S. HRG. 114–617

HOW FLOOD INSURANCE RATE INCREASES AND FLOOD MAPPING POLICY CHANGES WILL IMPACT SMALL BUSINESSES AND ECONOMIC GROWTH

FIELD HEARING

BEFORE THE

COMMITTEE ON SMALL BUSINESS AND ENTREPRENEURSHIP UNITED STATES SENATE

ONE HUNDRED FOURTEENTH CONGRESS

FIRST SESSION

MAY 1, 2015

Printed for the Committee on Small Business and Entrepreneurship

Available via the World Wide Web: http://www.fdsys.gov

U.S. GOVERNMENT PUBLISHING OFFICE

23–875 PDF WASHINGTON : 2017

For sale by the Superintendent of Documents, U.S. Government Publishing Office
Internet: bookstore.gpo.gov Phone: toll free (866) 512–1800; DC area (202) 512–1800
Fax: (202) 512–2104 Mail: Stop IDCC, Washington, DC 20402–0001

COMMITTEE ON SMALL BUSINESS AND ENTREPRENEURSHIP

ONE HUNDRED FOURTEENTH CONGRESS

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HOW FLOOD INSURANCE RATE INCREASES AND FLOOD MAPPING POLICY CHANGES WILL IMPACT SMALL BUSINESSES AND ECONOMIC GROWTH

FRIDAY, MAY 1, 2015

UNIVERSITY OF NEW ORLEANS
New Orleans, LA.

The Committee met, pursuant to notice, at 9:55 a.m., at the Homer Hitt Alumni Center, University of New Orleans, 2000 Lakeshore Drive, Hon. David Vitter, Chairman of the Committee, presiding.

Present: Senator Vitter.

OPENING STATEMENT OF HON. DAVID VITTER, CHAIRMAN, AND A U.S. SENATOR FROM LOUISIANA

Chairman VITTER. Well, that's a pretty natural segue into hearing from our witnesses, and as I suggested, we have two panels of witnesses today, two witnesses from the Federal Government, who I will introduce in a minute, and then following our discussion with them, we'll have a second panel, three witnesses from Louisiana, including those representing the real estate market and small business.

But first we'll hear from Brad Kieserman. Brad serves as the FEMA Deputy Associate Administrator for Insurance. Prior to serving in this position, he was Acting Assistant Administrator for Recovery and as FEMA Chief Counsel.

Brad is a graduate of State University of New York. Received his JD magna cum laude from Columbus Law School at Catholic University, in DC.

And following Brad, we'll hear from Roy Wright. Roy is a native of California and serves as FEMA's Deputy Associate Administrator for Mitigation, where he's responsible for FEMA's risk analysis and risk reduction programs.

Roy holds a Master's of Public Administration from George Washington and a Bachelor's in Political Science from Asuza Pacific.

His joint testimony, with Mr. Kieserman, will discuss the impacts of NFIP on small businesses. And, again, Bill and I will specifically ask them to address the Executive Order. Thank you all both for being here and for your work, and Brad, we'll start with you.

[The prepared statement of Chairman Vitter follows:]

Chairman David Vitter Hearing Summary Statement

U.S. Senate Committee on Small Business and Entrepreneurship

"How Flood Insurance Rate Increases and Flood Mapping Policy Changes Will Impact Small Businesses and Economic Growth"

May 1, 2015

Good morning, and thank you for joining me for today's Senate Small Business Committee field hearing to discuss the impact of flood insurance rates on small businesses. We will dig into the details of the National Flood Insurance Program (NFIP) and the need to avoid unaffordable rate increases in Louisiana.

In my role as Chairman of the Senate Committee on Small Business and Entrepreneurship, I am making every effort to give small businesses a larger voice in Congress and to shape policies that will allow these businesses to succeed and find stability in the marketplace.

To fully understand the issues that the NFIP has historically created for homeowners and small businesses in the marketplace, it is important to have a basic understanding of the recent changes in our country's flood policy.

For the most part, flood protection is not a partisan issue in Congress. Responsible disaster recovery and flood protection always manages to garner a bipartisan coalition of supporters.

Nationally, there are nearly 5.5 million flood insurance policy holders, and after the Biggert-Waters Flood Insurance Reform Act was signed into law in 2012 to help make the program solvent after Hurricane Sandy, many of these people were outraged at dramatic increases in their premiums – and rightfully so.

Rates were so dramatic that some families faced 10 times the price of their previous premium (or higher in some cases), and it was not uncommon to hear horror stories of families paying $20,000-30,000 for a policy that was previously $2,000 or less.

I met with many Louisianians about this, including with folks from Bayou Gauche who asked me to hand deliver copies of their house keys to FEMA's headquarters because if Biggert-Waters was not changed, they would not be able to afford their mortgage.

The Federal Emergency Management Agency's (FEMA) mishandling of the Biggert-Waters Act implementation resulted in inaccurate rate hikes that placed the viability of the entire National Flood Insurance Program at risk and caused turmoil in the real estate market.

Not only did FEMA publish inaccurate flood maps that could have permanently devalued the Louisiana housing market, they would have completely wiped out the life savings of thousands of middle class homeowners and small business owners.

Bill Bubrig, a resident of Plaquemines Parish lives in a home that was constructed at or above the NFIP required elevation at the time of construction. In 2013, he wrote to me that his flood insurance annual premium was increasing from $633 to $28,544 for an insurance policy worth $250,000.

This is one of the many nightmare scenarios that we heard about on a weekly basis and occurred largely due to incorrect information that regional FEMA officials provided directly to policy holders in Louisiana.

Because of stories like these, it was clear that the NFIP needed an urgent fix to prevent homeowners and small businesses from losing their savings and homes.

In 2010, the NFIP expired four times for a total of 53 days, adding uncertainty to an already fragile housing market and delaying or canceling more than 1,400 home closings each day the program expired.

One of the major reasons for passing Biggert-Waters in the first place was to ensure that there was no lapse of coverage for policy holders. FEMA's failed implementation actually priced out policy holders by excessively high rate increases and would have also created a lapse in coverage for these people if they could not meet the payments.

Congress acted in a completely bipartisan fashion to pass a permanent legislative fix that provided relief to homeowners. Unfortunately, FEMA was not as quick to implement these reforms, but under congressional pressure devised a plan to refund excessive overpayments back to the policy holders.

Going forward, we need to find a way to deal with the solvency of the NFIP in a responsible way, but - at the same time - does not do so solely on the back of policyholders. We need to examine how FEMA spends every dollar of premiums paid into the system.

In closing, I would also like to welcome and introduce our two panels of witnesses. The first of which are representatives from FEMA. The second panel is made up of business leaders in the Southwest Louisiana community.

I appreciate you all taking time away from your jobs and businesses to share your experiences and concerns about the NFIP and how the program has affected your industries and communities.

Again, thank you for being here this morning, and I look forward to hearing from our witnesses.

STATEMENT OF BRAD J. KIESERMAN, DEPUTY ASSOCIATE ADMINISTRATOR FOR FEDERAL INSURANCE, FEDERAL EMERGENCY MANAGEMENT AGENCY, WASHINGTON, DC

Mr. KIESERMAN. Chairman Vitter and Senator Cassidy, thank you very much for having Deputy Associate Administrator Wright and I here today, and I really appreciate the opportunity to come and talk about flood insurance with you all, and we would ask that our statement be entered into the record.

