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Private Flood Insurance and the National Flood Insurance Program

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Summary

The National Flood Insurance Program (NFIP) is the main source of primary flood insurance coverage in the United States, collecting approximately $4.6 billion in premiums, fees, and surcharges for over five million flood insurance policies. This is in contrast to the majority of other property and casualty risks, such as damage from fire or accidents, which are covered by a broad array of private insurance companies. One of the primary reasons behind the creation of the NFIP in 1968 was the withdrawal by private insurers from providing flood insurance coverage, leaving flood victims largely reliant on federal disaster assistance to recover after a flood. While private insurers have taken on relatively little flood risk, they have been involved in the administration of the NFIP through sales and servicing of policies and claims.

In recent years, private insurers have expressed increased interest in providing flood coverage. Advances in the analytics and data used to quantify flood risk along with increases in capital market capacities may allow private insurers to take on flood risks that they shunned in the past. Private flood insurance may offer some advantages over the NFIP, including more flexible flood polices, integrated coverage with homeowners insurance, or lower-cost coverage for some consumers. Private marketing might also increase the overall amount of flood coverage purchased, reducing the amount of extraordinary disaster assistance necessary to be provided by the federal government. Increased private coverage could reduce the overall financial risk to the NFIP, reducing the amount of NFIP borrowing necessary after major disasters.

Increasing private insurance, however, may have some downsides compared to the NFIP. Private coverage would not be guaranteed to be available to all floodplain residents, unlike the NFIP, and consumer protections could vary in different states. The role of the NFIP has historically been broader than just providing insurance. As currently authorized, the NFIP also encompasses social goals to provide flood insurance in flood-prone areas to property owners who otherwise would not be able to obtain it, and to reduce government's cost after floods. Through flood mapping and mitigation efforts, the NFIP has tried to reduce the future impact of floods, and it is unclear how effectively the NFIP could play this broader role if private insurance became a large part of the flood marketplace. Increased private insurance could also have an impact on the subsidies that are provided for some consumers through the NFIP.

The 2012 reauthorization of the NFIP (Division F, Title II of P.L. 112-141) included provisions encouraging private flood insurance; however, various barriers have remained. Legislation passed the House in the 114th Congress (H.R. 2901) and 115th Congress (H.R. 2874) which would have attempted to expand the role of private flood insurance; neither bill was taken up by the Senate.

In the 116th Congress, no NFIP legislation has advanced past introduction. The NFIP is currently operating under a short-term reauthorization until September 30, 2020.

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Introduction

Congress is currently considering long-term reauthorization of the National Flood Insurance Program (NFIP). Floods are the most common natural disaster in the United States, and all 50 states, plus DC, Puerto Rico, Guam, American Samoa, the U.S. Virgin Islands, and the Northern Mariana Islands have experienced flood events since May 2018.[1] The NFIP has paid a total of nearly $18.3 billion in claims over the past five fiscal years.[2]

Expanding the role of private insurers, including reinsurers, has been seen by many as an answer to the variability of the financial position of the NFIP.[3] Increasing participation by private insurers could transfer more flood risk from policyholders to the private insurance sector, as opposed to transferring the risk to the federal government through the NFIP. In addition to the possible advantage to the NFIP, the increased availability of flood insurance as private companies enter the market may benefit households and businesses, as insured flood victims are likely to recover more quickly and more fully after a flood.

Private insurer interest in directly providing and underwriting flood risk has increased in recent years. Advances in the analytics and data used to quantify flood risk along with increases in capital market capacities may allow private insurers to take on flood risks that they shunned in the past. However, increasing the private sector role in providing flood insurance coverage directly to consumers may have implications for the operations and fiscal solvency of the NFIP as currently structured. Increased access to private flood insurance could provide individual policyholders with a wider choice of coverage and possibly cheaper premiums, but may also lead to variable consumer protections.

The extent to which private insurance companies participate in the U.S. flood insurance market represents an area of congressional concern. Both the 114th and 115th Congress addressed the issue with legislation passing the House; however, no legislation was ultimately enacted. The NFIP is currently operating under its 15th short-term reauthorization, until September 30, 2020.[4]

This report describes the current role of private insurers in U.S. flood insurance, and discusses barriers to private sector involvement. The report considers potential effects of increased private sector involvement in the U.S. flood market, both for the NFIP and for consumers. Finally, the report outlines the provisions relevant to private flood insurance in House and Senate NFIP reauthorization bills from the 115th Congress and the 116th Congress.

Background[5]

The NFIP is the main provider of primary flood insurance coverage for residential properties in the United States, providing nearly $1.3 trillion in coverage for over five million residential flood

[1] Email correspondence from FEMA Congressional Affairs staff, August 5, 2019.

[2] Email correspondence from FEMA Congressional Affairs staff, October 22, 2019, and premium and fee data from *The Watermark Fourth Quarter 2019*, February 4, 2020, at https://www.fema.gov/media-library/assets/documents/161889.

[3] FEMA, *National Flood Insurance Program Report to Congress on Reinsuring NFIP Insurance Risk and Options for Privatizing the NFIP*, August 13, 2015, p. 41, http://www.floods.org/ace-files/documentlibrary/2012_NFIP_Reform/Reinsuring_NFIP_Insurance_Risk_and_Options_for_Privatizing_the_NFIP_Report.pdf.

[4] P.L. 116-93.

[5] For more detail on the NFIP, see CRS Report R44593, *Introduction to the National Flood Insurance Program (NFIP)*, by Diane P. Horn and Baird Webel.

insurance policies. In FY2018, the program collected about $3.51 billion in annual premium revenue, $1.09 billion in assessments, fees, and surcharges and $1.04 billion in payments from private reinsurers.[6] In FY2019, the program collected about $3.39 billion in annual premium revenue and $1.07 billion in assessments, fees, and surcharge, with no payments from private reinsurers.[7] Nationally, over 22,000 communities participate in the NFIP.[8] The role of the federal government in flood insurance is in contrast to the majority of other property and casualty risks, such as damage from fire or accidents, which are covered by a broad array of private insurance companies. Total premiums for private property and casualty insurance in 2018 totaled $611 billion, with the policies backed by over $2 trillion in assets held by private insurers.[9]

Objectives of the NFIP

The NFIP has two main policy goals: (1) to provide access to primary flood insurance, thereby allowing for the transfer of some of the financial risk of property owners to the federal government; and (2) to mitigate and reduce the nation's comprehensive flood risk[10] through the development and implementation of floodplain management standards. A longer-term objective of the NFIP is to reduce federal expenditure on disaster assistance after floods.

As a public insurance program, the NFIP is designed differently from the way in which private-sector companies provide insurance. As currently authorized, the NFIP also encompasses social goals to provide flood insurance in flood-prone areas to property owners who otherwise would not be able to obtain it, and to reduce the government's cost after floods.[11] The NFIP also engages in many "non-insurance" activities in the public interest: it disseminates flood risk information through flood maps, requires communities to adopt land use and building code standards in order to participate in the program, potentially reduces the need for other post-flood disaster aid, contributes to community resilience by providing a mechanism to fund rebuilding after a flood, and may protect lending institutions against mortgage defaults due to uninsured losses. The benefits of such tasks are not directly measured in the NFIP's financial results from selling flood insurance.[12]

From the inception of the NFIP, the program has been expected to achieve multiple objectives, some of which may conflict with one another:

- To ensure reasonable insurance premiums for all;

[6] Statistics on the National Flood Insurance Program (NFIP) policy and claims are available from the Federal Emergency Management Agency (FEMA) website "Policy and Claim Statistics for Flood Insurance," at https://www.fema.gov/policy-claim-statistics-flood-insurance; premium and fee data from *The Watermark Fourth Quarter 2019*, February 4, 2020, at https://www.fema.gov/media-library/assets/documents/161889.

[7] Fee data from *The Watermark First Quarter 2020*, March 27, 2020, at https://www.fema.gov/media-library/assets/documents/161889.

[8] Detailed information about which communities participate and where is available from the Community Status Book, found on FEMA's website at https://www.fema.gov/national-flood-insurance-program-community-status-book.

[9] Premium amounts used are net premiums written and asset amounts are admitted assets from A.M. Best, *2019 Best's Rankings: U.S. Property/Casualty - 2018 Financial Results*, March 25, 2019.

[10] In the context of this report, *comprehensive* flood risk means that the risk includes both financial risk (i.e., physical damage to property), and also the risk to human life.

[11] See 82 Stat. 573 for text in original statute (Section 1302(c) of P.L. 90-448). This language remains in statute (see 42 U.S.C. §4001(c)).

[12] American Academy of Actuaries Flood Insurance Work Group, *The National Flood Insurance Program: Challenges and Solutions*, April 2017, p. 79, http://www.actuary.org/files/publications/FloodMonograph.04192017.pdf.

- To have risk-based premiums that would make people aware of and bear the cost of their floodplain location choices;
- To secure widespread community participation in the NFIP and substantial numbers of insurance policy purchases by property owners; and
- To earn premium and fee income that, over time, covers claims paid and program expenses.[13]

Primary Flood Insurance Through the NFIP

The NFIP offers flood insurance to anyone in a community that chooses to participate in the program. Flood insurance purchase generally is voluntary, except for property owners who are in a Special Flood Hazard Area (SFHA)[14] and whose mortgage is backed by the federal government.[15] Flood insurance policies through the NFIP are sold only in participating communities and are offered to both property owners and renters and to residential and non-residential properties. NFIP policies have relatively low coverage limits, particularly for non-residential properties or properties in high-cost areas. The maximum coverage for single-family dwellings (which also includes single-family residential units within a 2-4 family building) is $100,000 for contents and up to $250,000 for building coverage. The maximum available coverage limit for other residential buildings is $500,000 for building coverage and $100,000 for contents coverage, and the maximum coverage limit for non-residential business buildings is $500,000 for building coverage and $500,000 for contents coverage.

The Mandatory Purchase Requirement

By law and regulation, federal agencies, federally regulated lending institutions, and government-sponsored enterprises (GSEs)[16] must require the property owners in an SFHA to purchase flood insurance as a condition of any mortgage that these entities make, guarantee, or purchase.[17] In addition to this legal mandatory purchase requirement, lenders may also require borrowers outside of an SFHA to maintain flood insurance as a means of financially securing the property.

