatives Hensarling and Waters.

Chairman LUETKEMEYER. The Subcommittee on Housing and Insurance will come to order. Without objection, the Chair is authorized to declare a recess of the subcommittee at any time.

Today's hearing is entitled, "Opportunities and Challenges Facing the National Flood Insurance Program."

I would like to thank the witnesses for appearing today. We look forward to your testimony.

I now recognize myself for 3 minutes to give an opening statement.

My district is home to many communities that lie in flood plains near major rivers, streams, and lakes. Many of the towns I represent, like so many communities across the Nation, are suffering from some of the most destructive flood scenes in years.

While the long-term repercussions are yet to be fully known, previous experience has continually brought to light many issues surrounding the National Flood Insurance Program (NFIP). Within the past 5 years, nearly every one of the 50 States has experienced flooding. In the past decade, insurance claims stemming from flood damage have averaged $3.5 billion a year. It is not surprising, then, that flooding is the number one natural disaster in the United States. As a result, the NFIP today has an outstanding debt of approximately $23 billion borrowed from the Treasury, with $7.45 billion remaining of its total temporary borrowing authority.

I have previously voiced concerns about the administration, operation, and suitability of the NFIP. Time and time again, we see Americans suffer because of governmental failure and inaction in times of greatest need. Authorization of the NFIP will expire on

September 30, 2017. Unlike in previous years, it is my hope that Congress can avoid coverage lapses that leave economies along the Missouri and Mississippi Rivers and local economies in every congressional district in a lurch. At the same time, we all recognize, regardless of political affiliation, that the status quo isn't acceptable.

Throughout this year, this committee will aim to garner more information on the NFIP, examine whether or not changes to flood insurance are likely to solve longstanding issues, and develop ways to fix a broken system in order to ensure it does more to benefit all parties involved.

I look forward to today's testimony and to the start of what I hope is a productive conversation on the future of flood insurance in America. My hope is that, at some point over the course of this year, we will be able to get enough information so that we can put together the reauthorization bill by the end of the year and that we will take next year, 2017, to be able to then authorize that bill, fine-tune it, and get it to the point where we can pass it and avoid the management by crisis that we do around here on a regular basis.

However, that being said, I look forward to today's testimony.

With that, the Chair now recognizes the ranking member of the subcommittee, the gentleman from Missouri, my good friend Mr. Cleaver, for 5 minutes for an opening statement.

Mr. CLEAVER. Thank you, Mr. Chairman, and members of the subcommittee, as well as the witnesses today, especially Tom Woods. Woods Custom Homes is one of the most significant and successful builders in my area. And Tom Woods, of course, served as a mayor of Blue Springs probably 10 years before I served as mayor of Kansas City. And I am so pleased that he is here. And he knows, as well as people in the State of Missouri, as you have already indicated, Mr. Chairman, this is a significant issue with which we are dealing.

And this hearing is particularly appropriate. In the last few weeks, flooding from the Mississippi River has damaged homes and businesses in Missouri. Now, my congressional district was spared much of the damage to homes and businesses that hit the western and southwestern part of our State. Closer to home, I do often hear from farmers in my district who remain extremely concerned over flooding risks in their fields.

As we all know, the National Flood Insurance Program was created in 1968 through the passage of the National Flood Insurance Act in response to a limited number of available companies—private companies—which were interested in providing flood insurance.

The NFIP provides flood insurance to many property owners in designated areas as well as develops the flood insurance rate maps and promotes mitigation activities.

Since 1968, the act of NFIP has been amended many times, more recently through what we all affectionately call the Biggert-Waters Act of 2012, and the Homeowner Flood Insurance Affordability Act of 2014.

With the need for authorization around the corner, today we have the opportunity to fully discuss this issue, and more specifically, it gives us a chance to consider the importance of retaining flood insurance as well as how we can improve this program.

I am going to be the last person to ever say that the issues we deal with in Federal agencies are perfect. They are imperfect. The only thing perfect is the 11 consecutive games won by the Kansas City Chiefs.

I look forward, Mr. Chairman, to this hearing.

And now I will ask if the ranking member, Ms. Waters, would like the remainder of my time?

Chairman LUETKEMEYER. Very good.

Good morning, Ranking Member, whenever you are ready.

Ms. WATERS. I'm ready.

Chairman LUETKEMEYER. Okay. The ranking member of the full Financial Services Committee, Ms. Waters from California, is recognized for 2 minutes.

Ms. WATERS. Thank you very much, Mr. Chairman.

I am pleased to see that this committee has chosen to prioritize the National Flood Insurance Program this year. At the end of last year, I requested that the committee hold this hearing because I believe that it is absolutely critical that we start thinking about the program and how we can improve it for the long term.

Now, let me briefly discuss the beginning before we discuss the future.

When I agreed to work with Ms. Biggert on what ultimately became the Biggert-Waters Act, our goal was to create a bipartisan solution to repair our ailing Flood Insurance Program. There was a broad consensus around the need for the program because it is essential to our housing market and to our disaster recovery. For years, instability and insolvency issues threatened the effectiveness of NFIP.

And since 2008, Congress has been extending the program a few months at a time. Twice, this led to shutdowns, including one that stalled more than 40,000 home sales in June 2010 alone. Short-term extensions cause lapses in the program that place communities at risk and undermine our housing market. In 2010, the National Association of REALTORS® estimated that approximately 1,400 home closings were adversely affected each day the program sat expired.

For this reason, and to address the NFIP's then-$24 billion debt, we attempted to fix the program through a 5-year extension and a 10-year repayment plan. But it soon became clear that our best intentions fell victim to circumstances that led to rate increases too severe for any family's budget. Together, we worked tirelessly to enact reform that provided much needed rate relief for thousands of homeowners and put FEMA back on the path to addressing affordability issues on a broader scale.

In 2013, when this committee refused to hold hearings, I convened a bipartisan meeting which led to the creation of a bipartisan and bicameral coalition. Ultimately, we were successful in passing legislation that addressed the unintended consequences of the Biggert-Waters Act. I stand ready to take these next 2 years to continue in that spirit and work across the aisle to ensure that the NFIP remains able to provide affordable flood insurance so that our Nation is resilient in the event of a disaster.

So I thank you, Mr. Chairman, and I yield back the balance of my time. And I hope that we can work together in a bipartisan effort in the way that we did to pass the bill that corrected the unintended consequences of Biggert-Waters. I enjoy doing that.

I yield back.

Chairman LUETKEMEYER. Thank you, Ms. Waters.

With that, we will open with our testimony for the day.

We have Mr. Stephen Ellis, vice president, Taxpayers for Common Sense; Mr. Christopher Heidrick, principal of Heidrick & Company Insurance and Risk Management Services, on behalf of the Independent Insurance Agents and Brokers of America; Ms. Patty Templeton-Jones, executive vice president and chief program advocate for Wright National Flood Insurance Company, on behalf of the Property Casualty Insurers Association of America; and Mr. Tom Woods, 2015 chairman of the board, National Association of Home Builders.

We had a roundtable last week, which was great from the standpoint that we were looking at the mapping problem, believing that we need to start there. In today's hearing, we hope to build on that with a more broad look at flood insurance as a whole and then on—in fact, tomorrow, we will look at a private sector solution with a bill that is out there to also take that into consideration. So we are starting off the year with a lot of research and looking into the aspect, different aspects of flood insurance, and we look forward to your testimony here today.

Just to give you a brief tutorial on the lighting system, you get 5 minutes to speak, and give us your testimony. At the 1-minute mark, a yellow light will come on. And when you hit red, that means my gavel is close behind.

With that, Mr. Ellis, welcome to the committee, and I look forward to your testimony. You have 5 minutes.

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

Mr. ELLIS. Thank you.

Good morning, Chairman Luetkemeyer, Ranking Member Cleaver, Chairman Hensarling, Ranking Member Waters, and members of the subcommittee. I am Steve Ellis, vice president of Taxpayers for Common Sense, a national nonpartisan budget watchdog. Thank you for inviting us to testify on opportunities and challenges facing the National Flood Insurance Program. Taxpayers for Common Sense is aligned with Smarter Safer, a coalition that is 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 consumer and housing advocates to environmental and insurance industry groups. All of the groups agree that NFIP should be made more responsible and greater reforms are needed.

I have a more extensive discussion of the opportunities and challenges facing NFIP in my written testimony, but in my short time now, I would like to address four of the points the committee raised in the letter inviting me to testify.

The committee asked, is the NFIP the ideal model for effective protection of residential and commercial property owners? No. And not just because it is $23 billion in debt to taxpayers. As was mentioned, the NFIP was created nearly 50 years ago because of a market failure. Today, the insurance industry is hungry for this risk and can provide it. To be clear, I am not suggesting eliminating NFIP tomorrow or anything close to that. The community rating system encourages mitigation, and there are properties that would see significantly higher premiums in the private marketplace.

But a primarily private sector program is where flood insurance is heading and should head, and FEMA has indicated as such, that it is heading this way. This is already happening, and in the coming decades, NFIP will likely become a residual market for policyholders who cannot obtain private flood insurance. This would be a limited set of policies, and it is not unlike residual homeowners' insurance programs at the State level. But Congress should be intentional about this development and ensure mitigation benefits achieved by NFIP are retained and funds for mapping maintained.

The committee asked about FEMA's efforts to accurately predict flood risks, price flood risk, and create an effective administrative mechanism to serve policyholders. I know FEMA is working hard to update the maps and has the new Technical Mapping Advisory Council to help guide them in their work. I also know that mapping efforts have not received full funding in the last several years, which inhibits their progress.

That said, more needs to be done for the public to have a greater understanding of their flood risk. FEMA is tasked with mapping this special flood hazard area for the mandatory purchase requirement. That is a Federal mandate that isn't likely to change. However, these maps are static; lines on a map designating various flood risk areas and charging various rates based on those risks. If a homeowner has an elevation certificate that proves they are elevated out of the flood plain, they can have those rates adjusted. But the creation of the rates as a sort of black box is not entirely clear that even full risk rates are actuarially sound. In some cases, there are significant cross subsidies where lower risk properties pay more to maintain subsidies for higher risk properties.

The committee also asked how NFIP in the private sector could better serve high-impacted communities and modernized mapping systems while incorporating local community mitigation efforts. There is no way around it. The maps have to be more accurate and smarter. There is a whole industry that has very accurate data. FEMA should explore data sharing and further contracting with them. There are also many different Federal agencies that engage in mapping. This should be better coordinated and shared among agencies to avoid duplication.

This is also where—and I know this is outside the committee's jurisdiction—the Nation's mitigation and pre-disaster programs have to dovetail with NFIP and post-disaster response.

Finally, the committee asked about the issue of affordability for families without the resources to pay actuarial flood rates. The affordability issue has to be addressed, but it must be done in a means-tested, targeted, and time-limited manner. Current subsidies are effectively hidden from the homeowner, which eliminates any price signal of risk or incentive to mitigate to reduce the risk and thereby the premium. Masking subsidies with lower rates prevents policyholders from understanding the true level of their risk. As was noted in the privatization report mandated by Biggert-Waters, subsidized rates "can promote and have promoted poor decisions on the part of property owners and political representatives. They also create a moral hazard, especially when the subsidies are not well targeted." The report continues, that the presence of subsidies "removes the incentive to undertake mitigation efforts, thereby encouraging ever-increasing societal costs." A far better approach is to encourage and fund mitigation measures that could serve to reduce rates by reducing risk.

In conclusion, private insurers are ready to write flood insurance, and as NFIP rates rise in the program to be more in line with risks, this will become even more so. With more insurers writing flood insurance, there should be a growth in overall coverage in the United States while the Federal program develops into a residual market. This will take a decade or maybe 2 decades or more, but Congress should work with the Executive Branch to manage the transition and use targeted mitigation tactics that make these remaining policies more commercially insurable.

There is no need for the Federal Government to further extend into the catastrophe insurance market through reinsurance or other means.

Thank you for the opportunity to testify. I am happy to answer any questions you may have.

[The prepared statement of Mr. Ellis can be found on page 36 of the appendix.]

Chairman LUETKEMEYER. Thank you, Mr. Ellis.

Mr. Heidrick, you are now recognized for 5 minutes.

STATEMENT OF CHRISTOPHER HEIDRICK, PRINCIPAL, HEIDRICK & COMPANY INSURANCE AND RISK MANAGEMENT SERVICES, LLC, ON BEHALF OF THE INDEPENDENT INSURANCE AGENTS AND BROKERS OF AMERICA

Mr. HEIDRICK. Thank you.

Good morning, Chairman Luetkemeyer, Ranking Member Cleaver, Chairman Hensarling, Ranking Member Waters, and members of the subcommittee. My name is Chris Heidrick, and I am pleased to be here today on behalf of the Independent Insurance Agents and Brokers of America, or the Big "I," to present the Association's perspective on flood insurance and the National Flood Insurance Program. We commend the subcommittee for looking at this very important issue.

I am the principal of an independent insurance agency located in Sanibel, Florida. I regulate and counsel clients of all sizes regarding flood insurance. I also hold the designation of associate in national flood insurance. I currently serve as the chairman of the Big "I" Flood Insurance Task Force and represent the Big "I" on the Flood Insurance Producers' National Committee.

The Big "I" is the Nation's largest and oldest trade association of independent insurance agents and brokers, and we represent a nationwide network of approximately a quarter of a million agents, brokers, and employees. Working with Write Your Own companies, many of these agents serve as the sales force for the NFIP. It is from this vantage point that Big “I” members understand the capabilities and challenges of the insurance market when it comes to ensuring against flood risks. The Big “I” believes the NFIP provides a vital service for the people and places that have been hit by a natural disaster. Recent severe flooding in Missouri and across the central United States has provided an unsettling reminder of the terrible damage that flooding can cause, and the NFIP is virtually the only way for many people to protect against the loss of their home and business due to flood damage.

Despite our support of the NFIP, the Big “I” also recognizes that the program is far from perfect. The program has recently faced scrutiny for its handling of Superstorm Sandy claims and has a debt of approximately $23 billion. But it is important to note that for more than 2 decades, up until the 2005 hurricane season, no taxpayer money had been used to support the NFIP. The NFIP was able to support itself using funds from the insurance premiums it collected.

In order for the NFIP to move forward toward financial solvency, rate adequacy should be examined. However, it must be done with careful consideration to avoid market disruption and other unintended consequences. For the NFIP to regain any sort of solid financial footing, the number of policies needs to increase, not decrease. As Congress considers possible reforms to the program, careful analysis of their potential impact on policy take-up rates and retention should be paramount.

Now, I would like to talk about the role of the insurance agent in the delivery of flood insurance, which is considerably more complex than most traditional property and casualty lines. Independent agents are an essential part of the consumer experience when purchasing a flood policy. Placing a new policy on a property located in a special flood hazard area where the government requires flood insurance for any home with a federally-backed mortgage is an intensive process that can take multiple days, if not weeks, to complete.

Furthermore, when consumers are “not in a flood zone,” they often believe they don’t need flood insurance when, in fact, this is not the case. Properties outside of this special flood hazard area comprise over 20 percent of all NFIP flood insurance claims and receive one-third of Federal disaster assistance for flooding. It is my job to explain the flood insurance options available to consumers and to make sure they understand the consequences of their purchase decision.

As you know, the NFIP is a congressionally authorized program that requires periodic extensions. The NFIP is currently scheduled to expire on September 30, 2017, and the Big “I” strongly urges Congress to pass a long-term extension as soon as possible. Instability and uncertainty created by short-term and sometimes retroactive or last-minute extensions can lead to concrete damages in the real estate and development market as well as the country’s economy overall.

Briefly, regarding the private market, which I know the subcommittee is exploring in a separate hearing tomorrow, the Big “I” supports H.R. 2901, the Flood Insurance Market Parity and Modernization Act, as introduced. I would like to thank Representatives Ross and Murphy for taking the lead on this bipartisan legislation. This bill ensures that policyholders can move seamlessly between the private market and the NFIP. The Big "I" believes that the private flood insurance market can play a valuable but limited role as a complement to the NFIP in protecting homes and businesses but lacks the capability to underwrite flood insurance on a pervasive basis to meet customer needs.

In conclusion, the Big "I" strongly supports the NFIP and the continued role of our members as the distribution force for the program. The NFIP is essential for millions of Americans, and ensuring the long-term stability of the program is of vital importance. I thank the subcommittee for holding this hearing and I look forward to answering any questions you may have.

[The prepared statement of Mr. Heidrick can be found on page 43 of the appendix.]

Chairman LUETKEMEYER. Thank you, Mr. Heidrick. Well done, you wound up within the time limit there. Good job.

Mr. HEIDRICK. Thank you.

Chairman LUETKEMEYER. Ms. Templeton-Jones, you are recognized for 5 minutes.

STATEMENT OF PATTY TEMPLETON-JONES, EXECUTIVE VICE PRESIDENT AND CHIEF PROGRAM ADVOCATE, WRIGHT NATIONAL FLOOD INSURANCE COMPANY, ON BEHALF OF THE PROPERTY CASUALTY INSURERS ASSOCIATION OF AMERICA

Ms. TEMPLETON-JONES. Good morning, Chairman Luetkemeyer, Ranking Member Cleaver, and members of the subcommittee. My name is Patty Templeton-Jones. I am executive vice president and chief program advocate of Wright National Flood Insurance Company, which is based in Florida and domiciled in Texas. Thank you for the opportunity to testify.

Wright National Flood Insurance Company is a Write Your Own flood insurance partner with the NFIP for the Write Your Own Program. WNFIC is the largest writer of flood insurance in the Nation. Wright National Flood Insurance Services, our processing center, is also active in the private flood insurance market growing outside of the NFIP. Wright National Flood is a member of the Property Casualty Insurers Association of America, which is composed of nearly 1,000 member companies, including two-thirds of the Write Your Own insurers that partner with the NFIP to administer the National Flood Insurance Program.

My testimony today is provided on behalf of PCI and its nearly 1,000 member companies. Today, I would like to: first, draw your attention to the dramatic increase in private capital available to underwrite flood coverage outside the NFIP; second, underscore the importance of consensus for the long-term reforms needed to provide stability in the NFIP throughout the lengthy transition period necessary for significant market for flood coverage to develop outside the NFIP; third, highlight several key issues policymakers need to consider before any period of transition begins; and finally, suggest several broad categories on which such long-term consensus reforms should focus.

Without question, the biggest change in the flood insurance landscape since Congress last authorized the NFIP is that now, for the first time in a generation, substantial sources of private capital are available and actively interested in writing primary flood insurance coverage. Today, an increasing number of private insurers are planning on entering into the private flood market.

In response, State insurance regulators, like those from Florida and Pennsylvania, are engaging insurers with the intention of fully incorporating flood insurance into the U.S. State system of insurance regulation.

The 48-year-old NFIP has experienced significant turmoil over its history. Program uncertainty and confusion peaked between 2008 and 2012 as the NFIP suffered through a period of more than a dozen short-term program lapses and extensions. Unfortunately, a decade of program uncertainty, lapses, and midstream operational changes have not only caused numerous insurers to leave the Write Your Own Program but have repeatedly disrupted the housing market and caused ripple effects throughout the larger economy.

Developing consensus on long-term reforms, and restructuring and reauthorizing the NFIP well before the September 2017 expiration, is the single most important thing Congress can do to foster certainty in the flood insurance marketplace and encourage the continued development of market-oriented solutions in flood risk management.

The availability and interests of significant sources of private capital to provide primary flood insurance coverage outside the NFIP represents a paradigm shift. It presents the opportunity for a gradual transition toward a flood insurance marketplace in which an increasing share of risk is borne by private capital.

However, the growth of a private primary flood insurance market does not mean the elimination of the need for the NFIP, particularly, as the private market will not be willing to assume all flood risk or be acceptable to all buyers. In advance of any significant transition into the flood insurance market, topics policyholders need to consider are: first, should the NFIP become a national residual market or market of last resort for the substantial number of properties the private market will be unable or unwilling to insure; second, how is the NFIP's mission to encourage the purchase of flood insurance by providing affordable coverage impacted by the growth of the private insurance market; and lastly, how will the NFIP's mapping and flood mitigation functions be funded if policyholders leave the NFIP and purchase private flood insurance?

Detailed in my written testimony are a number of immediate operational reforms that FEMA can take up on its own that the subcommittee may wish to consider in an oversight role. In the immediate term, Congress could and should bolster the development of a robust private flood insurance market by passing the bipartisan and bicameral Ross-Murphy-Heller-Tester Flood Insurance Market Parity and Modernization Act of 2015, H.R. 2901. This straightforward legislation addresses post-Biggert-Waters Flood Insurance Reform Act of 2012 (BW-12) regulatory confusion and provides homeowners greater coverage options in pricing.

In conclusion, PCI and Wright National supports the committee's review of NFIP in consideration of how to encourage additional private participation in flood underwriting and accordingly limit taxpayer risk. We would also suggest that even if the subcommittee and Congress ultimately reshape the marketplace, there will be a necessary long-term transition. Given the NFIP's important role in the lives of so many Americans, it is critical to develop a strong, bipartisan consensus for a stable, long-term reform in advance of the program's 2014 expiration.

I thank the members of the subcommittee for this timely subject: reimagining flood risk management in advance of the November 2017 reauthorization of the NFIP. I am happy to address any questions, and I look forward to working with the subcommittee throughout this process.