So, I guess, you heard the Senator talk for a moment about my bio. The most important fact about my bio is that I was stationed here for two years and lived in Jefferson Parish, and my oldest son was born here. He referred to himself as the "Fresh Prince of New Orleans." Never actually been here as an adult, but we're working on that, so we'll see.

So having lived here, I do think I have a—not just having lived here, but having worked on the river for two years, I think I have some understanding of the complexity of the landscape when it comes to flood insurance.

So let me begin. I have prepared remarks, which I am not going to read. I'm just going to chat with you all for a few minutes. Then I'll turn it over to Mr. Wright.

First of all, flood risk, as you all know, is probably one of the most significant hazards in the United States. If you look from like 1980 to 2013, the United States suffered more than $260 billion in flood-related damages. That's one of the reasons we have a National Flood Insurance Program is because the market and the industry really can't afford to provide you, whether you're a small business or a residence, with affordable flood insurance.

So all these concerns that you've expressed about affordability are spot-on, and I thought that the Senators answered your questions exactly as I would have answered your questions. Better, in fact, Senator Cassidy. So I think the affordability issue is critical, right.

So this is why you have a National Flood Insurance Program that was never designed to be actuarially sound. It was always, by design, meant to be a subsidized program, and now, as we've gotten further and further into the program, Congress has determined that we need to move from subsidized rates to actuarially sound rates, and there's a lot of tension around this issue, and Senator Vitter was spot-on.

Congress heard what the people had to say and slowed down the rate increases and tried to make those more affordable, but in the end, as I think you all know, the rates are going up, and so the question is how do we manage that and what protection can you get from it, and how can you mitigate your risk.

I guess I would turn for a minute, because this is a—the hearing is focused on small businesses. I do want to focus on small business, for a second, and the reason for that is small businesses, as you all know, are the economic engines of our community. The statistics vary a little bit, but the best numbers I see tell me that 40 percent of small businesses affected by floods don't reopen, and that's because they can't afford to repair, to recover, their merchandise is damaged, they lose their customers, people move.

And so while a lot of what we do is talk about the flood insurance program as it relates to residences—and that's because over 91 percent of the policies in the United States are residential-type policies—but the fact of the matter is, here in Louisiana, here in Louisiana, 11 percent of the flood insurance policies in the state are nonresidential policies. They deal with businesses, churches, schools.

So the small business issue is particularly important here, and I know from having lived here that many of you simply—you can't relocate because your business is the water.

The gentleman earlier talked about oil and gas, the chemical industry, the seafood industry, fishermen—and I was in the Coast Guard when I lived here. I was a buoy tender. So I really couldn't relocate. I needed to be near the boat and get out on the water. So we understand that.

But that means that we've got to figure out how to price that risk and how to make those prices affordable, and that's a challenge.

The National Academy of Sciences is working on several reports right now on affordability, and they have issued the draft of the first report, and they're going to produce a second report that will help us understand how to get through the cost-benefit analysis.

But it's a challenging issue and I don't want to come here and make it seem like there's simple answers. I do believe strongly, though, that your elected representatives are aggressively working these issues. You see that they both have an incredible command of the issue here, and we, in the Executive Branch, are here to try to make sure that we execute the law in a way that protects the public and the community and also in a way that gets you affordable rates.

So I'll be happy to take any questions you have, and then I'll turn the mike over to Mr. Wright.

Chairman VITTER. Great, thank you. Roy.

Mr. KIESERMAN. Thank you, Senator.

STATEMENT OF ROY WRIGHT, DEPUTY ASSOCIATE ADMINISTRATOR FOR MITIGATION, FEDERAL EMERGENCY MANAGEMENT AGENCY, WASHINGTON, DC

Mr. WRIGHT. I appreciate the opportunity to join you, Chairman Vitter and Senator Cassidy, and like Mr. Kieserman, I'm committed to make sure that we're collaborating with you all and the communities to make sure that we deliver on our commitments through the National Flood Insurance Program.

Mr. Kieserman spoke to the elements of insurance and affordability. I'm really here on the other complement to that program related to the flood hazard mapping and floodplain management and how we deal with mitigation grants and incentives.

At NFIP, when we talk about this, this is 22,000 communities across the country that are in partnership with us related to this. We've partnered with them. We've seen this as really some of the charges that Senator Vitter led us through that led into putting in place revisions to our Levee Analysis Mapping Process that we did three years back, where we slowed down that mapping process. We put in place those local levee partnership teams, and we're ensuring that the lines on the map reflect the best data from the community.

And we know that the risk changes, and as it changes, we see lines move, and we see structures come in and come out. In any given year, we see, on average, about as many come in as come out.

We have some updates happening in Orleans and Jefferson Parish right now. As those maps in Orleans Parish move forward, over the next year, 77,000 structures are going to come out of the Special Flood Hazard area. They will no longer have that mandatory purchase requirement. The risks changed; our maps changed.

And so as we look at these elements, we want to make sure that we have worked with communities, we're reflecting the risk, and we're preparing for what is to come.

And so the law requires that, as we lead these programs, we identify those flood risks, we engage communities to increase their understanding. We want to make sure we're reflecting the best credible data available. We look to set those kind of standards related to future construction in that area of known flood risk.

And we want to make sure that when Federal funds are used for projects, in communities, that we do build them higher and stronger so that the taxpayer doesn't need to come back and pay for that same building twice, and I think there's some of those elements that we can share together.

And so, with that, I'll say thank you, and we're available for your questions on the topics throughout that we've talked about this morning.

[The prepared statement of Mr. Kieserman and Mr. Wright follows:]

STATEMENT

OF

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U.S. DEPARTMENT OF HOMELAND SECURITY

BEFORE
THE

COMMITTEE ON SMALL BUSINESS AND ENTREPRENEURSHIP
U.S. SENATE
NEW ORLEANS, LA

"HOW FLOOD INSURANCE RATE INCREASES AND FLOOD MAPPING POLICY CHANGES WILL IMPACT SMALL BUSINESSES AND ECONOMIC GROWTH"

Submitted
By

Federal Emergency Management Agency
500 C Street, S.W.
Washington, D.C. 20472

May 1, 2015

Introduction

Chairman Vitter, Ranking Member Shaheen and Members of the Committee, I am Brad Kieserman, Deputy Associate Administrator for Federal Insurance at the Federal Insurance and Mitigation Administration (FIMA) in the Department of Homeland Security's (DHS) Federal Emergency Management Agency (FEMA). I am grateful for the opportunity to be here today, and appreciate your partnership on flood insurance issues.

In this testimony, I will discuss the impacts of the National Flood Insurance Program (NFIP) on small businesses.

Flooding and the Need for a National Program

Flooding has been, and continues to be, a serious risk in the United States. Most insurance companies have historically excluded flood damage from homeowners insurance because of adverse selection – only those most susceptible to flooding will purchase coverage. To address this need, Congress established the NFIP in 1968 to make flood insurance available, identify flood risks and encourage sound local flood risk management. The NFIP is administered by FIMA.

