

**GAO**

Testimony

Before the Subcommittee on Insurance,  
Housing, and Community Opportunity,  
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## FLOOD INSURANCE

# Public Policy Goals Provide a Framework for Reform

Statement of Orice Williams Brown, Managing Director  
Financial Markets and Community Investment



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Highlights of [GAO-11-429T](#), a testimony before the Subcommittee on Insurance, Housing, and Community Opportunity, Committee on Financial Services, House of Representatives

## Why GAO Did This Study

The National Flood Insurance Program (NFIP) has been on GAO's high-risk list since 2006, when the program had to borrow from the U.S. Treasury to cover losses from the 2005 hurricanes. The outstanding debt is \$17.8 billion as of March 2011. This sizeable debt, plus operational and management challenges that GAO has identified at the Federal Emergency Management Agency (FEMA), which administers NFIP, have combined to keep the program on the high-risk list. NFIP's need to borrow to cover claims in years of catastrophic flooding has raised concerns about the program's long-term financial solvency. This testimony 1) discusses ways to place NFIP on a sounder financial footing in light of public policy goals for federal involvement in natural catastrophe insurance and 2) highlights operational and management challenges at FEMA that affect the program.

In preparing this statement, GAO relied on its past work on NFIP and on its ongoing review of FEMA's management of NFIP, which focuses on its planning, policies, processes, and systems. The management review includes areas such as strategic and human capital planning, acquisition management, and intra-agency collaboration.

GAO has made numerous recommendations aimed at improving financial controls and oversight of private insurers and contractors, among others.

View [GAO-11-429T](#) or key components. For more information, contact Orice Williams Brown at (202) 512-8678 or [williamso@gao.gov](mailto:williamso@gao.gov).

March 11, 2011

## FLOOD INSURANCE

### Public Policy Goals Provide a Framework for Reform

## What GAO Found

Congressional action is needed to increase the financial stability of NFIP and limit taxpayer exposure. GAO previously identified four public policy goals that can provide a framework for crafting or evaluating proposals to reform NFIP. These goals are:

- charging premium rates that fully reflect risks,
- limiting costs to taxpayers before and after a disaster,
- encouraging broad participation in the program, and
- encouraging private markets to provide flood insurance.

Successfully reforming NFIP would require trade-offs among these often competing goals. For example, currently nearly one in four policyholders does not pay full-risk rates, and many pay a lower subsidized or "grandfathered" rate. Reducing or eliminating less than full-risk rates would decrease costs to taxpayers but substantially increase costs for many policyholders, some of whom might leave the program, potentially increasing postdisaster federal assistance. However, these trade-offs could be mitigated by providing assistance only to those who needed it, limiting postdisaster assistance for flooding, and phasing in premium rates that fully reflected risks. Increasing mitigation efforts to reduce the probability and severity of flood damage would also reduce flood claims in the long term but would have significant up-front costs that might require federal assistance. One way to address this trade-off would be to better ensure that current mitigation programs were effective and efficient. Encouraging broad participation in the program could be achieved by expanding mandatory purchase requirements or increasing targeted outreach to help diversify the risk pool. Such efforts could help keep rates relatively low and reduce NFIP's exposure but would have to be effectively managed to help ensure that outreach efforts were broadly based. Encouraging private markets is the most difficult challenge because virtually no private market for flood insurance exists for most residential and commercial properties. FEMA's ongoing efforts to explore alternative structures may provide ideas that could be evaluated and considered.

Several operational and management issues also limit FEMA's progress in addressing NFIP's challenges, and continued action by FEMA will be needed to help ensure the stability of the program. For example, in previous reports GAO has identified weaknesses in areas that include financial controls and oversight of private insurers and contractors, and has made many recommendations to address them. While FEMA has made progress in addressing some areas, preliminary findings from GAO's ongoing work indicate that these issues persist and need to be addressed as Congress works to more broadly reform NFIP.



