

United States House of Representatives
Committee on Financial Services
2129 Rayburn House Office Building
Washington, D.C. 20515

May 20, 2022

Memorandum

To: Members, Committee on Financial Services
From: FSC Majority Staff
Subject: May 25, 2022, Subcommittee on Housing, Community Development, and Insurance Hearing entitled, “Reauthorization and Reform of the National Flood Insurance Program”

The Subcommittee on Housing, Community Development, and Insurance will hold a hearing entitled, “Reauthorization and Reform of the National Flood Insurance Program” on Wednesday, May 25th at 12:00 p.m. in room 2128 of the Rayburn House Office Building and on the Cisco Webex platform. There will be one panel with the following witnesses:

- **Carolyn Kousky**, Executive Director, Wharton Risk Center
- **Karen McHugh**, Missouri State NFIP Coordinator
- **Ariel Rivera-Miranda**, Founder and Agency Principal, Deer Insurance
- **Roy Wright**, President & CEO, Insurance Institute for Business and Home Safety
- **Franklin W. Nutter**, President, Reinsurance Association of America

Background

Prior to 1950, flood insurance was a peril often included in standard homeowners’ insurance policies. However, in response to increasing frequency and severity in flood-related losses in the 1950s, insurance companies began excluding flood insurance coverage and selling it separately. By the 1960s, widespread flooding along the Mississippi River caused most private insurers to flee the business of flood insurance altogether, leaving many homeowners vulnerable with virtually no access to private flood insurance.¹ The lack of availability of flood insurance also left the public vulnerable to bearing the costs of flood damage through post-disaster relief funding.

In direct response to this private market failure, the National Flood Insurance Program (NFIP) was created in 1968 with the passage of the National Flood Insurance Act (NFIA). In doing so, Congress determined that “as a matter of national policy, a reasonable method of sharing the risk of flood losses is through a program of flood insurance which can complement and encourage preventive and protective measures”² and that transferring the costs of private property flood losses from the general taxpayer to individuals in the floodplains through premiums would ease the strain on the nation’s limited disaster resources. Congress also passed the Flood Disaster Protection Act of 1973 (FDPA) that requires most property owners in a designated Special Flood Hazard Area to purchase flood insurance.³

The last long-term reauthorization of the NFIP occurred when Congress passed the Biggert-Waters Flood Insurance Reform Act of 2012 (BW-12), which was subsequently amended by the Homeowner Flood Insurance Affordability Act of 2014 (HFIAA). Since the end of fiscal year (FY) 2017, the NFIP has

¹ See Testimony of Teresa D. Miller, Commissioner, Pennsylvania Insurance Department, [House Financial Services Committee hearing entitled, “How to Create a More Robust and Private Flood Insurance Marketplace”](#) (Jan. 13, 2016).

² 42 U.S.C. §4001(a).

³ For example, the mandatory purchase requirement only extends to the structure, although policyholders can purchase contents coverage if they choose. The requirement also only reaches those with a federally backed mortgage, so property owners who have paid off their mortgage or who have obtained a mortgage without federal backing are not affected.

had 19 short-term reauthorizations and has even experienced brief lapses. According to the National Association of Realtors, an estimated 40,000 home sales are lost or interrupted every month that the NFIP's authority lapses. The NFIP's authorization is currently set to expire on September 30, 2022. In the event of a lapse, the NFIP will be unable to enter into new flood insurance contracts, which will lead to widespread market instability due to the stalling of mortgage processing for homes that are statutorily required to have flood insurance.

Overview of the NFIP

Today, the NFIP is the principal provider of primary flood insurance in the U.S., covering nearly 5 million households and businesses across the country for a total of over \$1.3 trillion in flood insurance coverage.⁴ As of the end of May 2022, 22,563 communities participate in the NFIP, covering an estimated 93 percent of the U.S. population.⁵ The NFIP is administered by the Federal Emergency Management Agency (FEMA) through its Federal Insurance & Mitigation Administration (FIMA). The NFIP was designed to serve two interrelated goals: (1) provide access to primary flood insurance and (2) reduce flood risk through the adoption of floodplain management standards.⁶ The NFIP advances these goals by offering primary flood insurance exclusively for properties in communities that adopt minimum floodplain management standards under FEMA regulations.⁷ The NFIP also administers the Community Rating System (CRS), which is a voluntary incentive program that recognizes communities for implementing floodplain management practices that exceed the NFIP's minimum requirements and, in exchange, FIMA offers reduced flood insurance premiums to policyholders.