[The prepared statement of Ms. Templeton-Jones can be found on page 48 of the appendix.]

Chairman LUETKEMEYER. Thank you, Ms. Templeton-Jones.

And finally, we will go to Mr. Woods.

Mr. Woods, I want to thank you, again, for your participation last week in our flood mapping roundtable. I realize this is your second visit to D.C. in 2 weeks, so we appreciate your willingness to work with us, to enlighten us, and to represent your association, which you do very well.

So, again, as a fellow Missourian, welcome to our committee, Mr. Woods.

And you are recognized for 5 minutes.

STATEMENT OF TOM WOODS, 2015 CHAIRMAN OF THE BOARD, NATIONAL ASSOCIATION OF HOME BUILDERS

Mr. WOODS. Chairman Luetkemeyer, Ranking Member Cleaver, and members of the subcommittee, thank you for the opportunity to testify today. My name is Tom Woods, and I am a builder from Blue Springs, Missouri, and the National Association of Home Builders (NAHB) chairman of the board. NAHB has a long history of supporting NFIP, and we are committed to ensuring that it remains a viable and affordable program to its policyholders while being mindful of the costs to the American taxpayer.

NAHB commends the subcommittee on addressing this critical issue early in the year, and we look forward to working with you and your colleagues as you contemplate changes to the NFIP to ensure that federally-backed flood insurance remains available, affordable, and financially stable.

The unprecedented losses suffered in 2005 and in 2012, including the devastation brought on by Hurricanes Katrina and Sandy, have severely taxed and threatened the solvency of the NFIP.

While these events have been tragic and sobering, resulting reforms must not be overreaction to exceptional circumstances.

Instead, reforms should take the form of thoughtful, deliberate, and reasoned solutions. A key step in this process is to take stock of where we are today, what has worked, and what has not.

While the NAHB supports the passage of BW-12 to ensure the continuation of the NFIP, the legislation created unintended consequences that resulted in dramatic flood insurance premium hikes that hurt the sale, construction, and remodeling of homes. The combination of inaccurate mapping into higher risk flood zones, and the immediate shift to full actuarial rates for many homeowners resulted in increases that priced prospective buyers out of their developments and forced the cancellation of sales, harming communities.

HFIAA fixed many of the problems associated with BW-12. It provided that those who were charged higher rates should be refunded for excess premiums, specified that properties should and would continue to pay their grandfathered rates, and repealed the requirement that flood insurance premium increase immediately to full actuarial rates upon the sale of a home. The return to grandfathered rates provided a more affordable rate structure for policyholders. NAHB has estimated that in 2014, because of HFIAA, there was $755 million more in new construction and $361 million a year in additional remodeling.

Any reform efforts need to address the accuracy of the flood insurance rate maps. For flood maps to be fair and accurate, they have to take into account all flood-control structures. Consequently, many properties are incorrectly mapped into flood plains, which results in homeowners being forced to purchase unneeded flood insurance. It typically takes years for those mistakes to be fixed, often requiring a lengthy and costly appeals process for the community, the builder, and the homeowner.

There is an opportunity for home builders or landowners to elevate plots of land out of the flood plain through the letter of map change process. For example, I engaged in a CLOMR-F process in a subdivision I built in Independence, Missouri. It took over 8 months and a quarter of a million dollars for FEMA to approve the map change. In States with short construction seasons, going through the letter of map change process could create devastating costs and delays.

I would like to thank the subcommittee for the opportunity to share NAHB's views. Home builders have long supported commonsense changes to the NFIP, and we urge Congress to continue to support and protect small business owners and homeowners from the exorbitant rate hikes and inaccurate mapping we have seen in the past.

Thank you.

[The prepared statement of Mr. Woods can be found on page 60 of the appendix.]

Chairman LUETKEMEYER. Thank you, Mr. Woods.

I want to thank each of the individuals testifying today for your testimony.

And, without objection, your written statements will be made a part of the record.

With that, I want to recognize myself for 5 minutes and begin the questioning.

Mr. Ellis, you make a lot of different statements, a lot of interesting conjectures as to how things could be, should be. You are looking at private insurance, to go that direction. How do we get there? And what do we do with mapping if it is still necessary, if you go to a private insurance market?

Mr. ELLIS. Sure. Thank you, Mr. Chairman.

Chairman LUETKEMEYER. You still need the NFIP, I think, I guess also.

Mr. ELLIS. Right. So there is currently built into the rate structure a certain charge that goes to every policyholder under NFIP that is supposed to go for mapping. And then, there are also appropriations that augment that go for mapping. We believe that as you develop the private marketplace, there should be explicitly a similar fee, a matching fee, for mapping that is done on the private sector policies. It would be exactly the same as what somebody is do if paying an NFIP as they would paying the private sector, as this sort of a sur fee, if you would. And that way, one is we are still going to have the mapping required by the Federal Government to do the mandatory purchase requirement, unless you all decide to change that. And so we need to make sure that is retained. And so that would be how we would envision that would be addressed, Mr. Chairman.

Chairman LUETKEMEYER. Mr. Heidrick, one of the things that you were talking about was the low take-up rate. What is your solution for that, or do you have a solution, or do you believe that is just an inherent problem with the nature of flood insurance?

Mr. HEIDRICK. Thank you, Mr. Chairman.

I believe the inherent problem is the catastrophic nature of flood risk. As I am talking to clients, you think of homeowners' insurance, auto insurance, these are products they typically buy every day that can experience higher frequency, sometimes lower severity losses. Flood insurance doesn't work like that. Flood insurance is catastrophic in nature and often hits the people who least expect it.

And one of the largest challenges we have in communicating flood risk right now is the binary nature of the existing maps. When you look at frequency, there are only 3 categories the National Flood Insurance Program specifies: less than a 0.2 percent chance of flooding in a given year; 0.2 to 0.99 percent; or 1 percent or greater. So imagine you have two houses that are on either side of the line, whether that line is inside or outside of the SFHA or in between two flood zones. And consumers are led to believe that because they are on the safe side of that line, they don't need to purchase flood insurance. The rest of that statement is actually, they don't need to purchase flood insurance to satisfy their lender, but there certainly is still a risk. And the relative risk between those two homes that I just gave in that example is much closer than in or out.

Chairman LUETKEMEYER. Along those lines, if it is more difficult for people to ascertain they need it, and if you would go to a more private market, how would you market the insurance? Are you going to market like you do car insurance and homeowners insurance, or life insurance, where you would market it as one of those risks that is out there? Do you see a marketing program that would help do this, to show people the need for this, or is this something that the government is going to have to do, or the local communities who live in the flood plain areas are going have to do? How would you market the product if it is a private sector product?

Mr. HEIDRICK. I don't know that I would market it any differently than I market any other product. When I am meeting with a client, I am assessing their overall personal risk, whether that is wind or flood or auto or life or health, where each individual may have a different set of risks or those risks may be more severe or less severe from individual to individual.

One of the things that I believe the private market may be able to do better than the NFIP today is price in a more granular level. So the example I gave before, where there are 2 homes on either side of a line, and sometimes 10 feet can make several thousand dollars of difference in the cost of flood insurance for an individual, that is going to weigh heavily on their cost-benefit analysis. But if the private market is able to make it more granular, it would be a different outcome.

Chairman LUETKEMEYER. Mr. Woods, you deal with this every day. With the fact that you build homes and hopefully you can sell them, financiers are supposed to be required to have in their files a document that says this either is or is not subject to flood insurance. How do you see this playing out with the private market? How do we solve this problem of participation?

Mr. WOODS. I think, number one, again, and not to beat it to death, but the flood maps have to be accurate. Without that, you are at a loss. You can't make that judgment.

The second thing is simply an educational process. Right now, we are working where the only person having to have flood insurance is that person who is within the 1-percent area. And there are a number of answers to that question. Right now, with new construction in those areas or significant remodeling, you are required to move the base elevation of that house above the flood plain by whatever means. And then as you go down through the list, there are others. So I think you do it through education. But I think you have to have the confidence, and the home builder, the city, and the homeowner have to have the confidence that those maps are correct.

Chairman LUETKEMEYER. Okay. Very good. My time has expired.

With that, I will recognize the ranking member of the full Financial Services Committee, Ms. Waters, for 5 minutes.

Ms. WATERS. Thank you very much, Mr. Chairman.

I would like to thank all of our panelists who are here today. And I am especially listening to Mr. Woods from Missouri. I am from Missouri, and you have three members on this committee who represent Missouri. And the recent floods, all of the flooding that has taken place in Missouri and in that St. Louis area where rivers converge have caused me great concern as I have been concerned about other areas of this country. And I spent a lot of time after Hurricane Katrina working down there with the residents who were just so harmed by Katrina.

I was part of a problem. Biggert-Waters was not right, and it increased those premiums for homeowners, but I was part of a temporary solution also to fix that. And now, I am interested in a permanent solution.

And I agree with you. If we can't get the mapping right, we won't be able to do the reform that is absolutely needed in this program.

I guess you have already said it, but would you just reiterate how important it is for us to get the maps right? I don't know what it is going to take. I know it is going to take some more resources to do that. It is going to take expertise that should be both public and private, but would you reiterate for us the importance of mapping?

Mr. WOODS. Certainly. Without a correct map, all that we do, other than that is really wasted. None of us can guarantee what the outcome will be. But I want you to understand also about the mapping and why it is so important. The map is only good if the local community follows the map. And I will give you an example back to the Independence example. I could move all of my property, in fact, above the 500-year flood plain, simply by constructing some lakes in the area and elevating the rest of the ground. I could contain all of my water onsite. However, the one thing I could not address is waters that were coming to me from other areas.

So it can't be a piecemeal, one-spot area. It has to have the hydraulics in the entire flood plain within it.

The second thing is, I believe there are some tremendous cost savings to be realized. Two points. I, in fact, mapped the flood plain. I, in fact, knew where there were some errors in the flood plain that have existed for years, and yet we have not been able to get them addressed. All right? So I believe that we ought to rely on that data. If accurate, it wouldn't then require a second set of mapping; it would require a review.

And the second thing is—and this may be a novel approach for here, but we need to stop spending all our money suing each other to prove who is right. And, ultimately, I was a winner, but the bottom line is that money could have been well spent to have improved both the mapping and the area if we were working together.

Ms. WATERS. If I may just continue, there are some people who believe it is impossible to get this remapping done and that it is going to cost too much money. Some people even question the expertise. But you believe that it can be done, is that right?

Mr. WOODS. I believe it can be done if we all work together. I don't think you have to go with where is it important to remap. It is not all that important to, perhaps, remap many areas of the country where there isn't that much exposure. Those areas that have the most population, the most economic drought, those are certainly the ones that should come first. But those are also the areas where you are going to have the help of the home builders, the developers, and perhaps the cities. I think they are all interested in this.

Ms. WATERS. So you do believe that the private sector could really help us in getting this remapping done?

Mr. WOODS. It could help you, but they are going to have to know that there is an effort from the regulator side to—I am not asking to accept anything that is not right, but I am asking to stop being adversarial throughout this whole process.

Ms. WATERS. I do believe that the chairman of this subcommittee, Mr. Luetkemeyer, who is from Missouri, is headed in the right direction. And I do believe that he can get all of the forces together so that we can get this right. So I am very optimistic.

And I thank you for your testimony.

Chairman LUETKEMEYER. I thank the ranking member. The time has expired.

With that, we recognize the gentleman from New Mexico, Mr. Pearce, for 5 minutes.

Mr. PEARCE. Thank you, Mr. Chairman.

Mr. Woods, could you give us a little bit more explanation? You said, "if the regulators would stop being adversarial," I think was your last statement. Could you give us a little bit more insight into that adversarial relationship?

Mr. WOODS. Just recently, a flood map was adopted in the Little Blue River Basin in Independence, Kansas City; it runs through both cities. And, in fact, we knew there were errors in that map. The cities knew there were errors in that map. The two cities' maps did not match. And the bottom line was I was told, when I asked a question of some people, to FEMA, basically told, "Why didn't you step up and provide it?" Number one, in the economic conditions that we are in, I wasn't able to do that. It wasn't worth my time.

But they had that information. In fact, one of the major changes in that flood map was a realignment, a regrading of the Little Blue River, which is the river that would be flooding those grounds for the most part. And that was done by the Corps of Engineers 10, 12 years ago. The changes the Corps made were not reflected in the map, readily available, I would believe.

Second, there was a Federal road project in that area, and during that road project, they took two of the bigger bottlenecks out of the flood plain with some bridges and that kind of thing that they did. Those significantly changed the way that flood plain operated. And that information was readily available from the highway department. But they were still not included because they simply are not playing team ball. And so, those are all very important.

And the last thing was just the way, when we submitted for our Conditional Letter of Map Revision Based on Fill (CLOMR-F), we went out—we did it a little differently. Before we submitted and before we even did the plan, we invited all of the parties to the site, which is about 500 acres, and physically wanted to walk the site with them and show that we could be good stewards; we could improve wetlands; we could stop the flooding; we could enhance the property. And the result wasn't what I expected. We, quite frankly, became a guinea pig instead of—

Mr. PEARCE. We have undertaken two rewrites of flood plains ourselves as an office, and it is much more difficult than it should be. You have the facts, they have the facts, but they refuse to rewrite it. So, I just want to get your insights on that.

If a builder knows that an area is not being described in the flood plain, is he allowed to go in and make the changes with his knowledge that it is actually on the flood plain, or does the agency stop him from doing that?

Mr. WOODS. The agency stops him from doing that.

Mr. PEARCE. Yes, this is the craziness that is called the U.S. Government today.

Mr. Heidrick, basically, it is my understanding that the insurance program, the Flood Insurance Program, was solvent up until maybe 10 years ago, just as whatever flood it was before Katrina, so it was about a billion in and a billion out. Then we had a several billion dollar problem, and then Katrina followed up with about a $13 billion problem, and so now we are underwater in the program. Is the program basically back to being solvent, about the same amount in, same amount out, except for these catastrophic events, or is it not even close to solvent these days?

Mr. HEIDRICK. It is my understanding—excuse me, thank you for recognizing me—that the $23 billion in debt really represent those two extraordinarily rare catastrophic events, which are Katrina and Sandy. Outside of those events, the program would be operating just as it was originally designed, which is without surplus—instead of surplus, a line of credit to the U.S. Treasury where it would borrow during years of need and pay back during other years, which—

Mr. PEARCE. Yes. Mr. Ellis, do you know if anyone has done extensive studies on the fraud? I know that I was in New Orleans maybe a year or 2 years after the bailout and the money that was sent down there, and billions of dollars sent, and just story after story in the short time I was there about people collecting the money and never fixing the houses. Has anyone done an extensive study on that to determine the amount of fraud in these programs?

Mr. ELLIS. The lead inspector general after Katrina was the Department of Homeland Security's Inspector General, and they kind of led all the other agencies. And they did a lot of investigation into that area. And there has been some documentation on that. GAO also did a report on missed payments a couple of years ago as well.

Mr. PEARCE. Is it extensive?

Mr. ELLIS. It is present. I think any time you have a Federal program, you are going to have some waste, fraud, and abuse, unfortunately, which keeps people like me in business. And so, I think that is still going to be an issue.

One other thing, Mr. Pearce, I just want to point out, is that we knew these kinds of catastrophic events were going to happen. So even if it was on the margins that the program was actually solvent, in large scale, we knew that there would be some event. We didn't know it would be Katrina, and Rita and Wilma in 2005, and we didn't know it was going to be Sandy in 2012, but we knew something was going to happen to make this program insolvent.

Mr. PEARCE. Thank you.

I yield back, Mr. Chairman.

Chairman LUETKEMEYER. The gentleman's time has expired.

With that, we go to the gentleman from Missouri, Mr. Cleaver, the ranking member of the subcommittee.

Mr. CLEAVER. Thank you, Mr. Chairman.

And let me preface my questions to the panel by thanking you, again, for this hearing. There is a lot of criticism thrown at Congress for waiting till the last minute and so forth, and the fact that we are starting on this right after the New Year, giving us almost a year to do this, I think is commendable. So thank you very much.

I want to find out if any of you on the panel believe that Congress should completely eliminate the NFIP? Is there anyone?

[no response]

Mr. CLEAVER. I am glad. Because we tried that a couple of times, and it didn't work, which I understand. Most of the private carriers have suggested previously in hearings before us, not during this session of Congress, but previously, that the private insurers could not diversify their losses, and so it made it practically impossible. And if you pay $130 premiums, if you put all the premiums together, they are not sufficient to cover the cost of the damage of a flood.

So is there anything that you think we could do to further encourage private insurers to participate in this program? Anyone?

Mr. Ellis?

Mr. ELLIS. Ranking Member Cleaver, absolutely. Tomorrow, you are going to have a hearing on Mr. Ross' bill along with Mr. Murphy, that would actually fix, adjust the definition of what is or what would represent insurance that met the mandatory purchase requirement. There are insurers in other States, even after Biggert-Waters was enacted, before the subsequent legislation, that we are starting to—in West Virginia and in Florida—that wanted to write insurance. So there is definitely an appetite and effort there. Some of it is just making it easier for that program to develop.

And then, actually, also, I think that which will also bring the private sector in is some of the consumer demand, because flood insurance, as was indicated by Mr. Heidrick, is a pretty limited product. I mean, you can't insure your basements. You have a limited $250,000, plus $100,000 for contents. There are other things they can do with the products they can make that are going to attract new ratepayers—or new policyholders on a product basis.

Mr. CLEAVER. So how many of you would have thought or believe the revolving loan fund that actually at one time started was the right direction to go? There was a revolving loan fund up until, I think, maybe in the 1980s, sometime in the 1980s. And eventually the private sector was then—with FEMA, and they ended up in some kind of conflict and the both sides mutually agreed to discontinue the revolving loan fund.

Mr. ELLIS. My understanding, Ranking Member Cleaver, in the 1980s, was that also that was when they changed to actually having borrowing from the Treasury, and before that, there were appropriations that would backfill and dealt with that, and they forgave about a billion dollars of debt and then went to borrowing from the Treasury. That is my major recollection at that time.

Mr. CLEAVER. What would you suggest, any of you, that this committee look at in terms of trying to put together the best piece of legislation we can when the renewal time is closer to us?

Ms. TEMPLETON-JONES. I would like to also support Mr. Ellis' comment about H.R. 2901. I think H.R. 2901 is the first very important piece of legislation that would enable the private sector to start moving into the marketplace. We are starting to see, because of private capital, private markets are moving in, slowly but surely. We are seeing them move in with some better coverage, many times less expensive premiums. But in order to clarify the Biggert-Waters definition of what private flood insurance is acceptable, I think it is essential that H.R. 2901 be passed as well as we need to eliminate the noncompete clause in the program.

Mr. CLEAVER. Thank you.

Mr. Woods mentioned the 500-year floods. I served as mayor for 8 years in Kansas City. We had two 500-year floods in 8 years.

And, also, let me just conclude, Mr. Chairman, by saying that I think the mapping is a critical issue which has to be resolved. Thank you.

Chairman LUETKEMEYER. I thank the gentleman. The time has expired.

With that, we go to the gentleman from Florida, Mr. Ross, for 5 minutes.

Mr. ROSS. Thank you, Mr. Chairman.

And I thank the panel for being here.

In 1973, it seemed like a good idea that we would carve out from an all-perils policy flood insurance. It just seemed like the thing to do at the time on behalf of consumers. As we fast forward to today, it is somewhat akin to carved-out cardiology coverage under a health insurance policy and led to terrible results and not to the benefit of the consumer. So trying to put these back together, I think, is not necessarily a function of the Federal Government, but more a function of those who are willing to put at risk their capital to make sure that they can not only manage that risk but to do so at the benefit of the consumer.

Mr. Ellis, you talk in your testimony about an all-perils policy, that including flood into an all-perils policy may, quite frankly, not only engage the consumer into wanting to buy flood insurance at a cheaper price because they will have limited risk, but, yet, the price of it would be so much cheaper that we in fact may cover more people through the privatization of flood insurance than putting it into an all-perils policy. Would you expound on that?

Mr. ELLIS. Absolutely. Right now, there is about—it changes, and it has been going down. There are about 5.3 million national flood insurance policies in the country. To put that in perspective, leaving aside multi-unit housing, there are about 100 million housing units in this country. So we already have an adverse selection and not very many people buying flood insurance, and even though FEMA says that a lot of their payouts are to people who are outside the mandatory purchase requirement area.

And so if this becomes a product that insurance companies can sell to their clients, then all of a sudden, it becomes less expensive. More people will be covered. We know these floods happen in these areas that are not in the 100-year flood plain, as has been indicated. So, actually, we can see an expansion in coverage in this country, which is certainly what we would like to see happen.

Mr. ROSS. And more sharing or pooling of the risk across?

Mr. ELLIS. Absolutely. We also would like to see a lot of that risk removed from the taxpayer onto the private sector where it belongs. Absolutely.

Mr. ROSS. Right. In August of 2015, FEMA stated in their reinsurance study that, “Reinsuring a portion of the NFIP’s insurance risk would be a logical step toward privatization and could provide an additional lever in the financial management of the NFIP.”

To your knowledge, has the NFIP or FEMA attempted to broaden or cede their exposure to the reinsurance markets?

Mr. ELLIS. I don’t know that they have actually gone further from that study, and that was—the reinsurance study was done by Guy Carpenter, and then that was their opinion on top of it. So we would like to see the committee prod FEMA to go in that direction and to explore that more.