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Chairman Biggert, Ranking Member Gutierrez, and Members of the Subcommittee:

I appreciate the opportunity to participate in today's hearing on National Flood Insurance Program (NFIP) reform. As you know, NFIP is the key component of the federal government's efforts to minimize the damage from and financial impact of floods and is the only source of insurance against flood damage for most residents in vulnerable areas. NFIP has been on GAO's high-risk list since March 2006 after incurring billions of dollars in catastrophic losses from the 2005 hurricanes. Further contributing to NFIP's high-risk classification are operational and management challenges that we have identified within the Federal Emergency Management Agency (FEMA) that affect the program. As of March 2011, NFIP still owed approximately \$17.8 billion to the Department of the Treasury (Treasury) for loans used to cover losses from the 2005 hurricanes. The magnitude of this debt highlights the many financial challenges the program faces, including structural weaknesses in the way it is funded, and the managerial challenges that have affected FEMA's administration of NFIP. Any efforts to help stabilize NFIP will require addressing both the program's financial challenges and its operational and management issues.

My statement today discusses four public policy goals that GAO has developed for evaluating federal involvement in the provision of natural catastrophe insurance and identifies key program areas needing reform, potential ways to better fulfill these goals, and the trade-offs that would be required. This statement also sets out the operational and managerial challenges facing NFIP that we have identified in past reports and are examining in ongoing work. We performed our work in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence we obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

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## Background

The National Flood Insurance Act of 1968 established NFIP as an alternative to providing direct assistance after floods.<sup>1</sup> NFIP, which

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<sup>1</sup>Pub. L. No. 90-448, Title XIII, 82 Stat. 476 (1968).

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provides government-guaranteed flood insurance to homeowners and businesses, was intended to reduce the federal government's escalating costs for repairing flood damage after disasters. FEMA, which is within the Department of Homeland Security (DHS), is responsible for the oversight and management of NFIP. Since NFIP's inception, Congress has enacted several pieces of legislation to strengthen the program. The Flood Disaster Protection Act of 1973 made flood insurance mandatory for owners of properties in vulnerable areas who had mortgages from federally regulated lenders and provided additional incentives for communities to join the program.<sup>2</sup> The National Flood Insurance Reform Act of 1994 strengthened the mandatory purchase requirements for owners of properties located in special flood hazard areas (SFHA) with mortgages from federally regulated lenders.<sup>3</sup> Finally, the Bunning-Bereuter-Blumenauer Flood Insurance Reform Act of 2004 authorized grant programs to mitigate properties that experienced repetitive flooding losses. Owners of these repetitive loss properties who do not mitigate may face higher premiums.<sup>4</sup>

To participate in NFIP, communities agree to enforce regulations for land use and new construction in high-risk flood zones and to adopt and enforce state and community floodplain management regulations to reduce future flood damage. Currently, more than 20,000 communities participate in NFIP. NFIP has mapped flood risks across the country, assigning flood zone designations based on risk levels, and these designations are a factor in determining premium rates. NFIP offers two types of flood insurance premiums: subsidized and full risk. The National Flood Insurance Act of 1968 authorizes NFIP to offer subsidized premiums to owners of certain properties. These subsidized premium rates, which represent about 40 to 45 percent of the cost of covering the full risk of flood damage to the properties, apply to about 22 percent of all NFIP policies. To help reduce or eliminate the long-term risk of flood damage to buildings and other structures insured by NFIP, FEMA has used a variety of mitigation efforts, such as elevation, relocation, and demolition. Despite these efforts, the inventories of repetitive loss properties—generally, as defined by FEMA, those that have had two or more flood insurance claims payments of \$1,000 or more over 10 years—and policies with subsidized

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<sup>2</sup>Pub. L. No. 93-234, §102, 87 Stat. 975, 978 (1973).

<sup>3</sup>Pub. L. No. 103-325, 108 Stat. 2255 (1994).