In 1983, FEMA created the Write Your Own (WYO) Program in an effort to: increase the NFIP's policy base and geographic distribution of policies; improve service to NFIP policyholders through infusion of insurance industry knowledge and capacity; and, provide the insurance industry with direct operating experience with flood insurance.⁸ The WYO Program operates as a partnership between FEMA and participating property and casualty insurance companies – known as WYOs – that are compensated to write and service NFIP policies. The property and casualty insurance companies that operate as WYOs assume none of the risk by participating in this program. FEMA retains all of the insurance risk and underwrites any losses. Currently, approximately 60 different companies administer about 87 percent of NFIP policies through the WYO Program.⁹ The remainder of NFIP's policies are provided through the Direct Program, which is operated by a government contractor and performs the same basic functions as a WYO company.

The NFIP offers a Standard Flood Insurance Policy (SFIP) for properties in participating communities within a Special Flood Hazard Area (SFHA).¹⁰ By virtue of the mandatory purchase requirement, most property owners within the SFHA are required to purchase flood insurance. Many of the SFIP's policy terms are set in statute.¹¹ The maximum coverage amount for building coverage is \$250,000 for single-family homes, and \$500,000 for multi-family residential properties, and non-residential properties including commercial properties.¹² The maximum coverage amount for contents only is \$100,000.¹³ If the SFIP's maximum coverage amounts are insufficient to cover the full value of

⁴ FEMA, [The Watermark: FY2022, First Quarter, Volume 17](#) (2022).

⁵ *Id.*

⁶ 42 U.S.C. §4001 et seq.

⁷ *Id.*

⁸ GAO, [Flood Insurance: Opportunities Exist to Improve Oversight of the WYO Program](#) (Aug. 2009).

⁹ Insurance Information Institute, [Facts and Statistics, Flood Insurance](#) (accessed May 20, 2022); See also FEMA, [Write Your Own Flood Insurance Company List](#) (accessed May 20, 2022).

¹⁰ FEMA, [National Flood Insurance Program Dwelling Form, Standard Flood Insurance Policy](#) (Oct. 2015).

¹¹ CRS, [Introduction to the National Flood Insurance Program](#) (Nov. 19, 2021).

¹² *Id.*

¹³ FEMA, [Flood Insurance Manual](#) (Oct. 1, 2021).

the property, policyholders have the option of obtaining excess flood insurance in the private market if such coverage is available. People living in SFHAs can also satisfy the mandatory purchase requirement by purchasing private insurance.¹⁴ In response to concerns that there was ambiguity as to which private policies would meet the mandatory purchase requirement, multiple agencies issued joint guidance in 2019 to provide some clarity.¹⁵

The NFIP's Financial Status

The NFIP is generally self-funded through annual insurance premiums collected from policy holders. The national average for premiums paid by all NFIP policyholders is \$818.70 per year.¹⁶ Policyholders also pay surcharges and other fees, including an annual surcharge, which is paid at the time of application or renewal.¹⁷ Congress mandated this surcharge through the HFIAA to support the financial stability of the NFIP. Policyholders may also have to pay another surcharge if they live in a community that the NFIP has placed on probation for failing to meet NFIP's floodplain management requirements.¹⁸ In FY 2018, policyholders paid \$382 million in surcharges, \$188.162 million in federal policy fees, and \$496.82 million in reserve fund assessments.¹⁹ A portion of these premiums, fees, surcharges, and assessments goes towards the cost of flood mapping and floodplain management. A large portion also goes to paying interest on debt of the NFIP.