Mr. ROSS. And if I might, Ms. Templeton-Jones?

Ms. TEMPLETON-JONES. I would just like to advise you that I have been made aware that FEMA has reached out to some reinsurers. Reinsurers have met with FEMA. So I do think the process is beginning.

Mr. ROSS. Good. And is it your understanding that there is capacity in the reinsurance markets to take a significant portion of this risk?

Ms. TEMPLETON-JONES. Yes, there is. Absolutely, there is.

Mr. ROSS. Let's talk, Ms. Templeton-Jones, about the process that was alluded to earlier. Let's assume, because I have a good friend of mine who is a registered land surveyor, site work contractor, back home, who lives in a house on a hill, that the base of the hill is in a flood plain; there is this structures, but he is 20 feet above. He has all the documentation because he can do it himself, but it is not worth his time and effort to challenge FEMA about his flood map, and so he is buying flood insurance. Do you believe that if you were to put capital in the market from private companies, a consumer would have a better opportunity, a better due process, and a better result if they were able to prove their home was no longer in a flood zone?

Ms. TEMPLETON-JONES. Absolutely. And I would like to take that just one step further than that. I think as the private market evolves—and, again, I want to clarify that this is going to be a long-term process.

Mr. ROSS. It is.

Ms. TEMPLETON-JONES. It is not going to be something overnight. But as the private market evolves, they will utilize more and more tools. Modeling will become more efficient. We will see better risk-analysis tools to enable that company to take that insurance and properly price it better with better coverage.

Mr. ROSS. And manage that risk better. In other words, to be able to help the consumer mitigate their exposure.

Mr. Woods, you talked about how you would build a home, the site you would build above the flood zone, and you could contour the land. For every $1 that we spend in mitigation pre-events funding, we save $4 in disaster relief. What this big parcel is—not getting rid of NFIP. That is not our goal. Our goal, as Mr. Ellis pointed out, is to make it residual market. We did this in Florida to a great degree as a bad example for several years in windstorm, but what we have done is we have been able to create a residual market and create a competitive market so that consumers can get the best product at the best price. That entails the private market.

Mapping is not an exclusive function of FEMA. If we put private capital into the market, I submit to you, you would see so much technology come into the game to be able to map not only better but more granularly because the capital that is put at risk wants to be managed better. Would anybody disagree with that?

[no response]

Mr. ROSS. Thank you.

My time is up. I yield back.

Chairman LUETKEMEYER. I thank the gentleman. Time has expired. With that, we go to another gentleman from Missouri, Mr. Clay, for 5 minutes.

Mr. CLAY. Thank you, Mr. Chairman, and I thank you and the ranking member for conducting this hearing.

Mr. Ellis, the question of how to balance the goals of affordability and risk-based rates has been a key question for Congress in seeking to improve the National Flood Insurance Program over the years. Do you believe that these goals are fundamentally opposed, or do you believe that there is a way to appropriately balance these goals?

Mr. ELLIS. I believe there is a way, and we have to find a way, Congressman Clay. What we have said is that right now when you have the subsidies that are built into the program, they are relatively hidden from the consumer. There isn't an explicit knowledge of what the subsidy is, and then also they are not means-tested. That means it is basically if you owned the house that was before the flood insurance rate map, you get the subsidy. And so we think that as rates increase—and we think they do need to increase, if there are cases—we need to do a means-tested, and we need have very targeted assistance that is outside the rate structure. We are open to talking about ways to do that. The Wharton Risk Center has talked about vouchers. There have been other ways of looking at how to address that for that core.

And then also the other thing is that reducing the rate or making people pay less, doesn't reduce their risk at all. It doesn't encourage them to reduce their risk at all. And so to some extent, one of the things that we have talked about is also looking at even prefunding some of that subsidy so that people can actually use that to mitigate and reduce their rate by reducing their risk. And that way, we are not putting people in harm's way, encouraging and subsidizing people to be in harm's way, but we are actually helping them out of the flood plain.

Mr. CLAY. Thank you for that response. Mr. Woods, an example of Missourians rebuilding just recently, is that over the holidays, we experienced flooding in and around the St. Louis region. One community allowed for the homes to be elevated after the last flood. I guess they put some of the houses on stilts, I will say.

Do you think that is smart, as far as allowing them to remain there and raise the elevation? This time, they still had to evacuate the community because the water rose too high. What do you think about them elevating and raising the level of the house?

Mr. WOODS. I think that—

Chairman LUETKEMEYER. Your microphone is off, sir.

Mr. WOODS. I'm sorry. I think that there are all kinds of economic issues that start to play into this, and elevating may be the solution, but there are other solutions to look at. Would it have been less expensive, less catastrophic, to have moved those houses someplace else, out of the flood plain; and, again, where would that be? And what you really get into is many of those people are probably close to their jobs. That may be the only house they can afford. All kinds of things.

So it is not an easy question, and I think it is greatly driven by just the demographics of the area. But at the same time, I think you have to have a comprehensive solution that includes the city and the county, and the State, so that we are making good decisions based on good science.

Mr. CLAY. Another question: Can you explain why the removal of grandfathered and subsidized rates on existing homes is a concern to your organization, which represents the interests of builders of newly constructed homes?

Mr. WOODS. If you do that—basically for home builders, nearly 50 percent of all prospective home buyers are what are called move-up buyers, your person with a house on stilts or four stilts. Okay? These individuals must be able to sell their current home. And if you took away that subsidy or the grandfathering of the rates, you are going to devastate the price of that home, and they are no longer going to be move-up buyers. They will simply be trapped in that residence until the rest home. Again, we rely on the ability of homeowners to move up, and owners to buy newly constructed homes. Many home builders and many homeowners have lost the ability to buy or the ability to sell simply because of that rate structure.

Mr. CLAY. Thank you for your response. Mr. Chairman, I yield back.

Chairman LUETKEMEYER. The gentleman yields back. And with that, we go to the gentleman from Kentucky, Mr. Barr, for 5 minutes.

Mr. BARR. Thank you, Mr. Chairman. We will start with Mr. Ellis, and the question I have is, can you describe how the National Flood Insurance Program discourages private insurance, if at all?

Mr. ELLIS. We talked a little bit about Mr. Ross' bill, and one of the issues has been what exactly constitutes a private policy that would meet the mandatory purchase requirement, and his bill would clear that up in allowing the State insurance regulators to designate that. But that is just dealing with the mandatory purchase requirement. Obviously, there are people who do purchase flood insurance that are outside the flood plain. And part of it is that if the Federal Government is undercutting the rate, it is actually selling at a subsidized rate, both because either the rate is explicitly subsidized or because they can borrow from the Treasury, then you are really undercutting and crowding out the private marketplace. We believe that as rates increase, which they have been, that will become more competitive and actually allow the private sector to step in.

Mr. BARR. Thank you. For those who are at risk, who are presently not mandated to have flood insurance, how do we do a better job encouraging those individuals to go ahead and get the coverage? Is it the all perils policy? Is it more capacity in reinsurance, inviting more reinsurance in there? What is the best way to do that?

Mr. ELLIS. Congressman Barr, I think that it is all perils, and as the private sector gets more engaged in the flood insurance market, and some of that will be because of clearing up some of the issues in the hundred year flood plain or the Special Flood Hazard Area, then there will be more companies writing policies. There will be more experience with writing policies, and that should actually attract consumers and actually more policyholders. That is certainly what we believe and think that will happen.

Mr. BARR. The reason I ask is in flood-prone areas without the mandate to purchase flood insurance, I think the statistic is that only 1 percent of those structures are insured. So, developing that marketplace is very critical.

To Mr. Woods, though, my question to you all would be, is moving toward actuarially sound rates and risk-based pricing a real impediment to real estate transactions? And I would like to hear your thoughts on that.

Mr. WOODS. I don't know that it is. I don't have any information, and we don't have any policy. We are going to be discussing this very thing next week in depth at our meeting. I tend to lean on the side of open competition usually. It gets you the best answer.

Mr. BARR. We have seen, in my area in central and eastern Kentucky, real problems with the accuracy of the maps. And Mr. Woods, I couldn't agree with you more. We have to get to more accuracy in maps as part of that process of inviting more coverage. Can any of you all elaborate a little bit more on some of the issues that the members of your associations have had with these maps, and what are some of the ways that we can improve the mapping?

Mr. HEIDRICK. If I may?

Mr. BARR. Sure, yes. Go ahead.

Mr. HEIDRICK. Thank you, Mr. Barr. As I stated earlier, having a more granular view of flood risk is, I think, of paramount importance to consumers who live outside of the Special Flood Hazard Area. Twenty percent of all flood insurance claims occur outside of the Special Flood Hazard Area.

In Columbia, South Carolina, from what I understand about 792 people had flood insurance policies. These are examples where if you had a way to measure risk maybe on a scale of zero to 100 for instance, and I know that the NFIP is currently working on some way to articulate risk in this way, to help customers understand that they are not immune from flooding simply because they live on one side of a line or another, we would have much more recognition, it would improve the takeup rate.

Mr. BARR. Mr. Ellis?

Mr. ELLIS. Yes. Congressman Barr, also there is a lot of mapping that is being done and modeling that is being done by the private sector, companies like CoreLogic, that have some of this data, and I think it is important—I believe as Mr. Heidrick mentioned before—the maps that FEMA does are really a snapshot, and they are looking backwards.

The risk modeling is looking forward, recognizing there are changes in development and other patterns, and that can help inform consumers more that they have this risk. It is not this binary situation where you either have to buy it or you don't have to buy it, and if you don't have to buy it, then you think you are not at risk, when in reality you are at some risk and it could be quite considerable.

Mr. BARR. Yes, ma'am?

Ms. TEMPLETON-JONES. I would just like to elaborate one piece. I absolutely support flood modeling. I think we are seeing it, but I do want to make sure the committee realizes it is in its infancy. It is going to get better. Mapping needs to be the starting point, and then we need to build upon that with the modeling and so forth.

Mr. BARR. Thank you. I think my time has expired. Thank you for your testimony. I yield back.

Chairman LUETKEMEYER. The gentleman's time has expired. We now go to the gentleman from Texas. Mr. Green is recognized for 5 minutes.

Mr. GREEN. Thank you, Mr. Chairman. And thank you, Mr. Ranking Member. And I thank the witnesses for appearing as well. Let's for just a moment look at the markets in terms of how they impact affordability, more specifically, the residual market juxtaposed to the voluntary market.

For our purposes, I think it is fair to say that the residual market is a market of last resort. The voluntary market is a competitive market. And the way we structure the residual market is going to have a lot to do with affordability. So I would like, Mr. Ellis, to visit with you, because I have read your testimony in its entirety, and the last paragraph of it where you give your conclusion, I think, is quite revealing. You indicate that the Federal Government will develop the residual market. How will that market be developed such that we will still have competition in the voluntary market, and not have the taxpayers assume all of the high-risk persons that the voluntary competitive market does not find beneficial in the sense of profits and loss, market demands?

And I mention this to you because, as you know, with the health insurance we find ourselves with insurance companies assuming a lot of clients, if you will, who are not over age 62 to 65. When you get above that, insurance companies are not enthralled with the notion of having you as a client, customer. And given that I am above that age, I kind of look into these things, as you can well understand. I see you smiling, so you understand what I am talking about.

So what I am interested in is finding out how do we have a residual market that will have a positive impact on affordability given that the voluntary market is where everybody wants to be, and getting insurance companies to go residual can be exceedingly difficult?

Mr. ELLIS. Thank you very much, Congressman Green, for the question. Part of what we are observing, which was actually observed in the reports that came out after Biggert-Waters, the FEMA reports that came out, is that the residual market is where it is actually going. Unintentionally or intentionally, that is what is developing as the rates increase in the flood insurance program and as competition is going to come in. And so our point has been that it needs to be—and I think you are spot on, Congressman—an intentional decision by Congress on how to develop that and how to protect those consumers.

Also, as it becomes a more concentrated market, then it becomes something where Congress and the Executive Branch can target mitigation to help those people out. So it is not just about affordability because we are giving them subsidies or we are giving them a cheaper product, but we are actually reducing their risk so there becomes an appetite in the private sector to write policies for them as well. Because unlike your example in health care, and I am not an expert in that area at all, but it isn't that there is a 60-year-old house—it's not that houses get to being over 60 years—obviously there are houses that are 100 years old, but that same characteristic isn't analogous. We could actually make that 60-year-old house, at least in a risk standpoint, be a 30-year-old house if we do the right mitigation tactics.

Mr. GREEN. Given that I have about a minute and 18 seconds left, permit me to ask this. Help me to flesh it out. Help me to understand, and others who are listening at home to understand, what you would do specifically to make sure that the residual market is affordable for persons who are going to live along the Gulf Coast. I am from Texas. I went through Katrina, Rita, and those who are on the East Coast where we had Sandy, how do they have affordability? Give me some examples of how it can be done?

Mr. ELLIS. One of the things that came out of Wharton was this idea of vouchers to help people purchase their insurance. But I also think, and I know I am kind of going back to this, I think we should be trying to mitigate their risk and providing them assistance to mitigate their risk to reduce their rate rather than just giving them subsidies. But we already have certain affordability provisions built into flood insurance with the Pre-FIRM structures that have explicitly grandfathered and subsidized rates.

Mr. GREEN. And by mitigation, you mean cost to replace or repair?

Mr. ELLIS. Well, no, not to repair or replace. It could be to relocate. But it also could be to elevate or other mitigation tactics. I think that what we want to do is reduce the risk. It was brought up earlier that for every dollar we spend on mitigation, it is $4 less in disaster costs, and we think that would be the way to target it.

Mr. GREEN. Thank you, Mr. Chairman. I yield back.

Chairman LUETKEMEYER. The gentleman's time has expired. With that we go to the gentleman from Pennsylvania. Mr. Rothfus is recognized for 5 minutes.

Mr. ROTHFUS. Thank you, Mr. Chairman. Mr. Heidrick, in your written testimony you assert that "private insurance industry lacks the capability to underwrite flood insurance on a pervasive basis to meet customer needs." Could you elaborate on how you and the Big "I" arrived at that assessment?

Mr. HEIDRICK. Sure. It is a market that is in its infancy. In the United States, there are not a lot of insurers who have a lot of expertise. There is a dearth of claim data, and as the claim data is lacking. Without having loss experience and the ability to price accurately based on that experience, those are impediments that will, we believe, the Big "I" believes, will be overcome over time and modeling will get better over time. But as we sit here today, we don't believe that the private market is capable of fully replacing the NFIP.

Mr. ROTHFUS. Are there reforms outside of the Ross-Murphy legislation that the committee should consider to remove barriers preventing the private sector from contributing to the flood insurance market?

Mr. HEIDRICK. I believe there are a number of reforms that are already existing that will play out over time, will manifest themselves over time. The changes that were made in 2012 and 2014 were aimed to bring rates up to something that is more reflective of a market level. There is actually a flip side to that coin as well, though. It also resulted in a number of policies, and according to the NFIP, 80 percent of the NFIP policies had actuarially correct ratings before those measures were put in place.

So now there are additional surcharges and assessments that are outside of the true cost of risk that actually are going to give the private market an ability to come in, and they don't need to charge those for those costs, so it is going to make some risks more attractive to the private market.

Mr. ROTHFUS. Ms. Templeton-Jones, Biggert-Waters attempted to address the issue of those properties with multiple damage claims that have been a serious financial drain for the NFIP. Do you believe that FEMA and the NFIP have the tools necessary to address high-risk repetitive loss properties?

Ms. TEMPLETON-JONES. I think Biggert-Waters 2012 was absolutely the beginning of heading in the right direction. I think the challenge still is the biggest drain on the NFIP, is the severe repetitive loss properties, and I believe targeted mitigation efforts should be addressed at those properties.

Mr. ROTHFUS. Beyond the targeted mitigation efforts, would there be other reforms that you might propose?

Ms. TEMPLETON-JONES. I think targeted mitigation on those severe repetitive loss properties is the key on that.

Mr. ROTHFUS. Mr. Woods, with the NFIP being $23 billion in debt, GAO has classified the program as high-risk, citing NFIP's artificially low rates which are insufficient to cover obligations and projected losses. I worry, and many of us on both sides of the aisle are deeply concerned, that another catastrophic event could push the NFIP's debt level above the $30 billion mark.

In your testimony, you write about the importance of ensuring that this taxpayer-backed program is financially stable so that it can continue to meet the needs of its participants. I think we can both agree that the current situation is unacceptable to the taxpayer. What are some ways that we can improve the financial sustainability of the NFIP and reduce taxpayer exposure to significant losses?

Mr. WOODS. Again, I think from what Ms. Templetone-Jones said, I think also from the fact that if you got the private sector involved and the competition that would take place there, and, again, we go back to the mapping. But the reality of the mapping is there are many things, and I happen to think if we were all on the same side—the insurance company wanted to sell insurance. The home builder and developer wanted to develop ground—that we would work together to find a solution that gave each of us the best chance of success. That is not happening today in the system.

We are spending all of our money on people who are almost guaranteed—well, we are not spending all of our money there, but we are really spending the money on people who are guaranteed to have a flood. We have insured property, and if the ones we are insuring are pretty well guaranteed to have the loss, that is fine, but I think you could do these other things that would help us all in the free enterprise system. They won't do it in one afternoon, and unfortunately we might get that disaster in one afternoon. But the reality is that over a period of time, I believe they could.

Mr. ROTHFUS. There remains a concern with affordability in my district in Western Pennsylvania. Mr. Ellis, you touched on affordability. Can you elaborate on some of your ideas on how NFIP can address this affordability issue?

Mr. ELLIS. Congressman, as the rates increase, and one of the issues we talked about and I mentioned earlier was the Wharton study looking at vouchers and sort of something outside the rate structure. Our biggest thing is making sure that people know their risk by knowing their actual rate, and then whatever we do as a country to help those people purchase insurance, that it be outside the rate structure so that they can actually inform them of their risk and then help them mitigate that.

Mr. ROTHFUS. Mr. Heidrick or Ms. Templeton-Jones, do you have any thoughts? I guess I am over my time. I yield back. Thank you, Mr. Chairman.

Chairman LUETKEMEYER. Darn that clock, right? The gentleman's time has expired. With that, we go to the gentlelady from Wisconsin, Ms. Moore, for 5 minutes.

Ms. MOORE. Thank you so much, Mr. Chairman, and let me join the chairman and the ranking member in thanking and welcoming this distinguished panel.

It is hard to know who to ask questions of because all of your testimony has been very compelling. But I want to ask a question, and I want to prioritize getting answers from Mr. Ellis, Mr. Woods, and Mr. Heidrick.

And I just want to reference the fact that Ms. Templeton-Jones, in your testimony you talked about the number of insurers that are just leaving the program because of the lapses and so on. So with that in mind, my question relates to a provision that I was able to get into the Biggert-Waters legislation, just a simple study of community-based insurance, and I was just wondering how some of the challenges, I believe it was Mr. Ellis, you mentioned, you laid it out very clearly, the debt, adverse selection, subsidies, the accuracy or lack thereof of the mapping.

How would a community-based flood program fit in with some of the solutions that you all have suggested, giving incentives for cities and States to do mitigation, really bringing more re-insurance and money and private sector dollars into a program, maybe mitigating the adverse selection by having a community-wide effort? I'm just wondering what your thoughts were on that?

Mr. ELLIS. Thank you, Congresswoman Moore. So, that study did result in a National Academy of Sciences report that came out recently. Separately, there was also one done by Resources for the Future that was very interesting. I think the challenge is that in 1968, we went with an individual policyholder perspective, and having it house by house. You can see in certain ways that maybe even layering it on—you think about the fact that people will have lower homeowners' insurance rates if the community puts in fire hydrants and such a regular pattern. And so, there are certainly things that a community insurance could try to overall reduce the individual homeowners rates in that perspective.

And then also, that was part of what I think that when they created the community rating system and required communities to actually opt into the flood insurance program, agree to operate under certain restrictions, and then also gave them benefit to their homeowners if they actually did community-wide mitigation measures or whatever, that actually is trying to replicate that, but I would recommend the Resources for the Future analysis on that.

Ms. MOORE. Okay. Mr. Heidrick?

Mr. HEIDRICK. Thank you, Ms. Moore. The Big "I" doesn't have a formal position on community-based insurance in general. It is an organization that supports choice for consumers to make their own decisions based on their own individual risk, and of course as we discussed earlier, there is gradation of risk. There are some people who are at more risk than others when it comes to flood insurance. So we think that those are factors that would have to weigh into a proposal.

Ms. MOORE. Mr. Woods?

Mr. WOODS. This is a very technical place. I think there are, with the community's involvement, ways to allow people to have a choice, and I think that choice is always important, but I think it does take the involvement of many of us, the insurers, as well as the communities, as well as the builders, and remodelers, and the homeowners.

Ms. MOORE. You don't think this would help with the cost, some of the challenges that were mentioned, to have a community-wide plan? If I don't particularly live in a flood plain, but I find myself paying 15 cents per thousand dollars of value on my property for a community plan where maybe somebody else pays more because they actually live in a flood plain, just say, New Orleans if I am in the Garden District, but I pay a very small premium to sort of mitigate, as a community plan, you can't see a place for that?

Mr. WOODS. I guess I would say, yes, there is possibly a place for that, and that kind of falls to that answer I had about being able to control my own piece of property, but I can't do it without the community working with the others, so I think it is the same thing.