<sup>4</sup>Pub. L. No. 108-264, §§ 102, 104, 118 Stat. 712, 714, 722 (2004).

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premium rates have continued to grow.<sup>5</sup> In response to the magnitude and severity of the losses from the 2005 hurricanes, Congress increased NFIP's borrowing authority from the Treasury to \$20.8 billion.

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## Efforts to Reform NFIP's Financial Structure Will Require Balancing Public Policy Goals

We have previously identified four public policy goals for evaluating the federal role in providing natural catastrophe insurance:

- charging premium rates that fully reflect actual risks,
- limiting costs to taxpayers before and after a disaster,
- encouraging broad participation in natural catastrophe insurance programs, and
- encouraging private markets to provide natural catastrophe insurance.<sup>6</sup>

Taking action to achieve these goals would benefit both NFIP and the taxpayers who fund the program but would require trade-offs. I will discuss the key areas that need to be addressed, actions that can be taken to help achieve these goals, and the trade-offs that would be required.

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## Charging Full-Risk Rates Would Improve NFIP's Financial Soundness but Could Reduce Program Participation

As I have noted, NFIP currently does not charge all program participants rates that reflect the full risk of flooding to their properties. First, the act requires FEMA to charge many policyholders less than full-risk rates to encourage program participation. While the percentage of subsidized properties was expected to decline as new construction replaced subsidized properties, today nearly one out of four NFIP policies is based on a subsidized rate. Second, FEMA may "grandfather" properties that are already in the program when new flood maps place them in higher-risk zones, allowing some property owners to pay premium rates that apply to the previous lower-risk zone. FEMA officials told us that they made the

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<sup>5</sup>Bunning-Bereuter-Blumenauer Flood Insurance Reform Act of 2004, Pub. L. No. 108-264, 118 Stat. 712 (2004). The act amended the existing definition of the term repetitive loss structure to the current one: a structure covered by a contract for flood insurance that has incurred flood-related damage on two occasions, in which the cost of repair, on the average, equaled or exceeded 25 percent of the value of the structure at the time of each such flood event; and at the time of the second incidence of flood-related damage, the contract for flood insurance contains increased cost of compliance coverage, which can help property owners pay for the cost of mitigation measures for flood-damaged properties. 42 U.S.C. § 4121(a).

<sup>6</sup>See GAO, *Natural Disasters: Public Policy Options for Changing the Federal Role in Natural Catastrophe Insurance*, [GAO-08-7](#) (Washington, D.C.: Nov. 26, 2007).

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decision to allow grandfathering because of external pressure to reduce the effects of rate increases, and considerations of equity, ease of administration, and the goals of promoting floodplain management. Similarly, FEMA recently introduced a new rating option called the Preferred Risk Policy (PRP) Eligibility Extension that in effect equals a temporary grandfathering of premium rates.<sup>7</sup> While these policies typically would have to be converted to more expensive policies when they were renewed after a new flood map came into effect, FEMA has extended eligibility for these lower rates. Finally, we have also raised questions about whether NFIP's full-risk rates reflect actual flood risks. Because many premium rates charged by NFIP do not reflect the full risk of loss, the program is less likely to be able to pay claims in years with catastrophic losses, as occurred in 2005, and may need to borrow from Treasury to pay claims in those years.<sup>8</sup>

Increasing premium rates to fully reflect the risk of loss—including the risk of catastrophic loss—would generally require reducing or eliminating subsidized and grandfathered rates and offers several advantages. Specifically, increasing rates could:

- result in premium rates that more fully reflected the actual risk of loss;
- decrease costs for taxpayers by reducing costs associated with postdisaster borrowing to pay claims; and
- encourage private market participation, because the rates would more closely approximate those that would be charged by private insurers.

