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Senate Banking & Insurance and Senate Environmental Resources & Energy Committees

Joint Public Hearing on Flood Insurance

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**Respectfully submitted by:
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Honorable Chairs of the Banking & Insurance and Environmental Resources & Energy Committees, committee members and guests, thank you for the opportunity to talk with you today regarding the National Flood Insurance Program (NFIP), the basics of our industry's involvement in the administration of the program, and some of the recent challenges being faced as a result of the passage of the Biggert-Waters Flood Insurance Reform Act of 2012.

The Property Casualty Insurers Association of America (PCI) is a trade association with more than 1,000 insurance company members nationwide. Our members write more than 40 percent of the auto, home, business and workers compensation insurance in Pennsylvania. PCI members also make up two-thirds of the insurance companies that partner with the federal government through the "Write-Your-Own" (WYO) program to sell, service and settle flood claims.

My name is Don Griffin, I'm vice president of personal lines at PCI and I also chair the insurance industry's "Write-Your-Own" Flood Insurance Coalition since its inception in 2004 that includes the national industry trade associations and independent insurers formed to address NFIP legislation and regulation.

National Flood Insurance Program

The NFIP was created by Congress in 1968 to address the severe flooding in the mid-1960s from several storms and riverine flooding as well as to provide some basic coverage. Private insurers did not, and most still do not, provide coverage for loss due to flooding. The original goals of the program were to: 1) provide some funds coming in (through premiums) to offset post-disaster federal relief dollars going out; 2) encourage communities to prepare and mitigate against flood losses by establishing flood plain development standards; and, 3) make the protection available at a reasonable cost to property owners. At the time, Congress knew they would need to subsidize the risk and costs associated with the program since only those that would need (or later required to buy) the coverage would purchase it.

Following the passage of the law establishing the NFIP, it took the Army Corps of Engineers about six (6) years to map the flood hazards in our country. Properties built in an area prior to the flood map being available or prior to December 31, 1974 were provided with a “subsidy” in the form of a reduced premium. It was believed that these “pre-Flood Insurance Rate Map (pre-FIRM)” properties should not be charged the actual risk-based rates since they did not have the benefit of the map information showing potential flood areas. Also, they believed that, over time, these properties would be destroyed (perhaps by flooding or other perils) or be rebuilt and would then comply with the new requirements for “elevation” above the flood zone. As we all know now, these properties have shown remarkable resiliency.

From 1969 through 1977, the NFIP was underwritten by a consortium of private insurers. The program was under the Department of Housing and Urban Development (HUD) and it is now under the Department of Homeland Security (DHS) and the Federal Emergency Management Agency (FEMA). While part of HUD, the government decided it should take on this program – and the risk, as they thought it would save money. From 1978 through 1983, flood insurance was only available directly through the NFIP. In 1984, following one of the many program reauthorizing laws over the years, the “Write-Your-Own” program was established. This program was designed to: 1) increase the number of people purchasing this needed protection; and, 2) use the insurance industry infrastructure (agents, companies, adjusters) to help sell, service and settle claims. That program still exists today. Please keep in mind that WYO insurers DO NOT: 1) set the rates; 2) establish the rules or limits; 3) bear the risk of loss; or 4) establish the rules with regard to settling a claim. Also, it is important to note that since this is a federal program, the states have no regulatory jurisdiction over the program.

There are about 85 active insurance company WYO partners with the NFIP yet there are about 1,500 insurers writing property coverage throughout the US. While the WYO number was higher at one time (above 120), many of these insurers consolidated or decided for various cost and reputational issues to no longer participate as a WYO. Two household names that recently made that decision are State Farm and Travelers.

The NFIP is currently \$24 billion in debt to US taxpayers and even with the reforms included in the Biggert-Waters Act, it will be decades, if ever, before that debt is repaid. Most of this debt comes from significant losses in 2004 and 2005, but early in 2013, the program had to have its “borrowing authority” raised by Congress to just over \$30 billion so it could afford to pay the more than \$6 billion in losses from “Superstorm” Sandy. The program was up for reauthorization in 2008, but due to the approximately \$18 billion in debt at that time and mapping issues, it took more than 12 short-term extensions and almost four (4) years to get agreement in Congress on a “regular” five-year reauthorization and the other meaningful reforms that were part of the Biggert-Waters Act when it passed and was signed into law on July 6, 2012.