The NFIP serves as the foundation for national efforts to reduce the loss of life and property from flood. The program identifies areas with risk of flood, mitigates the long-term risks to people and property from the effects of flooding, and makes insurance against the risk of flood generally available in participating communities. The NFIP works with participating private insurance companies – commonly known as "Write Your Own" companies – to market, sell, administer and adjust claims for policyholders. By encouraging sound floodplain management efforts, the NFIP is estimated to save the nation $1.7 billion annually in avoided flood losses.

The NFIP was, by statute and design, not actuarially sound. Specifically, 20 percent of policyholders, including many of the NFIP's highest risk structures, paid premiums that were less than actuarially sound and the government was subsidizing on average 60 percent of the loss. This design, in addition to catastrophic flood events such as Hurricanes Katrina, resulted in an annual premium shortfall that required FEMA to use its statutory authority to borrow funds from the U.S. Department of Treasury. These funds were used to pay covered flood damage claims to policyholders. Although payments have been made to reduce this obligation, $23 billion in debt remains.

Recent NFIP Reforms

In this context, Congress passed the Biggert-Waters Flood Insurance Reform Act of 2012 (BW12). BW12 required major changes to components of the program. Many of the changes were designed to strengthen the fiscal soundness of the NFIP by ensuring that flood insurance rates more accurately reflect the real risk of flooding. FEMA began phasing in the rate increases for certain subsidized properties in 2013. BW12 also authorized a flood mapping program, created the Technical Mapping Advisory Council (TMAC), created a reserve fund, and called for a study on the affordability of flood insurance.

In March of 2014, Congress passed and President Obama signed the Homeowner Flood Insurance Affordability Act (HFIAA) into law, repealing and modifying certain provisions of BW12, and making additional program changes to other aspects of the program not covered by that Act. Many provisions of BW12 remain in effect and are still being implemented. Like BW12, HFIAA requires changes to the major components of the NFIP, including flood insurance, flood hazard mapping, grants, and floodplain management.

Impacts on Small Businesses

The NFIP offers policies designed specifically for commercial policyholders, providing up to $500,000 for building property, and up to $500,000 for contents of the business. For many large businesses, the commercial coverage under the NFIP is not adequate to cover their needs. However, for many small businesses, affordable flood insurance provided by the NFIP is an important protection against flood losses.

The NFIP is in the process of implementing reforms required by BW12 and HFIAA. HFIAA repeals or modifies some provisions of BW12. However, HFIAA maintains the requirement that flood insurance rates for business properties in high-risk areas reflect true risk. This means that the subsidized rates that previously applied to some older business buildings will continue to be phased out.

On October 1, 2013, the subsidized rates for these pre-Flood Insurance Rate Map (pre-FIRM) buildings began to phase out. At renewal, non-residential policyholders received a 25 percent rate increase. As required by both BW12 and HFIAA, the 25 percent rate increases are set to continue until rates reflect the property's true risk. However, a provision of HFIAA temporarily slows that rate of increase. Currently, business properties and non-business, non-residential buildings such as schools, churches, hospitals, and apartment buildings are included within a single non-residential policy rating class. HFIAA caps increases for these other buildings at 18 percent per year. Until FEMA begins to separately classify businesses on April 1, 2016, all non-residential properties—including businesses—will receive no more than an 18 percent annual increase.

Increasing fixed costs for expenses such as flood insurance can have a negative impact on small businesses. While FEMA encourages all business owners to avoid locating a business on property susceptible to high or moderate risk of flooding, the NFIP recognizes that this is not always feasible for a variety of reasons. However, there are ways in which businesses can mitigate their flood risks and lower their insurance premiums. Options for business owners to consider include: floodproofing, relocation, floodwalls and levees, and structural elevations. Not every option will work for every business. We encourage businesses who want to mitigate against flood losses to work closely with their flood insurance agent and their state and community officials to evaluate their options.

Implementation of the Homeowner Flood Insurance Affordability Act of 2014

FEMA is aggressively implementing changes to the NFIP as required by Congress after the passage of HFIAA. FEMA completed issuing refunds as required by HFIAA in February 2015. Refunds were provided to policyholders to align their rates to the changes that Congress provided in HFIAA and to be no more than 18 percent per individual per year. The average amount of refund was $92.96 and the NFIP paid over $65 million in refunds to policyholders. There are a limited number of policyholders who cancelled policies mid-term or moved that did not leave forwarding addresses that may have not received their refunds. We are working to get in touch with these people to provide their refunds. Additionally, FEMA is conducting a rigorous review of the refund data to ensure all eligible policyholders received refunds.

Policyholders eligible for a refund include:

- Policyholders who purchased or renewed policies on or after October 1, 2013 and were charged full-risk premiums for buildings constructed before FEMA issued flood insurance rate maps for a community (FEMA refers to these properties as pre-FIRM) because (1) the property was not insured when BW12 was enacted; or (2) the property was purchased after BW12 was enacted.
- Policyholders whose lapse in coverage was due to some property owners no longer being required to purchase flood insurance. HFIAA restores subsidies to policies for Pre-FIRM properties that were rated full-risk under BW12 due to a lapse in coverage where coverage was reinstated on or after October 4, 2014 (90 days after enactment of BW12).
- Some policyholders who purchased or renewed policies after March 21, 2014 and paid rates in excess of the new 18 percent rate increase cap per policy mandated under HFIAA.

Surcharges required by HFIAA went into effect on April 1, 2015. Upon renewal and for new policies, all policyholders will be required to pay $25 for policies on primary residences and $250 for all other policies. Surcharges are applied annually and are added on top of the no more than 18 percent per year annual increases. Congress instituted the surcharges with the passage of HFIAA to slow the rate of premium increases required by BW12. Surcharges will go into the NFIP reserve fund and can be used to pay claims and pay down the program's debt.

May 1, 2015 Bulletin Implementing Business Provisions

FEMA prepared a bulletin to be released on May 1, 2015 (today) that will implement the business provisions of BW12 and HFIAA. Starting November 1, 2015, the NFIP will have a new classification for business. Previously, all non-residential properties were classified in one category that included business, non-profits, and houses of worship. Once the business category is established, the WYO companies will work with the NFIP to re-underwrite an estimated 290,000 policies upon renewal. Some portion of the 290,000 properties currently classified as non-residential policies will be reclassified as business properties. Less than eight percent of our policies are non-residential and, therefore, I anticipate an even smaller percentage will be business properties.

Non-residential properties currently receive rate increases of no more than 18 percent per year until they reach the full actuarial rate. This rate will continue until March 31, 2016. Additionally, beginning, April 1, 2016, upon classification and underwriting as a business property, business properties will receive a 25 percent increase annually until they reach the full actuarial rate.

FEMA will then begin to capture data about businesses in the NFIP and we will complete the required study on the protection of small businesses, non-profits, houses of worship, and residences. This study is anticipated to be completed early 2017, as a one year data capture on the specific categories (small business, non-profits, houses of worship) is needed to complete the report.