I would also offer that we are already paying those rates. We are paying them in our taxes to the United States Government, and we are paying them in our taxes to the communities right now, because when it happens, we step up. That is what we do in the United States. And when we step up, we are spending that money.

Ms. MOORE. Thank you. I yield back.

Chairman LUETKEMEYER. The gentlelady's time has expired. With that, the gentleman from California, Mr. Royce, is recognized for 5 minutes.

Mr. ROYCE. Thank you, Mr. Chairman. I just would build on a conversation that Mr. Clay had, and this was, Mr. Ellis, in your testimony you said that masking subsidies with lower rates prevents policyholders from understanding their true level of risk. Is my understanding correct that under the current program, policyholders just see the premium payment that they need to make. Right?

Mr. ELLIS. That is my understanding, yes.

Mr. ROYCE. That is what they can see. How difficult would it be to break out the subsidy? How difficult would it be to make transparent the amount that the government or that the other taxpayers are covering on behalf of the homeowner?

Mr. ELLIS. One of the challenges would be for many of the policies that get the grandfathered or the subsidized rate, the preflood insurance rate map policies, they don't actually know the elevation of the actual policy, and so then there are some of the challenges in dealing with that. But I think that is something that would be worth doing, especially considering as we recommended that anything going forward as we are trying to do affordability issues, that the subsidy or whatever, the support be means-tested and be tested outside the rate structure. And so I think it would be a valuable effort, Congressman Royce.

Mr. ROYCE. It seems to me that if you can capture the information, that the increased transparency there would have a positive impact on future decision-making because it would probably decrease moral hazard. It would increase mitigation efforts, perhaps, but letting the policyholder understand that up front would be helpful.

My other point was that the Flood Insurance Program Act of 2012 attempted to address the issue of repetitive loss priorities, and this is where multiple claims have been made on the same property. So the GAO found that while these properties amount to 1 percent of policies, they account for 40 percent of all of the program claim losses. Do you think that 2012 reform bill gave the NFIP the tools necessary to address high-risk, repetitive loss properties, and what else could be done there?

Mr. ELLIS. Sure, Congressman Royce. Certainly in Biggert-Waters 2012, they had the provision there about increasing rates for severe repetitive loss properties. That did not get changed in the subsequent legislation, so that is still going on, and so we think that is a positive step.

But I think that also looking at some of the programs that FEMA already has to actually, they have the ICC program which is like a $30,000 cap and you could possibly increase that cap in trying to help people elevate or mitigate or relocate. And so I think there are things we should be targeting our resources because as you pointed out, Congressman, it is such a drain on the program that those are the most likely, the most beneficial, the best investment to try to mitigate or relocate them out of the flood plain.

Mr. ROYCE. And I think if people understand the risks they were taking or the likelihood, and if all of that data—well, let's hear some of the other perspectives on that issue, if I could just open it up.

Ms. TEMPLETON-JONES. I agree. I think we need to indicate what the actual rate is. We need to be actual rated policies. The challenge is, like Mr. Ellis has said, unless we have the elevation certificate, and not all properties, your PreFIRM properties, your older structures, your properties that are in the B, C, and X zones, which again we need to remember that 25 percent of all claims come out of your low- to moderate-risk properties, the B, C, and X areas, we don't have elevation data. Without that elevation data, we can get an idea, and come April 2016, FEMA is implementing clear, concise information to the policyholder; but again not having the elevation, is an impediment.

Mr. ROYCE. But it is not that many claims, there are not that many areas that we are discussing in the general scheme of things. How difficult would it be to try to obtain that information?

Mr. HEIDRICK. Mr. Royce, today it is house by house by house, and it requires a surveyor to go out, and the cost of that work is—it ranges by State, but somewhere between $200 and $1,000 per house. There probably are more efficient ways that it can be done—

Mr. ROYCE. There must be. Is there any way, with GPS or something, that would be cheaper in today's world?

Mr. HEIDRICK. There is a technology referred to as LIDAR which actually could be used, and I believe that the State of North Carolina has used LIDAR extensively in generating their own maps. North Carolina is a little bit different because North Carolina actually takes the lead on developing their flood maps.

Mr. ROYCE. Yes. We should probably ask the GAO to see if we can find a very inexpensive way in order to create a template here where we can get access to that information, and share it with the policyholders as well so that they understand in terms of the elevation, if you are in a flood plain. Anyway, my time has expired. Thank you very much.

Chairman LUETKEMEYER. The gentleman's time has expired. We have a few additional questions that we would like to ask. A few Members are still here. We will begin our second round with the ranking member, Mr. Cleaver from Missouri. He is recognized for 5 minutes.

Mr. CLEAVER. Thank you, Mr. Chairman. I want to direct this to Mr. Wood, but when we had the flood of 1993, one of the farmers famously said that to determine the 100-year flood mark, you put 99 white marbles in a jar, put in one blue marble, and shake it. And every time you pull the blue marble is the percentage of chances of having a 100-year flood. But you keep putting it back every time and shaking it again, so there is some unpredictability no matter what we do, but I think we ought to be intelligent about it.

Most people who are not familiar with Kansas City probably can't understand this, that in 1977 in the Country Club Plaza, the world's first shopping center, 25 people drowned in the middle of Kansas City, Missouri. I am not sure—I think we have fixed that with Brush Creek, as you know this, Mr. Wood. But I am pointing out, I think, to the best of our ability to also follow up with Mr. Royce, we have to use the highest level of technology possible and do this remapping.

But I am also concerned, and I would like to ask you, Mr. Wood, we have incurred a lot of debt. The NFIP has incurred a lot of debt over the past few years with all of the recent events. And then the opponents are always saying that the reason that the debt is so high is because of the subsidized policies in these exotic areas, these environmentally sensitive areas. Do you think that we ought to deal with trying to force people out of environmentally sensitive areas, the exotic places, building the house at the foot of a hill where you have annual mudslides, or do you think that we ought to just realize that is the way things are and try to build that into whatever program we put together?

Mr. WOODS. I will put it in the perspective, I guess, of the home builder, and talk about it from a new-construction perspective. That is the one I probably know the most about.

First, I don't believe that new construction within the flood plains is the reason why the NFIP is experiencing a shortfall in funding. It is quite the opposite. First, in order for a builder to construct a new home within a flood plain, the builder must ensure that the structure is compliant with all building standards within the flood plain. Second, all new homes, when purchased using a federally-regulated mortgage, are required under Federal law to obtain flood insurance under the NFIP. And third, as FEMA has already publicly acknowledged several times, new construction always pays a full-risk rate for that insurance, meaning newly constructed homes within the flood plains do not received subsidized insurance.

Additionally, NAHB has been told that in commonly flooded areas, new construction that is built today with current building codes routinely outperforms the existing housing stock that is there. So I think it is a process and the decisions need to be made based upon, again, we beat it to death, but the correct flood maps and the correct flow designs. And I would point out one other thing that I might add to it that goes back to our conversation, the elevation of a home, at least with new construction, is a very simple thing to gather. And that is a fact that we have to put that elevation on our building permit at the city, so a whole subdivision—and that is where most of the construction goes on—you could have those elevations immediately. They are part of the public record.

Mr. CLEAVER. Thank you.

Chairman LUETKEMEYER. The gentleman yields back. With that, we go to the gentleman from New Mexico, Mr. Pearce. He is recognized for 5 minutes.

Mr. PEARCE. Thank you, Mr. Chairman. Mr. Ellis, you mentioned here that 5.4 percent of the houses in the country have flood insurance. Have you broken that down also for the number of people in high-risk areas? Is that equally 5.4 percent?

Mr. ELLIS. I have not, Congressman. Basically, that number is realized by looking at the census data of how many housing units are in the country and then how many—

Mr. PEARCE. Would your guess be that it is a similar amount, that 5.4 percent in the high-risk areas have flood insurance, or do you think there are a little bit more?

Mr. ELLIS. There is a problem with the fact that there are properties in the mandatory purchases in the Special Flood Hazard Area that are not purchasing flood insurance, and GAO has done some analysis of that.

Mr. PEARCE. Mr. Heidrick, we get 9 inches of rain a year in New Mexico, in my district. Do we pay a higher insurance premium because of the events on the coastal areas?

Mr. HEIDRICK. Thank you, Congressman, no. The flood insurance rates are set by flood zone. An "A" zone is an "A" zone regardless of what State it is in. So if you are in a preferred-risk area, regardless of what State you are in, that is the rate you are going to pay.

Mr. PEARCE. If I could interrupt, several years ago we were paying hundred-year flood rates. Now, we are up to thousand-year flood rates. Doesn't that stick us with a higher premium? People would be more apt to have to pay flood insurance when we define it as a thousand year to get into the program, isn't that correct? That definition has not changed.

Mr. HEIDRICK. The mandatory purchase requirement is only to a 1 percent chance or greater of flooding. If your chance of flooding is less than 1 percent in any given year, then there is no mandatory purchase requirement. Did I understand your question correctly?

Mr. PEARCE. That doesn't gel with what banks and real estate people in New Mexico tell me. They tell me that previously they did not have to buy flood insurance, and after the great losses in Sandy and Katrina, they are having to buy flood insurance. And they said it is because of the redefinition of who has to buy flood insurance, who is required or encouraged to buy flood insurance. I will sort through that.

Ms. Templeton-Jones, are there areas that we absolutely should not rebuild in after they have been flooded and destroyed once or twice or 10 times, or should we have such a definition?

Ms. TEMPLETON-JONES. I think we need to mitigate losses. We need to take a property, if it is subject to having been flooded more than once or twice, the cost of that is to mitigate the property, raise the property, move the property outside of it. I think we need to also recognize that it is not just people who are wealthy who are living on the coast or at the bottom of this hill who will have these big, huge wonderful houses. Many times it is people who are just—I am originally from New Orleans. Granted, in New Orleans, Katrina was a huge disaster. But the vast majority of people are not wealthy people. These people live there because it is a major port. People have to live near where they work. So we have to find a way to protect these individuals, help them mitigate their properties, raise them, move them to a safer ground so that they don't experience the losses.

Mr. PEARCE. Would you go so far as to say that when it is within people's capability, or when a city has been told that they should mitigate and they don't mitigate, that they won't be covered under the program? Is that too extreme, that you would be somewhat responsible for your own actions?

Ms. TEMPLETON-JONES. I have my own personal opinions, but at the end of the day, people have to have a place to live.

Mr. PEARCE. I understand that, but there is no national tornado program. In other words, we don't have floods in New Mexico. We have tornados, and there is no national program to help us rebuild. We have forest fires that are created by whatever reasons, and there is no national program to help us rebuild from the forest fires. So where is the moral responsibility to people like us? We have to pay a higher program, and with all respect, Mr. Heidrick, I believe that we do pay higher rates. We pay rates because of people out there who suffer the problem, but they don't pay rates higher to help us suffer from our problems, so where is the moral component of that? If you would like to address that, or if you don't, it is okay, Ms. Templeton-Jones.

Ms. TEMPLETON-JONES. I think, and I have to agree with Mr. Heidrick, the rates are the rates across-the-board, and we see this every day. If you are in A zone, you pay A zone rates. If you are in a V zone or an X zone, you pay V or X zone rates. As far as the, there are some "gotchas" in it. If you don't have flood insurance and you experience a loss and you receive Federal funding, you have to carry flood insurance from that point forward. But I think we need to also recognize the fact that it floods everywhere. It is not just a coastal situation. Where it rains, it can flood. And unfortunately, people who experience flooding in coastal areas recognize it and do have a better uptake on the flood insurance policies. But it is areas that don't experience the floods often and we don't see the amount of flood insurance available.

Mr. PEARCE. We will leave the moral question hanging for another time. Thank you, Mr. Chairman. I yield back.

Chairman LUETKEMEYER. The gentleman's time has expired. I just want to kind of wrap it up. I have a question or two here myself. One of the things that was brought up was with regard to the debt of the NFIP. The gentleman from New Mexico makes a great point here about the different tragedies and catastrophes that we go through as a country.

Mr. Ellis, I am curious about your position on the debt that the NFIP has accumulated. Is that something that we should—whenever we did Hurricane Sandy, we found other monies in the budget and paid for it by doing that rather than extending the debt. Some of it is still there. And I guess the question becomes, actuarially, do you figure in those extreme events, or do you actuarially figure in the normal things that happen, like in my area here it just happened this last couple of weeks? What would your opinion be on that.

Mr. ELLIS. A couple of things, Mr. Chairman. So it is true that the debt was largely driven by the storms of 2005 and then by Sandy. One of the things, and just kind of getting to the point about people paying full-risk rates and not the subsidy, I would argue that the fact that the program can carry a $23 billion debt and still operate is a subsidy inherently. Subsidies are inherently baked into the program because no private sector, there is no profit that needs to be taken. You can operate with a $23 billion debt. And so I think that is actually already built into the program.

As far as the debt, it is pretty clear that it is very unlikely that it will ever be repaid under the program. They repaid a billion dollars 2 years ago. They hadn't repaid anything over several years. It is very unlikely that it is going to be repaid. But it does concentrate the minds of lawmakers and of the public about some of the challenges in this program and the need to reform it. So certainly we see that as an important symbol for actually continuing to reform and improve the program.

Chairman LUETKEMEYER. My second question, I guess, is, do you believe that we need to structure the program actuarially for the average losses per year, which are several billion dollars, versus the catastrophe that happens once every 10 years?

Mr. ELLIS. The way that FEMA had set rates before was that they looked at the average historical loss year over the previous decade, throwing out the highest loss and the lowest loss. You have to discount it, but you have to take into account these extremely large events, because we already know they can occur and they do occur. If you look at 2005 and the number of named hurricanes, we got into the Greek alphabet. We ran out of names. Clearly these are issues—and then there were a lot of people who said, well, that was a one-off. That was Katrina and it was a one year, but then not even a decade later, you had Sandy, which not only increased the borrowing authority for the Flood Insurance Program by $10 billion; it also required a $50 billion outlay from the Federal Government on dealing with that issue.

So I think you have to, Mr. Chairman, take that into account when you are setting the actuarial rates that there are these black swan events, there are these fat tail losses, but you have to discount it appropriately, and that is what actuaries are all about.

Chairman LUETKEMEYER. I guess the question becomes then, do you believe that when you structure the program, you need to structure in a governmental component as a reinsurance as a backstop on this? Because it appears that historically when these things occur, the government is going to be there as a backstop. Do you believe that should continue and, if not, how to do that?

Mr. ELLIS. We have testified before this committee in the past, and have been opposed to creating a national catastrophe reinsurance fund. We don't think that is necessary. There is a vibrant, very well-functioning reinsurance market. We can lay off debt on the worldwide marketplace, and so we don't think that is necessarily the route. Obviously, Uncle Sam is serving as a lender for this program to keep it afloat while it is underwater. We want to see further reforms in the program. We want to see more of the risk laid off on to the private sector through the primary insurers and reinsurers and deal with that issue that way, rather than creating some sort of Federal reinsurance.

Chairman LUETKEMEYER. Mr. Heidrick, what do you believe? What do you think about that? Can you actuarially make this thing work and have the private sector take all the risk on all the properties, just what Mr. Ellis is advocating?

Mr. HEIDRICK. I wouldn't have the expertise to say that they could take on all the risk, but what I can say is, and as we have proposed, that there is room for the private market to participate in this and to develop the expertise and to take on more and more risk over time in many markets, even auto insurance. States have residual markets, and that is a normal part of the insurance industry. I couldn't tell you whether or not I think the NFIP should become a residual market. It all depends on what the ultimate design would be. In terms of the debt, one of the things to keep in mind is, yes, the program is $23 billion in debt to the U.S. Treasury, but it has paid out over $50 billion in claims over its lifetime, so that is about $27 billion that otherwise would have been paid through disaster assistance that was actually paid by policyholders through premiums.

Chairman LUETKEMEYER. Very good. Well, my time has expired, and I think we have had a great discussion this afternoon. Our intention is to, with our discussion yesterday or last week with regards to mapping, begin the discussion of how we get the basics down and get the maps correct so we can begin to have some intelligent discussion about the rest of the program.

Today we want to discuss the important strengths and weaknesses of the NFIP, alternatives to the NFIP, if there are some, improvements to NFIP, whatever we can make, and I think mitigation is an important part of this. There is some action along that road. I can tell you from personal experience with this last flood we had in Missouri this last 2, 3 weeks—we had a historic flood back in 1993 along the Missouri River. A lot of the properties were mitigated. In fact, entire small towns were bought out and moved up on top of the ridges away from the lowlands. Levees were built up and improved and reinforced. As a result of that, even though we had a historic flood along the Missouri, on my half of the Missouri anyway, this past couple of weeks, the damage was not as great as it would have been. It actually worked. Mitigation worked. So I think there are a lot of things we need to talk about, anddiscuss along those lines.

We talked today a little bit about the affordability, of people being able to afford the rates, as well as the take-up rate, how you balance those things. And then we looked at the debt a minute ago. How do we look at the debt that we incur? Do we need to have a government component of this? Can we do it without the government component? Where do we need to go? All of these things are things that over the next several months, we want to ferret out. I want to try and get your input.

I know we have a lot of folks in the audience who are very interested in this. We want to continue to have a dialogue with all of you as we go through the process of trying to find a way to improve the situation. And the testimony is pretty general in agreement that at some point, part of it, if not all of it, will transition into the private market. So if that is the case, how do we facilitate that and not hinder it? So we have a lot of work to do and a lot of things to discuss.

We certainly appreciate all of the witnesses today. You did a great job. We appreciate all of what you did.

Without objection, I would like to submit the following statements for the record: the National Association of REALTORS®; the National Association of Professional Insurance Agents; the National Multifamily Housing Council and the National Apartment Association; and the American Insurance Association.

The Chair notes that some Members may have additional questions for this panel, which they may wish to submit in writing. Without objection, the hearing record will remain open for 5 legislative days for Members to submit written questions to these witnesses and to place their responses in the record. Also, without objection, Members will have 5 legislative days to submit extraneous materials to the Chair for inclusion in the record.

The hearing is adjourned.

[Whereupon, at 11:52 a.m., the hearing was adjourned.]

A P P E N D I X

January 12, 2016

TAXPAYERS FOR COMMON SENSE
MAKING GOVERNMENT WORK

Testimony of Steve Ellis
Vice President, Taxpayers for Common Sense

Subcommittee on Housing and Insurance
Committee on Financial Services
hearing
"Opportunities and Challenges Facing the National Flood Insurance Program"

January 12, 2015

Good morning, Chairman Luetkemeyer, Ranking Member Cleaver, members of the subcommittee. I am Steve Ellis, Vice President of Taxpayers for Common Sense, a national non-partisan budget watchdog. Thank you for inviting me to testify on opportunities and challenges facing the National Flood Insurance Program (NFIP). Given the ongoing flooding in the Mississippi River valley this hearing is tragically timely. My sympathies are with those affected by the floods. TCS has worked on flood insurance issues and reform of the program for our entire twenty year existence and I've been involved in flood issues dating back to my days as a young Coast Guard officer dealing with the aftermath of the Great Midwest Flood of 1993. This is a critical issue for taxpayers and we need better public policy that protects people and property.

Taxpayers for Common Sense is allied with SmarterSafer, 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 consumer and housing advocates to environmental and insurance industry groups.[1] All the groups agree that NFIP should be made more responsible and greater reforms are needed.

Background on the National Flood Insurance Program

It is important to understand the context of how the nation got into the flood insurance business. After years of ad hoc disaster aid being meted out by Congress, the National Flood

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

Insurance Program (NFIP) 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 lack of available flood insurance. But even at that 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 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.

$23 Billion in Debt and Subsidized Rates

For years NFIP teetered on either side of solvency, covering shortfalls with Treasury borrowing and repaying the loans in years of surplus. Then in 2005, the inevitable happened – a catastrophic loss year – and the program was roughly $18 billion in debt to the Treasury. That was followed by the Superstorm Sandy losses in 2012 and now the program is more than $23 billion in debt to taxpayers. To put that in perspective, FEMA data indicates that in 2014 the 5.4 million policies resulted in $3.6 billion in premium revenue to insure $1.3 trillion worth of property.[4] The Government Accountability Office has estimated that approximately 20 percent of policies are explicitly subsidized and paying only 35-45 percent of their actual full-risk level premiums.[5] These numbers have likely changed some subsequent to the enactment of the Homeowners Flood Insurance Affordability Act of 2014 also known as Grimm-Waters.

As this Subcommittee well knows, reforms to the NFIP were enacted in the Biggert-Waters Flood Insurance Reform Act of 2012 to increase premiums to more risk-based rates, which would not only help program solvency, but also help policyholders better understand their risk and take measures to mitigate that risk. Despite some concerns, TCS supported the 2012 legislation while also favoring additional efforts to help address affordability issues. Unfortunately, in Grimm-Waters, Congress rolled back many of the Biggert-Waters reforms that would have led to more actuarial rates.

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[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. http://www.loc.gov/law/find/hearings/floods/floods89-465.pdf
[4] Federal Emergency Management Agency. Available at: https://www.fema.gov/statistics-calendar-year
[5] Government Accountability Office. "Flood Insurance: More Information Needed on Subsidized Policies." July 2013.