However, eliminating subsidized and grandfathered rates and increasing rates overall would increase costs to some homeowners, who might then cancel their flood policies or elect not to buy them at all. According to FEMA, subsidized premium rates are generally 40 to 45 percent of rates that would reflect the full risk of loss. For example, the projected average annual subsidized premium was \$1,121 as of October 2010, discounted from the \$2,500 to \$2,800 that would be required to cover the full risk of

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<sup>7</sup>The PRP offers low-cost flood insurance to owners and tenants of residential and nonresidential buildings located in moderate- to low-risk areas as long as the property has not, within any 10-year period, incurred two or more flood insurance claim payments or disaster relief payments (including loans and grants) of more than \$1,000 each.

<sup>8</sup>Implementing rates that reflect the full risk of loss, including catastrophic losses might not eliminate NFIP's need to borrow funds for larger-than-expected losses that occurred before sufficient reserves had been built.



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loss. In a 2009 report, we also analyzed the possibility of creating a catastrophic loss fund within NFIP (one way to help pay for catastrophic losses).<sup>9</sup> Our analysis found that in order to create a fund equal to 1 percent of NFIP's total exposure by 2020, the average subsidized premium—which typically is in one of the highest-risk zones—would need to increase from \$840 to around \$2,696, while the average full-risk premium would increase from around \$358 to \$1,149. Such steep increases could reduce participation, either because homeowners could no longer afford their policies or simply deemed them too costly, and increase taxpayer costs for postdisaster assistance to property owners who no longer had flood insurance.

However, a variety of actions could be taken to mitigate these disadvantages. For example, subsidized rates could be phased out over time or not transferred with the property when it is sold. Moreover, as we noted in our past work, targeted assistance could be offered to those most in need to help them pay increased NFIP premiums.<sup>10</sup> This assistance could take several forms, including direct assistance through NFIP, tax credits, or grants. In addition, to the extent that those who might forego coverage were actually required to purchase it, additional actions could be taken to better ensure that they purchased policies. According to RAND Corporation, in SFHAs, where property owners with loans from federally insured or regulated lenders are required to purchase flood insurance, as few as 50 percent of the properties had flood insurance in 2006.<sup>11</sup>

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<sup>9</sup>See GAO, *Information on Proposed Changes to the National Flood Insurance Program*, [GAO-09-420R](#) (Washington, D.C.: Feb. 27, 2009). The creation of a catastrophic loss fund might not eliminate NFIP's need to borrow funds for larger-than-expected losses that occurred before the fund had been built. Further borrowing could require either a longer period to rebuild the loss fund or debt forgiveness from Congress.

<sup>10</sup>See GAO, *Flood Insurance: Options for Addressing the Financial Impact of Subsidized Premium Rates on the National Flood Insurance Program*, [GAO-09-20](#) (Washington, D.C.: Nov. 14, 2008).

<sup>11</sup>RAND, *The National Flood Insurance Program's Market Penetration Rate: Estimates and Policy Implications* (Santa Monica, Calif.: 2006).

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## Limiting Taxpayer Costs Could Be Achieved by Increasing Premium Rates, but Further Mitigation Efforts Could Incur Up-Front Costs

In order to reduce expenses to taxpayers that can result when NFIP borrows from Treasury, NFIP needs to be able to generate enough in premiums to pay its claims, even in years with catastrophic losses—a goal that is closely tied to that of eliminating subsidies and other reduced rates. Since the program’s inception, NFIP premiums have come close to covering claims in average loss years but not in years of catastrophic flooding, particularly 2005. Unlike private insurance companies, NFIP does not purchase reinsurance to cover catastrophic losses.<sup>12</sup> As a result, NFIP has funded such losses after the fact by borrowing from Treasury. As we have seen, such borrowing exposes taxpayers to the risk of loss. NFIP still owes approximately \$17.8 billion of the amount it borrowed from Treasury for losses incurred during the 2005 hurricane season. The high cost of servicing this debt means that it may never be repaid, could in fact increase, and will continue to affect the program’s solvency and be a burden to taxpayers.