In order to comply with this mandate, property owners may purchase flood insurance through the NFIP, or through a private company, so long as the private flood insurance "provides flood insurance coverage which is at least as broad as the coverage" of the NFIP, among other conditions.[18] The mandatory purchase requirement is enforced by the lender, rather than FEMA,

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[13] National Research Council of the National Academies, *Affordability of National Flood Insurance Program Premiums: Report 1*, 2015, p. 3, at http://www.nap.edu/catalog/21709/affordability-of-national-flood-insurance-program-premiums-report-1.

[14] A Special Flood Hazard Area (SFHA) is defined by FEMA as an area with a 1% or greater risk of flooding every year.

[15] This includes mortgages from banks insured by the Federal Deposit Insurance Corporation and mortgages backed by Fannie Mae or Freddie Mac, as well as federal entities such as the Federal Housing Administration and the Department of Veterans Affairs.

[16] Government-Sponsored Enterprises (GSEs) are private companies with congressional charters. Examples of GSEs providing mortgages that would be affected by the mandatory purchase requirement include the Federal Home Loan Mortgage Corporation (Freddie Mac) and the Federal National Mortgage Association (Fannie Mae).

[17] 42 U.S.C. §4012a.

[18] 42 U.S.C §4012a(b). For additional information on private flood insurance, see CRS Insight IN10450, *Private Flood Insurance and the National Flood Insurance Program (NFIP)*, by Baird Webel and Diane P. Horn. The "at least as broad as" requirement is discussed in more detail in the section titled "Flood Insurance Coverage "at Least as Broad as" the NFIP" in this report.

and lenders can be fined up to $2,000 by banking regulators for each failure to require flood insurance or provide notice.[19] Property owners who do not obtain flood insurance when required may find that they are not eligible for certain types of disaster assistance after a flood.[20]

Premium Subsidies and Cross-Subsidies

Flood insurance rates in the NFIP generally are directed by statute to be "based on consideration of the risk involved and accepted actuarial principles,"[21] meaning that the rate is reflective of the true flood risk to the property. However, Congress has directed FEMA *not* to charge actuarial rates for certain categories of properties and to offer discounts to other classes of properties.[22] FEMA is not, however, provided funds to offset these subsidies and discounts,[23] which has contributed to FEMA's need to borrow from the U.S. Treasury to pay NFIP claims.

There are three main categories of properties that pay less than full risk-based rates:

- *Pre-FIRM*: properties that were built or substantially improved before December 31, 1974, or before FEMA published the first Flood Insurance Rate Map (FIRM) for their community, whichever was later;[24]
- *Newly mapped*: properties that are newly mapped into a SFHA on or after April 1, 2015, if the applicant obtains coverage that is effective within 12 months of the map revision date;[25] and
- *Grandfathered*: properties that were built in compliance with the FIRM in effect at the time of construction and are allowed to maintain their old flood insurance rate class if their property is remapped into a new flood rate class.[26]

NFIP Reauthorization and Legislation

116th Congress

The NFIP is currently authorized until September 30, 2020.[27] Since the end of FY2017, spanning both the 115th and 116th Congresses, 15 short-term NFIP reauthorizations have been enacted. The

[19] 42 U.S.C §4012a(f).

[20] For additional information, see CRS Report R44808, *Federal Disaster Assistance: The National Flood Insurance Program and Other Federal Disaster Assistance Programs Available to Individuals and Households After a Flood*, by Diane P. Horn.

[21] 42 U.S.C. §4014(a)(1).

[22] For a full discussion of NFIP subsidies and cross-subsidies, see the section on Pricing and Premium Rate Structure in CRS Report R44593, *Introduction to the National Flood Insurance Program (NFIP)*, by Diane P. Horn and Baird Webel, the section on Premiums Subsidies and Cross-Subsidies in CRS Report R46095, *The National Flood Insurance Program: Selected Issues and Legislation in the 116th Congress*, by Diane P. Horn and Baird Webel, and the section on Premim Subsidies and Cross-Subsidies in CRS Report R45999, *National Flood Insurance Program: The Current Rating Structure and Risk Rating 2.0*, by Diane P. Horn.

[23] Government Accountability Office (GAO), *Flood Insurance: Comprehensive Reform Could Improve Solvency and Enhance Resilience*, GAO-17-425, April 2017, p. 17, https://www.gao.gov/products/GAO-17-425.

[24] 42 U.S.C. §4015(c).

[25] §6 of P.L. 113-89, 128 Stat.1028, as codified at 42 U.S.C. §4015(i).

[26] For a full description, see FEMA, *NFIP Grandfathering Rules for Agents*, March 2016, at https://www.fema.gov/media-library-data/1488482596393-dcc52e6c120c9327dcd75f1c08e802e4/GrandfatheringForAgents_03_2016.pdf.

[27] The statute for the NFIP does not contain a comprehensive expiration, termination, or sunset provision for the whole of the program. Rather, the NFIP has multiple different legal provisions that generally tie to the expiration of key

House Financial Services Committee completed markup of a bill for the long-term reauthorization of the NFIP, the National Flood Insurance Program Reauthorization Act of 2019 (H.R. 3167), and ordered it reported on June 12, 2019.[28] H.R. 3167 would reauthorize the NFIP until September 30, 2024. One bill has been introduced in the Senate, on July 18, 2019, to reauthorize the expiring provisions of the NFIP: the National Flood Insurance Program Reauthorization and Reform Act of 2019 (S. 2187), with a companion bill in the House, H.R. 3872.[29] The latter two bills have not yet been considered by the committees of jurisdiction. S. 2187 and H.R. 3872 would also reauthorize the NFIP until September 30, 2024.

Details of the provisions relating to private insurance in the House and Senate bills in the 116th Congress are described in the **Appendix**, and **Table A-1** relates the provisions in the bills in the 116th Congress to the issues discussed in this report.

Prior Congresses

The House passed standalone legislation to encourage private insurance in the 114th Congress (H.R. 2901); however, the Senate did not take up H.R. 2901 in the 114th Congress.

In the 115th Congress, a number of bills were introduced to provide a longer-term reauthorization of the NFIP as well as make numerous other changes to the program. The House of Representatives passed H.R. 2874 (The 21st Century Flood Reform Act) by a vote of 237-189 on November 14, 2017. Among its numerous provisions, H.R. 2874 would have authorized the NFIP until September 30, 2022.

Three bills were introduced in the Senate that would have reauthorized the expiring provisions of the NFIP:

- S. 1313 (Flood Insurance Affordability and Sustainability Act of 2017);
- S. 1368 (Sustainable, Affordable, Fair, and Efficient [SAFE] National Flood Insurance Program Reauthorization Act of 2017);[30] and
- S. 1571 (National Flood Insurance Program Reauthorization Act of 2017).

None of these bills were considered by the full Senate in the 115th Congress. Among their other provisions, S. 1313 would have authorized the NFIP until September 30, 2027; S. 1368 would have authorized the NFIP until September 30, 2023; and S. 1571 would have authorized the NFIP until September 30, 2023.

The four reauthorization bills in the 115th Congress differed significantly in the degree to which they would have encouraged private participation in flood insurance, particularly flood insurance sold by private companies in competition with the NFIP. In general, legislation passed by the House was more encouraging of private flood insurance than Senate legislation. In the 115th Congress, the House included the same provisions in H.R. 2874 and in an unrelated bill to reauthorize the Federal Aviation Administration (H.R. 3823). The Senate removed the flood

components of the program. Unless reauthorized or amended by Congress, the following will occur on September 30, 2020: (1) The authority to provide new flood insurance contracts will expire. Flood insurance contracts entered into before the expiration would continue until the end of their policy term of one year; and (2) The authority for NFIP to borrow funds from the Treasury will be reduced from $30.425 billion to $1 billion (42 U.S.C. §4016(a)). The most recent reauthorization of the NFIP is in P.L. 116-93.

[28] See H.Rept. 116-262, Part 1, at https://www.congress.gov/116/crpt/hrpt262/CRPT-116hrpt262.pdf.

[29] H.R. 3872 was introduced on July 22, 2019.

[30] A similar bill was introduced in the House, H.R. 3285.

insurance language from H.R. 3823 before passing it. Reportedly, the provisions relating to private flood insurance were a particular issue of concern.[31] The Senate ultimately did not take up H.R. 2874 during the 115th Congress. S. 1313 included some similar provisions to H.R. 2874 on private flood insurance, but S. 1368 and S. 1571 did not.

The Current Role of Private Insurers in the NFIP

Private insurers can be involved in the flood insurance market in a number of ways, including (1) by helping to administer the NFIP; (2) by sharing risk with the NFIP as a reinsurer; or (3) by taking on risk themselves as a primary insurer, where the insurer contracts directly with a consumer. Since 1983, private insurers have played a major role in administering the NFIP, including selling and servicing policies and adjusting claims, but they largely have not been underwriting flood risk themselves.[32] Instead, the NFIP retains the direct financial risk of paying claims for these policies. The NFIP has purchased reinsurance since 2016, thus transferring some of the flood risk to the private sector.

Servicing of Policies and Claims Management

While FEMA provides the overarching management and oversight of the NFIP, the majority of the day-to-day operation of the NFIP is handled by private companies. This includes marketing, selling and writing policies, and all aspects of claims management.[33] FEMA has established two different arrangements with private industry. The first is the Direct Servicing Agent, or DSA, which operates as a private contractor, selling NFIP policies on behalf of FEMA for individuals seeking to purchase flood insurance policies directly from the NFIP.[34] The DSA also handles the policies of severe repetitive loss properties.[35] The second arrangement is the Write-Your-Own (WYO) program, where private insurance companies are paid to issue and service NFIP policies. With either the DSA or WYO program, the NFIP retains the actual financial risk of paying claims for the policy, and the policy terms and premiums are the same. Approximately 13% of the total

[31] See, for example, Shaun Courtney, "'Hard to Envision' Senate Democrats Blocking FAA Extension, Thune Says," *Bloomberg BNA*, September 27, 2017, Daily Report for Executives, https://www.bna.com/hard-envision-senate-n73014470158/,

> Thune wants to see the Senate pass the House bill under unanimous consent, but committee ranking member Bill Nelson (D-Fla.) made that sound unlikely. "That will not get passed here," Nelson said Sept. 26 in response to Bloomberg BNA's inquiry about the House's flood insurance provision.… Senator Sherrod Brown (D-Ohio), ranking member on the Banking, Housing, and Urban Affairs Committee, which has jurisdiction over flood insurance proposals, said the House provision was unacceptable. "We're not going to do it," Brown said. "This would undermine all of our flood insurance efforts. It will cause all kinds of cherry-picking by private insurance."