The authorization for NFIP expires September 30, 2017. Before the long-term reauthorization in 2012, NFIP required 17 extensions after the 2004 reauthorization expired in 2009 and even occasionally lapsed only to be retroactively reauthorized. So while expiration is a year and half and another Congress away, now is the time to review possible changes and improvements to the program and what better way to start than to look at the challenges and opportunities facing the program.

Challenges

Debt – As I previously indicated, NFIP is $23 billion in debt plus interest. After a relatively light claim year in 2013, that total is $1 billion less than the $24 billion debt after Superstorm Sandy. Even without paying another claim, it would take decades to repay the debt the program owes to taxpayers. Clearly this is a challenge, but I would also argue that the debt is a clear reminder of some of the problems with the program and helps garner public and policymaker attention. In addition, after Superstorm Sandy the program's borrowing limit was set at a little more than $30 billion. Another storm of similar impact will push the program to the borrowing limit.

Adverse selection – The simple fact is that most of the people who are purchasing flood insurance are those most likely to get a payout. As I indicated there are 5.4 million policyholders in the program. According to the U.S. Census Bureau there are 134 million housing units[6] in the country and even leaving out multi-unit structures – that could be purchasing flood insurance – and commercial properties, roughly 5.4 percent of the houses in the country have flood insurance. Just about everybody has some level of flood risk, but for the most part unless it's acute they don't buy it. That puts strain on the program, particularly if you can't charge risk-based rates. The private sector would have other options, they could write multi-peril insurance that includes flood and is more attractive, and they can also lay off risk on the worldwide reinsurance marketplace.

Subsidies – Subsidies have been present in the program virtually from the beginning. Even with the supposed risk-based premiums, the fact that the program can borrow from the Treasury is a subsidy. As I mentioned earlier, the GAO has documented large cross-subsidies, many of which benefit high-income homeowners.[7] This represents a real challenge for the program's sustainability. While we are committed to rolling back premium subsidies, we realize that there needs to be a mechanism to provide means-tested, time-limited assistance outside the rate structure to lower income ratepayers. It is important that any assistance be outside the rate structure to not mask risk. Policyholders have a right to know their level of risk and price is an indicator of that. But in reality the best way to address price is to lower the rate by reducing the risk.

Maps – FEMA has to map the Special Flood Hazard Area. This delineates the area with a mandatory purchase requirement for federally backed mortgages. These maps are the backbone of the NFIP and are used to determine rates. The maps have to be accurate. The current lack of confidence in the flood maps hobbles FEMA implementation of the program. I will discuss more on mapping later in the testimony.

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

[7] Supra note 5.

Opportunities

Private sector alternatives - The only reason a policyholder will opt for private insurance over NFIP is that the private insurance offers a better product, a better price, or both. To stifle the private market would be akin to the federal government forcing policyholders to pay more. There is already interest in the private sector to write flood. It is true that NFIP was created because there wasn't a functioning private insurance marketplace, but that was nearly fifty years ago. It almost goes without saying that technology and modeling have advanced dramatically. Imagery and mapping technology has similarly developed. The reinsurance and financial instruments to manage risk are much larger and more diversified. I know the Committee will be having a hearing tomorrow on H.R. 2901, the Flood Insurance Market Parity and Modernization Act. We support this common sense measure to allow state insurance commissioners to certify that appropriate flood insurance products meet the mandatory purchase requirements.

Reinsurance - In the submission of the reinsurance study mandated by Biggert-Waters, FEMA stated that it has "determined that reinsuring a portion of the NFIP's insurance risk would be a logical step toward privatization and could provide an additional lever in the financial management of the NFIP."[8] We agree. There is interest and capacity in the reinsurance markets to take on U.S. flood risk. Obviously industry will have to gain a greater understanding of the nature of the underlying flood risk in the NFIP portfolio, but that can be managed through responsible data sharing. Laying off risk on the private sector will help protect taxpayers from debts racked up by future large storms.

Mitigation – Subsidized rates provide a disincentive to mitigation, but as rates gradually increase there is more incentive for individuals, and by extension communities, to mitigate. These should be encouraged by further federal investment. We know that each dollar of mitigation reduces post-disaster costs by four dollars or more.[9] Instead of providing premium subsidies the goal should be to reduce rates by reducing risk. Conversely, subsidizing rates does not reduce risk to people and property, in fact it encourages people to develop or stay in high risk areas.

Mapping – Mapping is both a challenge and an opportunity. Technology has enabled greater level of detail and accuracy in mapping. It also can be used by the private sector for more intensive risk analysis and modeling that can benefit private sector flood insurance alternatives (and NFIP as well) particularly in providing risk-based coverage in areas outside the SFHA.

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[8] FEMA. "Report to Congress on Reinsuring NFIP Insurance Risk and Options for Privatizing the NFIP." P6. Available at: http://www.floods.org/ace-files/documentlibrary/2012_NFIP_Reform/Reinsuring_NFIP_Insurance_Risk_and_Options_for_Privatizing_the_NFIP_Report.pdf

[9] Multi-Hazard Mitigation Council. Natural Hazard Mitigation Saves: An Independent Study to Assess the Future Savings from Mitigation Activities. Available at: https://c.ymcdn.com/sites/www.nibs.org/resource/resmgr/MMC/hms_vol1.pdf

Disaster Assistance - NFIP's inter-relationship with federal disaster aid programs under the Stafford Act is both an opportunity for reform and a challenge to a more rational holistic federal approach.

An observation from the FEMA privatization report early last year "... highly publicized instances of federal aid following catastrophic events have also created a public perception that individual property owners do not need to insure against low-probability high severity flood events, effectively creating moral hazard."[10] What people are not realizing is that the vast majority of the aid goes to rebuild public and federal infrastructure, not individuals to help them move on after disaster. A 2014 study by the Wharton Center for Risk Management and Decision Processes at the University of Pennsylvania found that increasing disaster assistance by $1,000 reduced subsequent insurance coverage by $6,000.[11] The average direct individual aid can be measured in the few thousand dollars, and absent flood insurance the homeowner is left with low interest Small Business Administration loans to rebuild. Piling a loan on top of a mortgage to rebuild a currently uninhabitable house is not conducive to efficient and resilient rebuilding.

Additional Points

In addition, the Committee asked me to address several specific points:

- *Is the NFIP the ideal model for effective protection of residential and commercial property owners?*

  No. NFIP was created nearly 50 years ago because of market failure. That same year, 1968, federal riot insurance was created. That ceased in the 1980s when it was clear the marketplace would bear that risk.[12] It is clear that the insurance industry is hungry for this risk and can provide it. To be clear, I'm not suggesting eliminating NFIP tomorrow or anything close to that. There are community mitigation benefits from the Community Rating System and there are properties that would see significantly larger premiums in the private marketplace. But a primarily private sector program is where flood insurance is heading and should head. This is already happening and in the coming decades NFIP will likely become a residual market for policyholders that cannot obtain private insurance. This will be a limited set of policies and is not unlike residual homeowners insurance programs at the state level. But Congress should be intentional about this development and ensure the mitigation benefits achieved by NFIP are retained and funds for mapping maintained.

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[10] Oliver Wyman. Flood Insurance Risk Study: "Options for Privatizing the NFIP. P52 Available at: http://www.floods.org/ace-files/documentlibrary/2012_NFIP_Reform/Reinsuring_NFIP_Insurance_Risk_and_Options_for_Privatizing_the_NFIP_Report.pdf

[11] Kousky, Michel-Kerjan, Raschky. Does Federal Disaster Assistance Crowd Out Private Demand for Insurance? Available at: http://opim.wharton.upenn.edu/risk/library/WP2013-10_FedDisasterAssistance.pdf

[12] Webel. "Terrorism Risk Insurance: Issue Analysis and Overview of Current Program," Congressional Research Service. April 26, 2013. P. 7.

- *FEMA's efforts to accurately predict flood risks, price for flood risks, and create an efficient administrative mechanism to serve policyholders.*

  I know that FEMA is working hard to update the maps, and has the new Technical Mapping Advisory Council to help guide them in their work. I also know that the mapping efforts have not received full funding the last several years which inhibits their progress. All that said, more needs to be done for the public to have a greater understanding of their flood risk. As discussed earlier, FEMA is tasked with mapping the Special Flood Hazard Area for the mandatory purchase requirement. That is a federal mandate that isn't likely to change. However these maps are static – lines on a map designating various flood risk areas and charging various rates based on those risks. If a homeowner has an elevation certificate that proves they are elevated "out" of the floodplain they can have those rates adjusted. But the creation of the rates is sort of a black box and it is not entirely clear that even "full-risk" rates are actuarially sound.[13] In some cases there are significant cross-subsidies where lower risk properties pay more to maintain subsidies for higher risk properties.

- *Reforms that could improve the program's efficiency and reduce fraud, abuse and waste.*

  As with any federal program, it is critical that taxpayers and participants in the program believe that it is operated fairly and that waste, fraud, and abuse will not be tolerated. I believe that as the private sector has greater involvement in the flood insurance marketplace it will be harder to abuse this system. This is not to suggest that there aren't scams and abusive practices in private sector insurance, but as envisioned by H.R. 2901 addressed above, it will be regulated at the state level by the insurance commissioner that has experience – more than FEMA – at dealing with these issues and the particular companies.

  In addition, there has to be greater communication between flood claims and mapping. While it is true that just because a property has never flooded in no way guarantees it won't flood, the converse does provide an indicator. Absent significant mitigation action for structural changes, a property that has flooded is certainly at risk of flooding again. Yet, in a three-part series published in early 2014, NBC News documented instances where FEMA agreed to remap large condominiums built in previously flooded areas out of the floodplain.[14] One company head that made the remapping program his business (only for commercial properties not residential) dubbed himself "Robin Hood." Hardly. Maps have to be accurate for both sides. Taxpayers and ratepayers.

  Also, there can be gamesmanship in determining whether a property is more than 50 percent damaged, triggering requirements to elevate or otherwise mitigate.

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[13] Beider. "Understanding FEMA's Rate-Setting Methods for the National Flood Insurance Program." Congressional Budget Office. October 7, 2014. Available at: https://www.cbo.gov/sites/default/files/presentation/49441-femaratemethodsnfip.pdf

[14] Dedman. "Why Taxpayers Will Bail Out the Rich When the Next Storm Hits US" http://www.nbcnews.com/news/investigations/why-taxpayers-will-bail-out-rich-when-next-storm-hits-n25901 NBC News.

- *How the NFIP and private sector could better serve high-impacted communities and modernize mapping systems while incorporating local community mitigation efforts.*

  There's no way around it. The maps have to be accurate. And smarter. There is a whole industry that has very accurate data. FEMA should explore data sharing and further contracting with them. There are also many different federal agencies that engage in mapping. This should be better coordinated and shared among agencies to avoid duplication. This is also where – and I know this is also outside the committee's jurisdiction – the nation's mitigation and pre-disaster programs have to dovetail with NFIP and post-disaster response.

- *The issue of affordability for families living in high-impacted communities with few personal or community resources to pay actuarial flood rates.*

  The affordability issue has to be addressed. But it must be done in a means-tested, targeted, and time-limited manner. Currently subsidies are effectively hidden from the homeowner, which eliminates any price signal of risk or incentive to mitigate to reduce the risk and thereby the premium. Masking subsidies with lower rates prevents policyholders from understanding their true level of risk. As was noted in the privatization report mandated by Biggert-Waters, subsidized rates "can promote (and have promoted) poor decisions on the part of property owners and political representatives ... they also create a moral hazard, especially when the subsidies are not well targeted."[15]

  The report continues that the presence of subsidies "removes the incentive to undertake mitigation efforts, thereby encouraging ever increasing societal costs." A far better approach is to encourage and fund mitigation measures that could serve to reduce rates by reducing risk.

Conclusion

Private insurers are ready to write flood insurance and as NFIP rates rise in the program to be more in line with risk this will become even more so. With more insurers writing flood insurance there should be a growth in overall coverage in the U.S. while the federal program develops into a residual market. This will take a decade or more, but Congress should work with the Administration to manage the transition and use targeted mitigation tactics that make these remaining policies more commercially insurable. There is no need for the federal government to further extend into the catastrophe insurance market through reinsurance or other means.

[15] Oliver Wyman. Flood Insurance Risk Study: "Options for Privatizing the NFIP. P60 Available at: http://www.floods.org/ace-files/documentlibrary/2012_NFIP_Reform/Reinsuring_NFIP_Insurance_Risk_and_Options_for_Privatizing_the_NFIP_Report.pdf

STATEMENT OF CHRISTOPHER HEIDRICK
ON BEHALF OF THE INDEPENDENT INSURANCE AGENTS & BROKERS OF AMERICA

BEFORE THE
FINANCIAL SERVICES COMMITTEE
HOUSING AND INSURANCE SUBCOMMITTEE
UNITED STATES HOUSE OF REPRESENTATIVES

JANUARY 12, 2016

Introduction

Good morning Chairman Luetkemeyer, Ranking Member Cleaver, and Members of the Subcommittee. My name is Christopher Heidrick and I am pleased to be here today on behalf of the Independent Insurance Agents and Brokers of America (Big "I" or IIABA) to present the association's perspectives on flood insurance and the National Flood Insurance Program (NFIP). I am the principal of Heidrick & Co. Insurance and Risk Management, an independent insurance agency located on Sanibel, Florida. I hold a designation of Associate in National Flood Insurance and my agency counsels clients of all sizes regarding flood insurance and the changes recently implemented by the Federal Emergency Management Association (FEMA). I currently serve as Chairman of the Big "I" Flood Insurance Taskforce.

The Big "I" is the nation's oldest and largest trade association of independent insurance agents and brokers, and we represent a nationwide network of approximately a quarter of a million agents, brokers, and employees. IIABA represents independent insurance agents and brokers that offer customers a choice of policies from a variety of insurance companies across all lines of insurance—property, casualty, life, health, employee benefit plans and retirement products.

The NFIP works as a private-public partnership through the Write-Your-Own (WYO) program and many IIABA members serve as the sales force for the NFIP, working with the WYO companies. The WYO program is a critical component of the NFIP, as it gives the program access to the expertise of insurers and independent agents operating in local markets across the country. The Big "I" strongly supports the NFIP and the continued role of our members as the distribution force for the program.

It is from this vantage point that Big "I" members understand the capabilities and challenges of the insurance market when it comes to insuring against flood risks. As such, my testimony today will focus on the importance of the NFIP for disaster assistance and recovery; the role of independent agents in the sale and servicing of NFIP policies; the need for a long term reauthorization of the NFIP to ensure the stability of the program; and finally, the potential role of the private market as a complement to the NFIP.

Critical Role of the NFIP

The NFIP provides a vital service to people and places that have been hit by a natural disaster. Prior to the NFIP's inception in 1968, the Federal Government provided costly ad hoc assistance in the form of post-disaster relief to flood victims. Since then, the NFIP has helped defray the cost of disaster assistance money and provided a more reliable and timely system of payments for people whose properties have suffered flood damage.

According to the National Weather Service, flooding causes more damage across the United States than any other severe weather-related event, and the NFIP is virtually the only way for people to protect against the loss of their home or business due to flood damage. In recent years there has been an increased focus on private market alternatives to the NFIP; however, the NFIP remains a necessity for millions of people across the country. While the private flood insurance market can play an important role as a counterpart to the NFIP in protecting homes and businesses, the Big "I" believes that the private insurance industry lacks the capability to underwrite flood insurance on a pervasive basis to meet customer needs.

Despite our strong support of the NFIP, the Big "I" certainly recognizes that the program is far from perfect. The program has recently faced scrutiny for its handling of Superstorm Sandy claims, and as a result of the disastrous 2005 and 2012 hurricane seasons the NFIP has a debt of approximately $23 billion, revealing some of the program deficiencies that have strained government resources.

It is important to note that for more than two decades—up until the 2005 hurricane season—no taxpayer money had been used to support the NFIP. The NFIP was able to support itself using funds from the insurance premiums it collected. Less than a quarter of NFIP policies are subsidized to account for structures that were built before floodplain management regulations were established in their community. In order for the NFIP to move toward financial solvency, rate adequacy should be re-examined, however, it must be done with careful consideration in order to avoid market disruption and other unintended consequences. For the NFIP to regain any sort of solid financial footing the number of policies needs to increase, not decrease. A broader and more diverse risk pool will help stabilize the NFIP and provide consistency within the program. As Congress considers possible reforms to the program, careful analysis of their potential impact on policy take up rates and retention should be paramount.

Important Role of the Agent in the Servicing of NFIP Policies

Under the NFIP, independent agents play an essential role in the delivery of the product through the WYO system. NFIP policies, procedures, and requirements are complex and agents serve as the conduits between the NFIP, the WYO companies, and consumers. Independent agents are an integral part of the consumer experience when purchasing a flood insurance policy. This consumer-facing relationship provides independent agents with a unique perspective on the issues surrounding flood insurance.

The role of the insurance agent in the delivery process of flood insurance is considerably more complex than that of most traditional property/casualty lines, whether obtaining coverage in a mandatory purchase area or elsewhere. Agents must possess a higher degree of training and expertise than their non-NFIP participating counterparts. Recognizing the complexities of selling and servicing flood insurance policies, in 2004 Congress passed the Flood Insurance Reform Act, in which Section 207 of the law requires agents and brokers who sell NFIP policies to have special training.

On top of complying with federal training requirements, flood insurance agents regularly update state-required continuing education credits, attend classes and seminars highlighting NFIP changes and updates, and participate in various privately-run conferences and programs. This is done frequently and involves traveling to different regions of the country, costing personal time and money. Every agent assumes these responsibilities voluntarily and does so as part of being a professional representative of the NFIP.

Through my experience servicing NFIP polices, I have established close relationships with many of my policyholders. These relationships stem from the extensive time commitment, complexities and thorough understanding of the NFIP policies being purchased by my clients. It is my job to explain the flood insurance options available to consumers and to make sure they understand the consequences of their purchase decision.

For example, placing a new flood insurance policy on a "Post-FIRM" single family residence (i.e. home construction after the effective date of the community's flood map) located in a Special Flood Hazard Area (SFHA) is extremely complicated and the whole process can take multiple days, if not weeks to complete. As you can imagine, when placing flood insurance for condominium buildings and commercial properties this process only becomes more complex.

While properties outside the SFHA generally have a less complicated underwriting process, they require extensive conversations with consumers in order to explain why flood insurance, when not required by the lender, should nevertheless be obtained. Often consumers believe they are "not in a flood zone" and therefore don't need flood insurance, when in fact this is not the case. According to FEMA, properties outside of the SFHA comprise over 20% of all NFIP flood insurance claims and receive one-third of federal disaster assistance for flooding.

The Big "I" urges the Subcommittee to remember the important role that independent insurance agents and brokers play in the sale and servicing of NFIP policies as you consider future reforms to the program.

Necessity for a Long Term Extension of the NFIP

As you know all too well, the NFIP is a congressionally authorized program that requires periodic extensions. The NFIP is currently scheduled to once again expire on September 30, 2017. Historically, these extensions have been for multiple years, often five-year periods. However, immediately prior to passage of the Biggert-Waters Flood Insurance Reform Act in 2012 (Biggert-Waters), Congress had opted to pass numerous short term, and often retroactive extensions. The instability and uncertainty created by short term extensions can lead to concrete damages in the real estate and development market, as well as the country's economy overall. Every time the program is set to expire, WYO companies must send notices to consumers about the pending expirations, agents must work with clients to explain the ramifications of a potential expiration, and realtors and mortgage lenders must decide how to proceed when issuing and servicing mortgages that have or require flood insurance, all in an unsettled regulatory environment.

In addition to ensuring market stability, a long term extension is important to the soundness of the NFIP. Biggert-Waters and the Homeowner Flood Insurance Affordability Act of 2014, enacted substantial changes to the NFIP, changes which are still being implemented by FEMA. These changes, intended to help streamline the program and set the NFIP on a path to financial solvency, must be given time to take effect. Should Congress enact multiple short term, or retroactive extensions, or approve substantial and significant changes to the program, it will delay the implementation of ongoing changes and could hinder the effectiveness of these reforms already in law. While the Big "I" appreciates the past program reauthorizations, we strongly urge Congress to pass a long term extension that will allow positive reforms currently underway to be realized, well in advance of the September 30, 2017 deadline.

Developing the Private Market and Support for H.R. 2901

The Big "I" supports allowing the private market, where possible and practical, to offer flood insurance policies as a complement to the NFIP, provided the policies are properly regulated. When Congress passed Biggert-Waters in 2012 it inadvertently resulted in a lack of clarity regarding if and when private flood insurance could be accepted to satisfy the mandatory purchase requirement. Consequently, there has largely been a rejection of private primary flood insurance by lenders. As such, the Big "I" supports H.R. 2901, "The Flood Insurance Market Parity and Modernization Act", as introduced, which would remedy this problem. The Big "I" would like to thank Reps. Dennis Ross (R-Florida) and Patrick Murphy (D-Florida) for introducing this bi-partisan legislation.

H.R. 2901 clarifies that a private flood policy can satisfy the mandatory purchase requirement for flood insurance under the terms of the NFIP. The legislation also mandates that state insurance regulators, and not federal banking regulators, will be in charge of determining what constitutes "acceptable" private market flood insurance. This language further strengthens the NFIP by increasing the likelihood that private insurers will continue to explore entering the flood insurance market as a complement to the NFIP.