Another way to limit costs to taxpayers is to decrease the risk of losses by undertaking mitigation efforts that could reduce the extent of damage from flooding. FEMA has taken steps to help homeowners and communities mitigate properties by making improvements designed to reduce flood damage—for example, elevation, relocation, and demolition. As we have reported, from fiscal year 1997 through fiscal year 2007, nearly 30,000 properties were mitigated using FEMA funds.<sup>13</sup> Increasing mitigation efforts could further reduce flood damage to properties and communities, helping to put NFIP on a firmer financial footing and reducing taxpayers’ exposure.

FEMA has made particular efforts to address the issue of repetitive loss properties through mitigation. These properties account for just 1 percent of NFIP’s insured properties but are responsible for 25 to 30 percent of claims. Despite FEMA’s efforts, the number of repetitive loss properties increased from 76,202 in 1997 to 132,100 in March 2011, or by about 73 percent. FEMA also has some authority to raise premium rates for property owners who refuse mitigation offers in connection with the

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<sup>12</sup>Reinsurance is essentially insurance for insurers—that is, companies buy coverage for all or a part of a policy’s liability from other insurers in order to offset exposure.

<sup>13</sup>See [GAO-09-20](#).

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Severe Repetitive Loss Pilot Grant Program.<sup>14</sup> In these situations, FEMA can initially increase premiums to up to 150 percent of their current amount and may raise them again (by up to the same amount) on properties that incur a claim of more than \$1,500. However, FEMA cannot increase premiums on property owners who pay the full-risk rate but refuse a mitigation offer, and in no case can rate increases exceed the full-risk rate for the structure. In addition, FEMA is not allowed to discontinue coverage for those who refuse mitigation offers. As a result, FEMA is limited in its ability to compel owners of repetitive loss properties to undertake flood mitigation efforts.

Mitigation offers significant advantages. As I have noted, mitigated properties are less likely to be at a high risk for flood damage, making it easier for NFIP to charge them full-risk rates that cover actual losses. Allowing NFIP to deny coverage to owners of repetitive loss properties who refused to undertake mitigation efforts could further reduce costs to the program and ultimately to taxpayers.

One disadvantage of increased mitigation efforts is that they can impose up-front costs on homeowners and communities required to undertake them and could raise taxpayers' costs if the federal government elected to provide additional mitigation assistance. Those costs could increase still further if property owners who were dropped from the program for refusing to mitigate later received federal postdisaster assistance. These trade-offs are not insignificant, although certain actions could be taken to reduce them. For example, federal assistance such as low-cost loans, grants, or tax credits could be provided to help property owners pay for the up-front costs of mitigation efforts. Any reform efforts could explore ways to improve mitigation efforts to help ensure maximum effectiveness. For example, FEMA has three separate flood mitigation programs.<sup>15</sup> Having multiple programs may not be the most cost-efficient and effective

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<sup>14</sup>Under this program, for single-family properties, a severe repetitive loss is defined as a property covered under a contract for flood insurance that has incurred flood-related damage 1) for which 4 or more separate claims payments have been made, with the amount of each claim exceeding \$5,000, and with the cumulative amount of such claims payments exceeding \$20,000, or 2) for which at least 2 separate claims payments have been made, with the cumulative amount of such claims exceeding the value of the property. 42 U.S.C. § 4102a(b).

<sup>15</sup>These programs include the Flood Mitigation Assistance Program (FMA), the Repetitive Flood Claims Program (RFC), and the Severe Repetitive Loss Program (SRL). Moreover, the Hazard Mitigation Grant Program (HMGP) and the Pre-Disaster Mitigation Program (PDM) are two additional hazard mitigation programs that are not specific to flooding.

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way to promote mitigation and may unnecessarily complicate mitigation efforts.

