Challenges in Reforming the National Flood Insurance Program (NFIP)

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Then: 1966 Vision for the NFIP

“Flood insurance is viewed as both a means of helping the individual bear more easily the risks of flood damage..., and equally, as a means of discouraging unwise occupancy of flood prone areas”

“...moreover, some continuing Federal subsidy will also be necessary to a comparably small number of present occupants of high risk areas. Otherwise the cost of their insurance will be more than they can bear...”

“The insurance program should be designed to encourage construction in locations where there is no special flood hazard”

Report to the President on recommendation for establishing NFIP - Secretary of the Department of Housing and Urban Development (HUD) August 1966
Now: How It Played Out

- Federal policy has not prevented development in high risk areas
- Flood insurance available in more than 22,000 communities
- 1,368 communities participate in the Community Rating System, accounting for 68% of policies
- Lender compliance for mandatory purchase ranges from 50-75%
- Half of all flood damage occurs outside the Special Flood Hazard Area (SFHA)
- Market penetration outside the SFHA is only about 1%

- Flood policies in force: 5,133,036
- Insurance in force: $1,251,578,068,030
- Written Premium: $3,541,816,175
- Average Premium: $690
- Outstanding Debt: $23 billion
- Repetitive loss properties: 127,702
  - Includes 15,035 severe repetitive loss properties
- 21% of policies are rated at less than actuarial rates
- 1% of insured properties represent 30% of all claims
NFIP Subsidized Policies by State and Community

Legend

Total Subsidized Policies by State
NFIP Flood Insurance

- 124 - 5,000
- 5,001 - 10,000
- 10,001 - 25,000
- 25,001 - 100,000
- Over 100,000
Interactions & interdependencies between the NFIP’s four functional areas create sustainable & mutually reinforcing reform.
Legislative Reforms

- **July 2012**: Biggert-Waters Flood Insurance Reform Act
- **October 2012**: Hurricane Sandy
- **March 2014**: Homeowner Flood Insurance Affordability Act
- **Summer 2017**: NFIP Re-authorization

Dramatic flood insurance increases could force residents to flee the coast, restoration officials say.

Fugate: FEMA has no authority to delay or lessen flood insurance rate increases.

Cost of Flood Insurance Rises, Along With Worries

- Move to full actuarial rates to reflect risk
- End subsidies
- Stop grandfathering
- Affordability
- Keep grandfathering
- Redesign claims and appeals process
- Stop or slow rate increases
- Improve communications

Make the program financially sound
Thinking About the Problem

System 1 operates automatically and quickly with little or no effort

- Individuals use simple associations including emotional reactions
- Highlight importance of recent past experience
- Basis for systematic judgmental biases and simplified decision rules

System 2 allocates attention to effortful and intentional mental activities

- Recognizes relevant interconnectedness and need for coordination
- Focuses on long-term strategies for coping with extreme events
- Individuals undertake trade-offs implicit in benefit-cost analysis
12% of respondents are not sure if their community is vulnerable to floods

**Using Risk as a Pricing Function**

**Risk**

Price can influence a property owner’s understanding of their risk

**Pricing**

Does property owner have the ability to pay? If not, who pays?
“Flood insurance can promote the public interest by providing appropriate protection against the perils of flood losses and encouraging sound land use by minimizing exposure of property to flood losses. The objectives of a flood insurance program should be integrally related to a unified national program for floodplain management.”

- Congress, National Flood Insurance Act of 1968
Privatization encompasses an array of options

Flood Insurance Privatization Spectrum

**TODAY—Write Your Own (WYO)**
FEMA partners WYO companies who sell NFIP insurance for the government

**Government Exclusively Sells Flood Insurance**

**Private Sector Exclusively Sells Flood Insurance**

**Greater Secondary Market**

**Reinsurance and ILS**
What is the Right Answer?

- How do we address the competing lenses and perspectives?
- Should the government be in this business?
- What would happen if the government were to get out?
- What should the government’s role be?
- What does the future look like?
  - Affordability
  - Social aspects of mitigation and insurance
  - Fiscal responsibility
  - Greater secondary market