[32] Underwriting risk refers to the potential loss to an insurer or reinsurer. An insurer takes on this risk in return for a premium, and promises to pay an agreed amount in the event of a loss. See NAIC, *Glossary of Insurance Terms*, http://www.naic.org/consumer_glossary.htm#U.

[33] See primarily 42 U.S.C. §4081 and §4018, and 44 C.F.R. Part 62.

[34] The current Direct Servicing Agent is a company called Torrent Technologies, Inc., who was awarded the contract in 2017. See https://content.govdelivery.com/accounts/USDHSFEMA/bulletins/1c9da05.

[35] Severe repetitive loss properties are those that have incurred four or more claim payments exceeding $5,000 each, with a cumulative amount of such payments over $20,000; or at least two claims with a cumulative total exceeding the value of the property. See 42 U.S.C. §4014(h) and 44 C.F.R. §79.2(h).

NFIP policy portfolio is managed through the DSA and 87% of NFIP policies are sold by the 60 companies participating in the WYO program.[36]

Companies participating in the WYO program are compensated through a variety of methods, but this compensation is not directly based on the costs incurred by the WYOs. In the Biggert-Waters Flood Insurance Reform Act of 2012 (Division F, Title II of P.L. 112-141, hereinafter BW-12), Congress required FEMA to develop and issue a rulemaking on a "methodology for determining the appropriate amounts that property and casualty insurance companies participating in the WYO program should be reimbursed for selling, writing, and servicing flood insurance policies and adjusting flood insurance claims on behalf of the National Flood Insurance Program."[37] This rulemaking was required within a year of enactment of BW-12. FEMA published an Advanced Notice of Proposed Rulemaking to revise the compensation structure of the WYOs on July 8, 2019.[38] The comment period closed on September 6, 2019. Until the analysis is complete, it is difficult to ascertain how much it actually costs WYO companies to administer the NFIP policies, or the WYO's profit margins (if any).

In the 115th Congress, H.R. 2874 would have capped the allowance paid to the WYOs at 27.9% of premiums, while S. 1368 would have capped the allowance at 22.46%.

In the 116th Congress, Section 302 of S. 2187 would establish that the total amount of reimbursement paid to WYO companies could not be greater than 22.46% of the aggregate amount of premiums charged by the company. This section would also require FEMA to ensure that the commission paid by a WYO company to agents of the company would not be less than 15%. Section 304 of S. 2187 would require FEMA, within 12 months of enactment, to develop a schedule to determine the actual costs of WYO companies and reimburse the WYO companies only for the actual costs of the service or products. It would require that all reimbursements made to WYO companies be made public, including a description of the product or service provided to which the reimbursement pertains. Section 405 of S. 2187 would require FEMA to establish penalties for underpayment of claims by WYO companies that are not less than the penalty for overpayment of a claim. Both H.R. 3872 and S. 2187 contain provisions giving FEMA the authority to terminate a WYO contract under certain conditions, such as fraud or other conduct detrimental to the NFIP.

Reinsurance

In the Homeowner Flood Insurance Affordability Act of 2014 (P.L. 113-89, HFIAA), Congress revised the authority of FEMA to secure reinsurance[39] for the NFIP from the private reinsurance and capital markets.[40] The purchase of private market reinsurance reduces the likelihood of FEMA needing to borrow from the Treasury to pay claims. In addition, as the U.S. Government

[36] Email correspondence from FEMA Congressional Affairs staff, March 1, 2019. A list of companies participating in the WYO program is available at https://www.fema.gov/wyo_company.

[37] §100224 of P.L. 112-141, 126 Stat. 936.

[38] Federal Emergency Management Agency, "National Flood Insurance Program (NFIP); Revisions to Methodology for Payments to Write Your Own (WYO) Companies," 84(130) *Federal Register* 32,371-32,379, July 8, 2019, and Federal Emergency Management Agency, "National Flood Insurance Program (NFIP); Revisions to Methodology for Payments to Write Your Own (WYO) Companies; Correction," 84(170) *Federal Register* 45,933-45,934, September 3, 2019.

[39] Reinsurance is defined as a transaction between a primary insurer and another licensed (re)insurer where the reinsurer agrees to cover all or part of the losses and/or loss adjustment expenses of the primary insurer. See NAIC, *Glossary of Insurance Terms*, http://www.naic.org/consumer_glossary.htm#R.

[40] See §10 of P.L. 113-89, 128 Stat. 1025, as codified at 42 U.S.C. §4081(e).

Accountability Office (GAO) noted, reinsurance could be beneficial because it allows FEMA to price some of its flood risk up front through the premiums it pays to the reinsurers rather than borrowing from Treasury after a flood.[41] From a risk management perspective, using reinsurance to cover losses in only the more extreme years could help the government to manage and reduce the volatility of its losses over time.

Transfer of risk to the private sector through reinsurance, however, is unlikely to lower the overall cost of the NFIP because reinsurers understandably charge FEMA premiums to compensate for the risk they assume. The primary benefit of reinsurance is to transfer and manage risk rather than to reduce the NFIP's long-term fiscal exposure.[42] For example, a reinsurance scenario which would provide the NFIP with $16.8 billion coverage (sufficient for Katrina-level losses) could cost an estimated $2.2 billion per year.[43] Such a reinsurance premium, however, would be a large portion of the total premiums paid into the NFIP, approximately two-thirds of the current premium amounts. Devoting such a large portion of premiums to reinsurance could leave insufficient funds for paying claims outside of large disasters,[44] or for covering the other purposes for NFIP funds, such as flood mitigation, mapping, and improving NFIP rating structures.

Reinsurance has been purchased by FEMA through two different mechanisms, "traditional" reinsurance and reinsurance backed by catastrophe bonds.[45] The traditional reinsurance has been purchased from a varied group of reinsurance companies with each reinsurer bearing part of the risk. The catastrophe bond reinsurance is facilitated by a single company, with the risk then transferred to capital market investors who purchase the bonds. The specifics of each reinsurance purchase has varied, but in general, the reinsurance has been designed to pay a certain percentage of the losses from a single, large scale event, with a higher percentage if losses are higher.[46] Coverage has typically started after $4 billion in losses, a loss level that has only been reached by the NFIP in three events—Hurricane Katrina, Superstorm Sandy, and Hurricane Harvey. **Table 1** outlines the various reinsurance purchases, including the dates in force, type of reinsurance, amount of coverage, premiums paid by FEMA, and claims paid to FEMA.

In the 115th Congress, H.R. 2874, S. 1313, and S. 1571 all contained provisions that would have required or encouraged the NFIP to transfer a portion of its risk to the private reinsurance market.

In the 116th Congress, H.R. 3167, Section 406, would require FEMA annually to evaluate ceding a portion of the risk of the NFIP to the private reinsurance or capital markets, if the Administrator determines that the rates and terms are reasonable and doing so would further the development and maintenance of a sound financial framework for the NFIP. S. 2187 does not contain any provisions related to reinsurance.

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[41] GAO, *Flood Insurance: Comprehensive Reform Could Improve Solvency and Enhance Resilience*, GAO-17-425, April 2017, p. 19, https://www.gao.gov/products/GAO-17-425.

[42] Ibid.

[43] FEMA, *National Flood Insurance Program Report to Congress on Reinsuring NFIP Insurance Risk and Options for Privatizing the NFIP*, August 13, 2015, p. 171, http://www.floods.org/ace-files/documentlibrary/2012_NFIP_Reform/Reinsuring_NFIP_Insurance_Risk_and_Options_for_Privatizing_the_NFIP_Report.pdf.

[44] The NFIP reinsurance purchases have been designed to cover claims for only one large flood, and smaller flood claims will continue to be paid from NFIP premiums.

[45] For more details see FEMA, *National Flood Insurance Program (NFIP) Reinsurance Program*, at https://www.fema.gov/nfip-reinsurance-program, and CRS Insight IN10965, *The National Flood Insurance Program (NFIP), Reinsurance, and Catastrophe Bonds*, by Diane P. Horn and Baird Webel.

[46] For example, the 2020 traditional reinsurance purchase covers 10.25% of NFIP losses from $4 billion to $6 billion, 34.68% of losses from $6 billion to $8 billion, and $21.80% of losses from $8 billion to $10 billion.

Table 1. NFIP Reinsurance Purchases

($ billion)

Date	Type	Coverage amount	Coverage Levels	Premiums Paid by FEMA	To Date Claims Paid to FEMA
CY2017	Traditional	$1.042	$4-8	$0.150	$1.042
CY2018	Traditional	$1.46	$4-8	$0.235	$0
August 2018-July 2021	Catastrophe Bond	$0.5	$5-10	$0.124[a]	$0
CY2019	Traditional	$1.32	$4-10	$0.186	$0
April 2019-March 2022	Catastrophe Bond	$0.3	$6-8	$0.07[b]	
CY2020	Traditional	$1.33	$4-10	$0.205	$0
February 2020- January 2023	Catastrophe Bond	$0.4	$6-10	$0.053	$0

Source: FEMA websites at https://www.fema.gov/nfip-reinsurance-program and information provided by FEMA Congressional Affairs staff, April 15, 2020.

a. Premiums of $62 million in each of first and second years.

b. Premiums of $32 million in first year and $38 million in second year.

To date, the reinsurance purchases have been a net fiscal positive for the NFIP with a total of $1.023 billion in premiums paid and $1.042 billion received from claims. This is due to the extremely high losses experienced after Hurricane Harvey, which resulted in over $9 billion paid by the NFIP to policyholders and triggered the full claim of $1.042 billion on the 2017 reinsurance. Unless another large scale flooding event occurs, the balance of premiums vs. claims is likely to turn negative in the next two to three years if FEMA continues similar reinsurance purchases.

Private Flood Insurance Outside the NFIP: Issues and Barriers

One of the reasons that Congress created the NFIP in 1968 was the general unavailability of flood insurance from private insurers. Private flood insurance was offered between 1895 and 1927, but losses incurred from the 1927 Mississippi River floods and additional flood losses in 1928 led most insurers to stop offering flood policies.[47] Private flood insurance companies largely concluded that flood peril was uninsurable because of the catastrophic nature of flooding, the difficulty of determining accurate rates, the risk of adverse selection,[48] and the concern that they

[47] National Research Council of the National Academies, *Affordability of National Flood Insurance Program Premiums: Report 1*, 2015, p. 23, http://www.nap.edu/catalog/21709/affordability-of-national-flood-insurance-program-premiums-report-1.