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### Depending on How They Were Implemented, Efforts to Encourage Broader Participation Could Reduce Costs

Increasing participation in NFIP, and thus the size of the risk pool, would help ensure that losses from flood damage did not become the responsibility of the taxpayer. Participation rates have been estimated to be as low as 50 percent in SFHAs, where property owners with loans from federally insured and regulated lenders are required to purchase flood insurance, and participation in lower-risk areas is significantly lower.<sup>16</sup> For example, participation rates outside of SFHAs have been found to be as low as 1 percent, leaving significant room to increase participation.

Expanding participation in NFIP would have a number of advantages. As a growing number of participants shared the risks of flooding, premium rates could be lower than they would be with fewer participants. Currently, NFIP must take all applicants for flood insurance, unlike private insurers, and thus is limited in its ability to manage its risk exposure. To the extent that properties added to the program were in geographic areas where participation had historically been low and in low- and medium-risk areas, the increased diversity could lower rates as the overall risk to the program decreased. Further, increased program participation could reduce taxpayer costs by reducing the number of property owners who might draw on federally funded postdisaster assistance.

However, efforts to expand participation in NFIP would have to be carefully implemented, for several reasons. First, as we have noted, NFIP cannot reject applicants on the basis of risk. As a result, if participation increased only in SFHAs, the program could see its concentration of high-risk properties grow significantly and face the prospect of more severe losses. Second, a similar scenario could emerge if mandatory purchase requirements were expanded and newly covered properties were in communities that did not participate in NFIP and thus did not meet standards—such as building codes—that could reduce flood losses. As a result, some of the newly enrolled properties might be eligible for subsidized premium rates or, because of restrictions on how much FEMA can charge in premiums, might not pay rates that covered the actual risk of flooding. Finally, historically FEMA has attempted to encourage participation by charging lower rates. However, doing so results in rates

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<sup>16</sup>RAND, *The National Flood Insurance Program's Market Penetration Rate*.

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that do not fully reflect the risks of flooding and exposes taxpayers to increased risk.

Moderating the challenges associated with expanding participation could take a variety of forms. Newly added properties could be required to pay full-risk rates, and low-income property owners could be offered some type of assistance to help them pay their premiums. Outreach efforts would need to include areas with low and moderate flood risks to help ensure that the risk pool remained diversified. For example, FEMA's goals for NFIP include increasing penetration in low-risk flood zones, among homeowners without federally related mortgages in all zones, and in geographic areas with repetitive losses and low penetration rates.

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### Encouraging Private Market Participation Could Reduce the Federal Government's Exposure but Could Also Decrease NFIP's Stability if Only High-Risk Properties Remained

Currently, the private market provides only a limited amount of flood insurance coverage. In 2009, we reported that while aggregate information was not available on the precise size of the private flood insurance market, it was considered relatively small.<sup>17</sup> The 2006 RAND study estimated that 180,000 to 260,000 insurance policies for both primary and gap coverage were in effect.<sup>18</sup> We also reported that private flood insurance policies are generally purchased in conjunction with NFIP policies, with the NFIP policy covering the deductible on the private policy. Finally, we reported that NFIP premiums were generally less expensive than premiums for private flood insurance for similar coverage.<sup>19</sup> For example, one insurer told us that for a specified amount of coverage for flood damage to a structure, an NFIP policy might be as low as \$500, while a private policy might be as high as \$900. Similar coverage for flood damage to contents might be \$350 for an NFIP policy but around \$600 for a private policy.

Given the limited nature of private sector participation, encouraging private market participation could transfer some or all of the federal government's risk exposure to the private markets and away from taxpayers. However, identifying ways to achieve that end has generally been elusive. In 2007, we evaluated the trade-offs of having a mandatory all-perils policies that would include flood risks.<sup>20</sup> For example, it would

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<sup>17</sup>See [GAO-09-420R](#).

<sup>18</sup>RAND, *The National Flood Insurance Program's Market Penetration Rate*.

<sup>19</sup>See [GAO-09-420R](#).

<sup>20</sup>See [GAO-08-7](#).

