Insurance Regulatory & Transactions | Alert

June 2017

U.S. House Financial Services Committee Holds Hearing on Flood Insurance Reform and Passes Legislation

On June 7, 2017, the U.S. House Financial Services Committee held a hearing entitled "Flood Insurance Reform: A Taxpayer's Perspective." The hearing examined the National Flood Insurance Program (NFIP) and six legislative concepts to reform the program. Witnesses discussed how the reforms would strengthen taxpayer protections; provide greater private market access, competition, and consumer choice; enhance mitigation efforts; encourage flood mapping fairness; address consumer costs and affordability; and incorporate NFIP claims processing reforms.

Following the hearing, the Committee held a two-day markup of legislation to reform the NFIP. The legislation considered by the Committee covers a wide range of issues from mitigation to mapping to private insurer participation. All legislation considered was ultimately passed by the Committee. Four of the seven bills considered by the Committee were passed unanimously. The other three bills passed largely along party lines, with Republicans supporting and Democrats opposing. This *GT Alert* provides a summary of the testimony given at the hearing and the outcome of the Committee votes on the bills to reform the NFIP.

<u>Hearing Witnesses List</u>

- Steve Ellis
  - *Vice President, Taxpayers for Common Sense*
- Caitlin Berni
  - *Vice President, Policy and Communication, Greater New Orleans, Inc.*
- Josh Saks
  - *Legislative Director, National Wildlife Federation*
- Rebecca Kagan Sternhell
  - *Deputy Director and General Counsel, New York City Federal Affairs Office*
- R.J. Lehmann
  - *Senior Fellow, R Street Institute*

Summary of Hearing Witness Testimony

Steve Ellis: Taxpayers for Common Sense (TCS) is a national non-partisan budget watchdog. The organization is allied with SmarterSafer, a coalition in favor of promoting public safety through fiscally sound, environmentally responsible approaches to natural catastrophe policy. For a decade the coalition has advocated reforms in the NFIP that ensure the program is smarter and safer for those in harm's way, the environment, and for federal taxpayers.

Mr. Ellis and TCS believe that NFIP must be significantly reformed to ensure it is financially sustainable, that there are sufficient incentives for reducing future flood damages and vulnerabilities, that it provides better protection for taxpayers who have repeatedly backstopped the program, and that it better protects the environment and promotes the use of nature-based mitigation solutions that have a long term benefit for homeowners and the taxpayers. TCS further believes that rates in the program must, over time, be linked to risk while understanding that there may be some in the program who will need assistance in order to pay higher rates or reduce their risk. To that end, TCS commended the Committee on its legislation that includes provisions to make premium methodology clearer to policyholders, along with providing an explanation of each policyholder's full flood risk and increased public access to historic loss and flood claims information. TCS, however, opposes the artificial rate cap in the legislative proposal. Through private competition, purchase of reinsurance, and a continued move toward risk based rates, TCS argues that NFIP would be able to meet its obligation in a 100-year flood with little Treasury borrowing.

TCS supports the legislative proposals for greater public involvement, the use of risk assessment tools in determining rates, and directing FEMA to work with the Technical Mapping Advisory Council to improve the mapping process. TCS finds merit in the community mapping initiative proposal and believes that it would enable communities to move the mapping process along. However, TCS warns that this will only work if there are sufficient standards and safeguards to ensure the maps are accurate. TCS supports provisions to require an annual independent actuarial review of the NFIP as well as provisions from H.R. 2246, the Taxpayer Exposure Mitigation Act that require FEMA to increase use of risk transfer tools. TCS gave its support to provisions that prospectively restrict access to NFIP for properties with extreme loss profiles.

Caitlin Berni: The Greater New Orleans, Inc. (GNO), is the regional economic development organization for Southeast Louisiana. Since April 2013, GNO, Inc. has led the Coalition for Sustainable Flood Insurance (CSFI), a national coalition of approximately 250 organizations across 35 states, formed during the implementation of the Biggert-Waters Act.