Affordability Study

As required by BW12 and HFIAA, the National Academy of Sciences recently issued its Phase 1 report to define affordability concepts and outlined program policy options. The Phase 2 report is expected to be released in fall 2015, and will propose alternative approaches for a national evaluation of affordability program policy options. FEMA will issue an Affordability Framework within 18 months after the completion of the Phase 2 report. With the NFIP authorization expiring on July 7, 2017, we look forward to working with Congress to continue to reform the program, and ensure it is focused on policyholder recovery and disaster survivors.

Conclusion

Congress continues to be an active partner in providing direction to FEMA as we seek to implement a program that will serve the needs of individuals, businesses, and communities to help them protect themselves and their properties from flood risks as well as recover from flooding disasters. I look forward to our continued work together in finding better ways to protect against flood risks in Louisiana, and across the country.

Thank you again for the opportunity to appear before you today. I am happy to answer any questions you may have.

Chairman VITTER. Great. Thank you both very much. I'll get things kicked off, and then we'll turn to Senator Cassidy.

You both heard a lot of concern about this Executive Order. What we're talking about, just for everyone's benefit, is an Executive Order by President Obama, 13690, and the corresponding Federal Flood Risk Management Standards, that they would be raised significantly and that this Executive Order basically directs all Federal agencies to define the floodplain in a different way than we have traditionally, at the 100-year floodplain, and in a more draconian way, either a floodplain based upon, quote, "climate-informed science," closed quote, whatever that means, or No. 2, a 500-year floodplain, or No. 3, expanding the existing 100-year floodplain to add an additional two or three feet of freeboard elevation, which is a big deal.

Now, FEMA has said none of this is going to impact NFIP, but under the terms of the Executive Order, it's supposed to include all Federal grants, loans, and federally backed financing programs, like FHA-backed single family mortgages.

Those two statements seem to be in conflict. What are we missing?

Mr. WRIGHT. So when this Executive Order came out, it put some new pieces in motion, Senator Vitter, but it also went back and amended an Executive Order from President Carter, in 1977. And so what we were directed to do——

Chairman VITTER. Just as an aside, the fact that we're building on a Carter Executive Order does not give us great comfort either. I'm sorry, I couldn't help myself.

Mr. WRIGHT. Fair enough. And so it is that piece from 1977 that looks across all federal action, and it then told agencies to go through and look at the impact on various programs.

In an attempt to be open and transparent with folks, what came out was a document that looks at how these two fit together, and that document has been something that we have been going around the country, sitting and talking with people, because it's in draft, and it needs to be clarified.

And so one of the points is—I've gone to eight different cities, I've held public meetings, and I was even meeting with some folks here in New Orleans last night on this topic, because we have the ability to ensure that the implementing guidelines match what people's expectations are.

And so to this point, it will not change the National Flood Insurance Program in terms of how we map today, the rates that are set on the ability for people to have claims. It will not do that. We don't see that the Executive Order directs us to do so.

What I was asked last night, and I think it was very fair, is they said if that's the case, show us that language directly in that implementing interagency guideline.

And so one of the challenges I offered back to folks is, that is the intent. Can you tell me what words that we would put on this page that would bring that level of assurance?

The intent of the Executive Order, and it's clear in the policy section of Section 1, is to focus on federal investments in construction projects. So that's if there's going to be Federal dollars put in, we should build it higher and stronger so that it can withstand. That's the intent.

Part of what has been going on, through this now 90 days of public engagement, has been, help us understand where these uncertainties may be and help me understand what words would bring the kind of certainty that people want.

Chairman VITTER. Roy, let me follow up on that. So you're saying that this Executive Order would not change the definition of floodplains for NFIP?

Mr. WRIGHT. That is correct.

Chairman VITTER. Okay. Now, you just said it would be about any federal investment.

Mr. WRIGHT. Investment.

Chairman VITTER. Aren't mitigation programs, all sorts of things directly related to NFIP, federal investments?

Mr. WRIGHT. So this is where I will separate the part related to those who have insurance policies, the 5.2 million people who have insurance policies. It does not change it for that.

If you received a grant from FEMA for a mitigation project—and there is one grant program under the NFIP, it's called Flood Mitigation Assistance—and we do a number of different kinds of projects, including elevations, and if you are getting an elevation funded through a grant, this could have an effect on that part, but we're already paying to build something up at that point, so that's the incremental element, but as it gets to the insurance piece of the equation, how the maps are drawn, how the policies are sold, rated, priced, it does not.

And one of the things that we've been asked is—we see that we can make that interpretation, based off the Executive Orders, both the one from 1977 and the new one. Folks have said, if that's the case, then make that plainly clear in this document that that separation exists.

Chairman VITTER. And wouldn't it still potentially impact federally supported mortgage programs that are all balled up for a homeowner with NFIP?

Mr. WRIGHT. So it's not best for me to speak definitively for another Federal agency, but as I've worked with the other agencies and had these conversations, the way that HUD, for example, has looked at this—because, frankly, they've been implementing this requirement already over the last 37 years, under the old Executive Order—and what they have determined, and we believe is the right answer to continue, is if you're getting a loan for construction, as a Federal dollar for construction, this would likely have an application to you.

But if you are getting a federally backed mortgage, if you're getting financing or refinancing, those agencies have determined that the structure already exists. There would be nothing to implement. It's simply a financial transaction.

Some of that is already in the document, but we have been asked, again, make that plainly clear, plainly clear that this application to this would not have an adverse impact on the availability of mortgage financing.

Chairman VITTER. Right. Well, I would just echo that request.

Mr. WRIGHT. Okay.

Chairman VITTER. I mean, if that is the absolute commitment, it can certainly be stated in a much more precise way, including in an actual Executive Order, not just, you know, agency guidelines, so that's No. 1.

And to the extent anybody in the Administration doesn't want to do that, it obviously makes us ask, "Why not?" And you're saying, "No problem." But why not state it very precisely in an actual instrument that has the same standing as the Executive Order we're talking about, that's No. 1.

No. 2, I would just restate that even were that to occur, there are plenty of other impacts about federal investments that you are saying are directly impacted that we think is going to shut down a bunch of necessary activity in large parts of the United States, huge parts of Louisiana.

Mr. WRIGHT. And so, again, I have learned, and again, having conversations last night, I learned more, and what I said to folks, "Help us with those words." I'm not in a position to make a commitment about a subsequent Executive Order, but I am in a position by which we were very clearly directed to look at this implementation and start by putting a draft out so people could legitimately respond to it, and bring the kind of clarification that you are seeking on this.

As that comment period is played out, I do believe, even talking to some folks last night, there are specific comments that will come in that say, "Here's the kind of words in the interagency guidance"——

Chairman VITTER. Right.

Mr. WRIGHT [continuing]. "That would produce that kind of increased certainty."

Chairman VITTER. Well, again, you just said in the interagency guidance. I mean, my request is for more than that, because guidance can change on a moment's notice.

Mr. WRIGHT. It can. In this instance, this document was last updated in 1978. It's not one that has been frequently changed, but as you well know, I can't make a commitment about the issuance of an Executive Order.

Chairman VITTER. Right.

Mr. WRIGHT. But I can make sure that, consistent with those Executive Orders, the interpretation of it is clear and sound and aligned to the outcomes that we're describing today.

Chairman VITTER. Right. Brad, do you have anything to add? And then we'll move to Senator Cassidy.