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alleviate uncertainty about the types of natural events homeowners insurance covered, such as those that emerged following Hurricane Katrina. However, at the time the industry was generally opposed to an all-perils policy because of the large potential losses a mandatory policy would entail.

Increased private market participation is also not without potential disadvantages. First, if the private markets provide coverage for only the lowest-risk properties currently in NFIP, the percentage of high-risk properties in the program would increase. This scenario could result in higher rates as the amount needed to cover the full risk of flooding increased. Without higher rates, however, the federal government would face further exposure to loss. Second, private insurers, who are able to charge according to risk, would likely charge higher rates than NFIP has been charging unless they received support from the federal government. As we have seen, such increases could create affordability concerns for low-income policyholders. Strategies to help mitigate these disadvantages could include requiring private market coverage for all property owners—not just those in high-risk areas—and, as described earlier, providing targeted assistance to help low-income property owners pay for their flood coverage. In addition, Congress could provide options to private insurers to help lower the cost of such coverage, including tax incentives or federal reinsurance.

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## FEMA's Operational and Management Issues May Limit Progress in Achieving NFIP Goals

As Congress weighs NFIP's various financial challenges in its efforts to reform the program, it must also consider a number of operational and management issues that may limit efforts to meet program goals and impair NFIP's stability. For the past 35 years, we have highlighted challenges with NFIP and its administration and operations. For example, most recently we have identified a number of issues impairing the program's effectiveness in areas that include the reasonableness of payments to Write-Your-Own (WYO) insurers, the adequacy of financial controls over the WYO program, and the adequacy of oversight of non-WYO contractors. In our ongoing work examining FEMA's management of NFIP—covering areas including strategic planning, human capital planning, intra-agency collaboration, records management, acquisition management, and information technology—some similar issues are emerging. For example, preliminary results of our ongoing work show that FEMA:

- does not have a strategic plan specific to NFIP with goals, objectives, and performance measures for guiding and measuring the program;

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- lacks a strategic human capital plan that addresses the critical competencies required for its workforce;
  - does not have effective collaborative practices that would improve the functioning of program and support offices;
  - lacks a centralized electronic document management system that would allow its various offices to easily access and store documents;
  - has only recently implemented or is still developing efforts to improve some acquisition management functions, making it difficult to assess the effects of these actions; and
  - does not have an effective system to manage flood insurance policy and claims data, despite having invested roughly 7 years and \$40 million on a new system whose development has been halted.

While FEMA has begun to acknowledge and address some of these management challenges, additional work remains to be done to address these issues. Our final report will include recommendations to address them.

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## Closing Comments

Congressional action is needed to increase the financial stability of NFIP and limit taxpayer exposure. GAO previously identified four public policy goals that can provide a framework for crafting or evaluating proposals to reform NFIP. First, any congressional reform effort should include measures for charging premium rates that accurately reflect the risk of loss, including catastrophic losses. Meeting this goal would require changing the law governing NFIP to reduce or eliminate subsidized rates, limits on annual rate increases, and grandfathered or other rates that did not fully reflect the risk of loss. In taking such a step, Congress may choose to provide assistance to certain property owners, and should consider providing appropriate authorization and funding of such incentives to ensure transparency. Second, because of the potentially high costs of individual and community mitigation efforts, which can reduce the frequency and extent of flood damage, Congress may need to provide funding or access to funds for such efforts and consider ways to improve the efficiency of existing mitigation programs. Moreover, if Congress wished to allow NFIP to deny coverage to owners of properties with repetitive losses who refused mitigation efforts, it would need to give FEMA appropriate authority. Third, Congress could encourage FEMA to continue to increase participation in the program by expanding targeted outreach efforts and limiting postdisaster assistance to those individuals who choose not to mitigate in moderate- and high-risk areas. And finally, to address the goal of encouraging private sector participation, Congress could encourage FEMA to explore private sector alternatives to providing

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flood insurance or for sharing insurance risks, provided such efforts do not increase taxpayers' exposure.

