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Flood Insurance Affordability-Update

ASFPM Recommendations to address the impact of NFIP Reform 2012 (BW-12)

ASFPM supports many of the provisions of the 2012 NFIP Reform bill, otherwise known as Biggert-Waters 2012, or shortened to BW-12. A centerpiece of this reform bill was to make the NFIP more financially sound. At the time the bill passed (May 2012) and was signed (July 6, 2012), the NFIP was over \$17 billion in debt to the US Treasury (taxpayer), with little chance the program could ever repay that debt. The NFIP is now over \$25 billion in debt to the US Treasury. As such, Congress looked closely at why the program was in debt and what could be changed to improve its financial solvency. The changes include many provisions for increases in flood insurance premiums to move them toward full risk rates and other measures to improve the financial soundness of the NFIP. If we hope to have the NFIP available, fiscal soundness will be critical.

It is important to understand the background and facts about the current NFIP in order to have context for those changes in the 2012 NFIP Reform bill (BW-12):

- About 19% of the current NFIP policies are Pre-FIRM structures which receive discounted (subsidized) rates and they pay about 40 to 45% of full risk rates. Currently, of the 5.6 million NFIP policies, there are a total of 1,082,201 (19.3%) policies that are Pre-FIRM discounted policies, and of that group, roughly 578,000 are primary residential structures.
- Structures that were grandfathered at the discounted rates included both those that were built before the community Flood Insurance Rate Map was effective (pre-FIRM), and those that are now in the SFHA (Special Flood Hazard Area) due to updated maps that better reflect the changing risk.

To address fiscal soundness of the NFIP, Congress made the following insurance changes in BW-12:

- Section 205 phases out many policy discounts for Pre-FIRM structures, either immediately or incrementally. Discounted Pre-FIRM policies losing their discount include non-primary residences (e.g., second homes), severe repetitive loss properties, business properties, and homes which have had substantial damage or improvements. About 400,000 non-primary homes will move toward actuarial rates with a permissible increase of 25% per year or until full-risk rates are achieved. In addition, pre-FIRM properties that on or after July 6, 2012 have a new policy written on them or are newly purchased or had a policy and it lapsed and a new one is written, will be written at full-risk rates.
- Section 207 calls for eliminating grandfathering and replacing it with a 20% increases for 5 years starting in October 2014. FEMA has not yet been determined how or if it can implement this provision.

What the legislation did not address is the affordability of flood insurance policies for those that truly cannot afford the increases. While there was a study included in BW-12 to examine affordability issues; it had no pilot or implementation mechanism. There are now a number of bills being proposed that would roll back the premiums or delay the start of moving to full risk premium rates. This paper discusses BW-12, the need for a financially sound NFIP, and the options to address the affordability issue, especially for people who truly may not be able to afford the premium rate increases and may need time to adjust to the premium increases.

ASFPM suggests 9 principles related to flood insurance affordability

Just like solutions to complex flood problems, the solution to the affordability issue must be met through multiple approaches. While the subset of those policies most affected by premium increases is a minority of the entire policy

base, (19.3% of policies are subsidized), the impact of the increases can be significant to those affected. The following principles have been identified by ASFPM as those which would improve financial stability while also addressing affordability issues as BW-12 is implemented:

- 1. The policy holders impacted by major disasters should not be treated differently with respect to premiums than those in flood hazard areas in the rest of the nation.** In fact, because of post-disaster mitigation programs and other assistance, those in recent Presidentially-declared disaster areas will have more opportunities for financial and technical assistance to mitigate their structures to reduce future flood insurance rate increases.
- 2. Flood insurance premiums must move toward full-risk rates in order to show property owners the true flood risk they face (so they can make informed decisions) and to put the NFIP on sound financial footing.** The issue is how much and how fast. BW-12 sets a 4-5 year schedule to move various classes of policies to full-risk rates. This “glide path” to full-risk rates could be evaluated by Congress, and could be lengthened to allow more time for property owners to mitigate properties to reduce the premiums and allow FEMA to implement pilot affordability actions. Also, while BW-12 purported to shield primary residences from the impacts of the discount reduction, some provisions will actually have a significant impact on primary residences. The most dramatic of those provisions is the movement to actuarial rates on the sale or transfers of pre-FIRM properties. This provision should be fully evaluated to see if it needs to be modified.
- 3. Not all existing property owners with discounted rates will be able to afford full actuarial rates, so some means tested program to assist in transitioning them to either full-risk rates or better yet, to help them mitigate their structure, will be necessary or some people may be priced out of their home.** Such programs could include a system whereby assistance is provided to pay for some of the increase in flood insurance premiums. This could be a sliding scale which can range from picking up all or most of the premium increase to picking up none of the increase, based on income status. Such a flood insurance voucher program could function similar to the HUD Section 8 Housing Choice vouchers, which are administered by public housing agencies that collect information on income and assets to determine eligibility and voucher amounts. This collected data would be used to assess need, determine eligibility, and provide appropriate amounts of financial assistance to families who could not otherwise afford their flood insurance premiums. This must progress with the property owner seeing the full risk flood insurance rate so they are made aware of their flood risk and the full risk rate, and then the voucher is applied.
- 4. The voucher assistance should be used in combination with low interest loans or grants to achieve mitigation whenever possible.** When it is determined that a property owner needs assistance with the flood insurance premium, that property owner should be offered a low interest loan to mitigate the building through elevation or other means (must be cost effective). Once the structure is mitigated, the flood insurance premium is likely to be decreased significantly so the voucher assistance can be used to cover a portion of the much lower insurance premium and the costs of the loan. One could consider requiring the property owner to mitigate their building as a condition for receiving a voucher. The savings and reduced suffering to both the homeowner and the Federal government in relation to a non-mitigated home can be significant. In many cases the voucher will only be used to cover the loan cost. In this case after the loan is paid off, the subsidy would no longer be necessary. This concept and how it would be applied to specific property owners and structures is spelled out in [this paper](#) from Kousky and Kunreuther.
- 5. Loans to help mitigate structures make people safer and reduce premiums.** A potential option to assist homeowners perform mitigation is a variation of a housing repair loan program now used by some states in administering their HUD CDBG funds. The current revolving loan funds (RLFs) are used for activities such as plumbing, weatherization, electrical, roofing, and lead paint mitigation. Given the flexibility afforded by the Housing and Community Development (HCD) Act of 1974 and provided that the state’s Consolidated and Annual Plans are revised to include flood hazard mitigation, it should be possible to adapt this program to assist with flood insurance affordability for lower income individuals by using the loan to mitigate the structure. A significant advantage to this

approach is the loan does not need to be paid back until the home is sold in the future. Since the mitigated home will retain good assessed value, the community will not lose tax base and the property owner retains full equity. Another mitigation option would to offer pre-disaster mitigation loans through the U.S. Small Business Administration (SBA). In 1999, Congress authorized a 5-year pilot program to implement the Pre-Disaster Mitigation Loan Program. The statute allowed SBA to make low interest, fixed rate loans to small businesses for the purpose of implementing mitigation measures to protect their property from disaster related damage. However, the demand for these loans was poor during the timeframe of the pilot and the program was discontinued. However, with BW-12 being implemented, many property owners and businesses that face increased flood insurance premiums now recognize the return on investment that mitigation will provide. These loans could address the need for mitigation to counteract the premium increases from the sale of property or map changes that are part of the BW 12.

- 6. Flood insurance rating should be reevaluated by FEMA and refined to better reflect both risk and recognize partial mitigation if such mitigation is found to be effective.** In the early days of the NFIP, more variation in flood insurance rating was used, but given certain concerns from the insurance side, the rates were consolidated. Given today's computerized environment and available flood risk data, consideration should be given to reinstating variable risk factors or similar refinements. For example, a recently released report by the National Academies of Sciences recommends refined rating zones in areas protected by levees based on actual calculated risk.

Another rating issue is the concept of credit for mitigation measures that do not achieve full building compliance. FEMA should analyze its claims data to determine if there can be recognition of partial mitigation measures to reduce premiums, especially for pre-FIRM structures. Measures might include elevation or relocation of utilities and other mitigation options if they truly reduce NFIP claims.

- 7. Develop innovative and new flood insurance approaches, such as community-based insurance and long-term policies that stay with a structure and can assist in financing mitigation.** The benefit of a community-based policy is that the local unit of government, flood district, or levee district provides flood insurance for all properties at risk and can decide how the premium is paid. An approach would be to assess all properties benefitting from the insurance and/or from community mitigation measures. Since the rating would be on a community basis as opposed to the current parcel basis, there is more equity in future rate increases or decreases because it is usually the community, not the property owner, that makes future development or neighborhood type decisions that either increase or decrease risk in the community. This approach ties in well with the Community Rating System to provide premium discounts for communities that are reducing their flood risk. Long term policies would stay with the property, not the owner, so that the flood policy does not get dropped, leaving the property owner with only limited taxpayer disaster relief when trying to recover, and leaving the community less resilient because its residents are unable to recover after the event.