Mr. KIESERMAN. Nothing, Senator, thank you.

Chairman VITTER. Okay, Bill.

Senator CASSIDY. So just to be sure—and, again, I apologize if I was gathering wool or a little dense, but you said if it is a federally backed mortgage for an existing structure, I've already laid the foundation, not affected, but what if I'm a developer about to make a lot of small neighborhoods so people can move to, you know, to respond to the need for housing, and those are federally backed mortgages to be issued in the future? Would it affect those federally backed mortgages?

Mr. WRIGHT. So I want to be clear and precise with you, to the best of my ability. In almost—there's—and I'm trying to be precise, because there is one particular program——

Senator CASSIDY. You may have to bring the microphone to you.

Mr. WRIGHT. I'm sorry. As I understand it, HUD has one small program by which they do, in a rural context, provide funding for construction. It's a very small part of the FHA portfolio, very small.

And the other instance is when people are getting loans for—when they're getting loans for construction, those are not federally backed mortgages, and so usually what happens is the end——

Senator CASSIDY. Yeah, but they sell it. They sell it.

Mr. WRIGHT. At the end. So the financing for the construction is a much riskier proposition than when it's complete. So the homeowner is involved with a completed structure, and so at that point, it exists.

Chairman VITTER. So are you saying definitively that it would not in any way affect federally backed mortgages for new construction homes?

Mr. WRIGHT. If the—to the degree that there is not a Federal dollar involved in the construction. If there's Federal dollars in the construction, this will have an application to them. But if it is simply using a financial instrument, for a Freddie, Fannie, FHA kind of loan——

Chairman VITTER. Well, I mean, I'm sure in some of these sorts of developments Bill is describing, I would guess——

Senator CASSIDY. Community block grant. A community block grant that's going to make mixed use housing.

Mr. WRIGHT. Okay. So now we're going to a different category. We're not talking about a financial transaction any more. This will have an impact on the CDBG funds, and when we're doing those kind of housings, we should build them higher and stronger and plan for it on the way in.

And I think that there's some sound public policy behind that. Often, we're dealing with those with less income means, and that means they also have less economic means to recover from a given disaster, and so we want to make sure that they can withstand, in that instance.

Again, I can't speak definitely for HUD, that's not my agency, but as we've looked at this across, the conversations with others, if you're receiving CDBG for a construction project, this would have an application.

Senator CASSIDY. So let me ask you another point. How do you figure out assumptions for a 500-year flood risk? Could you have imagined the Army Corps would have built levees that would fail? That's one example.

Can we imagine that Sandy, where it was a new moon, with a high tide, with a storm at a certain angle—you follow what I'm saying? There's so many assumptions, and are you being transparent about your assumptions? Because whether or not, in 500 years—500 years ago, it was 1514. Who would have known that they would have leveed the Mississippi River in a way that our wetlands have died and not have helped us mitigate the wetlands lost? And so New Orleans, which formerly was protected, is now at high risk? You follow what I'm saying? How in the heck can you do that?

Mr. WRIGHT. So—I follow the line of questioning and I'm going to give you a statistical answer, which is to say, what is usually referred to as the 100-year is actually a one percent annual chance statistical calculation, and what is often referred to as the 500-year is actually a .2 percent annual chance statistical calculation, and it is not a presumption related to whether or not certain structures would fail or not.

None of the calculations are related to that. Rather, it's looking particularly at what does it mean to deal with the rainfall that would occur under the .2 annual chance.

But let me use this as a point to highlight for you why, in this instance, the standard gives three options. Because if we look at various places across the country, different options may be the right answer.

So the first one says, do you have data about the future risk, and if you're doing a specific project, whether it's a flood control project or a large-scale transportation interchange, in those instances, they're looking for over the life of that project, often 50 years, and they are making some projections about what they would anticipate, and frankly, that's where we're going to largely see that first approach related to the future risk informed science.

In other instances, dealing with the plus two-foot freeboard, is the right answer, which has been an engineering safety factor that has been in practice for more than 40 years, or other cases by which the .2 percent annual chance piece or the 500-year may be applicable.

Those are the three options that are on the table, and those options are intended to ensure we have flexibility so that we can look at the realities in a community and separate them.

Senator CASSIDY. So who chooses the option to use? If I am, again, a small businesswoman trying to develop a neighborhood, and I have got to comply—maybe I'm doing low income houses as part of a CDBG, then can I pick which of those three apply to my project?

Mr. WRIGHT. So this has been part of the conversation, as I've talked across the country, and right now the guidance is silent about which one to choose. There's a preference that says if you've got the climate-informed science about the future, you should use it. But when you're looking at the other options, it doesn't.

The thought behind that was that as you look at the different character of various Federal programs, we should ensure that you choose an option that is consistent with its mission, consistent with the intent of that program.

What I have heard from folks is that they are looking for a way to have more predictability in this, and we've had some great conversations with folks about how we live in this tension between predictability that says you must take this path and also having flexibility so that the realities in a given community can be incorporated and addressed.

And so that's one of the things, as we've gone through the public engagement, we've asked for insight from folks about how they would prefer for that decision to be made.

Senator CASSIDY. David.

Chairman VITTER. Okay. Two things, as we close out this panel. First, there are obviously a lot of continuing questions about this. The comment period on this closes next Wednesday. Can the Administration extend the comment period, which has been formally requested?

Mr. WRIGHT. Right. So I have a number of requests to extend this. Initially this was a 60-day comment period, and given the nature of the conversations we were having, we agreed and we extended it to make it 90 days, and that's where we're at, so we've already given an extension.

And when we come out of this, each agency is going to be directed, later in the year, to engage, as they do their own protocols, with another engagement of the public. We are all being directed and mandated to do that.

We have a request. I am working with the team in D.C. so that we can make a decision on that. I expect that to happen early next week.

Chairman VITTER. Okay. And, finally, Brad, you have looked at a lot of things in the program, particularly in the context of Superstorm Sandy. Do you have any developing or formed thoughts including about the "Write Your Own" end of the program?

Mr. KIESERMAN. Thank you. Roy says, "Thank you, Senator, for moving on," for moving to something I will talk about. Thanks for doing this. So just to give you some background, ——

Chairman VITTER. Actually, I didn't think you were minding that I was staying with Roy.

Mr. KIESERMAN. I wasn't minding at all. I had some of the same questions and now I've got the answers.

So in the aftermath of Superstorm Sandy, as many of you may know, there's an extensive amount of litigation that's going on up in New York and New Jersey, on the eastern seaboard. Sixty days or about 70 days ago, I was brought in to troubleshoot that, and I have been drinking from the fire hose ever since, but I will share with you my initial observations, if that's okay.

First of all, the National Flood Insurance Program, which is run—the gentleman talked about resources at the NFIP earlier. Here's 70 Federal employees in Washington. They are the National Flood Insurance Program, Risk Insurance Division. They are the ones who—who do what? And here's the answer. What they do and what they're supposed to do—and they're hard-working people just like you are—but they're in a program that frankly is in dire need of an overhaul.

So what's happened, over the course of the years, there are 82 companies that sell flood insurance, as well as the National Flood Insurance Program itself, that has about 20 percent or 18 percent of the policies that we actually sell and market because other companies won't do that. Generally, they're higher-risk policies.