[48] Adverse selection is the phenomenon whereby persons with a higher than average probability of loss seek greater insurance coverage than those with less risk. See National Association of Insurance Commissioners (NAIC), *Glossary of Insurance Terms*, http://www.naic.org/consumer_glossary.htm.

could not profitably provide risk-based flood coverage at a price that consumers felt they could afford.[49]

Currently, the private flood insurance market most commonly provides commercial coverage, secondary coverage above the NFIP maximums, or coverage in the lender-placed market.[50] The 2018 premiums for private flood insurance as reported to the National Association of Insurance Commissioners (NAIC)[51] totaled $644 million, up from $589 million in 2017 and $376 million in 2016,[52] compared to the $3.5 billion total amount of NFIP premiums. In general, the private flood market tends to focus on high-value properties, which command higher premiums and therefore the extra expense of flood underwriting can be more readily justified.[53]

Currently few private insurers compete with the NFIP in the primary residential flood insurance market. One illustration of this is that the NAIC only began systematically collecting separate data on private flood insurance in 2016.

As discussed in the following sections, private insurers have identified a number of potential barriers to more widespread private sector involvement in providing flood insurance. Increasing private insurance may present a number of issues for the NFIP and for consumers.

Flood Insurance Coverage "at Least as Broad as" the NFIP

In BW-12, Congress explicitly provided for private flood insurance to fulfill the mandatory purchase mortgage requirement as long as the private flood insurance "provides flood insurance coverage which is at least as broad as the coverage" of the NFIP, among other conditions.[54] Implementation of this requirement has proved challenging. The crux of the implementation issue is in answering the question of who would evaluate whether specific policies met the "at least as broad as" standard and what criteria would be used in making this evaluation. Some lending institutions feel that they lack the necessary technical expertise to evaluate whether a flood insurance policy meets the definition of private flood insurance set forth in BW-12.[55]

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[49] See GAO, *Flood Insurance: Strategies for Increasing Private Sector Involvement*, GAO-47-127, January 2014, p. 6, https://www.gao.gov/products/GAO-14-127, and Caroline Kousky and Howard Kunreuther, *The National Flood Insurance Program: Yesterday, Today and Tomorrow*, NAIC, Center for Insurance Policy and Research Study Series 2017-1: Flood Risk and Insurance, Kansas City, MO, April 2017, pp. 23-45, http://www.naic.org/documents/cipr_study_1704_flood_risk.pdf.

[50] The lender-placed or forced-place market is where lenders can force-place flood insurance on properties that are out of compliance with the mandatory purchase requirement.

[51] The NAIC is an organization of the state regulators of insurance and, among other things, collects the data that the regulators require to be reported by insurance companies.

[52] Statistics provided by the National Association of Insurance Commissioners to CRS. They do not include coverage written in the surplus lines marketplace by non-U.S. insurers.

[53] FEMA, *National Flood Insurance Program Report to Congress on Reinsuring NFIP Insurance Risk and Options for Privatizing the NFIP*, August 13, 2015, p. 32, http://www.floods.org/ace-files/documentlibrary/2012_NFIP_Reform/Reinsuring_NFIP_Insurance_Risk_and_Options_for_Privatizing_the_NFIP_Report.pdf.

[54] 42 U.S.C §4012a(b).

[55] Department of the Treasury, Federal Reserve System, Federal Deposit Insurance Corporation, Farm Credit Administration, National Credit Union Administration, "Loans in Areas Having Special Flood Hazards, Proposed Rule," vol. 78, no. 201 *Federal Register* 65113, October 30, 2013.

The responsible federal agencies[56] issued two separate Notices of Proposed Rulemaking (NPRM) on the question, the first in October 2013,[57] and the second in November 2016.[58] On February 12, 2019, the agencies announced a final rule implementing this BW-12 requirement.[59] Of particular note, the agencies indicate the rule

- "allows institutions to rely on an insurer's written assurances in a private flood insurance policy stating the criteria are met; [and]
- clarifies that institutions may, under certain conditions, accept private flood insurance policies that do not meet the Biggert-Waters Act criteria."[60]

This second point may seem unusual, because BW-12 included a specific definition of private flood insurance, while the agencies indicate that the rule allows acceptance of private flood insurance that does not meet this statutory definition. In creating the exception that allows private flood insurance that does not follow the statutory definition of "private flood insurance," the agencies relied on the usage of the more general term "flood insurance" in 42 U.S.C. 4012a(b)(1)(A) combined with the perceived congressional intent to promote private insurance in BW-12.[61]

The rule took effect on July 1, 2019. Press reports described it as generally welcomed by the banking industry,[62] but it is unclear to what extent this new rule will encourage private flood insurance or whether additional legislative changes might be needed if Congress seeks to further encourage development of the private flood insurance market.

In the 115th Congress, H.R. 2874 and S. 1313 included provisions that would have revised the definition of private flood insurance, striking existing statutory language requiring private flood insurance to provide coverage "at least as broad as the coverage" provided by the NFIP in order to meet the mandatory purchase requirements. Instead, the new definition would have relied on whether the insurance policy and insurance company were in compliance with the laws and regulations in the state where the insurance was purchased. S. 1368 and S. 1571 had no similar provisions. Neither of the bills in the 116th Congress include any provisions related to the definition of private flood insurance.

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[56] Office of the Comptroller of the Currency, Board of Governors of the Federal Reserve System, Federal Deposit Insurance Corporation, Farm Credit Administration, and National Credit Union Administration.

[57] Department of the Treasury, Federal Reserve System, Federal Deposit Insurance Corporation, Farm Credit Administration, National Credit Union Administration, "Loans in Areas Having Special Flood Hazards, Proposed Rule," vol. 78, no. 201, *Federal Register* 65108-65144, October 30, 2013.

[58] Department of the Treasury, Federal Reserve System, Federal Deposit Insurance Corporation, Farm Credit Administration, National Credit Union Administration, "Loans in Areas Having Special Flood Hazards—Private Flood Insurance," vol. 81, no. 215, *Federal Register* 78063-78080, November 7, 2016.

[59] Department of the Treasury, Federal Reserve System, Federal Deposit Insurance Corporation, Farm Credit Administration, National Credit Union Administration, "Loans in Areas Having Special Flood Hazards—Private Flood Insurance," vol. 84, no. 34, *Federal Register* 4953-4975, February 20, 2019.

[60] Federal Reserve System, Farm Credit Administration, Federal Deposit Insurance Corporation, National Credit Union Administration, and Office of the Comptroller of the Currency, "New Rule Covers Private Flood Insurance," press release, February 12, 2019, at https://www.occ.gov/news-issuances/news-releases/2019/nr-ia-2019-15.html.

[61] For the complete agency rationale, see the section entitled "Discretionary Acceptance" in Department of the Treasury, Federal Reserve System, Federal Deposit Insurance Corporation, Farm Credit Administration, National Credit Union Administration, "Loans in Areas Having Special Flood Hazards—Private Flood Insurance," vol. 84, no. 34, *Federal Register* 4959-4960, February 20, 2019.

[62] See, for example, Sinnock, Bonnie, "Banks Claim Victory in New Private Flood Insurance Rule," *American Banker*, February 11, 2019.

Continuous Coverage

An associated issue is that of continuous coverage, which is required for property owners to retain any subsidies or cross-subsidies in their NFIP premium rates. Under existing law, if an NFIP policyholder allows their policy to lapse, any subsidy that they currently receive would be eliminated immediately.[63] Unless legislation specifically allows private flood insurance to count for continuous coverage, a borrower may be reluctant to purchase private insurance if doing so means they would lose their subsidy should they later decide to return to NFIP coverage.

In the 115th Congress, H.R. 2874 included a provision that would have specified that if a property owner purchases private flood insurance and decides then to return to the NFIP, they would be considered to have maintained continuous coverage. S. 1313 included a provision to allow private flood insurance to count as continuous coverage. S. 1368 and S. 1571 had no similar provisions. In the 116th Congress, Section 401 of H.R. 3167 would consider any period during which a property is covered by a flood insurance policy, either through the NFIP or a private company, to be a period of continuous coverage. S. 2187 does not contain any provisions related to continuous coverage.

The "Non-Compete" Clause

Before FY2019, the Write Your Own carriers, private insurers who sell and service NFIP policies, were restricted in their ability to sell flood insurance policies on their own behalf while also participating as a WYO, due to a "non-compete" clause contained in the standard NFIP contracts.[64] These contracts governing the WYO companies' participation in the NFIP restricted the WYO carriers from selling their own standalone private flood products.[65] A non-compete clause would require WYO companies to decide whether to offer private flood insurance policies in their own right or to act as WYO carriers, thus potentially limiting the size of the private flood market. In the 115th Congress, H.R. 2874 would have eliminated the non-compete clause in place at the time, while S. 1313 would have provided temporary authorization for WYOs to sell private flood insurance for certain types of properties,[66] with a follow-up study by FEMA to determine if the authorization should be made permanent.

The CBO cost estimate of H.R. 2874[67] considered the impact of eliminating the WYO companies' non-compete agreement. CBO estimated that, over the 2017-2027 period, holders of about 690,000 properties that, under existing law, would have been purchased under the NFIP would instead choose to buy private flood insurance to cover those properties if H.R. 2874 were enacted. CBO did not expect any property owners who are subsidized by the NFIP to be among those

[63] As required by §100205(a)(1)(B) of BW-12 (P.L. 112-141, 126 Stat. 917), only for NFIP policies that lapsed in coverage as a result of the deliberate choice of the policyholder.

[64] Details of the WYO company arrangements are available at https://www.fema.gov/media-library-data/1504278934379-6bdf86cd243d53170e7ff8a2afc6770d/FY2018_Financial_Assistance_Subsidy_Arrangement_Oct_2017.pdf.

[65] GAO, *Flood Insurance: Potential Barriers Cited to Increased Use of Private Insurance*, GAO-16-611, July 14, 2016, p. 31, https://www.gao.gov/assets/680/678414.pdf.

[66] Non-residential properties, severe repetitive loss properties, business properties, or any property that has incurred flood-related damage in which the cumulative amount of payments equaled or exceeded the fair market value of the property.