CSFI is concerned that the inclusion of the Repeatedly Flooded Communities Preparation Act will not achieve stronger levels of mitigation, because instead of empowering communities with the mitigation tools they need, the bill threatens to punish communities with sanctions, including suspension from the NFIP. This proposal, which captures all communities with 50 repetitive loss properties or 5 or more severe or extreme repetitive loss properties, combined with the Committee's proposal to lower the threshold for repetitive loss properties to any property with two claims of any amount, will potentially redline coastal communities all across America from participating in the NFIP, according to CSFI. The organization argues that bill does not provide communities with any additional funding for mitigation or support to develop the required mitigation plans. CSFI warns that smaller governments regularly do not have the capacity or technical expertise to develop mitigation plans. CSFI suggests that Congress and FEMA instead focus on providing communities with the tools needed to become more resilient. According to Ms. Berni, Congress should consider requiring FEMA to reallocate the existing surcharges established in HFIAA to better finance the Pre-Disaster Mitigation and the Flood Mitigation Assistance Programs. She believes that this proposal to redirect existing fees would yield approximately $400 million annually for flood mitigation activities.

Ms. Berni provided the Committee with proposals for inclusion in order to fully and meaningfully improve the mapping process. CFSI suggests the Committee increase the authorization of the National Flood Mapping Program, which would help communities better understand and plan for risk. It also asked the Committee to require FEMA to allow communities to adopt portions of a flood map that they agree with at one time while still allowing for map appeals in other areas of the community.

CSFI is concerned that increasing the floor of rate increases from 5 percent to 8 percent will have a detrimental effect on premium affordability. While the bill does propose to lower the overall premium cap from 18 percent to 15 percent, increasing the floor will negatively impact many more policyholders than lowering the ceiling will help, especially when considering that premiums are increasing an average of 6.3 percent this year. CSFI urged Congress not to increase rates during this reauthorization. Instead, CSFI argued that Congress should obtain detailed information on how all changes to costs, both by increases in surcharges and increases in rates, would impact policyholders in different geographic areas and zone classifications. It should also be a goal of the Committee to analyze what impact it would have on the overall program.

As to the Committee's proposal to ease private market entry and increase consumer choice, the organization noted that, while a fuller entry of the private market would bring competition and discipline to the flood insurance market, Congress must be mindful of the risk of cherry-picking. A scenario where the private market comes in and takes all of the low risk properties while leaving the NFIP with nothing but high risk properties will not serve the policyholder or taxpayer well and leaves the NFIP open to needing further loans from the U.S. Treasury. Congress should consider requiring private carriers to assume a certain portion of high-risk properties as well.

Finally, Ms. Berni argued that it is critically important that to reauthorize the NFIP for a multi-year period. Short-term extensions, and especially lapses in authorization, have real world implications. Lapses in authorization stall or kill home closings, according to Ms. Berni.

Josh Saks: The National Wildlife Federation (NWF) is the nation's largest member-based conservation group, representing 6 million members and supporters and affiliate conservation organizations in 51 states and territories. The National Wildlife Federation is also a member of the SmarterSafer Coalition.

NWF takes the position that naturally functioning floodplains provide vital habitats for countless species, providing grounds for breeding, foraging, and other parts of the life cycles of a variety of plants, insects, reptiles, amphibians, birds, and mammals. Floodplains are also crucial to the survival and recovery of many threatened and endangered species, including salmon, steelhead trout, sturgeon, and sea turtles. NWF warned the Committee that alterations to floodplains create multiple threats to wildlife through a range of impacts including: changing the flow and hydrology of rivers; eliminating wetlands and side channels, destroying nesting and rearing areas and other important habitats; straightening and deepening channels; and causing siltation, nutrient, and other water quality problems.

According to NWF, the current floodplain management system in the United States is not working. Instead of reducing floodplain development, one of the NFIP's original goals, the system in place has incentivized and exacerbated development. Flood-prone coastal population growth and development in the United States has skyrocketed since the NFIP's creation. NWF believes that heavily subsidized insurance rates have contributed to or enabled coastal and riverine development, which has in turn contributed to the loss of functioning floodplains and natural features that reduce flood damages. NWF argued to the Committee that risk-based rates help send appropriate signals that will lessen new development in high risk areas and encourage individuals and communities to take steps to reduce or mitigate their risk.

NWF reiterated its support for the efforts in the Biggert-Waters Flood Reform Act of 2012 to increase rates and its opposition to rollbacks in the Homeowner Flood Insurance Affordability Act (HFIAA). However, NWF stated that the organization understands the need to provide targeted assistance for low-income homeowners, through outside of the rate-structure support and mitigation assistance, as well as the need to more thoughtfully and slowly transition primary residences to risk-based rates. While NWF supports the Committee's proposals to keep flood insurance premiums affordable, the organization said that the best way to keep rates low and to protect people and property is through proactive mitigation actions that would avoid and minimize damages on the ground, rather than premium support that subsidizes development in risky places, is reactive by nature, and provides a sense of false security to flood-prone areas.