So between us and one other company, Wright Flood Insurance, between the direct side and Wright Flood Insurance, we have about 30 to 40 percent of all the policies nationally. Then the other 81 entities have the other 60 percent. Does that make any sense to anybody?

So it made sense before the internet. It made sense before you could go online and by E-insurance, because you needed people all over the country to sell and market your product.

So it is very clear to me that 31 percent of every premium dollar you pay, at least 31 percent, goes to a "Write Your Own." I don't know about you all, when I give to charity, I look and see what their overhead costs are, because what I want is my dollars going to the people I'm giving to. I don't want my dollars going to overhead.

And so as I've looked at the program just over the last 70 days, Senators, what I am seeing is that we are paying a lot more in overhead than we should be in 2015. The program structure is a 1980s era business structure. I don't think it's the correct business model today.

And I want to be clear. A lot of people say, the Write Your Owns are bad and the insurance companies are bad, and I'm not saying that. Insurance companies are necessary, they serve a purpose, and there are many responsible insurance companies. I just don't know that the business model for delivering a subsidized Federal program that is virtually unavailable anywhere else in the commercial market is the model we have today.

What's clear to me is that we have a capacity issue, especially in disaster or catastrophic events. Where are the agents coming from? Where are the adjusters coming from? Where are the engineers coming from? And who's making sure that the people who come to your homes and your businesses are reputable, reliable people of integrity? Because as John Houghtaling knows, we have encountered—and I know you all encountered it down here, as well—but we have seen, in the Sandy aftermath of the Sandy storms, that not everybody who came to somebody's home or business was reputable or a person of integrity, and we certainly have seen evidence that fraud was committed. So there's a huge need to fix the oversight piece of this.

There's another part, if I can, for just one moment. We've lost touch with the customer. I'll tell you what, the people who are running the program at the national headquarters, they are good people, but they view their customer as the "Write Your Own" insurance company, and there's a reason for that. They have virtually no contact with you at all. The contact is carried out through—by literally a hundred thousand people, agents and adjusters and engineers and people that—we've lost touch. We have just lost—and I can show it to you in the numbers.

The last piece, not only have we lost touch, many people who buy a flood insurance policy don't know what they bought, and they are very surprised at the time of their loss that something's not covered, or that the pricing that we're using to replace something or repair it is way off what their expectations were.

So we have to do a couple things. We have to get way better—and I'm not talking about little increments here, I'm talking about way better—at educating policy holders and perspective policy holders about what their policies really cover. And I have to say, I have never seen so many exclusions, exceptions. And I know why they're there. They're there because this is a subsidized program, and so you have to have a lot of exclusions and exceptions to keep it affordable.

But you have to understand what those are and make decisions about your risk, and we have got to just up the game on that.

So I see the reforms going forward as evaluating the business model and making sense about—making better decisions about what an efficient, economically efficient customer survivor-centric business model looks like. I don't think it's the model we have today, but I don't have a replacement in mind.

I just know that we've got to look at it, and we're going to look to our partners to help us understand that, including insurance companies, Congress, the plaintiffs' bar, our policy holders, small businesses to help us understand that, that business model change.

We've got to get more survivor-centric and get back in touch with the customer, and we've got to do a better job providing customer service and that's—if you've ever been frustrated trying to get your paperwork cleared, you've been frustrated with your adjuster or your engineer—many of you are small business owners. You wouldn't run your business that way, and we've got to run our business that way. So thank you.

Senator CASSIDY. David, can I ask him one question?

Chairman VITTER. Sure.

Senator CASSIDY. I want to link the next panel with this panel. My concern is that if we go to this 500-year or three feet above the base flood elevation, et cetera, that that will impact the real estate market indirectly, but profoundly.

For those of us who are homeowners in this room, our principal investment, our principal equity in life is our home.

Now, David McKey is going to be on as a real estate broker, and he is going to be on a follow-up panel, but just for the benefit of us homeowners, David—and then if you could respond—to what degree do you think that the proposed 500-year storm surge, et cetera, for Federal buildings, will spill over into the risk underwriting or risk perception of a primary residence which would otherwise be unaffected?

Mr. MCKEY. Well, the critical factor that we have is—and what a lot of people don't understand is the flood insurance impacts, and if it increases on one piece of property, that's not just an impact on that piece of property. It impacts the subdivision, it impacts the community, so it's really a widespread effect anytime we see rates on our homes or even our businesses increase.

Senator CASSIDY. So if we have a Community Block Grant Development with mixed-income housing, and it has to be built to a certain level in order to be certified, and that is different from the neighborhood next door. Nonetheless, you feel as if—I'm asking, I don't know this—that there will be a spillover of increased rates because a perception has been created that it is a higher risk than previously assumed?

Mr. MCKEY. That would be absolutely correct. When an appraiser comes into an area, a lot of times he doesn't look strictly at that particular subdivision when he's trying to assess the value of that home. He looks around the area and tries to pick up comparables to make an evaluation of that property. So if he's pick-ing up comparables in an area that, like you're talking about, it is going to, no doubt, affect surrounding properties.

Senator CASSIDY. And I was going to say, my fear is that the Administration is so committed to climate science and their understanding of it that they are going to make assumptions which are quite variable. Forty years ago, we thought we were entering a mini ice age, and now we speak of global warming, that we will have assumptions made that will impact, sure, federally, but then spill over. Roy, any comment to that?

Mr. WRIGHT. What I would simply say is that building higher and stronger in areas of flood risk is a good idea. It is something that communities and parishes here——

Senator CASSIDY. I accept that, but if you take that to a logical extension, we'd all live in lighthouses.

Mr. WRIGHT. No, I—no, sir, I wouldn't assert that. What I would say is there are elements related to additional freeboard. We see this in places like Mandeville Slidell, St. James, St. Tammany, Ascension parishes, in which people have looked and said, building higher and stronger is the right answer for what we're doing, going forward.

And I understand there may be some debate about exactly what to forecast, yet whether it's through subsidence, other kinds of elements by which we deal with changes in risk, here in southern Louisiana, on an ongoing basis, that we want to ensure that when future events come in, we are creating an ability by which the community and those who live there will be able to withstand that event, and to the degree that it has an impact on them, they would be able to recover and rebound quickly.

And so we need to do that in a way that is consistent and engaging with the community so that they understand where they are headed with these elements.

Chairman VITTER. Okay. I think this is a good transition to our second panel, of which David is a member, but let's give our first panel a round of applause.

[Applause].

Now, I'd like to ask our second panel to come up. I'll be introducing them as they get situated, if I could have everybody's attention.

Dwayne Bourgeois is a native of Thibodaux and a lifelong resident of Lafourche Parish. He serves as the Executive Director for the North Lafourche Levee District. Hurricane Katrina brought about many changes, including involving FEMA, that have caused Dwayne to become much more involved regarding flood elevations and related issues in Lafourche.

Jerry Passman is a native of Baton Rouge and Immediate Past President of the Louisiana Home Builders Association. He has been a member of the Capital Region Builders Association for 18 years and has been very involved in that directly related industry.