For its part, FEMA needs to take action to address a number of fundamental operational and managerial issues that also threaten the stability of NFIP and have contributed to its remaining on GAO's high-risk list. These include improving its strategic planning, human capital planning, intra-agency collaboration, records management, acquisition management, and information technology. While FEMA continues to make some progress in some areas, fully addressing these issues is vital to its long-term operational efficiency and financial stability.

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Chairman Biggert, Ranking Member Gutierrez, and Members of the Subcommittee, this concludes my prepared statement. I would be pleased to respond to any of the questions you or other members of the Subcommittee may have at this time.

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## GAO Contact and Staff Acknowledgments

Contact points for our Offices of Congressional Relations and Public Affairs may be found on the last page of this statement. For further information about this testimony, please contact Orice Williams Brown at (202) 512-8678 or [williamsor@gao.gov](mailto:williamsor@gao.gov). This statement was prepared under the direction of Patrick Ward. Key contributors were Tania Calhoun, Emily Chalmers, Nima Patel Edwards, and Christopher Forys.



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# Related GAO Products

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*FEMA Flood Maps: Some Standards and Processes in Place to Promote Map Accuracy and Outreach, but Opportunities Exist to Address Implementation Challenges.* [GAO-11-17](#). Washington, D.C.: December 2, 2010.

*National Flood Insurance Program: Continued Actions Needed to Address Financial and Operational Issues.* [GAO-10-1063T](#). Washington, D.C.: September 22, 2010.

*National Flood Insurance Program: Continued Actions Needed to Address Financial and Operational Issues.* [GAO-10-631T](#). Washington, D.C.: April 21, 2010.

*Financial Management: Improvements Needed in National Flood Insurance Program's Financial Controls and Oversight.* [GAO-10-66](#). Washington, D.C.: December 22, 2009.

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

*Information on Proposed Changes to the National Flood Insurance Program.* [GAO-09-420R](#). Washington, D.C.: February 27, 2009.

*High-Risk Series: An Update.* [GAO-09-271](#). Washington, D.C.: January 2009.

*Flood Insurance: Options for Addressing the Financial Impact of Subsidized Premium Rates on the National Flood Insurance Program.* [GAO-09-20](#). Washington, D.C.: November 14, 2008.

*Flood Insurance: FEMA's Rate-Setting Process Warrants Attention.* [GAO-09-12](#). Washington, D.C.: October 31, 2008.

*National Flood Insurance Program: Financial Challenges Underscore Need for Improved Oversight of Mitigation Programs and Key Contracts.* [GAO-08-437](#). Washington, D.C.: June 16, 2008.

*Natural Catastrophe Insurance: Analysis of a Proposed Combined Federal Flood and Wind Insurance Program.* [GAO-08-504](#). Washington, D.C.: April 25, 2008.

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*National Flood Insurance Program: Greater Transparency and Oversight of Wind and Flood Damage Determinations Are Needed.* [GAO-08-28](#). Washington, D.C.: December 28, 2007.

*National Disasters: Public Policy Options for Changing the Federal Role in Natural Catastrophe Insurance.* [GAO-08-7](#). Washington, D.C.: November 26, 2007.

*Federal Emergency Management Agency: Ongoing Challenges Facing the National Flood Insurance Program.* [GAO-08-118T](#). Washington, D.C.: October 2, 2007.

*National Flood Insurance Program: FEMA's Management and Oversight of Payments for Insurance Company Services Should Be Improved.* [GAO-07-1078](#). Washington, D.C.: September 5, 2007.

*National Flood Insurance Program: Preliminary Views on FEMA's Ability to Ensure Accurate Payments on Hurricane-Damaged Properties.* [GAO-07-991T](#). Washington, D.C.: June 12, 2007.

*Coastal Barrier Resources System: Status of Development That Has Occurred and Financial Assistance Provided by Federal Agencies.* [GAO-07-356](#). Washington, D.C.: March 19, 2007.

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