Congress designed the NFIP as a program that would operate on a cash flow basis, borrowing from the Treasury in bad years and returning funds to the Treasury in good years. The NFIP was largely self-supporting in this way from 1986 until 2005. Due to extraordinary losses incurred as a result of hurricanes Katrina, Rita, and Wilma in 2005, and then Superstorm Sandy in 2012 and Hurricanes Harvey, Irma, and Maria in 2017, the program currently carries a debt of \$20.5 billion.²⁰ It is also important to note that a significant portion of the NFIP's debt accrued as a result of Hurricane Katrina (\$19 billion) could not possibly have been properly accounted for in NFIP's risk modeling; specifically, the U.S. Army Corp of Engineers took responsibility for the engineering and design failures in the levees that should have been able to provide better protection for New Orleans in the face of Katrina.²¹

The public is not responsible for paying off this debt; instead, policyholders pay off the debt through growing premiums and fees. The NFIP must pay millions of dollars just in interest payments to the Department of the Treasury every year (currently approximately \$400 million annually or a total of \$5.5 billion since 2005) at the expense of policyholders. In 2017, following a proposal submitted by OMB Director Mick Mulvaney, Congress passed legislation to partially forgive \$16 billion of the NFIP's debt of \$30.4 billion, after the NFIP's debt ballooned following Hurricanes Harvey, Irma and Maria and other historic flooding that year.²² House Financial Services Committee Chairwoman Maxine Waters has led legislation to fully forgive this debt.

¹⁴ Wharton Risk Management and Decision Process Center, University of Pennsylvania, [The Mandatory Purchase Requirement: Origins and Effectiveness in Achieving NFIP Goals](#) (Sept. 2019).

¹⁵ CRS, [Private Flood Insurance and the National Flood Insurance Program](#) (Dec. 21, 2021).

¹⁶ CRS, [National Flood Insurance Program: The Current Rating Structure and Risk Rating 2.0](#) (April 4, 2022).

¹⁷ The amount of the surcharge is determined based on the use of the building. Policyholders who are renters and owners of primary residences are charged \$25 per year, while owners of non-primary residences and non-residential buildings are charged \$250 per year. FEMA, [Flood Insurance Rules and Legislation](#) (May 27, 2021).

¹⁸ When a community has been placed on probation, policyholders must pay an additional \$50 probation surcharge for a year. CRS, [National Flood Insurance Program: The Current Rating Structure and Risk Rating 2.0](#) (April 4, 2022).

¹⁹ FEMA [The Watermark, FY18 Volume 4](#) (2018).

²⁰ *Id.*

²¹ CBS News, [Katrina Report Blames Levees](#), (June 2006).

²² [Letter from the Office of Management and Budget Director Mulvaney](#) (Oct. 4, 2017).

Affordability and Racial Equity Challenges

In 2018, FEMA submitted its congressionally mandated Affordability Framework demonstrating, among other things, that low-income homeowners and renters face significant affordability challenges.²³ The report documents that those who are least able to afford higher premiums tend to live in the highest flood hazard areas writing, “generally, incomes are higher outside the SFHA than they are inside the SFHA. The median household income for residential policyholders is \$82,000, although it is substantially lower in the SFHA than outside the SFHA.”²⁴ Further, FEMA found that “the combination of higher premiums and lower incomes in the SFHA creates affordability pressure on households.”²⁵

Affordability pressures can be greater for communities and homeowners of color. Despite facing higher flood risks, communities of color are often located outside of the SFHA and homeowners of color are more likely to go uninsured, leaving many with few resources to turn to for disaster recovery assistance.²⁶ Evidence also shows that even when homeowners in communities of color have flood insurance through the NFIP, they experience a higher rate of unpaid claims and a lower rate of claims filed in some communities of color located within flood zones.²⁷ Racial disparities in flood insurance coverage are further compounded as communities and homeowners of color also receive less federal disaster recovery assistance compared to white homeowners for the same level of damage.²⁸

Mitigation Investments

On November 15, 2021, President Biden signed the Infrastructure Investment and Jobs Act, which included \$3.5 billion for flood mitigation and \$500 million in grants to states for revolving loans for hazard mitigation through a new program called the Safeguarding Tomorrow through Ongoing Risk Mitigation (STORM) Act.²⁹ On November 19, 2021, the House passed the Build Back Better Act, which includes provisions to forgive the NFIP’s \$20.5 billion in debt and invests \$600 million in setting up an affordability program for low-income policyholders, as well as \$600 million toward updating flood maps.³⁰ According to FEMA, the NFIP saves the nation an estimated \$1.87 billion annually in flood losses avoided because of the NFIP’s building and floodplain management regulations.³¹