And David McKey, who you've already heard from briefly, is the Broker/Owner of Coldwell Banker One, a real estate company in Baton Rouge. He serves as Chairman of the National Association of Realtors Work Group on Flood Insurance. He's been very, very involved in his related part of business for many years.

Welcome to all of you. I really appreciate your being here, and we'll hear from each of you, in turn, for five minutes, starting with Dwayne, and then we'll have a conversation about it. Dwayne.

STATEMENT OF DWAYNE BOURGEOIS, EXECUTIVE DIRECTOR, NORTH LAFOURCHE CONSERVATION, LEVEE, AND DRAINAGE DISTRICT, THIBODAUX, LA

Mr. BOURGEOIS. Good morning, and I'd like to thank you, Chairman Vitter and Senator Cassidy, for the opportunity to testify today.

I am the Director of the North Lafourche Levee District, a political subdivision in the state of Louisiana, but I'm here today representing a broader group of agencies, citizens, businesses in the state of Louisiana who rely heavily on the National Flood Insurance Program.

As I am sure everyone here is aware, the Biggert-Waters Flood Insurance Reform Act of 2012 extended the authorization of the NFIP for a 5-year period, which ends September 30th, 2017. Biggert-Waters 2012 was supposed to be a permanent fix to the solvency of the NFIP. It clearly was not.

In 2014, the Homeowners Flood Insurance Affordability Act was passed to fix parts of Biggert-Waters 2012, and from a residential homeowner's point of view, it repealed the most damaging parts of Biggert-Waters 2012; but most everyone agrees, there is still much room for improvement across the board.

So now we find ourselves with another opportunity to address the issues of this very important Federal program. Biggert-Waters 2012 has caused many organizations locally and nationally to take a close look at the NFIP and to question the approaches taken to address solvency and long-term stability. The Association of Levee Boards of Louisiana, working with other state and local organizations, has compiled suggested changes to the NFIP into a few specific reforms that I would like to outline for you today.

First and foremost, all new changes to the NFIP will have made, going forward, should be looking forward, okay. We can't punish people who have followed FEMA's rules for participation in the NFIP.

So with the exception of Severe Repetitive Loss properties, we suggest that all new legislation should be structured so that the existing policyholders of any property class must be allowed to purchase Flood Insurance at approximately the same cost as before any new legislation as long as there is no lapse in coverage or accumulative flood claims equal to the fair market value of the property.

Further, these same property owners should be allowed to sell or otherwise transfer the title of their property to a new owner who will then be able to continue with insurance coverage, as described.

Flood insurance policies are offered by FEMA as part of a quid pro quo arrangement to mitigate flood-related cost to the Federal Government. They are offered by the Federal Government to the policyholders under the belief that doing so was equally beneficial to the Federal Government. All policies came with floodplain management restrictions that FEMA required for a community to participate in the National Flood Insurance Program.

The Federal Government not only implied that this affordable insurance would be available for the life of the property; it published and promoted the program accordingly. Citizens and businesses made huge financial decisions, in most cases the largest financial decision of their entire life, based on the promise of the Federal Government.

Second, the solvency of the program must be addressed in a more equitable manner. We need to address program cost, not just revenue. From 1978 to 2013, the program collected over $9.67 billion more in premiums than it paid in claims, and yet the program remains $25 billion in debt. This suggests severe issues with the cost of administrating and operating the program. The "Write Your Own" insurance companies make a 30 percent margin on policy sales without having to underwrite any of the risk.

In all of the NFIP reform legislation proposed and passed, to date, the only group asked to give more to correct the programmatic deficit in the NFIP was the policyholders through increased premiums. There must be alternatives.

Third, there appears to be a huge lack of mandatory participation in the program. It has been law since 1973 that any property mapped by FEMA in a Special Flood Hazard Area must purchase flood insurance if the property is mortgaged by a lending institution regulated by the Federal Government. Nationally, a study done in 2006 showed that only 49 percent of those required to have flood insurance actually had it.

Further, it was estimated that when Superstorm Sandy was heading up the U.S. eastern seaboard, only 15 to 25 percent of the at-risk population had flood insurance. Biggert-Waters 2012 increased the penalties to lending institutions for non-compliance, but this law must be rigorously enforced in some manner.

The Federal Government has performed very poorly at enforcing this cornerstone issue in the NFIP. The intent was to have all of these properties in the NFIP for two primary reasons. First, to increase the revenue base of the NFIP, and second, to be able to use the insurance principle of the Law of Large Numbers to spread the risk to the program geographically.

Fourth, Biggert-Waters 2012 caused a big problem with the actuarial calculations used to determine the cost of insurance for the program by requiring FEMA to include catastrophic loss years in the actuarial calculations. This greatly changes the method FEMA uses to determine the cost of insurance.

The American Academy of Actuaries reported to Congress that including catastrophic loss years in these actuarial calculations was not in line with Standard Actuarial Principles before Biggert-Waters 2012 was even passed into law.

So, finally, we must also consider how a program designed to mitigate for a 100-year flood loss through a quid pro quo relationship with local community's floodplain management can reasonably be expected to absorb the cost of 400-year events.

In conclusion, I would like to point out that ours is a working delta, the fruits of which are enjoyed by and enrich our entire Nation. As such, the availability of federally backed affordable and financially stable flood insurance is of vital importance to our region and the entire Nation.

We commend the Committee for addressing long-term reauthorization and reform of the National Flood Insurance Program. We thank you for this opportunity to share both our situation and our views on this important issue.

[The prepared statement of Mr. Bourgeois follows:]

Testimony of

Dwayne Bourgeois

Executive Director

North Lafourche Conservation, Levee and Drainage District

Before the

Senate Committee on Small Business and Entrepreneurship

United States Senate

The National Flood Insurance Program:

May 1, 2015

I would like to thank you Mr. Chairman and members of the Committee, for this opportunity to testify today. I am the Executive Director of the North Lafourche Levee District, a political subdivision of the State of Louisiana. However, I am here today representing a broader group of agencies, citizens and businesses in the State of Louisiana who rely heavily on the National Flood Insurance Program.

As I am sure everyone here is aware, the Biggert-Waters Flood Insurance Reform Act of 2012 extended the authorization of the NFIP for a 5 year period which ends September 30th, 2017. BW12 was also supposed to be a permanent "FIX" to the solvency of the NFIP. It clearly was not. In 2014, the Homeowners Flood Insurance Affordability Act was passed to "FIX" parts of BW12. From a residential homeowner's point of view, it repealed the most damaging parts of BW12; but, most everyone agrees, there is still much room for improvements across the board.

Now, we find ourselves with another opportunity to address the issues of this very important Federal program. BW12 has caused many organizations locally and nationally to take a close look at the NFIP and to question the approaches taken to address solvency and long term stability. The Association of Levee Boards of Louisiana, working with other state and local organizations, have compiled suggested changes to the NFIP into a few specific reforms that I would like to outline for you today.