- 8. Fully utilize and refine existing hazard mitigation programs to address flood insurance affordability.** There are several existing hazard mitigation programs that can be brought to bear on the flood insurance affordability issue:
- The Hazard Mitigation Grant Program (HMGP) from FEMA, is a post disaster grant program to assist mitigating damaged structures after a federally declared disaster and widely used to mitigate at-risk structures against flooding;
 - FEMA's Flood Mitigation Assistance (FMA) programs can be used pre-disaster to mitigate structures, especially those with repetitive losses;
 - Pre-Disaster Mitigation (PDM) grant programs provide grant funds to mitigate existing at-risk buildings and develop community mitigation plans before the disaster occurs. In states that have not experienced a disaster, but where thousands of property owners will experience increased premiums, this program will be especially key to addressing the affordability issue;
 - Increased Cost of Compliance (ICC) is part of the flood insurance policy that provides mitigation funds directly to property owners after a damaging triggering event provided they have a NFIP policy. ICC can be used to match federal mitigation funds;

- The Community Rating System (CRS) provides community-wide (all policyholders in the community in the SFHA or standard-rated Zone X policies) discounts on flood insurance premiums for measures the community takes that go beyond minimum standards for construction, as well as other actions that will reduce future flooding and claims; and
- The Community Assistance Program (CAP-SSSE) provides technical assistance and training to communities participating in the NFIP. In the post BW-12 environment, floodplain managers must be educated and knowledgeable about all many mitigation options that get credit in CRS, as well as ensure that local regulations are administered and enforced – otherwise significant flood insurance premiums can result.

All of these and other programs need to be adjusted to efficiently address affordability issues. For example, FEMA mitigation grant programs must more quickly get funds to property owners and adjustments to the ICC program need to be implemented as required in 2004 to be triggered when an offer of mitigation is made as well as exploring raising limits. Unnecessary hurdles to CRS participation need to be removed and flood insurance affordability must be incorporated into long term community recovery.

All of these programs need to be fully resourced and funded. Adequate resources need to be provided to address increased interest that will be driven by higher insurance rates (e.g., CRS program application assistance, pre-disaster mitigation grants program funding). Technical assistance programs such as CAP and others (even from outside of FEMA like the HUD Community Development Block Grants for Disaster Recovery [CDBG-DR], SBA loans and Corps of Engineers Silver Jackets, Floodplain Management Services and Planning Assistance to States programs) will become more important as property owners and communities seek solutions and technical advice on measures to explore, evaluate and implement options to reduce flood risk and insurance costs.

For example, PAS and FPMS can support local efforts to evaluate flood risk and identify measures to reduce risk without requiring a federally-approved flood control project. Similarly, Silver Jackets teams are currently operating in more than 30 states to leverage expertise across all relevant federal and state agencies to address flood challenges at the river basin or watershed levels. Lastly, the HUD CDBG-DR program helps communities working to recover from a disaster with support for activities that help address the needs of low-income families that are disproportionately affected by natural hazards, including flood, but can least afford to be uninsured.

9. Evaluate and implement changes in the tax code to incent mitigation.

Current tax code provisions provide tax breaks for uninsured losses, and there are considerations to provide credits for flood insurance premium increases. Both of these send precisely the wrong message and take away the motivation for individuals to take responsibility for their actions. A much better use of the tax code would be to provide tax credits or other incentives for actually mitigating at risk structures. Such a program could be modeled after those used for energy efficiency and/or special provisions made to write off the cost of mitigation measures for disaster affected property owners. One option being considered in Congress is to allow property owners to set aside up to \$5,000/year into a tax free disaster savings account that could only be used for mitigating their structure. Tax breaks for real estate taxes can also be given by local governments to those who mitigate—this has been done in some communities.

For more information, please visit ASFPM at <http://www.floods.org>, or contact ASFPM Executive Director Chad Berginnis cberginnis@floods.org. The Association of State Floodplain Managers is a non-profit organization of professionals involved in floodplain and flood risk management, flood hazard mitigation, the National Flood Insurance Program, and flood preparedness, warning and recovery.