Of greatest importance to Big "I" members, this bill ensures that policyholders can move smoothly between the private market and the NFIP without being penalized for obtaining a private flood insurance policy. Currently, an NFIP policyholder must maintain "continuous coverage" with the NFIP in order to maintain a subsidized or grandfathered rate. The public policy behind this makes sense, as consumers should be encouraged to maintain their flood insurance policies. However, in all other lines of property/casualty insurance "continuous coverage" does not mean coverage from one particular source. H.R. 2901 makes clear that a private flood policy approved by a state insurance regulator counts as "continuous coverage" by the NFIP and allows for a more seamless interaction between the NFIP and the private market.

Conclusion

The NFIP plays an important role in ensuring that people are protected against flood-related losses and the Big "I" thanks the Subcommittee for holding today's hearing on this critical program. Floods occur in every state and often lead to great tragedy. Most recently severe flooding in Missouri and across the central United States has proven an unsettling reminder of the terrible damage that flooding can cause. The NFIP is essential for millions of Americans and ensuring the long-term stability of the program is of vital importance. It is our hope that this hearing will contribute to the dialogue necessary to do that. The Big "I" appreciates the opportunity to express its views and looks forward to working with Congress as reauthorization of the NFIP is considered.

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TESTIMONY OF PATTY TEMPLETON-JONES
EXECUTIVE VICE PRESIDENT AND
CHIEF PROGRAM ADVOCATE
WRIGHT NATIONAL FLOOD INSURANCE COMPANY
ON BEHALF OF THE
PROPERTY CASUALTY INSURERS ASSOCIATION OF AMERICA

"Opportunities and Challenges Facing the National Flood Insurance Program"

HOUSE FINANCIAL SERVICES SUBCOMMITTEE
ON HOUSING AND INSURANCE

JANUARY 12, 2016

Introduction

Chairman Luetkemeyer, Ranking Member Cleaver, and members of the Subcommittee, my name is Patty Templeton-Jones and I am the Executive Vice President and Chief Program Advocate of Wright National Flood Insurance Company, based in Florida. Thank you for the opportunity to testify. Wright National Flood Insurance Company (WNFIC) is a "Write-Your-Own" (WYO) flood insurance partner with the National Flood Insurance Program (NFIP) and through the WYO program, WNFIC is the largest writer of flood insurance in the nation. Wright National Flood Insurance Services (WNFIS), our processing center, is also active in the private flood insurance market growing outside of the NFIP.

Wright National Flood is a member of the Property Casualty Insurers Association of America (PCI) which is composed of nearly 1,000 member companies, representing the broadest cross section of insurers of any national trade association. PCI members write more than $195 billion in annual premium and 35% of the nation's home, auto and business insurance, with a membership epitomizing the diversity and strength of the U.S. and global insurance markets. PCI members also include two thirds of the WYO insurers that partner with the NFIP to administer the flood insurance program. My testimony today is provided on behalf of PCI and its nearly 1,000 member companies.

As a company also active in the private flood insurance market, Wright National is uniquely positioned to assist the Subcommittee as you start deliberations on flood insurance reforms well before the September 30, 2017 NFIP expiration. PCI and my company look forward to helping the Subcommittee balance the continued development of opportunities for private capital to provide flood coverage outside of the NFIP while maintaining stability and certainty within the NFIP for consumers and the marketplace.

Attached to my testimony is previously submitted written testimony that, while addressing Superstorm Sandy claims oversight, includes a summary of the evolution of the NFIP that describes previous Congressional consideration of restructuring the public and private roles in providing flood insurance (entitled, "The National Flood Insurance Program: Oversight of Superstorm Sandy Claims").

Today, I would like to: (1) draw your attention to the dramatic increase in private capital available to underwrite flood coverage outside of the NFIP; (2) underscore the importance of consensus for long term reforms needed to provide stability in the NFIP throughout the lengthy transition period necessary for a significant market for flood coverage to develop outside the NFIP; (3) highlight several key issues policymakers need to consider before any period of transition begins; and (4) suggest several broad categories on which such long term, consensus reforms should focus.

Availability of Private Capital

Without question, the biggest change in the flood insurance landscape since Congress last reauthorized the NFIP is that now, for the first time in a generation, substantial sources of private capital are available and actively interested in writing primary flood insurance coverage. Previously in the flood insurance market, private insurance capital focused on providing gap, excess or reinsurance coverage beyond the limited flood insurance coverage available through the NFIP. Today, both because of the Biggert-Waters Flood Insurance Reform Act (BW-12) and despite some unintended regulatory confusion created by BW-12, an increasing number of private insurers, including WNFIS, have entered or are planning to enter the primary flood insurance market. In response, state insurance regulators, like those from Florida and Pennsylvania, are engaging insurers with the intention of fully incorporating flood insurance into the U.S. state system of insurance regulation.

NFIP Stability

The 48-year old NFIP has experienced significant turmoil over its history, particularly in 2005 following the effects of Hurricanes Katrina, Rita & Wilma. Program uncertainty and confusion perhaps peaked between 2008 and 2012 as the NFIP suffered through a period of more than a dozen short-term program lapses and extensions. Some stability returned to the program in 2012 with the passage of BW-12, but was suspended as unintended consequences from BW-12 implementation led to the March 2014 passage of the Homeowners Flood Insurance Affordability Act (HFIAA).

Unfortunately, a decade of program uncertainty, lapses and mid-stream operational changes have not only caused numerous insurers to leave the WYO program but have repeatedly disrupted the housing market and caused ripple effects throughout the larger economy. Appropriate and timely long-term reforms could improve both the private and public protections provided to consumers. Developing consensus on long-term reforms, then restructuring and reauthorizing the NFIP well before its September 2017 expiration is the single most important thing Congress can do to foster certainty in the flood insurance marketplace and encourage the continued development of market-oriented solutions in flood risk management.

Transition Period

The availability and interest of significant sources of private capital to provide primary flood insurance coverage outside the NFIP represents a paradigm shift. It presents the opportunity for a gradual transition towards a flood insurance marketplace in which an increasing share of risk is borne by private capital. However, the growth of a private, primary flood insurance market does not mean the elimination of the need for a national NFIP – particularly as the private market will not be willing to assume all flood risks or be acceptable to all buyers. A successful transition to a more private-based flood insurance market also presents several critical questions policymakers must address as they consider various restructuring options.

In advance of any significant transition in the flood insurance market, topics policymakers need to consider are: (1) should the NFIP become a national residual market, or market of last resort, for the substantial number of properties the private market will be unable and unwilling to insure? (2) how should such a residual market be structured and funded? (3) how is the NFIP's mission to encourage the purchase of flood insurance by providing 'affordable' coverage impacted by the growth of the private insurance market? and, (4) how will the NFIP's mapping and flood mitigation functions be funded if policyholders leave the NFIP and purchase private flood insurance?

Another key variable important to any such discussion is the alarming drop in the number of flood insurance policies in force in the United States. Although coastal population density continues to increase, since 2013, the number of NFIP policies in force has dropped from an eight-year sustained level in excess of 5.5 million policies to just over 5 million policies at the end of 2015. While some of this change represents NFIP participants entering the private marketplace for coverage, data suggests that a majority of policyholders leaving the NFIP are simply going without flood insurance. Further, anecdotal evidence shows that the $250 HFIAA surcharge on second homes and businesses is disproportionately driving relatively low risk, voluntary participants from the NFIP. How best to increase the take-up rate for flood insurance may be a subject worthy of its own hearing.

Operational and Long Term Consensus Reforms

There are a number of immediate, operational reforms that FEMA could take up on its own and that the Subcommittee may wish to consider in its oversight role, including: (1) release of FEMA flood claims data that would immediately and significantly enhance private market development; (2) elimination of the WYO non-compete clause that prevents the insurers with the most experience serving flood consumers to better provide options to their customers; (3) simplification of the NFIP underwriting and rating process; (4) increasing transparency and consistency in NFIP claims processing; (5) reviewing of the NFIP appeals process; (6) targeting mitigation towards the highest risk properties; and (7) identifying and implementing mapping methodologies best suited to identify and mitigate actual risk. These reforms need not require Congressional action and would improve the efficiency and effectiveness of the program for consumers and the marketplace in addition to larger public-private rebalancing.

In the immediate, Congress could and should bolster the development of a robust private flood insurance market by passing the bi-partisan, bi-cameral, Ross-Murphy, Heller-Tester Flood Insurance Market Parity and Modernization Act of 2015 (H.R. 2901). This straight-forward legislation addresses the post-BW-12 regulatory confusion referenced earlier in my testimony and provide homeowners greater coverage options and pricing.

Conclusion

PCI and Wright National support the Subcommittee's review of potential restructuring of the NFIP and consideration of how to encourage additional private participation in flood underwriting and accordingly limit taxpayer risk. We would also suggest that even if the Subcommittee and Congress ultimately reshape the marketplace there will be a necessary long-term transition. Given the NFIP's important role in the lives of so many Americans, it is critical to develop a strong bipartisan consensus for stable long-term reform in advance of the program's September 2017 expiration. PCI and Wright National stand fully ready to help the Subcommittee in this endeavor to protect consumers and create a stronger foundation for the private and public marketplaces that serve consumers.

I thank the members of the Subcommittee for this thoughtful, proactive and timely start to reimagining flood risk management in advance of the September 2017 reform and reauthorization of the NFIP. I am happy to address any questions and look forward to working with the Subcommittee throughout this process.

PCI

Property Casualty Insurers
Association of America

Advocacy. Leadership. Results.

TESTIMONY SUBMITTED
ON BEHALF OF THE
PROPERTY CASUALTY INSURERS ASSOCIATION OF AMERICA

"THE NATIONAL FLOOD INSURANCE PROGRAM: OVERSIGHT OF SUPERSTORM SANDY CLAIMS"

BEFORE THE HOUSE FINANCIAL SERVICES COMMITTEE
UNITED STATES HOUSE OF REPRESENTATIVES
JUNE 2, 2015

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Thank you Mr. Chairman, Ranking Member and Members of the Committee for the opportunity to provide testimony on "The National Flood Insurance Program and Oversight of Superstorm Sandy Claims." The Property Casualty Insurers Association of America (PCI) is composed of almost 1,000 member companies, representing the broadest cross section of insurers of any national trade association. Our members write more than $183 billion in annual premium and 35 percent of the nation's home, auto and business insurance, reflecting the diversity and strength of the U.S. and global insurance markets. PCI members include two-thirds of the "Write-Your-Own" (WYO) insurers that partner with the Federal Emergency Management Agency (FEMA) to administer the National Flood Insurance Program (NFIP).

PCI appreciates the continuing interest of the Committee in the National Flood Insurance Program. While the program has undergone numerous changes over the past several years PCI and our members are ready to work with Congress on continuing improvements to the program to better serve consumers. This testimony provides a broad overview of the evolution of the program, private sector involvement in providing flood insurance coverage, and some of the lessons learned from the response to Superstorm Sandy.

Evolution of Flood Insurance and the Private and Public Sector Roles

Flood insurance was provided in the United States by the private sector in the late 1800's and early 1900's. After catastrophic floods in 1927 and 1928, private flood insurance became decreasingly commonplace. Flood losses were borne primarily by consumers and, over time, increasingly by the federal government in the form of disaster relief. President Truman in the 1950's proposed a flood program based on private insurance with federal reinsurance, with mandatory purchasing required for homeowners with federally insured mortgages. The program was enacted but never funded or implemented. Critics at the time were concerned about adverse selection with most homeowners unwilling to voluntarily pay risk-based rates, a high concentration of risks, and inadequate land-use planning and mitigation efforts. In 1966, President Johnson raised with Congress four possibilities for providing flood insurance – purely private sector underwriting, private underwriting with government backing, a purely government program, or a government program run with private assistance. The Administration ultimately recommended a public-private partnership for offering flood insurance, although requiring homeowners to bear their full risk costs.

In 1968, Congress created the National Flood Insurance Program that provided for a public-private partnership with communities agreeing to land-use restrictions in order to be eligible to purchase flood insurance from a risk pool (the National Flood Insurers Association) run by the private sector with oversight by the Federal Insurance Administration (FIA), then part of the Department of Housing and Urban Development (HUD). The federal government made loans to the private pool to pay claims, repaid with premiums over time, as well as providing reinsurance for catastrophic flood losses (lowering the premiums by eliminating the catastrophic risk costs). An explicit subsidy was provided for existing structures determined to be in a special flood hazard area with the expectation that those structures would disappear over time after severe weather events.

In 1977, disagreements between the private sector and the government over the authority and the financial control of the program led to the FIA exercising an existing section (Part B) of the

1968 legislation that allowed for an all federal program in which the federal government bears all of the risk while making use of insurance industry resources. This also led to a period of tension between the industry and NFIP. In 1979, President Carter created the Federal Emergency Management Agency (FEMA) and the NFIP, along with several other disaster-related agencies were brought into that Agency.

From 1977 through 1983, property owners purchased flood insurance through an agent that in turn dealt directly with the federal government. However, during these early years, there was extremely limited participation in the NFIP, despite a congressionally imposed requirement in 1973 that all properties in a flood zone with federally backed or regulated mortgage purchase flood insurance. On its own, the federal government lacked adequate marketing and distribution channels as well as sufficient claims handling and payment capacity.

In 1983, the government turned again to the private sector to help market, service and settle claims for the program. The "Write-Your-Own" (WYO) program was created to use the existing private insurance infrastructure of insurance agents, companies and claims adjusters to help increase market participation and settle claims, while the risk of flood loss was retained by the government to keep premiums low. Participation in the flood program ultimately soared, climaxing at a post-Katrina high of 5.7 million NFIP policyholders.

<u>How the NFIP and Write Your Own (WYO) Claims Process Works</u>

Roughly 80 of the more than 1300 active home, auto and business insurers in the U.S. have agreed to help administer the NFIP program as Write Your Own (WYO) insurers. WYO's act as a fiduciary for the federal government and taxpayers to market flood insurance and settle flood insurance claims. In return for their marketing, claims adjustment, legal fees and other administrative costs, NFIP pays WYO's a servicing fee as well as additional fees based on the amounts and volume of settled claims. Approximately 12-14 percent of flood insurance policies are written directly by the NFIP Direct Program, although even the direct program relies largely on outsourced claims adjusting and processing resources as well as private sector agents.

Decisions on federal flood insurance claims payments are made by claims adjusters. When policyholders experience a flood loss, they contact their insurance agent or WYO insurer. The insurer then assigns a flood claims adjuster, who may be an employee of the WYO, a contractor with a third party vendor or an independent contractor. The flood claims adjuster determines the amount payable on a claim based on very specific guidelines and rules established by the NFIP. Flood claims adjusters and the independent contracting firms they represent are generally compensated in proportion to the amount of the loss paid. The compensation formulas are set by the NFIP and periodically updated.

WYO insurers can be penalized for either underpayments or overpayments, and WYOs are audited regularly by the federal government under the Improper Payments Elimination and Recovery Act (IPERA) to ensure that they follow federal requirements. WYOs also have strong incentives to pay the right amount to maintain their reputation and consumer retention.

Federal compensation and settlement guidelines are periodically adjusted by Congress and the NFIP. For example, following Hurricane Katrina the Government Accountability Office (GAO) raised concerns that the existing compensation structure could result in WYOs being overcompensated for claims settlement, particularly following a catastrophic event. As a result, the claims compensation formula was refined in 2009 by reducing the portion tied to the claim value and basing a portion of the payment on the WYO insurer's NFIP premium volume. There are also specific processes in place for dissatisfied policyholders to appeal claims decisions to the NFIP. The most recent, admittedly imperfect appeals process was put in place as a result of the enactment of the Flood Insurance Reform Act of 2004.

Recent Challenges in the WYO Program

Administering and marketing the NFIP is very complex and expensive, particularly with numerous recent statutory changes to the program (many retroactive). The number of private participants in the WYO program has declined significantly in recent years, with several current participants preparing to exit the program after the recent changes. Most WYOs sell and administer a small number of NFIP policies, largely as an extra service to their consumers. The recent turmoil in the program has further increased costs and reputational concerns, weighing heavily on insurers ability to continue offering access to the NFIP as a service for their policyholder. While the NFIP's Brad Kieserman stated at the April Senate ad hoc Sandy Claims Task Force meeting that FEMA has "seen no evidence of wrongdoing by insurers who handled Sandy claims," there have been demands for WYOs to make Sandy flood litigation payments to policyholders that the DHS General Counsel determined the NFIP could not legally pay out of the National Flood Insurance Fund.

PCI and our WYO members are also concerned about the increasing polarization and uncertainty over the future of the program. Unfortunately, as WYO private participation in the program has declined and many of the recent legislative changes have been implemented, the number of households and businesses in the program has also dropped significantly. Sadly, after nine years (2006-2013) of having about 5.6 million policies in force, the NFIP's number of policies in force is now about 5.2 million and continues to fall.

Lessons Learned from Superstorm Sandy and Potential Areas of Reform

While Superstorm Sandy was a significant storm causing tragic human and physical losses, it was not significantly different from other large-scale natural disasters with regard to the litigation that ensued. Almost 99 percent of the flood loss claims (142,000+) have been settled and only 1.04 percent remain in litigation. Of course, no level of wrongdoing is acceptable and to the extent that Sandy claims differ in this regard, they should be treated differently. However, there are several lessons that the marketplace learned or relearned in the aftermath of Sandy that Congress might revisit.

Governmental Coordination

In the immediate aftermath of a natural catastrophe it is critical for local, state, and federal officials to coordinate their efforts to get basic services up and running as quickly as possible, to get people back to their homes, and to get businesses to begin remediation and rebuilding. Insurers need to be at the table during pre- and post-disaster emergency planning and coordination to ensure that smooth claims adjustment can be a part of the catastrophe response planning. It is also essential to the rebuilding process that local law enforcement and government officials allow insurers and insurance claims adjusters into damaged areas as soon it is safe – at least as soon as property owners are provided access. Following Superstorm Sandy's landfall, despite being granted authority by the states, insurance personnel access to affected areas was denied.

Available Claims Adjusters

A unique aspect of Superstorm Sandy was the lack of locally licensed flood insurance adjusters willing to adjudicate Sandy losses, which delayed the claims settlement and the rebuilding process. Most flood insurance adjusters are located in areas that frequently flood, while Superstorm Sandy hit regions that flood less frequently. Many states implement reciprocal recognition of claims adjusters from other states to help, and the state insurance department grant such access if the proper credentials are provided. However, it can often be difficult in the middle of a catastrophic event with an unusual number of claims to process the necessary paperwork in a timely manner. PCI supports federal legislation to require more reciprocal claims adjuster recognition.

Engineering Reports

Another unique feature of Sandy was the need for more engineering reports due to the prevalence of below ground building substructures. There are a limited number of engineering firms. With both non-flood and flood insurers requiring engineering services after any catastrophe, engineering firms necessarily encounter challenges managing both the volume of work as well as the short time frames for adjusting claims due to media and public official pressures. Engineering on-site inspectors are not always familiar with the particular requirements and guidelines of the NFIP. One of the engineering subcontractors, used by both the NFIP Direct Program and some WYOs has been accused of altering the reports of one of its on-site inspectors. Subsequent to these allegations, the NFIP has worked to facilitate remaining open claims and allow unsatisfied claimants to have their claims reviewed by NFIP staff.

Balancing the Pendulum of Overpayment and Underpayment Concerns

Congress and the NFIP have periodically revisited the flood program's guidelines to balance concerns about the risks of overpayment and underpayment. After hurricane Katrina, the Department of Homeland Security's Office of Inspector General released a report considering allegations that insurers were overpaying consumers. While the Government Accountability Office (GAO) in a subsequent investigation concluded that they found no evidence of inappropriate attribution of losses, FEMA reviewed the settlement guidelines. The criticisms after Sandy have been of underpayment rather than overpayment. However, PCI and our WYO members welcome a thorough review of the claims settlement process to ensure the optimal fiduciary balance between protecting policyholders and taxpayers.

Mitigation

Preparation is a key factor in minimizing financial loss after a natural catastrophe. Strong, uniform statewide building codes that are regularly updated play a significant role in reducing the risk of injury or death to homeowners during a natural catastrophe. Structures built or retrofitted to comply with the most recent edition of the *International Building Code*, and other recognized building standards, incur less property damage during a significant weather event. Less property damage following an event reduces the need for federal disaster aid and can help expedite a community's recovery after a natural catastrophe. PCI promotes strong building codes and responsible land use policies, which are crucial for all stakeholders, to promote public safety and to be as prepared as possible for the next hurricane, tornado, or flood disaster. Updating flood maps immediately following such an event may be critical to ensuring that homes and businesses being rebuilt meet the appropriate flood elevation criteria.

Private Sector Participation

PCI also supports increasing consumer choice in flood insurance. In particular, PCI supports legislation facilitating a consumer's choice to choose private flood insurance that can be accepted as conforming by mortgage lenders. Also, PCI notes that the recent Biggert-Waters and HFIAA flood reform legislation authorizes FEMA to obtain reinsurance from the private market, although this has not yet been pursued. PCI believes that there are additional challenges and opportunities in this area and looks forward to working with Congress in reviewing opportunities for expanding coverage and protections for consumers.

Program Growth and Risk Spread

A number of Sandy losses were not covered by insurance, often because homeowners were not aware of the risks or the potential gaps in their existing coverage, or because they were simply uninsured or underinsured. There are additional opportunities for the government and private sector to educate consumers about flood insurance and reduce future gaps and consumer vulnerabilities.