Risk Rating 2.0

Until 2021, FEMA had not updated its methodology for setting NFIP premium rates since the 1970s, when it adopted a risk rating method that accounts only for the 1% annual chance of fluvial and coastal flooding.³² In coordination with the US Army Corps of Engineers, US Geological Survey, and other experts, FEMA has now developed a new risk rating methodology, known as Risk Rating 2.0 (RR2). RR2 went into effect for new policyholders on October 1, 2021, and for new policyholders on April 1, 2022.³³ RR2 is designed to more accurately “reflect an individual property’s risk, reflect more types of flood risk in rates, use the latest actuarial practices to set risk-based rates, provide rates that are easier to understand for agents and policyholders, and reduce complexity for agents to generate a flood insurance quote.”³⁴ Under RR2, FEMA will continue to comply with statutory restrictions on annual premium

²³ Department of Homeland Security, [An Affordability Framework for the National Flood Insurance Program](#) (April 17, 2018).

²⁴ *Id.*

²⁵ *Id.*

²⁶ RisQ, Inc. [Economic and Racial Inequality in FEMA SFHA Flood Zone Designations](#) (Jul. 20, 2021).

²⁷ Urban Institute, [Federal Disaster Policy Reforms—Including Flood Insurance Treatment—Should Center Racial and Economic Equity](#) (Sept. 30, 2020).

²⁸ New York Times, [Why Does Disaster Aid Often Favor White People?](#) (Jun. 7, 2021).

²⁹ FEMA, [Infrastructure Deal Provides FEMA Billions for Community Mitigation Investments](#), (Nov. 15, 2021).

³⁰ House Committee on Financial Services Committee, [Summary of Title IV](#) (Nov. 2021).

³¹ CRS, [Introduction to the National Flood Insurance Program](#) (Nov. 19, 2021).

³² CRS, [National Flood Insurance Program: The Current Rating Structure and Risk Rating 2.0](#) (April 4, 2022).

³³ FEMA, [Risk Rating 2.0: Equity in Action](#) (April 2021).

³⁴ CRS, [National Flood Insurance Program: The Current Rating Structure and Risk Rating 2.0](#) (April 4, 2022).

increases, which are limited to 18% for primary residences.³⁵ FEMA estimates that RR2 will result in monthly premium increases of between \$0-10 for 66% of policyholders, while 23% of policyholders are expected to see substantial savings from RR2, an average of \$86 per month.³⁶

As full risk-based premiums are phased in under RR2, some policyholders could be faced with large price increases either because they are currently buying coverage at subsidized rates and/or because the new rating system indicates that they now have a higher risk.³⁷ The introduction of a means-tested NFIP affordability program has been under consideration by Congress for years. However, FEMA does not currently have the authority to implement an affordability program, nor does the NFIP's current rate structure provide the funding required to support one.³⁸ If an affordability program were to be funded from NFIP funds, this would require either raising flood insurance rates for NFIP policyholders or diverting resources from another existing use. Alternatively, an affordability program could be funded fully or partially by congressional appropriations.³⁹

Legislation

- **H.R. _____, “The National Flood Insurance Program Authorization Act of 2022,” (Waters)** is a discussion draft that would reauthorize the NFIP through September 30, 2027 and make additional reforms intended to strengthen the NFIP in the long term, including the establishment of a pilot program to assist policyholders with affordability, a section making improvements to the Community Rating System (CRS) by requiring that credits be issued to the maximum number of communities practicable, a section authorizing a community assistance program for floodplain management, as well as other reforms.
- **H.R. 7482, “The Protecting Families and the Solvency of the National Flood Insurance Program Act of 2022” (Casten)** would authorize FEMA to provide additional mitigation assistance to families affected by flooding, and seek to expedite the buyout process for homeowners in communities facing repetitive losses.
- **H.R. _____, (Velázquez), “The National Flood Insurance Program Administrative Reform Act of 2022,”** is a discussion draft that instructs FEMA to reform its appeals process for policyholders to receive compensation for flood policies after storm damage.
- **H.R. _____, (Waters)** is a discussion draft forgiving the NFIP’s \$20.5 billion in debt.

H.R. _____, is a discussion draft that would institute a 9 percent annual cap on NFIP premium rate increases..

³⁵ FEMA, [Risk Rating 2.0: Equity in Action](#), (April 2021).

³⁶ FEMA, [Risk Rating 2.0 National Analysis](#), (2021).

³⁷ Congressional Research Service, [Options for Making the National Flood Insurance Program More Affordable](#), (Dec. 21, 2021).

³⁸ *Id.*

³⁹ *Id.*