[67] Congressional Budget Office, *Cost Estimate. H.R. 2874, 21st Century Flood Reform Act.*, Washington, DC, September 8, 2017, pp. 1-13, https://www.cbo.gov/publication/53088.

leaving the program.[68] CBO estimated that eliminating the non-compete clause and making NFIP data publically available would lead to an increase in spending of $39 million for the 2018-2022 period and $393 million for the 2018-2017 period.[69]

FEMA implemented changes in the standard WYO contracts for FY2019 removing the restrictions on WYO companies offering private flood insurance, while maintaining requirements that such private insurance lines remain entirely separate from a WYO company's NFIP insurance business.[70] The non-compete clause has again been excluded from the WYO agreements for FY2020.[71] This action removes the non-compete clause without legislation, although FEMA in the future would retain the authority to reinstate the non-compete clause.

NFIP Subsidized Rates

FEMA's subsidized rates are often seen as one of the primary barriers to private sector involvement in flood insurance.[72] However, even without the subsidies mandated by law, the NFIP's definition of full-risk rates differs from that of private insurers. Whereas the NFIP's full-risk rates must incorporate expected losses and operating costs, a private insurer's full-risk rates must also incorporate a profitable return on capital. As a result, even those NFIP policies which are considered to be actuarially sound from the perspective of the NFIP may still be underpriced from the perspective of private insurers.[73] In order to make the flood insurance market attractive, private insurers would want to be able to charge premium rates that reflect the full estimated risk of potential flood losses while still allowing the companies to make a profit. A reformed NFIP rate structure could have the effect of encouraging more private insurers to enter the primary flood market because NFIP full-risk based rates would be closer to the rates that private insurers would likely charge; however, this could lead to higher rates for households.

In the 115th Congress, H.R. 2874 would have phased out the pre-FIRM subsidy for primary residences at a rate of 6.5%-15% (compared to the current rate of 5%-18%),[74] in a staged manner. In the first year after enactment, the minimum rate increase would have been 5%; in the second year after enactment, the minimum rate increase would have been 5.5%; and in the third year of enactment, the minimum rate increase would have been 6%. The phaseout of the pre-FIRM subsidy for other categories of properties[75] would have remained at 25%. The Senate bills in the 115th Congress did not contain any provisions related to premium rate subsidies. In the 116th

[68] Ibid., p. 9.

[69] Ibid., p. 5.

[70] FEMA, "National Flood Insurance Program (NFIP); Assistance to Private Sector Property Insurers, Notice of FY 2019 Arrangement," 83(52) *Federal Register* 11772-11778, March 16, 2018.

[71] FEMA, Federal Insurance and Mitigation Administration, Financial Assistance/ Subsidy Arrangement, October 1, 2019, https://www.fema.gov/media-library-data/1572968146685-72df1f4c423446afef8104ba79ee81c3/FY2020-WYO-Financial-Assistance-Subsidy-Arrangement.pdf.

[72] GAO, *Flood Insurance: Comprehensive Reform Could Improve Solvency and Enhance Resilience*, GAO-17-425, April 2017, p. 34, https://www.gao.gov/products/GAO-17-425.

[73] FEMA, *National Flood Insurance Program Report to Congress on Reinsuring NFIP Insurance Risk and Options for Privatizing the NFIP*, August 13, 2015, p. 58, http://www.floods.org/ace-files/documentlibrary/2012_NFIP_Reform/Reinsuring_NFIP_Insurance_Risk_and_Options_for_Privatizing_the_NFIP_Report.pdf.

[74] For a discussion of the rates at which NFIP subsidies can be phased out, see the section on Pricing and Premium Rate Structure in CRS Report R44593, *Introduction to the National Flood Insurance Program (NFIP)*, by Diane P. Horn and Baird Webel.

[75] Non-primary residences, non-residential properties, severe repetitive loss properties, properties with substantial cumulative damage, and properties with substantial damage or improvement after July 6, 2012.

Congress, H.R. 3167 would not change the rates at which subsidies can be phased out. S. 2187, Section 102, would prohibit FEMA from increasing the amount of covered costs above 9% per year on any policyholder during the five-year period beginning on the date of enactment. Covered costs include premiums, surcharges (including the surcharge for ICC coverage and the HFIAA surcharge), and the Federal Policy Fee. This would limit the rate of increase of covered costs for all categories of policies, not just policies for primary residences, and would be particularly significant for those policies where the pre-FIRM subsidy is currently being phased out at 25% per year.

FEMA is in the process of developing a redesigned risk rating system for the NFIP, known as Risk Rating 2.0.[76] The new premium rates are scheduled to go into effect on October 1, 2021, for all NFIP policies across the country. According to FEMA, Risk Rating 2.0 will reflect an individual property's risk and reflect more types of flood risk in rates. Premiums will be calculated based on the specific features of an individual property, including structural variables such as the foundation type of the structure, the height of the lowest floor of the structure relative to base flood elevation, and the replacement cost value of the structure. Risk Rating 2.0 will incorporate a broader range of flood frequencies and sources than the current rating system, as well as geographical variables such as the distance to water, the type and size of nearest bodies of water, and the elevation of the property relative to the flooding source. Risk Rating 2.0 will continue the overall policy of phasing out NFIP subsidies, but will not be able to increase rates annually beyond the limitations on annual premium increases which are set in statute.[77] As proposed, Risk Rating 2.0 will not eliminate the three categories of properties which pay less than the full risk-based rates, nor the process of phasing out subsidies which began with BW-12, but rate changes will not necessarily be uniform within each category. In general, Risk Rating 2.0 is expected to lead to the reduction of cross-subsidies between NFIP policyholders, and the eventual elimination of premium subsidies and cross-subsidies once all properties are paying the full risk-based rate. This should bring NFIP premiums closer to the premiums of private insurers and could potentially increase competition.

Regulatory Uncertainty

As addressed above, the rules on the acceptance of private insurance for the mandatory purchase requirement, and whether or not private flood insurance would count for continuous coverage, have had a significant impact on the market potential for private insurers.[78] Another driver of private sector concern is regulatory uncertainty at the state level. The role of state regulators would increase in a flood insurance market with increased private sector involvement, which could increase the burden of oversight. The involvement of 56 state and territorial insurance regulators is likely to add complexity and additional costs for insurers, lenders, or property owners.[79] For example, some private insurers cited the intervention of state regulators in

[76] For additional information on Risk Rating 2.0, see CRS Report R45999, *National Flood Insurance Program: The Current Rating Structure and Risk Rating 2.0*, by Diane P. Horn.

[77] 42 U.S.C. §4015(e).

[78] See FEMA, *National Flood Insurance Program Report to Congress on Reinsuring NFIP Insurance Risk and Options for Privatizing the NFIP*, August 13, 2015, p. 62, http://www.floods.org/ace-files/documentlibrary/2012_NFIP_Reform/Reinsuring_NFIP_Insurance_Risk_and_Options_for_Privatizing_the_NFIP_Report.pdf; and GAO, *Flood Insurance: Potential Barriers Cited to Increased Use of Private Insurance*, GAO-16-611, July 14, 2016, pp. 26-29, https://www.gao.gov/assets/680/678414.pdf.

[79] Ibid., p. 63.

controlling rates for wind insurance in Florida as a reason for withdrawing from that market.[80] However, this could also lead to the development of state-specific insurance solutions, which might better suit local social and economic conditions.[81] In the 115th Congress, H.R. 2874 and S. 1313 referenced state laws and regulations in their definition of private flood insurance that could meet the mandatory purchase requirements. Neither of the bills in the 116th Congress include any provisions related to state laws or regulation of private flood insurance.

Ability to Assess Flood Risk Accurately

Many insurers view the lack of access to NFIP data on flood losses and claims as a barrier to more private companies offering flood insurance. It is argued that increasing access to past NFIP claims data would allow private insurance companies to better estimate future losses and price flood insurance premiums, and ultimately to determine which properties they might be willing to insure.[82] However, FEMA's view is that the agency would need to address privacy concerns in order to provide property level information to insurers, because the Privacy Act of 1974[83] prohibits FEMA from releasing policy and claims data which contain personally identifiable information. Private insurers have also suggested that better flood risk assessment tools such as improved flood maps and inland and storm surge models are needed in order to price risks at the individual and portfolio level.[84] In the 115th Congress, H.R. 2874 would have required FEMA to make all NFIP claims data publicly available in a form that does not reveal personally identifiable information, while S. 1313 would have authorized FEMA to sell or license individual claims data while requiring FEMA to make aggregate claims data available. In the 116th Congress, H.R. 3167, Section 404, would allow FEMA to provide current and historical property-specific information on flood insurance program coverage, flood damage assessments, and payment of claims to private insurers, on the condition that private insurers provide the same information to FEMA, homeowners and home buyers. S. 2187, Section 305, would require FEMA to report on the feasibility of selling or licensing the use of historical structure-specific NFIP claims data to non-governmental entities, while reasonably protecting policyholder privacy.

Adequate Consumer Participation

Insurers need sufficient consumer participation to manage and diversify their risk exposure. Many private insurers have expressed the view that broader participation in the flood insurance market would be necessary to address adverse selection and maintain a sufficiently large risk pool.[85] A

[80] Ibid., p. 105.

[81] Ibid., p. 41.

[82] American Academy of Actuaries Flood Insurance Work Group, *The National Flood Insurance Program: Challenges and Solutions*, April 2017, p. 60, http://www.actuary.org/files/publications/FloodMonograph.04192017.pdf.

[83] P.L. 93-579, 5 U.S.C. §552a, as amended.

[84] See, for example, GAO, *Flood Insurance: Strategies for Increasing Private Sector Involvement*, 14-127, January 2, 2014, pp. 10-11, https://www.gao.gov/products/GAO-14-127; FEMA, *National Flood Insurance Program Report to Congress on Reinsuring NFIP Insurance Risk and Options for Privatizing the NFIP*, August 13, 2015, p. 61, http://www.floods.org/ace-files/documentlibrary/2012_NFIP_Reform/Reinsuring_NFIP_Insurance_Risk_and_Options_for_Privatizing_the_NFIP_Report.pdf; and Albert Kuller and Eleanor Gibson, *After the Storms: Harvey, Irma and Maria: Lessons Learned*, Lloyds, Market Insight Report 2018, May 24, 2018, pp. 1-30, https://www.lloyds.com/news-and-risk-insight/risk-reports/library/natural-environment/afterthestorms.

[85] GAO, *Flood Insurance: Strategies for Increasing Private Sector Involvement*, 14-127, January 2, 2014, p. 14, https://www.gao.gov/products/GAO-14-127.

long-standing objective of the NFIP has been to increase purchases of flood insurance policies, and this objective was the motivation for introducing the mandatory purchase requirement.