According to NWF, accurate mapping is critical to the NFIP. Without accurate maps, communities, and their residents cannot be confident in the federal program or their projected flood rates. Although there are new tools to get more accurate, up-to-date mapping including property level elevation, FEMA does not use the latest technology. NWF also urges the Committee to consider that maps, to accurately detail risk, be graduated to include: not only the 100-year floodplain, but also the 50, 200 and 500-year floodplain areas (for example); residual risk areas and associated depths of flooding; other flood-related hazards and additional risk areas; and important habitat and key natural ecosystem functions areas.

Rebecca Kagan Sternhell: The government of New York City (NYC or City) believes that a citizen should only be paying insurance premiums today for his/her risk today, not the risk ten years out. The issue of greatest concern to NYC is affordability. The affordability challenge affects take-up rates, the real estate market, and City planning overall. A few months ago, NYC shared with the Committee and other interested stakeholders, a RAND report commissioned to look at what "affordability" meant and model out options to remedy the issue. The report utilized a metric called a PITI ratio (a ratio of mortgage principal and interest, property taxes, and property insurance (PITI) payments to income), that looked at the cost of owning a given home, not merely property value or income alone. This tool enabled researchers to see what small changes could affect the ability of a person to stay in their home, whether it was a mandatory rate increase or even just additional fees.

Ms. Sternhell said that the City has long-endorsed utilizing mitigation to avoid risk and drive down costs to homeowners. Since the passage of Biggert-Waters, the City has pushed for FEMA to develop cost-effective mitigation options that result in meaningful premium reductions for dense urban areas where homes cannot be elevated and homeowners cannot "build up." In addition to largescale mitigation initiatives like the Staten Island sea wall and the Rockaway Beach hardening, the City has also evaluated smaller scale options like mitigation loans and block level measures to help manage risk. The City believes these are not bad policy ideas but NYC found the ROI for many simply do not pan out for either the homeowners or the City.

Another area of concern to the City is the elimination of the non-compete clause for the Write Your Own insurance companies, and the requirement that NFIP share their data in full with any party. Such actions might bring more private participation, but it will be at the expense of the NFIP and its solvency. Ms. Sternhell pointed out that past witnesses representing the insurance industry in both Senate and House hearings have admitted to "cherry-picking" the "healthiest" policies, which will leave NFIP with only the riskiest properties, thus undermining its solvency. The City argued that this will do nothing for the program's debt or for the residents holding NFIP policies, who will see increased rates and fees. Flood insurance will become more unaffordable for those that can least afford the increase.

R.J. Lehmann: R Street is a nonpartisan, nonprofit public policy research organization based here in Washington, D.C. Through the organization's research and outreach, it seeks to promote free markets and limited, effective government at both the state and federal level, with a particular focus on issues that might be considered relatively low salience and high complexity. R Street is a part of the SmarterSafer coalition, a group of taxpayer advocates, conservation groups, insurance interests, and housing advocates that supports NFIP reform.

R Street argued that over much of program's history, the NFIP has subsidized irresponsible floodplain development at taxpayers' expense. According to R Street, NFIP is not sustainable in its current form, as evidenced by its $24.6 billion debt to federal taxpayers. Transitioning to a private, risk-based insurance market for floods will not be easy, but R Street believes that it is a challenge private insurers and reinsurers can meet. Advances in mapping risk modeling and the ability to spread risk across the globe means that many of the logistical problems the insurance industry once faced in attempting to underwrite flood risks have been significantly addressed, if not completely resolved.

R Street applauded the discussion draft's inclusion of Representative Luetkemeyer's Taxpayer Exposure Mitigation Act, which would make it a requirement that FEMA's administrator use reinsurance and other risk-transfer tools to lower taxpayers' direct exposure to catastrophic losses. As FEMA gains more experience buying reinsurance, and as reinsurers gain more experience absorbing risk from the NFIP, R Street anticipates that future risk transfers could be significantly larger.