Biggert-Waters Act

Biggert-Waters included numerous reforms that are designed to put the program on a sound financial footing for the future. These included: 1) a “glide-path” (with a maximum 25 percent increase per year – referred to as Section 205); 2) elimination of the subsidies for certain “pre-FIRM” properties, a “glide-path” (with a 20 percent per year for five years increase to get to the “actuarial rate) for properties newly mapped into a flood zone or now in a flood zone due to a revised map – referred to as Section 207); 3) establishment of a reserve fund (eventually, it must be equal to 1 percent of the total exposure in the program); 4) an increase in the maximum annual rate change from 10 to 20 percent for all properties; and, 5) the ability to purchase reinsurance and encourage private sector participation in the program – among many other provisions.

The elimination of the pre-FIRM subsidies (Section 205) are what many of you have heard about from your constituents or may have experienced. These changes started last January for non-primary residential structures. These property owners started seeing the 25 percent annual increase that will continue until the “NFIP actuarial” rate is reached. The next set of changes started October 1, 2013. These included 25 percent annual increases for non-residential (business) properties, severe repetitive loss properties, and properties where the claims paid exceed the market value of the property. Also included as part of the October changes is a provision that completely and immediately eliminates the subsidy for pre-FIRM properties where the ownership changed (since July 6, 2012) or if the policy has

lapsed. It is this category of premium changes that has caused the most “uproar” at the state and federal levels and presented significant challenges for property owners and potential property owners (particularly with regard to affordability) as well as impacting real estate transactions.

The “real-life” implications are huge! For example, we have seen annual premiums go up tens of thousands of dollars (one as high as \$84,000 - for \$250,000 of building and \$100,000 of contents coverage) for pre-FIRM properties where the ownership has changed or the policy has lapsed.

Rate changes as the result of new or revised maps (Section 207) were set to be effective later this year (October 1, 2014); however, included in the recently passed appropriations legislation was a provision that prohibits the NFIP from using any funds to implement the provisions of this section in this fiscal year (that ends September 30, 2014). Therefore, we know that this change will be delayed, despite the fact that we believe that the NFIP has done the bulk of the work on these changes already.

What’s Going to Happen?

The Senate is set to consider a bill (S. 1846 or S. 1926 – both called “The “Homeowner Flood Insurance Affordability Act”) sometime this week (January 27) that would delay or retroactively revise the implementation of Sections 205 and 207 – at least until an “affordability study” can be done and an “affordability framework” to address the issues completed. The bill provides that the NFIP has roughly until the expiration of the current reauthorization (September 30, 2017) to complete this work – essentially eliminating the increases for many of these properties. While well-intentioned, if not carefully constructed, the new legislation could create more unintended consequences even as it seeks to address some of the unintended consequences as a result of the implementation of the Biggert-Waters Act.

Once legislation passes the Senate, then the House will be under pressure to take action as well. However, the chair of the House Financial Services Committee (with jurisdiction over flood legislation) and many others in the House, do not want to see wide-

spread delays in the provisions associated with the Biggert-Waters Act; but rather support a “targeted” approach to making changes.

PCI and the WYO Flood Insurance Coalition support making changes to address those most hard hit (where the premium has increased more than 25 percent) due to implementation of the legislation. We support putting ALL properties on the 25 percent “glide-path”. It is also VERY important to note that, even if Congress were to enact legislation by February 1, it would likely be at least August 1 or September 1 before consumers would see the changes reflected in their flood policy premium bill. These issues need to be addressed in any legislation passed by Congress – to avoid even more marketplace problems for constituents, policyholders, state and federal lawmakers and insurers.

These are difficult problems with no “easy” solutions, but we believe that specific changes can be made that will, eventually, address the key problems without putting property ownership, the future of the program and taxpayers at risk.

Again, thank you for holding this hearing, your time and interest in this important issue and I'd be happy to answer any questions you may have.