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Morris & Reynolds Insurance Presents: **December 2013**

New Law To Raise Flood Insurance Rates Dramatically

Biggert—Waters Flood Insurance Reform Act of 2013 Update

Hurricane Katrina devastated New Orleans. The storm that caused extensive flooding in the Crescent City and along the Gulf Coast has, in the years since, also nearly destroyed the National Flood Insurance Program (NFIP).

Speaking of New Orleans, Congress created the National Flood Insurance Program in 1968 after Hurricane Betsy hit the city, causing over a billion dollars in damage. Prior to that time flood insurance was provided by the private insurance market, but repeated claims along the Mississippi River Valley region, and then finally Betsy, led to private insurers no longer wanting to pay to replace the same structures again and again over time from flood claims.

Flood insurance became impossible to obtain so the federal government created the NFIP to help property owners along our nation's coast. For decades everything worked fine, but in 2005 Hurricanes Katrina then Rita, Wilma and other storms caused the NFIP to go $24 billion into debt. With 5.6 million policyholders depending on the NFIP and natural disaster claims on the rise lawmakers became concerned about the NFIP's sustainability.

In 1968 when the NFIP was created it was conceived as a federal program to share the risk of flooding, nationally, over a large pool of property owners, establish good flood plain management and help communities recover quickly after a flood. Initially, to participate in the NFIP, a community agreed to enact flood mitigation building codes in high risk flood areas in exchange for the availability of flood insurance for buildings in that community, regardless of risk. They established flood insurance rate maps (FIRM) to identify risky areas and buildings and low rates to encourage participation to cover all buildings.

As technology grew and the water drainage patterns of a community changed, flood maps were revised to maintain an accurate picture of flood risks. The NFIP premium rate structure evolved to include, among other criteria:

- What is known as risk-based rates for new construction in high risk flood zones based on an Elevation Certificate.
- Preferred Risk policy rates, lower rates based on their low to moderate flood risk location.
- "Subsidized "premium rates for high risk buildings built before the community enacted those flood mitigation building codes and established flood maps (known as Pre-FIRM rates).
- "Subsidized" premiums for buildings built to comply with flood maps that were subsequently revised including "grandfathered" flood zones or base flood elevations.

Fast forward to 2012, with more than 21,000 participating communities, lending laws requiring flood insurance for high risk properties, and flood maps revised to reflect changing land use and updated mapping technology, as well as a $20 billion dollar debt from Hurricane Katrina, and more recently Superstorm Sandy, along with a "subsidized" rate structure that prevents the NFIP from generating adequate premium to cover future claims.

That's the backdrop for the federal government to dramatically change the availability and cost of flood insurance in America.

First, a Congressional Budget Office study found that current rates were not enough to cover expected costs. Then some stated that subsidizing flood insurance for coastal residents was unfair and called for the government to get out of the business. "*I would say that this is a program that would make Bernie Madoff blush*," announced Michigan Congresswoman Candice Miller, who introduced a bill in 2011 to eliminate the NFIP entirely.

The Biggert-Waters Flood Insurance Reform Act of 2012

The Biggert-Waters Act passed with overwhelming support in Washington. The House passed it 373-52. The Senate 74-19. Initially the law was seen as a compromise to continue the federal program while making changes to return NFIP to financial stability.

As of October 1, 2013, the NFIP began implementing the law by **reducing premium subsidies** including the following **changes related to high risk (A or V zone properties) built before their communities joined the NFIP or 12/31/1974 (pre-FIRM):**

- **Premium subsidies will be phased out for secondary homes, non-residential buildings, severe repetitive loss buildings and severely flood damaged buildings.** For high risk, pre-FIRM flood policies issued prior to July 6, 2012 a 25% increase will apply each year until they reach what are called 'risk-based levels', which won't be known until the owner obtains a new elevation certificate.
- **New policies written between July 6 2012 and October 1, 2013 will be rewritten with risk based rates: Pre-Firm and High Risk policies** will be non-renewed and require a new Application and Elevation Certificate after their first renewal after October 1st, 2013.
- **Policies on primary homes with subsidized rates will see subsidies phased out gradually.** On existing policies for primary, pre-FIRM, high risk homes--subsidies will remain, but renewal premium rates will increase each year (16%-17% this year) until the owner obtains a new elevation certificate so as to determine the new risk-based rate.
- **All new policies must use risk-based rates:** New policies, pre-FIRM, high risk, (including reinstated, lapsed policies) now must use risk-based rates.

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NEW FLOOD INSURANCE LAW RAISES RATES

THE BIGGERT-WATERS FLOOD INSURANCE REFORM ACT OF 2012

(*Continued*)

- **Future NFIP annual rate increases can be raised as much as 20%:** The historic premium cap on average annual premium increases for NFIP policies was raised by the new law to 20% from 10%.

- **Establishes a Reserve Fund to pay claims:** A 5% surcharge of the premium amounts will be assessed on all NFIP policies (except Preferred Risk) to build a Reserve fund for payment of future claims.

- In the future, **additional subsidies will be phased out including those policies grandfathered after map changes, or those granted extended preferred risk rates due to changes in the NFIP flood maps**.

- Also the BW12 Flood Reforms included **plans to establish installment payments, raise lender fines for not covering high risk properties and about a dozen flood risk studies**. However, no implementation plan has yet been established for those sections.

As of this newsletter it is still possible that Congress may amend parts of the BW12 Flood Reform Act and we are still hopeful that provisions that would make these changes more affordable could be enacted. But, pending an Act of Congress, the meaningful reform of the NFIP is now underway.

NFIP FACTS & FIGURES

As you consider how the law impacts you a few facts might be useful, including;

- The National Flood Insurance Program (NFIP) operates under the Federal Emergency Management Association (FEMA). Many well known, private insurers, sell flood insurance under what NFIP calls its "*Write Your Own*" program, but all of the rates, rules and regulations related to primary flood insurance are set by NFIP and claims are, ultimately, paid for by NFIP.

- **NFIP collects over $3.5 billion in annual premiums and FEMA estimates that an additional $1.5 billion annually is needed from subsidized policyholders to break even**.

- FEMA estimates that **20% of its 5.5 million policyholders — about 1.1 million — receive subsidies**.

- **Under Biggert-Waters, about 250,000 policyholders will see immediate increases: business owners, those owning second homes and people with frequently flooded properties, according to FEMA.**

- **An added 578,000 policyholders living in hazardous areas will retain their subsidies until they sell their home or suffer repeated flood losses. The same is true for people in condominiums**.

SUMMARY OF CHANGES

The affected properties are among those built before the community joined the NFIP and adopted its first Flood Insurance Rate Map (FIRM). Communities began joining the NFIP in the late 1960s. To find out when your community joined, contact us. Properties built before that date and not improved since are known for flood purposes as "pre-FIRM."

Many of the "pre-FIRM" properties in high-risk flood areas do not meet current standards for construction and elevation, and they have been receiving subsidized rates that do not reflect their actual risk. The subsidized rates are being eliminated in some cases. Some current policyholders and all future policyholders owning pre-FIRM properties in high-risk areas will pay rates based on their full risk of flood damage. However, most NFIP-insured properties (80% or more) are not affected by the changes.

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