Despite the mandatory purchase requirement, not all covered mortgages carry the insurance as dictated, and no up-to-date data on national compliance rates with the mandatory purchase requirement are available. A 2006 study commissioned by FEMA found that compliance with this mandatory purchase requirement may be as low as 43% in some areas of the country (the Midwest), and as high as 88% in others (the West).[86] A 2017 study of flood insurance in New York City found that compliance with the mandatory purchase requirement by properties in the SFHA with mortgages increased from 61% in 2012 to 73% in 2016.[87] The escrowing of NFIP insurance premiums, which began in January 2016, may increase compliance with the mandatory purchase requirement more widely, but no data are yet available.

The mandatory purchase requirement could potentially be expanded to more (or all) mortgage loans made by federally regulated lending institutions for properties in communities participating in the NFIP.[88] Another possible option would be to require all properties within the SFHA to have flood insurance, not just those with federally backed mortgages.[89] Consumer participation could also be increased if the federal government were to mandate that homeowners' insurance policies include flood coverage or require all homeowners to purchase flood insurance.[90] All four 115th Congress bills contained provisions for some form of study to assess the compliance with the mandatory purchase requirement. H.R. 2874 would also have increased civil penalties on lenders for failing to enforce the mandatory purchase requirement. In the 116th Congress, both H.R. 3167, Section 408, and S. 2187, Section 108, would require GAO to determine the percentages of properties with federally backed mortgages located in SFHAs that satisfy the mandatory purchase requirement, and the percentage of properties with federally backed mortgages located in the 500-year floodplain[91] that would satisfy the mandatory purchase requirement if the mandatory purchase requirement applied to such properties. Both bills would also require GAO to conduct a study to address how to increase participation rates through programmatic and regulatory changes.

[86] Lloyd Dixon, Noreen Clancy, and Seth A. Seabury, et al., *The National Flood Insurance Program's Market Penetration Rate: Estimates and Policy Implications*, RAND Corporation, prepared as part of the Evaluation of the National Flood Insurance Program, February 2006, p. 23, https://www.fema.gov/media-library-data/20130726-1602-20490-2804/nfip_eval_market_penetration_rate.pdf.

[87] Lloyd Dixon, Noreen Clancy, and Benjamin M. Miller, et al., *The Cost and Affordability of Flood Insurance in New York City: Economic Impacts of Rising Premiums and Policy Options for One- to Four- Family Homes*, Rand Corporation, RAND RR1776, Santa Monica, CA, April 2017, pp. 15-18, https://www.rand.org/pubs/research_reports/RR1776.html.

[88] NFIP, *Report to Congress on Reinsuring NFIP Insurance Risk and Options for Privatizing the NFIP*, Appendix C: Flood Insurance Risk Study: Options for Privatizing the NFIP, August 13, 2015, p. 86, https://www.floods.org/ace-files/documentlibrary/2012_NFIP_Reform/Reinsuring_NFIP_Insurance_Risk_and_Options_for_Privatizing_the_NFIP_Report.pdf.

[89] Association of State Floodplain Managers, Inc., *Rethinking the NFIP*, ASFPM Comments on NFIP Reform, January 11, 2011, p. 5, http://www.floods.org/ace-files/documentlibrary/National_Policy/Rethinking_the_NFIP_Comments_from_ASFPM_1-11-11.pdf.

[90] GAO, *Flood Insurance: Strategies for Increasing Private Sector Involvement*, 14-127, January 2, 2014, p. 22, https://www.gao.gov/products/GAO-14-127.

[91] The 500-year floodplain is defined by FEMA as an area with a 0.2% or greater risk of flooding every year.

Potential Effects of Increased Private Sector Involvement in the Flood Market

Increased Consumer Choice

Current NFIP policies offer a relatively limited array of coverages, particularly compared to what is available in private markets for similar insurance against perils other than floods. Private insurance companies could potentially compete with the NFIP by offering coverage not available under the NFIP, such as business interruption insurance, living expenses while a property is being repaired, basement coverage, coverage of other structures on a property, and/or by offering policies with coverage limits higher than the NFIP. The NFIP currently also has a 30-day waiting period in almost all cases before the insurance coverage goes into effect,[92] whereas private insurance companies may have a shorter waiting period. Private companies could also offer flood coverage as an add-on to a standard homeowners' policy, which could eliminate the current problem of distinguishing between flood damage (which is covered by the NFIP) and wind damage (which is often covered by standard homeowners' insurance). Unlike the NFIP, private flood insurance companies may also issue a policy without necessarily requiring elevation certificates, perhaps by using new technology to measure the elevation of individual structures.

Cheaper Flood Insurance

Since some properties receive lower NFIP rates due to cross subsidies from other NFIP policyholders, it seems likely that some of the non-subsidized NFIP policyholders would be able to obtain less expensive flood insurance from private insurers. Private insurers may also be able to offer premiums more closely tied to individual risks than the NFIP currently does, which would provide lower premiums for some policyholders. Quantifying the potential savings for some policyholders from private insurance is, however, difficult, as the amount and extent of cross-subsidization within the NFIP is not fully known. One example of an attempt to provide estimates of NFIP versus private insurance is a modeling exercise carried out by two private companies, Milliman and KatRisk, which looked at premiums for single-family homes in Louisiana, Florida, and Texas. Their modeling suggested that 77% of single-family homes in Florida, 69% in Louisiana, and 92% in Texas would pay less with a private policy than with the NFIP; however, 14% in Florida, 21% in Louisiana, and 5% in Texas would pay over twice as much.[93] Milliman did not provide any details of the coverage offered by these private policies, nor the basis on which their figures were estimated.

Variable Consumer Protections

The consumer protections associated with private policies are likely to be enforced at a state level and will therefore be variable; some states may offer a higher level of protection than others. Because private insurers are free to accept or reject potential policyholders as necessary in order to manage their risk portfolio, private insurers may not necessarily renew a policy. A private flood

[92] See FEMA, *Flood Insurance Manual, Before You Start* Revised October 2019, pp. 2-10 to 2-13, https://www.fema.gov/media-library-data/1569523554826-8c1d47a539c8e21b3b8f80cf7b108fae/2_before-you_start_oct2019.pdf.

[93] Nancy P. Watkins, *Could Private Flood Insurance Be Cheaper Than the NFIP?* Milliman, Milliman Briefing Paper, San Francisco, CA, July 10, 2017, pp. 1-2, http://www.milliman.com/insight/2017/Could-private-flood-insurance-be-cheaper-than-the-NFIP/.

insurance policy might be less expensive than an NFIP policy, but it might also offer less extensive coverage, which a policyholder may not realize until they make a claim following a flood. Unlike the NFIP, the language in private flood insurance policies is not standardized and has not yet been tested in court in the same way as, for example, homeowners' insurance. Thus there may be greater variability in claims outcomes for consumers in the early years of private flood insurance penetration.

Adverse Selection

Private sector competition might increase the financial exposure and volatility of the NFIP, as private markets will likely seek out policies that offer the greatest likelihood of profit. In the most extreme case, the private market may "cherry-pick" (i.e., adversely select against the NFIP) the profitable, lower-risk NFIP policies that are "overpriced" either due to cross-subsidization or imprecise flood insurance rate structures, particularly when there is pricing inefficiency in favor of the customer.[94] This could leave the NFIP with a higher density of actuarially unsound policies that are being directly subsidized or benefiting from cross-subsidization. Because the NFIP cannot refuse to write a policy, those properties that are considered "undesirable" by private insurers are likely to remain in the NFIP portfolio—private insurers will not compete against the NFIP for policies that are inadequately priced from their perspective.[95] Private insurers, as profit-seeking entities, are unlikely independently to price flood insurance policies in a way that ensures affordable premiums as a purposeful goal, although some private policies could be less expensive than NFIP policies. It is likely that the NFIP would be left with a higher proportion of subsidized policies, which may become less viable in a competitive market.[96]

The extent of such "cherry picking" is uncertain with some arguing that it would have little effect.[97] However, evidence from the UK flood insurance market suggests that even in an entirely private market "cherry picking" can be difficult to avoid. Interviews of private insurers indicate that one of the key drivers for the introduction of Flood Re, the UK private flood insurance scheme which was introduced in 2016, was the emergence of new entrants in the flood insurance market after 2000. These new entrants had little or no existing high-flood-risk business and no commitment to continue to insure this business under the terms of the then-existing informal agreement with the government. This gave them a competitive advantage, as they could choose to select the more profitable lower-risk business. One driver for change therefore was that Flood Re would include these new entrants and force them to contribute by charging their clients for the cross-subsidy for Flood Re, leveling the playing field between the private insurers.[98]

A significant increase in private flood insurance policies that "depopulates" the NFIP may also undermine the NFIP's ability to generate revenue, reducing the amount of past borrowing that can

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[94] David Altmaier, Andy Case, and Mike Chaney, et al., *Flood Risk and Insurance*, NAIC Center for Insurance Policy and Research, CIPR Study Series 2017-1, April 2017, p. 47, http://www.naic.org/documents/cipr_study_1704_flood_risk.pdf.

[95] FEMA, *National Flood Insurance Program Report to Congress on Reinsuring NFIP Insurance Risk and Options for Privatizing the NFIP*, August 13, 2015, p. 85, http://www.floods.org/ace-files/documentlibrary/2012_NFIP_Reform/Reinsuring_NFIP_Insurance_Risk_and_Options_for_Privatizing_the_NFIP_Report.pdf.

[96] American Academy of Actuaries Flood Insurance Work Group, *The National Flood Insurance Program: Challenges and Solutions*, April 2017, p. 66, http://www.actuary.org/files/publications/FloodMonograph.04192017.pdf.

[97] See, for example, R.J. Lehman, "Private Flood Insurance Market Is Getting Bigger, More Competitive, Less Profitable," *Insurance Journal*, March 18, 2018, at https://www.insurancejournal.com/blogs/right-street/2018/03/18/483689.htm.