R Street also supports provisions of the draft legislation that would require FEMA's administrator to raise the assessment rate by one percentage point each year until the program meets the minimum reserve ratio phase-in of 7.5 percent. The organization believes that the language could be further improved if, rather than either a flat percentage assessment or flat fee surcharges, the Committee considered applying Reserve Fund charges that are based on the catastrophe risk posed by each individual property. Private insurers already use similar catastrophe loads to buy reinsurance and R Street argues that the NFIP should as well.

R Street supports moving to risk-based rates for all NFIP properties, with an understanding that, for some lower-income policyholders, assistance may be needed to ensure those rates are reasonably affordable. Such assistance must be targeted, limited, means-tested, and executed outside the rate structure of the NFIP. R Street believes that the draft legislation's proposal to authorize states to create affordability programs for lower-income policyholders, financed by surcharges on other NFIP policyholders within that state, represents an important step in the right direction. Not only does this comport with the principles of federalism, but states already collect income data for a variety of means-tested programs, which R Street believes should ease what might otherwise be substantial compliance costs.

Legislative Proposals Discussed and Passed

All proposals discussed by the Committee during the hearing were ultimately passed. Below is a brief description of each bill as well as the vote totals for each. The bills will now be considered by the full House of Representatives. As of the time of the writing of this *GT Alert*, no date has been set for consideration by the full House of Representatives.

- H.R. 2875 - National Flood Insurance Program Administrative Reform Act of 2017
  - This legislation requires FEMA to identify and eliminate fraudulent practices in the flood insurance claims process and ensure that all policyholders receive the full benefit of the insurance coverage they purchased. Included are: penalties for fraudulent practices and false statements; enhanced policyholder appeals rights; prohibition on hiring disbarred attorneys; improved disclosure requirements for policies; and a Government Accountability Office (GAO) study of claims adjustment practices.
  - The bill passed the Committee by a vote of 58-0.

- H.R. 1558 – the Repeatedly Flooded Communities Act
  - The legislation seeks to limit the financial resources expended by the NFIP on claims for properties flooded multiple times. It requires communities with a significant number of repetitive loss properties to: map repeatedly flooded properties and public infrastructure to determine the specific areas that should be priorities for voluntary buyouts, drainage improvements, or other mitigation efforts; develop and implement plans for mitigating flood risk in these problem areas; and submit these plans as well as reports on progress to FEMA, an organization that is under the purview of Congressional oversight.
  - The bill passed the Committee by a voice vote.

- H.R. 1422 – the Flood Insurance Market Parity and Modernization Act
  - The legislation clarifies that flood insurance policies written by private carriers satisfy the mandatory purchase requirement. The bill would remove excessive restrictions and would give states more flexibility to license and regulate private flood insurance.
  - The bill passed the Committee by a vote of 58-0.

- H.R. 2246 – the Taxpayer Exposure Mitigation Act of 2017
  - The legislation allows localities to use their own resources to develop community-specific alternatives to NFIP-developed flood maps. It also requires FEMA to purchase reinsurance or some capital market alternative to protect taxpayers from footing the bill for future losses. The bill further allows commercial properties to opt-out of the mandatory purchase requirement, allowing for businesses to more easily purchase private flood coverage
  - The bill passed the Committee by a vote of 36-24.

- H.R. 2565 – a bill to require the use of replacement cost value in determining the premium rates for flood insurance coverage under the National Flood Insurance Act.
  - The bill requires the Federal Emergency Management Agency (FEMA) to look at properties on an individual basis and incorporate a structure's actual replacement cost in National Flood Insurance Program policies.
  - The bill passed the Committee by a vote of 34-25

- H.R. 2686 – the National Flood Insurance Program Policyholder Protection Act of 2017
  - The legislation limits annual premium increases by lowering the cap on annual rate increases from 18 to 15 percent per year and limits the chargeable risk premium for single family residences to $10,000 per year. Additionally, the bill requires FEMA to move toward providing coverage for co-op units within the NFIP program.

    - The bill passed the Committee by a vote of 53-0.

- H.R. 2874 – the 21st Century Flood Reform Act of 2017
    - The bill seeks to improve the financial stability of the National Flood Insurance Program; enhance the development of more accurate estimates of flood risk through new technology and better maps; increase the role of private markets in the management of flood insurance risks; and provide for alternative methods to insure against flood peril.
    - The bill passed the Committee by a vote of 30-26.

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