Ongoing Discussions of NFIP Reforms

As we look towards the reauthorization of the NFIP program in 2017 and Congress considers short and long-term changes to it we have already started to discuss such reforms. PCI hosted the 2015 National Flood Insurance Conference in mid-May that included all the stakeholders in this program. That conference agenda included potential program improvements, other approaches to address the risk, technical issues and challenges to private sector participation and risk bearing. PCI will continue these discussions with stakeholders and would welcome further conversations on improvements with regard to oversight and operation of the NFIP with the Committee.

Conclusion

The flood insurance program protects millions of American businesses and families from catastrophic flood risk. PCI members and our WYO companies appreciate the opportunity to service the federal government and consumers and welcome a discussion with the Committee about how to improve the claims process and shape the program in the future.

Testimony of Tom Woods

President, Woods Custom Homes

On Behalf of the

National Association of Home Builders

Before the

House Financial Services Committee

Subcommittee on Housing and Insurance

Hearing on

"Opportunities and Challenges Facing the National Flood Insurance Program"

January 12, 2016

Chairman Luetkemeyer, Ranking Member Cleaver, and members of the Subcommittee, thank you for the opportunity to appear before you to today on behalf of the National Association of Home Builders (NAHB) to discuss the National Flood Insurance Program. My name is Tom Woods and I am a builder from Blue Springs, Missouri and NAHB's 2015 Chairman of the Board.

NAHB represents over 140,000 members who are involved in building single family and multifamily housing, remodeling, and other aspects of residential and light commercial construction. Collectively, NAHB's members employ more than 1.26 million people and construct approximately 80 percent of all new housing in America each year. As a leading advocate for the residential construction industry, NAHB promotes policies that maintain housing as a national priority.

NAHB has a long history of supporting the National Flood Insurance Program (NFIP) and we are committed to ensuring that it remains a viable and affordable program to its policyholders while being mindful of the costs to the American taxpayer. NAHB commends the Subcommittee on addressing this crucial issue early in the year, and we look forward to working with you and your colleagues as you contemplate changes to the NFIP to ensure that federally-backed flood insurance remains available, affordable, and financially stable.

Background

Since 1968, the Federal Emergency Management Agency's (FEMA) NFIP has played a critical role in directing the use and development of flood-prone areas and managing the risk of flooding for residential properties. A strong national flood insurance program helps ensure that the housing industry can provide safe, decent, and affordable housing to consumers.

The NFIP provides flood insurance to more than 5.1 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.

The unprecedented losses suffered in 2005 and 2012, including the devastation brought about by Hurricanes Katrina and Sandy, have severely taxed and threatened the solvency of the NFIP. While these events have been tragic and sobering, resulting reforms must not be an overreaction to exceptional circumstances. Instead, reform should take the form of thoughtful, deliberative and reasoned solutions. A key step in this process is to take stock of where we are today, what has worked and what has not.

Legislative Fixes

Congress reformed the NFIP through the passage of the *Homeowner Flood Insurance Affordability Act of 2014* (HFIAA). This legislation repealed provisions of the *Biggert-Waters Flood Insurance Reform Act of 2012* (BW-12) that triggered increases to full-actuarial rates based on the sale of a home.

While NAHB supported passage of BW-12 to ensure the continuation of the NFIP program, the legislation created unintended consequences that resulted in dramatic flood insurance premium hikes that hurt the sale, construction and remodeling of homes in affected communities. The combination of inaccurate mapping into higher risk flood zones and the immediate shift to full risk actuarial rates for many homeowners resulted in increases that priced prospective buyers out of their developments and forced the cancellation of sales, harming several communities.

HFIAA fixed many of the problems associated with BW-12. HFIAA provided that those who were charged higher rates should be refunded for excess premiums, specified that properties would continue to pay their "grandfathered" rates and repealed the requirement that flood insurance premiums increase immediately to full actuarial rates upon the sale of a home. The return to grandfathered subsidized rates provided a more affordable rate structure for policyholders.

FEMA is now required to notify their congressional delegations before updating FIRMs. This is invaluable for pre-FIRM property owners who are selling their homes, who now will be informed if they have been remapped into a new floodplain and will be able to inform the home buyer of any additional NFIP requirements. Congress also created the Flood Insurance Advocate, an office within FEMA responsible for ensuring NFIP policyholders and property owners understood FEMA's process for appealing a preliminary FIRM maps.

NAHB has estimated that in 2014 because of HFIAA there was:

- $755 million more in new construction (from existing homeowners who wouldn't lose value when they sell, and therefore will have more to spend on their next homes, a share of which will be new), plus
- $361 million a year in additional remodeling (from eliminating the extra cost of increased insurance some homeowners would had to have paid on certain remodeling jobs).

Additionally, HFIAA increased the "substantial improvement" threshold to its traditional amount of 50% or more of the market value of a structure. If it were not for HFIAA, NAHB estimates that the move from the 50% to the 30% threshold in BW-12 would have placed up to $8.5 billion in annual remodeling activity at risk because it would have deterred property owners from making necessary and appropriate renovations for fear of triggering exorbitant premium increases. This change will help existing homeowners stay in their homes and make necessary repairs and upgrades without the fear of triggering unsustainable insurance rate hikes.

Challenges Moving Forward

It is equally important to discuss the accuracy of FIRMs. For flood maps to be fair and accurate, they have to take into account all flood control efforts, like levees and dams. In many cases, FEMA has neglected to factor in privately funded flood control structures, or any flood control structures that were not built by the U.S. Army Corps of Engineers. Consequently, many properties are being mapped into higher rate-zones, which results in homeowners being forced to purchase unneeded flood insurance or pay higher than necessary premiums because their homes have been inaccurately mapped as being below the Base Flood Elevation (BFE).

FEMA has a long history of inaccurate flood mapping. There have been reported cases of FEMA drawing in rivers or streams where none exist or mistakenly using data from one community for another. Inaccurate mapping has resulted in homes unnecessarily being drawn into flood maps or placed into higher rate zones. It typically takes years for those mistakes to be fixed, often requiring a lengthy and costly appeals process for the community and homeowner, as well as forcing the payment of escalated premiums until the problem is resolved.

Through the strong leadership of both chambers, FEMA has been directed to implement a number of mapping initiatives. During the map modernization effort, FEMA was able to digitize, update, and modernize many of the nation's aging flood maps. While FEMA was successful in digitizing most of the FIRMs, not all were based on updated hydrologic data. As a result, a National Academy of Sciences report faulted some of the maps because of a lack of reliable topographical data. Because of these data deficiencies, there are large discrepancies between what was mapped in the 100-year floodplain decades ago, what areas may be reflected as falling within the 100-year floodplain on the newer maps and what the actual 100-year floodplain is today.

While FEMA is currently addressing this oversight through its RISKMAP program, continued congressional oversight is necessary. Most recently, BW-12 established the Technical Mapping Advisory Council, a federal advisory committee that is charged with developing recommendations for updating the mapping process. The council is expected to issue its report by the end of 2016.

Additionally, the NFIP must continue to allow state and local governments, not the federal government, to shape local land use policies and make decisions on how private property may be used. While officials at all levels of government must work together so that lives, homes, schools, businesses and public infrastructure are protected from the damages and costs incurred by flooding, the local communities must provide the first line of defense in terms of land use policies and practices.

If a local government deems an area fit for residential building, flood insurance and mitigation standards allow homebuyers and homeowners the opportunity to live in a home of their choice in a location of their choice, even when the home lies in or near a floodplain.

Furthermore, a common misconception when discussing NFIP and mapping involves new construction of homes in floodplains. NFIP provisions require that all new construction and substantial improvements of residential structures within a Special Flood Hazard Area (SFHA) on the community's FIRM must have the lowest floor (including the basement) elevated to or above the BFE level. Additionally, new construction does not affect the solvency of the NFIP because homeowners of new construction units are required to pay full-actuarial rates and do not receive a subsidy. In many commonly flooded areas, such as the state of Florida, NAHB has been told that new construction that is built to the current building codes routinely outperform the older existing housing stock during storm events. There is also an opportunity for home builders or landowners to elevate plots of land out of the floodplain.

Letter of Map Change Appeals Process

Landowners and local governments can file letters requesting map changes (LOMC) on a case-by-case basis as they relate to particular projects. However, this process can be both costly and time consuming. There are six different types of FEMA recognized LOMCs that can be further divided into two broad categories.

The first category is conditional letters of map amendment or revision (i.e., CLOMA, CLOMR, and CLOMR-F). These are statements from FEMA on whether or not a project, as designed, would either be located outside a SFHA or result in modifying a floodplain as depicted on an existing FIRM. The important factor here is conditional letters represent FEMA's opinion on projects not yet constructed. Once these structures or actions have actually been completed, FEMA still needs to take a separate administrative action to revise the map.

The second category is letters of map amendment or revision (i.e., LOMA, LOMR, and LOMR-F) that represent FEMA's acknowledgment of structures already built that require revisions to an existing FIRM. These LOMCs are corrections to an existing FIRM, and become part of the public record for that map. Subsequently, whenever FEMA decides to update or replace the existing FIRM, these LOMCs are to be incorporated into the new FIRM for the particular area.

I engaged in the CLOMR-F process in a subdivision I built in Independence, Missouri. It took over 8 months and a quarter of a million dollars for FEMA to approve the map change. In some states with short construction seasons, going through the lengthy LOMC process could create devastating costs and delays.

Despite best efforts and ambitious plans to update the nation's 92,222 FIRMS, many outdated and inaccurate maps remain in place. Efforts to update these maps must be carefully designed and implemented to account for the very real impacts they can have on communities. Oftentimes the updated maps will show a drastic increase in the amount of land designated as being within the 100-year flood zone. The reason for the increase is that measuring equipment used today is more accurate than the equipment used during previous mapping projects, including more meteorological history to draw upon.

Because flood hazards are dynamic and usually increase over time as development occurs, old maps tend to understate actual, existing flood hazards. As a result, the updated maps will continue to include increased flood elevations and expanded SFHAs. This not only extends the obligation for those with financing provided by a federally-insured or licensed lending institution to obtain flood insurance, but also includes mandatory construction requirements.

NAHB Urges Caution

As Congress considers strategies to ensure the availability of insurance and to bolster the financial stability of the NFIP, NAHB remains concerned that some reform measures under consideration could result in far-reaching and unintended consequences that decrease housing affordability and the ability of communities to meet current and future growth needs.

Any revision of the SFHA would not only affect homeowners, but also home builders, local communities and FEMA. An expanded floodplain would likely result in an increased number of flood map amendments and revisions, placing additional burdens on federal resources to make these revisions and amendments in a timely fashion. Residents located in a newly designated SFHA would need to be notified through systematic outreach efforts. Communities would likely need to modify their floodplain ordinances and policies to reflect the new SFHA. In short, the entire infrastructure of flood management and mitigation practice and procedures institutionalized around the 100-year floodplain standard would need to change, all at a time when FEMA has admitted its lack of resources to provide current services.

Conclusion

I would like to thank the Subcommittee for the opportunity to share NAHB's views. Home builders have long-supported common sense changes to the NFIP, and we urge Congress to continue to support and protect small business owners and homeowners from the exorbitant rate hikes and inaccurate mapping we have seen in the past.

NMHC NATIONAL MULTIFAMILY HOUSING COUNCIL NAA NATIONAL APARTMENT ASSOCIATION

January 12, 2016

The Honorable Blaine Luetkemeyer
Chairman
Subcommittee on Housing and Insurance
House Financial Services Committee
2440 Rayburn House Office Building
Washington, DC 20515

The Honorable Emanuel Cleaver II
Ranking Member
Subcommittee on Housing and Insurance
House Financial Services Committee
2335 Rayburn House Office Building
Washington, DC 20515

Dear Chairman Luetkemeyer and Ranking Member Cleaver:

The National Multifamily Housing Council (NMHC) and National Apartment Association (NAA) applaud the Subcommittee for calling a hearing on "Opportunities and Challenges Facing the National Flood Insurance Program (NFIP)." We appreciate the Committee exploring the issues facing the NFIP early this year in advance of the program's needed reauthorization by September 30, 2017. We support the efforts of Congress to ensure the NFIP is functioning properly and continuing to reduce taxpayer funded disaster assistance for flooding.

For more than 20 years, NMHC and NAA have partnered in a joint legislative program to provide a single voice for America's apartment industry. Our combined memberships are engaged in all aspects of the apartment industry, including ownership, development, management and finance. NMHC represents the principal officers of the apartment industry's largest and most prominent firms. As a federation of nearly 170 state and local affiliates, NAA is comprised of over 69,000 members representing more than 8.1 million apartment homes throughout the United States and Canada.

NMHC/NAA join the broader real estate community in understanding that the future stability of the property insurance market and its ability to withstand the continued occurrence of catastrophic events must remain a top concern of our sector. With floods being the most common natural disaster in the United States, the NFIP ensures that affordable flood insurance is available at all times, in all market conditions for every at-risk rental property. These include more than just high rise multifamily properties in urban centers along the East and West coasts of our country but extend across every state to include low-rise structures and even single family rental homes. Ensuring that all types of rental property continue to have access to affordable, quality flood insurance through the NFIP is a top priority for our membership to not only protect their property investment but to help manage the increasing costs of providing housing.

Our industry acknowledges that the NFIP does not come without its challenges and we agree that further reforms are necessary to protect the long-term financial viability of the program. It took several catastrophic weather events to force the NFIP into negative fiscal standing and returning it to solid footing cannot happen overnight. We believe that many of the reforms included in both the Biggert-Waters Flood Insurance Reform Act and the Homeowner Flood Insurance Affordability Act of 2014 will help slowly return the program to solvency. To that end, several provisions described below could offer significant improvements to the efficiency, affordability, and long-term health of the NFIP:

- **Long-Term Authorization** – Prior to the enactment of Biggert-Waters in 2012, the NFIP had been operating on a series of short-term extensions that began in

2008. The stop-gap measures continually created an environment of uncertainty for multifamily property owners and managers who rely on this program for coverage. More broadly, during a time of economic recovery, real estate transactions across both the residential and commercial sectors could not legally be secured without this critical protection in place. **We, therefore, strongly urge Congress to prevent disruption in the marketplace and pass a long-term reauthorization of the NFIP that maintains the government's backstop well before it is set to expire on September 30, 2017.**

- **Mapping** - It has not been uncommon for apartment owners to have their properties misclassified as being in high-risk flood zones, or Special Flood Hazard Areas (SFHA). Yet the process for property owners to challenge those designations and the maps they are based on is overly complex and financially burdensome. The onus is wrongly put on the property owner to prove the maps inaccurate and is forced to incur engineering and surveying expenses as well as spend vast amounts of time to appeal under the current system. Inaccurate maps not only have financial repercussions for existing property owners but also have a chilling effect on development in inaccurately zoned areas, which is problematic in a time of a rental housing shortage. **We, therefore, encourage Congress to provide sufficient resources to appropriate federal agencies to coordinate and build upon efforts such as the U.S. Geological Service's 3D Elevation Program (3DEP) that could provide increased accuracy to existing tools currently used to determine risk and premium levels under the NFIP. Further, we urge Congress to improve the appeals process to make it more affordable, transparent, and less time-consuming for both communities and property owners.**

- **Flood Risk Mitigation** – The Federal Emergency Management Agency (FEMA) currently administers several mitigation grant programs in an effort to reduce damage, claims, and overall risk in the event of a natural disaster such as flooding. While apartment communities are not explicitly excluded from eligibility for these funds, the grant programs are overwhelmingly focused on primary, single-family homes. Even further, FEMA has only recently focused attention on the importance of mitigation efforts for properties that cannot benefit from traditional mitigation techniques like building elevation. Consistent with the requirements under the Homeowner Flood Insurance Affordability Act of 2014, FEMA recently issued advisory guidelines to property owners on alternative methods of mitigation. Unfortunately, many of the recommendations made are impractical for apartment communities and the majority would not afford any flood insurance premium reduction despite the large cost of implementation. **NMHC/NAA would urge Congress to require FEMA to undertake further actuarial work and issue alternative guidance specific to multifamily property owners that is both realistic and cost effective. Additionally, NMHC/NAA would ask that Congress direct FEMA to expand the focus of existing mitigation programs to better include multifamily properties or consider establishing a multifamily specific mitigation grant program to address the unique challenges faced by our property owners.**

cc: Members of the House Financial Services Committee

Not specific to multifamily but important to the overall preparedness of our nation in face of increased threats of flooding disasters is the need to invest more in pre-disaster mitigation efforts. According to the Government Accountability Office (GAO) most federal assistance for mitigation efforts is only available after a disaster occurs. Data shows that between 2011 and 2014, over $3 billion was spent on post-disaster mitigation as compared to just $222 million in pre-disaster mitigation efforts. While we'll never eliminate the need for post-disaster aid, **Congress should aim to reverse this and invest more in pre-disaster mitigation programming across all at-risk communities in an effort to drive down the number of NFIP claims and overall taxpayer liability.**

- **Business Interruption Coverage** – Offering the opportunity to allow additional coverage for loss of business due to serious flood damage, would permit a property owner to more quickly recover from an event. Property owners frequently purchase this line of coverage when property damage forces the relocation of business operations, resident relocations, and other expenses. **Therefore we encourage Congress to support this addition as part of the NFIP's reauthorization.**

We thank you for the opportunity to present the views of the multifamily industry as you begin deliberations to reauthorize and reform the NFIP. The NFIP serves an important purpose and is a valued and necessary risk management tool for apartment owners and managers. We stand ready to support the efforts of Congress to make the necessary improvements to the program to ensure its long-term success.

Sincerely,

Douglas M. Bibby
President
National Multifamily Housing Council

Douglas S. Culkin, CAE
President & CEO
National Apartment Association

cc: Members of the House Financial Services Committee

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January 12, 2016

The Honorable Blaine Luetkemeyer
Chairman
Subcommittee on Housing and Insurance
House Financial Services Committee
2128 Rayburn House Office Building
Washington, DC 20515

The Honorable Emanuel Cleaver
Ranking Member
Subcommittee on Housing and Insurance
House Financial Services Committee
4340 Thomas P. O'Neill, Jr., Office Building
Washington, DC 20515

Dear Chairman Luetkemeyer and Representative Cleaver:

In September 2017, authorization for the National Flood Insurance Program will expire. On behalf of our members, we commend you and the Committee for taking a proactive role in examining the National Flood Insurance Program. Today's hearing is a welcomed step toward informing the debate on reauthorizing the NFIP and invigorating the flood insurance market more broadly.

AIA is the leading property-casualty insurance trade organization, representing approximately 325 insurers that write more than $127 billion in premiums each year. AIA member companies offer all types of property-casualty insurance, including personal and commercial auto insurance, commercial property and liability coverage, workers' compensation, homeowners' insurance, medical malpractice coverage, and product liability insurance. Several AIA member companies provide flood insurance in partnership with NFIP through the Write-Your-Own (WYO) program.

Recent flooding along the Mississippi river reminds us that communities all across the United States remain vulnerable to severe flooding. Our country's ability to properly manage catastrophic risk depends on our willingness to undertake a thoughtful debate on how best to make our communities more resilient, protect property, and reduce taxpayer exposure. Flood insurance does and will continue to play a critical role in managing the risks associated with flooding. As flood insurance plays a key role in assisting homeowners, businesses, and communities recover from the damages that flooding causes, it is critical that we explore ways to incentivize those at risk to purchase flood insurance.

Much of the recent discussion of the NFIP has been dominated by examination of claims arising from Superstorm Sandy. That storm was, of course, tremendously challenging and akin to what happened after Hurricane Katrina in scope if not absolute numbers. Such unprecedented storm based flooding provides unique challenges compounded by hundreds of thousands of claims. Notwithstanding these challenges approximately only 1 percent of claims resulted in any form of regulatory complaints. Moreover, of the more than 142,000 policyholders with Sandy-related NFIP claims only about 13% (18,500) sought an additional review established by the NFIP. Of those, as of December only 594 received further payments after reviewing approximately 2,700. Consequently, despite NFIP system challenges that WYOs are eager to have solved and notwithstanding media coverage that focused on a small minority of claims, our industry responded quite well under incredibly challenging circumstances in a mass catastrophe in one of the most densely populated parts of our nation.

Currently, the National Flood Insurance Program (NFIP) is the primary flood insurer for homeowners across the country. The NFIP has approximately 5million policies in force and has on outstanding debt of approximately $23 billion. The program's debt is primarily a result of catastrophic events over the past decade, including

Chairman Luetkemeyer and Rep. Cleaver
January 12, 2016
Page 2

Hurricanes Katrina in 2005, Hurricane Ike in 2008 and more recently Superstorm Sandy in 2013. In addition to the financial stress, these events have exposed weaknesses and inefficiencies in how program operates. After large catastrophic events, policyholders, communities, and insurance companies are often frustrated by a complex and opaque system that, for some, can hinder post event recovery. In addition, the NFIP is struggling to maintain its base of policyholders. As a result, policymakers, insurers, and other stakeholders are asking important questions about how to make the NFIP work better for communities, policyholders, and taxpayers.