[98] Edmund C. Penning-Rowsell, Sally Priest, and Clare Johnson, "The Evolution of UK Flood Insurance: Incremental Change Over Six Decades," *International Journal of Water Resources Development*, vol. 30, no. 4 (2014), pp. 694-713.

be repaid or extending the time required to repay the debt. If the number of NFIP policies decreases, it would likely become increasingly difficult for the remaining NFIP policyholders to subsidize policies, raising prices for the non-subsidized policyholders and thus accelerating the move to private insurance. In the long term the program could be left as a "residual market" for subsidized or high-risk properties. Residual market mechanisms are used in areas such as auto insurance, where consumers may be required to purchase insurance, but higher risk individuals may be unable to purchase it from regular insurers. The exact form of residual market mechanisms vary in different states and for different types of insurance, but they typically require some form of outside support either from the government or from insurers themselves.

In the 115th Congress, S. 1313 would have required FEMA, within two years of enactment, to report on the extent to which the properties for which private flood insurance is purchased tend to be at a lower risk than properties for which NFIP policies are purchased (i.e., the extent of adverse selection), by detailing the risk classifications of the private flood insurance policies. S. 1313 would also have provided the FEMA Administrator the power to limit the participation of WYO companies in the broader flood insurance marketplace if the Administrator determined that private insurance adversely impacts the NFIP. Neither of the bills in the 116th Congress include any provisions related to adverse selection.

Issues for NFIP Flood Mapping and Floodplain Management

If the number of NFIP policyholders were to decrease significantly, it might also be difficult to support the NFIP's functions of reducing flood risk through flood mapping and floodplain management.[99] NFIP flood mapping is currently funded in two ways, through (1) annual discretionary appropriations; and (2) discretionary spending authority from offsetting money collected from the Federal Policy Fee (FPF).[100] The FPF is paid to FEMA and deposited in the National Flood Insurance Fund (NFIF). The income from the FPF is designated to pay for floodplain mapping activities, floodplain management programs, and certain administrative expenses.[101] About 66% of the resources from the FPF are allocated to flood mapping, with floodplain management receiving about 19% of the overall income from the FPF.[102] To the extent that the private flood insurance market grows and policies move from the NFIP to private insurers, FEMA will no longer collect the FPF on those policies and less revenue will be available for floodplain mapping and management. Concerns have been raised about maintaining the activities funded by the FPF, with some stakeholders arguing that a form of FPF equivalency, or some form of user fee, should be applied to private flood insurance.[103] In the 115th Congress, both S. 1313 and S. 1368 contained mechanisms by which private insurance companies could have contributed to the costs of floodplain mapping in lieu of paying the FPF. In the 116th Congress, S. 2187, Section 303, would require FEMA to develop a fee schedule based on recovering the actual costs of providing FIRMs and charge any private entity an appropriate fee for use of such maps.

[99] For a further discussion of the NFIP's floodplain management and mapping functions, see CRS Report R46095, *The National Flood Insurance Program: Selected Issues and Legislation in the 116th Congress*, by Diane P. Horn and Baird Webel.

[100] For an additional explanation of NFIP funding, including the funding for mapping, see CRS Report R44593, *Introduction to the National Flood Insurance Program (NFIP)*, by Diane P. Horn and Baird Webel.

[101] 42 U.S.C. §4014(a)(1)(B)(iii).

[102] Email correspondence from FEMA Congressional Affairs staff, December 6, 2016.

[103] Association of State Floodplain Managers, *ASFPM Detailed Priorities for NFIP Reauthorization and Reform*, June 17, 2016, p. 1, http://www.floods.org/ace-images/Priorities.pdf.

Enforcement of floodplain management standards could be more challenging within a private flood insurance system, as the current system makes the availability of NFIP insurance in a community contingent on the implementation of floodplain management standards. For example, the Association of State Floodplain Managers (ASFPM) has expressed concerns that the widespread availability of private flood insurance could lead some communities to drop out of the NFIP and rescind some of the floodplain management standards and codes they had adopted, leading to more at-risk development in flood hazard areas.[104] ASFPM suggested that this issue could be addressed by allowing private policies to meet the mandatory purchase requirement only if they were sold in participating NFIP communities.[105] FEMA suggested that access to federal disaster assistance could be made partially contingent on the adoption of appropriate mitigation policies, but noted that this approach could be politically challenging.[106] However, a positive consequence is that government investment in mitigation could increase private market participation by reducing the flood exposure of high-risk properties and thereby increasing the number of properties that private insurers would be willing to cover.[107]

Concluding Comments

The policy debate surrounding NFIP and private insurance has evolved over time. The discussion in 2012 was framed in the context of privatization of the NFIP and actions that might be taken to create conditions for private sector involvement. One of the primary interests of Congress at the time was to reduce the federal government's role in flood insurance by transferring its exposure to the private sector,[108] with an expectation that a realignment of roles would allow the federal government to focus on flood risk mitigation while private markets focused on providing flood insurance.[109] One argument for increasing private sector participation in the U.S. flood market was that competition should lead to innovation in flood risk analytics and modeling and produce new flood insurance products that would better meet customer needs and lead to greater levels of insurance market penetration.[110] In fact, private sector flood risk analytics and modeling have improved significantly before any sizable entry of private insurers into the market. Another argument was that, in contrast to the NFIP, which cannot diversify its portfolio of flood risk by insuring unrelated risks, the insurance industry can diversify catastrophic risks with uncorrelated or less correlated risks from other perils, other geographic regions, non-catastrophic risks, or risks from unrelated lines of business.[111]

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[104] Association of State Floodplain Managers, *ASFPM's Comments on Loans in Areas Having Special Flood Hazards - Private Flood Insurance Joint Notice of Proposed Rulemaking*, January 6, 2017, pp. 1-4, http://www.floods.org/ace-images/PrivateFloodIns_OCC_Jan2017.pdf.

[105] Ibid.

[106] FEMA, *National Flood Insurance Program Report to Congress on Reinsuring NFIP Insurance Risk and Options for Privatizing the NFIP*, August 13, 2015, p. 92, http://www.floods.org/ace-files/documentlibrary/2012_NFIP_Reform/Reinsuring_NFIP_Insurance_Risk_and_Options_for_Privatizing_the_NFIP_Report.pdf.

[107] Ibid., p. 108,

[108] Ibid., p. 2.

[109] Ibid., p. 52.

[110] FEMA, *National Flood Insurance Program Report to Congress on Reinsuring NFIP Insurance Risk and Options for Privatizing the NFIP*, August 13, 2015, p. 50, http://www.floods.org/ace-files/documentlibrary/2012_NFIP_Reform/Reinsuring_NFIP_Insurance_Risk_and_Options_for_Privatizing_the_NFIP_Report.pdf.

[111] Ibid., p. 51.

FEMA considered a range of concrete steps by which the barriers to private sector involvement could be addressed.[112] Two of these have been introduced: the purchase of reinsurance and reporting to make premium subsidies and cross-subsidies more transparent.[113] The reduction of premium subsidies for some properties will occur with the introduction of Rating 2.0.[114] Although BW-12 directed FEMA to make a recommendation about the best manner in which to accomplish the privatization of the NFIP, FEMA presented the report without a recommendation, arguing that any privatization strategy is complex and involves significant policy decisions that would require input from a variety of stakeholders. They concluded that there is no single, clear solution; it is heavily politicized; and harsh criticism of any change is inevitable.[115]

Currently the discussion is more focused on sharing risk and increasing penetration rates, with the recognition that neither the NFIP nor the private sector is likely to be able to write all of the policies needed to cover all of the flood risk in the United States. FEMA has identified the need to increase flood insurance coverage across the nation as a major priority for NFIP reauthorization, and this also forms a key element of their 2018-2022 strategic plan.[116] FEMA has developed a "moonshot" with the goal of doubling flood insurance coverage by 2023 through the increased sale of both NFIP and private policies.

FEMA's view is that both the NFIP and an expanded private market will be needed to increase flood insurance coverage for the nation and reduce uninsured flood losses.[117] However, the private market is unlikely to expand significantly without congressional action. The concerns of private companies related to the mandatory purchase requirement and continuous coverage and the concerns of some Members of Congress about adverse selection are among the most pressing issues likely to be addressed in any long-term NFIP reauthorization.

[112] Ibid., pp. 82-84.

[113] The requirement in §28 of HFIAA (P.L. 113-89, 128 Stat. 1033) that the Administrator "clearly communicate full flood risk determinations to individual property owners regardless of whether their premium rates are full actuarial rates."

[114] For a full discussion of NFIP subsidies and cross-subsidies, see the section on Pricing and Premium Rate Structure in CRS Report R44593, *Introduction to the National Flood Insurance Program (NFIP)*, by Diane P. Horn and Baird Webel; the section on Premiums Subsidies and Cross-Subsidies in CRS Report R46095, *The National Flood Insurance Program: Selected Issues and Legislation in the 116th Congress*, by Diane P. Horn and Baird Webel; and the section on Premium Subsidies and Cross-Subsidies in CRS Report R45999, *National Flood Insurance Program: The Current Rating Structure and Risk Rating 2.0*, by Diane P. Horn.

[115] FEMA, *National Flood Insurance Program Report to Congress on Reinsuring NFIP Insurance Risk and Options for Privatizing the NFIP*, August 13, 2015, p. 84, http://www.floods.org/ace-files/documentlibrary/2012_NFIP_Reform/Reinsuring_NFIP_Insurance_Risk_and_Options_for_Privatizing_the_NFIP_Report.pdf.

[116] FEMA, *2018-2022 Strategic Plan*, https://www.fema.gov/media-library/assets/documents/160940.

[117] Roy Wright, *Keynote Remarks to National Flood Conference*, May 1, 2017, https://www.fema.gov/media-library-data/1493727672905-9f2950b534607c3f9ef3e771d28a81e2/PreparedRemarks_Wright_NationalFloodConference_May2017.pdf.

Appendix. Provisions Related to Private Flood Insurance in Legislation in the 116th Congress

The provisions in the 116th Congress legislation that relate to private flood insurance, and the issues raised as barriers to private sector involvement, are summarized below and compared side-by-side in **Table A-1**. S. 2187 also includes provisions related to administrative reforms of the NFIP, some of which may be relevant to private insurance companies, which are not described in this report. Comparable administrative reforms are included in H.R. 3111, the National Flood Insurance Program Administrative Reform Act of 2019, rather than H.R. 3167.

H.R. 3167, National Flood Insurance Program Reauthorization Act of 2019

- H.R. 3167, Section 107, would direct FEMA, if an NFIP policyholder switches to private flood insurance but has already paid the NFIP premiums for the whole year up front, to provide a prorated refund of the NFIP premium. This section would also direct that Increased Cost of Compliance (ICC) premiums[118] would not be refunded if measures had been implemented using ICC coverage, and that premiums would not be refunded if a claim has been paid or is pending under the policy term for which the refund is sought.
- H.R. 3167, Section 401, would direct FEMA to consider private flood insurance that satisfies the mandatory purchase requirement as also satisfying the continuous coverage requirement to keep NFIP premium subsidies in place.
- H.R. 3167, Section 404, would allow FEMA to provide current and historical property-specific information on flood insurance program coverage, flood damage assessments, and payment of claims to private insurers, on the condition that private insurers provide the same information to FEMA, homeowners, and home buyers. Section 404 could potentially create conflicts with the Privacy Act of 1974, which prohibits federal agencies from releasing data which contains Personally Identifiable Information. In addition, although these data could be used to better inform the participation of private insurers in offering private flood insurance, the availability of NFIP data could make it easier for private insurers to identify the NFIP policies that are "overpriced" due to explicit cross-subsidization or imprecise flood insurance rate structures. Private insurers may adversely select such properties, while the government would likely retain the policies that benefit from those subsidies and imprecisions, potentially increasing the deficit of the NFIP.[119]
- H.R. 3167, Section 406, would require FEMA annually to evaluate ceding a portion of the risk of the NFIP to the private reinsurance or capital markets.
- H.R. 3167, Section 407, would give FEMA the authority to terminate any WYO arrangement in its entirety upon 30 days written notice for (1) fraud or

[118] The NFIP requires most policyholders, excluding condominium units and contents-only policies, to purchase Increased Cost of Compliance (ICC) coverage, which is in effect a separate insurance policy to offset the expense of complying with more rigorous building code standards when local ordinances require them to do so. ICC coverage provides an amount up to $30,000 in payments for certain eligible expenses.

[184] American Academy of Actuaries Flood Insurance Work Group, *The National Flood Insurance Program: Challenges and Solutions*, April 2017, p. 79, http://www.actuary.org/files/publications/FloodMonograph.04192017.pdf.

misrepresentation; (2) nonpayment to FEMA of any amount due; or (3) material failure to comply with the requirements of the arrangement or with the written standards, procedures, or guidance by FEMA.

- H.R. 3167, Section 408, would require GAO to determine the percentages of properties with federally backed mortgages located in SFHAs that satisfy the mandatory purchase requirement, and the percentage of properties with federally backed mortgages located in the 500-year floodplain[120] that would satisfy the mandatory purchase requirement if the mandatory purchase requirement applied to such properties.

S. 2187, National Flood Insurance Program Reauthorization and Reform Act of 2019

- S. 2187, Section 102, would prohibit FEMA from increasing the amount of covered costs above 9% per year on any policyholder during the five-year period beginning on the date of enactment. Covered costs include premiums, surcharges (including the surcharge for ICC coverage and the HFIAA surcharge), and the Federal Policy Fee. This would limit the rate of increase of covered costs for all categories of policies, not just policies for primary residences, and would be particularly significant for those policies where the pre-FIRM subsidy is currently being phased out at 25% per year. This cap on premium increases could potentially limit FEMA's ability to implement rate increases under Risk Rating 2.0. Section 102 would also amend the basis on which premiums are determined so that the calculation of an average historical loss year[121] would exclude catastrophic loss years. This would probably lower premiums for all policyholders.
- S. 2187, Section 108, would require GAO to determine the percentages of properties with federally backed mortgages located in SFHAs that satisfy the mandatory purchase requirement, and the percentage of properties with federally backed mortgages located in the 500-year floodplain that would satisfy the mandatory purchase requirement if the mandatory purchase requirement applied to such properties.
- S. 2187, Section 302, would establish that the total amount of reimbursement paid to WYO companies could not be greater than 22.46% of the aggregate amount of premiums charged by the company. It would also require FEMA to ensure that the commission paid by a WYO company to agents of the company would not be less than 15%.

[120] The 500-year floodplain is defined by FEMA as an area with a 0.2% or greater risk of flooding every year.

[121] The average historical loss year is the minimum target amount that the NFIP needs to collect from all premiums to cover at least average annual losses, as determined by historical data. FEMA uses this estimate to calculate the premium that would be sufficient to pay for the average level of losses that occurred in past years and help set the rate level for subsidized flood insurance policies. When the NFIP was originally established, the average historical loss year did not include catastrophic loss years. BW-12 directed FEMA to review the basis on which it was setting NFIP rates, with specific attention to ensuring that catastrophic loss years would be fully incorporated into the NFIP calculation of average historical loss year. See GAO, *Financial Challenges Underscore Need for Improved Oversight of Mitigation Programs and Key Contracts*, GAO-08-457, June 16, 2008, p. 19, http://www.crs.gov/reports/IN10835?source=HPinsight; and National Research Council of the National Academies, *Affordability of National Flood Insurance Program Premiums: Report 1*, 2015, p. 42, http://www.nap.edu/catalog/21709/affordability-of-national-flood-insurance-program-premiums-report-1.

- S. 2187, Section 303, would require FEMA to develop a fee schedule based on recovering the actual costs of providing FIRMs and charge any private entity an appropriate fee for use of such maps. This requirement could provide a mechanism by which private insurance companies could contribute to the costs of floodplain mapping in lieu of paying the FPF.
- S. 2187, Section 304, would require FEMA, within 12 months of enactment, to develop a schedule to determine the actual costs of WYO companies and reimburse the WYO companies only for the actual costs of the service or products. It would require that all reimbursements made to WYO companies be made public, including a description of the product or service provided to which the reimbursement pertains.
- S. 2187, Section 305, would require FEMA to report on the feasibility of selling or licensing the use of historical structure-specific NFIP claims data to non-governmental entities, while reasonably protecting policyholder privacy.
- S. 2187, Section 405, would require FEMA to establish penalties for underpayment of claims by WYO companies that are not less than the penalty for overpayment of a claim.
- S. 2187, Section 408, would give FEMA the authority to direct a WYO company, on 14 days' notice, to terminate a contract or other agreement with any covered entity[122] that provides services to the WYO company, if FEMA determines that the covered entity has engaged in conduct that is detrimental to the NFIP.
- S. 2187, Section 415, would authorize FEMA to create a pilot program under which WYO companies and NFIP direct servicers would be required to investigate pre-existing structural conditions that might result in the denial of an NFIP claim, at the request of a policyholder or potential policyholder, before providing or renewing flood insurance coverage.

[122] A covered entity is defined in S. 2187, §408, as any attorney, law firm, consultant, or third-party company that provides services to a WYO company.

Table A-1. Provisions Related to Private Flood Insurance in Legislation in the 116th Congress

Provision	H.R. 3167	S. 2187
Continuous coverage	§401. Would direct FEMA to consider private flood insurance that satisfies the mandatory purchase requirement as also satisfying the continuous coverage requirement to keep NFIP premium subsidies in place.	No comparable provisions
Cap on premium increases	No comparable provisions	§102. Would prohibit FEMA from increasing the amount of covered costs[a] above 9% per year on any policyholder during the five-year period beginning on the date of enactment.
Risk transfer	§406. Would require FEMA annually to evaluate ceding a portion of the risk of the NFIP to the private reinsurance or capital markets, if the Administrator determines that the rates and terms are reasonable and doing so would further the development and maintenance of a sound financial framework for the NFIP.	No comparable provisions
WYO allowance	No comparable provisions	§302. Would establish that the total amount of reimbursement paid to WYO companies could not be greater than 22.46% of the aggregate amount of premiums charged by the company.
WYO costs	No comparable provisions	§302. Would require FEMA to ensure that the commission paid by a WYO company to agents of the company would not be less than 15%. §304. Would require FEMA, within 12 months of enactment, to develop a schedule to determine the actual costs of WYO companies and reimburse the WYO companies only for the actual costs of the service or products. Would also require that all reimbursements made to WYO companies be made public, including a description of the product or service provided to which the reimbursement pertains.
WYO pilot program	No comparable provisions	§415. Would authorize FEMA to create a pilot program under which WYO companies and NFIP direct servicers would be required to investigate pre-existing structural conditions that might result in the denial of an NFIP claim, at the request of a policyholder or potential policyholder, before providing or renewing flood insurance coverage.

Provision	H.R. 3167	S. 2187
WYO penalties	No comparable provisions	§405. Would require FEMA to establish penalties for underpayment of claims by WYO companies that are not less than the penalty for overpayment of a claim.
	§407. Would give FEMA the authority to terminate any WYO arrangement in its entirety upon 30 days written notice for (1) fraud or misrepresentation; (2) nonpayment to FEMA of any amount due; or (3) material failure to comply with the requirements of the arrangement or with the written standards, procedures, or guidance by FEMA.	§408. Would give FEMA the authority to direct a WYO company, on 14 days' notice, to terminate a contract or other agreement with any covered entity[b] that provides services to the WYO company, if FEMA determines that the covered entity has engaged in conduct that is detrimental to the NFIP.
NFIP claims data	§404. Would allow FEMA to provide current and historical property-specific information on flood insurance program coverage, flood damage assessments, and payment of claims to private insurers, on the condition that private insurers provide the same information to FEMA, homeowners, and home buyers.	§305. Would require FEMA to report on the feasibility of selling or licensing the use of historical structure-specific NFIP claims data to non-governmental entities, while reasonably protecting policyholder privacy.
Funding for flood mapping	No comparable provisions	§303. Would require FEMA to develop a fee schedule based on recovering the actual costs of providing FIRMs and charge any private entity an appropriate fee for use of such maps.
Study of compliance with mandatory purchase requirement	§408. Would require GAO to determine the percentages of properties with federally backed mortgages located in SFHAs that satisfy the mandatory purchase requirement, and the percentage of properties with federally backed mortgages located in the 500-year floodplain that would satisfy the mandatory purchase requirement if the mandatory purchase requirement applied to such properties.	§108. Would require GAO to determine the percentages of properties with federally backed mortgages located in SFHAs that satisfy the mandatory purchase requirement, and the percentage of properties with federally backed mortgages located in the 500-year floodplain that would satisfy the mandatory purchase requirement if the mandatory purchase requirement applied to such properties.

Source: CRS analysis of legislation from http://www.congress.gov.

Notes: H.R. 3167, as reported by the House Financial Services Committee (H.Rept. 116-262, Part I).

a. Covered costs include premiums, surcharges (including the surcharge for ICC coverage and the HFIAA surcharge), and the Federal Policy Fee.

b. A covered entity is defined as any attorney, law firm, consultant, or third-party company that provides services to a WYO company.

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