Since the 1983 the program has operated as a partnership with private insurance carries through the Write-Your-Own (WYO) program. Under the WYO model, private insurers enter into an agreement with the NFIP to sell and administer the NFIP's standard flood insurance policy (SFIP). Per the arrangement, the NFIP sets the rules and regulations under which the WYO companies must operate. Importantly, those mandates include how to process and adjust claims, the rates charged, which losses that are covered, what proof is necessary from policyholders and how WYO companies are compensated. The terms of the agreement also prohibit a WYO partner from offering competing flood insurance coverage. As the Committee investigates ways to improve the NFIP and encourage market oriented alternatives we urge that the concepts of simplicity, transparency, and certainty guide the debate. A program that provides insurers and property-owners certainty in the market place, transparency in the process and clarity regarding coverages will enhance the experience of all stakeholders. Achieving transparency, certainty and simplicity will allow insurers and property owners to make better choices regarding the risk they face and the best products to meet their needs.

Rates that reflect risk are absolutely critical if we want to reduce the risk to the Treasury while encouraging the development of private market alternatives to the NFIP. Simply put, suppressing rates for the private sector or permitting the NFIP to have artificially low rates will preserve the status quo as private insurers will not be able to effectively compete for the business on the scale necessary. We are all mindful that rate shock can be an issue for some consumers, and we look forward to working with the Committee to explore options to address the issue.

Finally, while providing choice to property owners is a key component to a competitive marketplace, it is critical that homeowners work with their insurance carriers, and their agents or brokers, to understand the scope of the coverages and to ensure that they have the proper coverage amounts. There may be opportunities within the NFIP to provide additional coverage options to broaden appeal for the product and thereby expand the opportunities to spread the flood risk further.

Again, thank you for your leadership on this important issue and we look forward to working with you to better prepare homeowners and communities recover from damages caused by flooding. Please feel free to contact AIA if we can be of any further assistance.

Sincerely,

Thomas Santos

Vice President, Federal Affairs

CC: The Honorable Jeb Hensarling, Chairman, House Committee on Financial Services
The Honorable Maxine Waters, Ranking Member, House Committee on Financial Services

NATIONAL ASSOCIATION OF PROFESSIONAL INSURANCE AGENTS

Local Agents Serving Main Street America℠

STATEMENT BEFORE THE U.S. HOUSE OF REPRESENTATIVES COMMITTEE ON FINANCIAL SERVICES SUBCOMMITTEE ON HOUSING AND INSURANCE HEARING ON "OPPORTUNITIES AND CHALLENGES FACING THE NATIONAL FLOOD INSURANCE PROGRAM"

January 12, 2016

Founded in 1931, the National Association of Professional Insurance Agents (PIA) is a national trade association that represents independent insurance agencies and their employees who sell and service all kinds of insurance but specialize in coverage of automobiles, homes, and businesses. PIA represents independent insurance agents in all 50 states, Puerto Rico, and the District of Columbia. They operate cutting-edge agencies and treat their customers like neighbors, providing personal support and service. PIA members are *Local Agents Serving Main Street America*℠.

Background

The enactment of the enabling legislation creating the federal National Flood Insurance Program (NFIP) in 1968 finally provided the opportunity for property owners in the U.S. to secure flood insurance coverage for their homes. Exposure to and damage from major flooding events continues to be the most common natural disaster experienced in the U.S., and it affects all regions of the country. The NFIP was created to address the fact that the private insurance market historically did not provide insurance coverage for this unpredictable and catastrophic peril. As a result, the NFIP has long been virtually the only means by which people could protect their financial interests and obligations, and prepare for damage to their homes, rental properties, businesses, and/or municipal properties.

PIA continues to strongly support the NFIP because it continues to be the most reliable source of insurance coverage for the flood perils faced by PIA members' insurance customers and communities. The program also requires responsible and effective land use, the implementation and maintenance of building codes and mitigation measures by participating communities, as well as compliance by policyholders with applicable community standards. This critical "compliance" component of the NFIP is one of its fundamental principles. Congress intends for such compliance efforts to cultivate more resilient communities that can avoid and/or better withstand the impact of such events. This type of unique risk management role can only be fulfilled by the federal government.

The NFIP is currently in debt due to the significant claims that arose following the record-setting 2005 Atlantic hurricane season (which included Hurricanes Katrina, Rita, Wilma), and "Superstorm" Sandy in 2012. Absent these rare mega-events, historically, the program has been self-sustaining. Prior to the 2005 hurricane season, the NFIP program had never exceeded $4 million in paid losses.[1]

However, the lingering $23 billion debt incurred after these two unique events continues to threaten the ongoing financial viability of the NFIP, which insures, as of September 30, 2015, an aggregated

[1] https://www.fema.gov/loss-dollars-paid-calendar-year, *accessed January 12, 2016*

property value of over $1.2 trillion, with total written premium of over $3.6 billion.[2] Further, most of the NFIP-insured property has outstanding mortgages with loans backed by U.S. federal financial institutions. Therefore, the NFIP has a significant effect on the U.S. lending, real estate, property, and insurance sectors.

In recent years, the reauthorization of the NFIP has not been smooth, with over 15 short-term extensions since 2002. In 2010 alone, the program lapsed four separate times, and flood insurance could not be purchased for a total of 53 nonconsecutive days.[3] In July 2012, the enactment of the new flood bill finally removed this aspect of uncertainty for the 5-year extension period authorized by the Biggert-Waters Flood Insurance Reform Act, PL 112-141 (Biggert-Waters).

PIA was active during the NFIP's reauthorization via Biggert-Waters in 2012 and endorsed the reforms contained therein. Biggert-Waters was enacted with bipartisan support to put the NFIP on a financially stable track by setting forth a plan to gradually phase out subsidies in favor of risk-based rates.

However, the time required to implement the reform provisions of Biggert-Waters using the specific NFIP regulations, rules, and instructions was underestimated. In March 2014, Congress adopted the Homeowner Flood Insurance Affordability Act (HFIAA), which modified several of the reforms in Biggert-Waters to provide more rational, slower-paced premium increases, moving towards risk-based rates. PIA also strongly advocated for the reinstatement of the NFIP core grandfathering provisions regarding insured properties built in the past but in compliance with the code applicable at the time; the reinstatement of said provisions stabilized the real estate industry after the uncertainty that came with the passage of Biggert-Waters.

In addition, PIA supported Congress's requirement that flood insurance policyholders reduce losses by implementing common-sense mitigation practices. We were pleased that Congress included a provision requiring the Federal Emergency Management Agency (FEMA) to account for flood mitigation activities in estimates of premium rates and to create guidelines for property owners that provide methods of mitigation other than building elevation to reduce flood risk to residential buildings.

The net effect of Biggert-Waters and the HFIAA will help the NFIP in the long term. However, PIA remains concerned about how to resolve the program's underlying long-term problems of achieving adequate risk-based rates and ensuring the affordability of those rates to policyholders. The most significant underlying problem with the NFIP is its considerable debt, currently estimated at $23 billion.[4]

As Congress begins to consider the prospect of reauthorizing the program, we would like to take this time to discuss the opportunities and challenges for the NFIP going forward.

Critical Role of the Agent

PIA National has been invested in the creation and improvement of the NFIP since its implementation to serve the safety and financial stability of our communities and for the customers we serve. Insurance agents play a vital role in serving the flood insurance needs of consumers. PIA agents help consumers better understand the NFIP, an essential and often misunderstood program. Independent insurance agents are most often the face of the NFIP and the first person policyholders turn to when they have

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[2] Aggregated property value and total premium figures provided by Federal Insurance & Mitigation Administration (FIMA) on 1-6-16

[3] The extension that followed each lapse included language retroactively providing coverage during the lapse period.

[4] http://www.gao.gov/highrisk/national_flood_insurance/why_did_study, *accessed January 12, 2016*

questions on their policy or when it comes time to file a claim. As such, agents are the backbone of the NFIP system. They provide consumers with the knowledge and expertise to find and purchase the right coverage.

On behalf of our members serving their customers, PIA members work diligently to improve the NFIP's efficiency, effectiveness, and stability. A long-term reauthorization of the program would give FEMA more time to deliberately pace the many changes needed from current (and forthcoming additional) reforms and for those changes to be more successfully communicated to agents and consumers.

FEMA must have the time to craft clear communications and develop informational materials that agents and consumers can rely upon and easily access when they discuss the NFIP. This goal of clarity and consistency of communication between agents and consumers concerning the NFIP has never been more important than it is today, as the Biggert-Waters and HFIAA reforms continue to be implemented. As a result of the legislative reforms enacted over the last several years, PIA members report that they invest more time in discussing NFIP-related issues with their customers as well as developing options for customers to compare and contrast as they make their purchasing decisions.

PIA strongly supports increased educational resources to make sure producers can speak fluently about the NFIP program. Agents have the expertise to advise consumers on the program, but as it has changed over the last several years, and with continuing rulemaking by FEMA, educational resources must be made available for producers to ensure they are up to date on all aspects of the NFIP.

Congress should keep in mind the agent's key role in supporting the program when reauthorizing the NFIP. We may express concern about changes that would be detrimental to an agent's ability to fulfill his/her required role in the program or that would negatively affect fair compensation for doing so. Effectively lowering compensation for NFIP agents could lead some current producers to leave the NFIP, which would create a void for consumers and for the NFIP.

Private Carrier Approach

The current Write Your Own (WYO) private carrier approach, in which private insurance companies engage in a business relationship with FEMA to provide flood coverage under the auspices of the NFIP, has proven successful since it was created in early 1980s. The approximately 80 WYO companies handle 86% of the flood policies in the program. Substantially changing this model would ostensibly mean that NFIP Direct—the part of the program in which FEMA directly oversees claims management, without WYO involvement—and that currently handles less than 15% of policies, would be expected to handle all of them. NFIP has tried the "direct" model several times and has returned to the WYO model, which supports more stable growth for the program. WYOs working with insurance agents to write NFIP policies have vastly more expertise and experience to handle these policies than FEMA.

Congress should be guided by the past experiences of the NFIP. The combination of independent agents and WYOs delivering the vast majority of policies in the NFIP has proven its value and should be retained to prevent a federal government model that will only add to the bureaucracy and opacity already experienced by consumers.

Risk-Based Rates and Affordability

The current NFIP debt is primarily the result of the two extraordinary mega-events, Katrina and Sandy. PIA strongly supports the forgiveness of the $23 billion debt owed to the Treasury Department. Failure to forgive the debt will only cause the debt to grow, continuing to threaten the stability of the program and continuing to place its financial future in doubt.

Biggert-Waters sought to put the program on a path toward fiscal stability by introducing a gradual approach toward achieving the imposition on policyholders of actuarially sound rates while continuing to provide the necessary coverage. Together with the HFIAA, which provided an even more gradual path to risk-based rates, the NFIP is presently on a good path toward fiscal strength.

The gradual implementation of actuarially sound rates is the only realistic way of accomplishing the twin goals of developing a financially sound program along with the maintenance of policyholder capacity. Risk-based rates are essential for putting the NFIP on the path to fiscal stability, but they must be implemented gradually over time with clear and frequent communication from FEMA. Otherwise, consumers will be left bewildered by sudden increases in their premiums.

By forgiving the existing debt of the NFIP, Congress better ensures that the program can build reserves for future flooding events. By gradually moving away from subsidized rates, the NFIP can move toward solvency, a goal that PIA strongly supports.

Mitigation

Mitigation is one area that could help control costs for the NFIP. Success in this area allows communities, homeowners, and businesses to resume normal activity more quickly after a disaster. Both Biggert-Waters and the HFIAA tasked FEMA with researching mitigation methods for property owners other than elevation of a home to reduce flood risk. The HFIAA also authorized FEMA to consider and incorporate various flood mitigation activities when estimating and calculating premium rates.

Future flood-related legislation should incentivize homeowners to mitigate loss to their homes by making it easier and more affordable to do so. To this end, PIA supports H.R. 2230, the Disaster Savings Accounts Act, introduced by Rep. Dennis Ross (R-FL), which would allow homeowners to contribute up to $5,000 a year to a tax-deductible savings account, where unused funds would roll over each year. The savings could be used to pay for home mitigation and fortification expenses to minimize a loss or for recovery expenses after a loss. This bill is a simple and effective way to encourage and reward homeowners who actively prepare for future disasters.

Further, Congress should increase the incentives for communities to participate in the NFIP and to continue to participate by keeping up to date with their land-use, mitigation, and building code requirements. This would assure that communities implement and continue to maintain and upgrade necessary land-use restrictions and mitigation methods.

Cultivating the Private Market

PIA continues to support the engagement of private sector insurers in offering flood insurance policies and endorsement coverages. Opportunities for private sector insurers are better now than they have been in the past. However, the private flood insurance market is in need of legislative solutions to create sensible options for it to grow.

To move in this direction, PIA strongly supports H.R. 2901, the Flood Insurance Market Parity and Modernization Act, introduced by Reps. Dennis Ross (R-FL) and Patrick Murphy (D-FL). Currently, lenders are unsure of the validity of privately-issued flood insurance in terms of lenders' obligations under the mandatory purchase requirement and their own internal mandates to have key risk exposures securely covered. It is critical for agents, lenders, and consumers to have a simple and clear definition of what constitutes acceptable private flood insurance. This legislation provides a solution by defining private flood insurance as a policy that provides flood insurance coverage issued by an insurance company that is licensed and approved by the state insurance regulator to engage in the business of insurance in the state in which the insured building is located. It also includes a critical provision to ensure that private flood insurance can be used to satisfy the NFIP's continuous coverage requirement, an essential aspect of ensuring policyholders are not penalized for moving from one policy to another.

Conclusion

PIA supports the NFIP, as it provides critical flood coverage that the private market is presently unable to supply. PIA remains concerned that delaying the implementation of risk-based rates, while providing needed economic relief for many homeowners ignores the underlying long-term problem continuing to threaten the stability of the program.

The highlighted issues in this submission are our key reform concerns. In 2016, PIA will continue to work with FEMA and Congress to support solutions that will eliminate the NFIP's debt and put the program on a path to financial stability ahead of its scheduled expiration on September 30, 2017. PIA will continue to emphasize the essential role of the independent agent in delivering the products associated with this complex program. We will also support legislative solutions to create sensible options for developing the private market and incentivizing insureds to mitigate losses to homes and businesses. PIA also urges Congress to work towards a long-term reauthorization of the program to provide it with more stability and attract both policyholders and private insurers.

NATIONAL ASSOCIATION *of* REALTORS®

Tom Salomone
2016 President

Dale A. Stinton
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January 12, 2016

The Honorable Blaine Luetkemeyer	The Honorable Emanuel Cleaver
Chairman	Ranking Member
Subcommittee on Housing and Insurance	Subcommittee on Housing and Insurance
House Financial Services Committee	House Financial Services Committee

Dear Chairman Leutkemeyer and Ranking Member Cleaver:

Thank you for holding this important hearing on the opportunities and challenges facing the National Flood Insurance Program (NFIP). Reauthorizing the NFIP is a top priority of our membership. NAR appreciates the opportunity to outline some of the challenges needed to be addressed as part of the 2017 reauthorization legislation.

Long-term Reauthorization – The September 30, 2017 deadline for Congress to reauthorize NFIP is fast approaching. Prior to the most recent reauthorization, Congress passed 18 month-to-month extensions and twice, the NFIP shut down, costing 40,000 home sales each month according to NAR research. The nation cannot afford to repeat that experience. The Association applauds the Subcommittee for beginning work on a critical issue.

A Stronger NFIP – The NFIP is currently billions of dollars in debt to the Treasury because of past claims. NAR supports strengthening the long term solvency of the NFIP and believes that a strong NFIP is integral to the success of any future flood insurance landscape. As we learned in the last reauthorization, any major reforms should be incremental, gradual and phased in over time to avoid major disruptions in communities or markets. The discussion should also include reforms that would improve the uptake in purchase of flood insurance; temporarily establish nominal surcharges, and allow the NFIP to buy reinsurance.

Private Market Options – REALTORS® believe that private insurance alternatives can provide a complement to a strong and vibrant NFIP. Because NFIP is over charging some property owners, especially in the low risk X zone, more opportunities exist for the private market to offer comparable coverage at lower cost. NAR supports the development of private market options. It is important, too, that consumers are allowed to move to and from the private flood insurance without the NFIP considering it a break in continuous coverage; such a break would trigger a rate increase, should the owner return to the NFIP. The combination of private market options and a strong NFIP will ensure that flood insurance remains available in all markets at all times.

EQUAL HOUSING OPPORTUNITY

Unaffordable Flood Insurance – Approximately one million properties in the NFIP were built before the first flood insurance rate map (or are "pre-FIRM"). NFIP does not collect elevation data for these pre-FIRM structures. Nevertheless, the NFIP believes that most are located below the base flood elevation (BFE) – i.e., the expected depth of the flood waters in a 100-year storm.[1] Depending on how far below BFE these structures sit, over the next 5-10 years, the owners could be facing rate increases until they reach the maximum rate of $62,500 per year.[2] Under these circumstances, owners would have limited options: They could not sell their property without taking a substantial loss. The private market will not insure them. There is only limited if any access to financing in order to mitigate, buy out, relocate or elevate the structure. And the longer we wait, the more expensive the problem becomes. NAR would like to work with the Subcommittee to add a strong mitigation financing section to the 2017 reauthorization legislation. Providing the property owners most at risk with the ability to help themselves is a "win-win" not only for the owner (who becomes able to mitigate and keep their NFIP rate down) but also for taxpayers who will spend less on mitigated properties' claims.

Cross Subsidization in the NFIP – Attached is the summary of a report on NFIP insurance rates conducted by independent actuaries with the Milliman Company. The study looked at NFIP rates in 5 counties – Pinellas, FL; Harris, TX; Ocean, NJ; Merced, CA; and Hancock, OH, and compared them with the way a private insurance company would price the risk. The study shows how many property owners are overcharged potentially by thousands of dollars under the NFIP. By having only one "A zone" rate table for most high risk properties, NFIP rates do not align well with the property's specific risk. In addition, the X zone rate table does not account for the property's elevation or other risk factors, so the low risk property owners may be charged more than high risk properties if they are elevated. This is a counterintuitive result. Moving toward more granular data and property specific hazard assessments, along with creating additional rate tables, would help to increase fairness in NFIP's rating structure. This in turn would encourage greater voluntary participation and help improve the program's solvency.

"Guilty until Proven Innocent" – If a property is incorrectly mapped into the flood zone, either the owner must buy flood insurance or prove that the map is incorrect. When the NFIP began flood mapping, there were not the technological innovations that now exist. NFIP should take advantage of advances in LIDAR and computer modeling in order to improve the accuracy of the flood maps upfront. Doing so will reduce the number of property owners who now have to appeal an incorrect map on the back end. At the same time, NAR does support streamlining the flood map appeal process and reimbursing homeowners when they win their appeal.

Thank you for considering the views of NAR's 1.1 million members. NAR looks forward to working with you and the rest of the Committee to develop a comprehensive reauthorization package that is timely, carefully considered, and fully deliberated in order to address as many of the challenges as possible.

Sincerely,

Tom Salomone
2016 President, National Association of REALTORS®

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[1] National Research Council. "Tying Flood Insurance to Flood Risk for Low-Lying Structures in the Floodplains," August 2015, page 1.
[2] The top rate in NFIP tables appears to be $25 per $100 of coverage; $250,000 is the maximum amount of structure-only coverage available under NFIP: $250,000 x $25/$100 = $62,500 per year. For NFIP's Specific Rating Guidelines: http://www.fema.gov/media-library-data/1450374017262-8d8a14ee8c48efb5356e9fb5b24ff2a1/SRG_April2016.pdf

NAR Brief
MILLIMAN FLOOD INSURANCE STUDY

Top Line Summary
- Independent actuaries studied National Flood Insurance Program (NFIP) rates in 5 counties.
- The study finds that many property owners are overcharged while others are undercharged.
- NAR recommends several changes to better align NFIP rates to the property-specific risk.

Key Study Findings
- NFIP rates are currently not well aligned with risk.
- NFIP rates do not track with other risk factors such as distance to coast/river.
- Doing so could increase NFIP participation and strengthen solvency.
- "A Zones" (high risk areas): NFIP uses one rate table to charge most high risk properties across the U.S.
  - As a result, two property owners facing different risks could pay the same premium rate.
    - For example, storm surge flooding in coastal areas causes more damage than riverine flooding – yet in the A zone, rates do not reflect this difference.
  - Also, because 20% of properties are subsidized, adjacent properties with identical risk profiles could pay dramatically different rates.
- "X Zones" (low risk): While the A zone table accounts for the relative elevation of the property, the X zone table does not; many will not voluntarily opt in as long as the average rate is so high.
  - Thus some low risk properties pay more than high risk properties that are elevated.

Recommendations
- Divide the A zone into coastal and inland subzones and calculate a rate table for each.
- Incorporate risk factors such as distance to river/coast, in addition to property elevation.
- Develop an X zone table that accounts for property elevation and other appropriate risk factors.

Methodology
- This is a case study, not a full actuarial study of FEMA's rate-making process.
- Selected 5 counties: Pinellas, FL; Harris, TX; Ocean, NJ; Merced, CA; and Hancock, Ohio.
- Identified a typical high risk property for each county (e.g., 1-story $175,000 masonry structure built in 1970) then varied one attribute (e.g., built in 1995 instead of 1970).
- Assumed that all properties in the county reflect these characteristics so only the location and elevation of the property would vary.
- Calculated the rate two ways: first as NFIP would then as a private insurance company would, and compared the results.
- Evaluated how the rates change with other risk factors including the distance to coast/river.

Complete Study & Results: Available upon Request

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