First and foremost, **ALL** new changes to the NFIP should be made going forward. We can't punish people who have followed FEMA's rules for participation in the NFIP. With the exception of Severe Repetitive Loss properties, all new legislation should be structured such that all existing policyholders of any property class must be allowed to purchase Flood Insurance at approximately the same cost as before any new legislation as long as there is no lapse in coverage or accumulative flood claims equal to the FMV of the property. These same property owners must be allowed to sell or otherwise transfer title of the property to a new owner who will then be able to continue with insurance coverage as described. Flood insurance policies are offered by FEMA as part of a quid pro quo arrangement to mitigate flood related cost to the Federal Government. They are offered by the Federal Government to the policyholders under the belief that doing so was equally beneficial to the Federal Government. All policies came with floodplain management restriction that FEMA required for a community to participate in the NFIP. The Federal Government not only implied that this affordable insurance would be available for the life of the property; it published and promoted the program accordingly. Citizens and businesses made huge financial decisions, in most cases the largest financial decision of their entire life, based on this promise of the Federal Government.

Second, the solvency of the program must be addressed in a more equitable manner. We need to address program COST, not just REVENUE. From 1978 to 2013 the program collected over $9.67B more in premiums than it paid in claims and yet the program remains $25B in debt. This suggests severe issues with the cost of administrating and operating the program. The WYO insurance companies make a 30% margin on policy sales without having to underwrite any of the risk. In all of the NFIP reform legislation proposed and passed to date, the only group asked to give more to correct the programmatic deficit in the NFIP was the policyholders through increased premiums. There must be alternatives.

Third, there appears to be a huge lack of mandatory participation in the program. It has been law since 1973, that any a property mapped by FEMA in a Special Flood Hazard Area must purchase flood insurance if the property is mortgaged by a lending institution regulated by the Federal Government. Nationally, a study done in 2006 showed that only 49% of those required to have flood insurance actually had it. Further, it is estimated that when "Super-storm Sandy" was heading up the US eastern seaboard, only 15-25% of the at risk population had flood insurance. BW12 increased the penalties to lending institutions for non-compliance. But, this law must be rigorously enforced in some manner. The Federal Government has performed very poorly at enforcing this cornerstone issue in the NFIP. The intent was to have all of these properties in the NFIP for two primary reasons. First, to increase the revenue base of the NFIP and second, to be able to use the insurance principle of the "Law of Large Numbers" to spread the risk to the program geographically.

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Insurance. The American Academy of Actuaries reported to Congress that including catastrophic loss years in these actuarial calculations was not in line with Standard Actuarial Principles before BW12 was even passed into law.

Finally, we must consider how a program designed to mitigate for 100 year flood loss through a quid pro relationship with local community's floodplain management can or should be expected to absorb the cost of 400 year events.

In conclusion, I would like to point out that ours is a working delta, the fruits of which are enjoyed by and enrich our entire nation. As such, the availability of federally-backed, affordable and financially stable flood insurance is of vital importance to our region and the entire nation.

We commend the Committee for addressing long-term reauthorization and reform of the National Flood Insurance Program. We thank you for this opportunity to share both our situation and our views on this important issue. We look forward to working with all of you to make these changes to the National Flood Insurance Program.

Chairman VITTER. Thank you very much, Dwayne, and now we'll hear from Jerry Passman. Jerry.

STATEMENT OF JERRY PASSMAN, PRESIDENT, LOUISIANA HOME BUILDERS ASSOCIATION, PASSMAN HOMES, INC., BATON ROUGE, LA

Mr. PASSMAN. Well, again, I would also——

Chairman VITTER. If you can pull the mike to you. Thank you.

Mr. PASSMAN. I would also like to thank you all for the opportunity to testify today. Again, I'm Jerry Passman. As you mentioned, I'm a third-generation home builder and small business owner from Baton Rouge, Louisiana, and the Immediate Past President of the Louisiana Home Builders Association.

We, the home builders, have a long history of supporting the NFIP. However, recent actions of FEMA and the Administration continue to create uncertainty for home buyers, home builders, and small businesses. Due to major disasters, NFIP solvency has been threatened. Many thought Biggert-Waters would ensure the physical soundness of the NFIP; however, there were unintended consequences.

Biggert-Waters impacted to sell both pre-FIRM and grandfathered properties by triggering an immediate shift of full rate risk with premiums increasing by 25 percent with a full rate risk each year. Home builders from across the country were witnessing how drastic rate increases were negatively affecting the sales of homes and saw rates increase 10-fold over what homeowners were previously paying

For example, due to inaccurate mapping, a young couple from New Orleans had to cancel the purchase of their first home because of an unexpected increase in the flood insurance rates, from $2,000 to $6,550.

In another example, a Louisiana builder bought a home, only to realize that the flood insurance rates on the home had increased from the anticipated $412 to over $13,000.

Home remodels were severely affected by Biggert-Waters with a substantial improvement threshold rate increasing from the traditional 50 percent to 30 percent or more of the market value of the structure.

This provision represented a major deterrent for grandfathered property owners located within the floodplain for making minor renovations, such as adding energy efficient appliances to a kitchen or updating their homes, or even performing normal maintenance, at the risk of paying significant premium increases.

Under your leadership, Congress acted quickly to change many of the unintended consequences of Biggert-Waters. The Homeowner Flood Insurance Affordability Act of 2014, HFIAA, no longer triggered the immediate increases to full-rate risk for pre-FIRM or grandfathered properties, and FEMA was required to provide refunds to eligible property owners whose NFIP rates increased.

Additionally, the important substantial improvement threshold was restored to the traditional 50 percent, giving homeowners the ability to make needed renovations without risking drastic increases in their insurance rates.

Thanks to Congressional oversight, FEMA is now required to notify the community affected and their Congressional delegation before updating new mapping models. They are required to reimburse the policyholders or the communities for successful challenges to the errors, in confirmed maps.

Although there are many positive changes that arose from HFIAA, some changes with the NFIP remain. Specifically, a recent Executive Order that President Obama signed will require each Federal agency to expand the definition of a floodplain well beyond the longest 100-year floodplain for all federally funded or approved projects.

In establishing the definitions, agencies may use the best available climate-informed science, the freeboard approach, which adds two to three feet of freeboard to the base flood elevation, on the 500-year floodplain, or any combination of the three.

While FEMA stresses that this will not impact NFIP rates, home builders and property owners are left wondering if structures in these new areas will soon require mandatory purchase of flood insurance. This uncertainty will devalue land and existing homes and businesses well beyond the 100-year floodplain.

Home builders are also concerned about the EEOs impact to private construction receiving Federal financing or permitting.

According to my experience, almost every home I've built has either had some sort of Federal financing, i.e., a government guaranteed mortgage, such as Fannie Mae, Freddie Mac, or VA, or requires some sort of permit. Every home I've built, we have to get a permit because we have to comply with the Clean Water Act.

I'd like to thank the Committee for this opportunity to testify before you today and allow small builders from Baton Rouge, Louisiana, to have a voice on this issue. I'd also like to express my and my fellow home builders gratitude to Chairman Vitter for your leadership on this issue. We, the home builders, look forward to working with Congress on the NFIP reauthorization to ensure homeowners, home builders, and small businesses are protected from exorbitant rate hikes, inaccurate mapping, as we have seen in the past.

[The prepared statement of Mr. Passman follows:]

Testimony of

Jerry Passman
Passman Homes, Inc.

On Behalf of the

Louisiana Home Builder's Association

Field Hearing Before the
U.S. Senate Committee on Small Business and Entrepreneurship

May 1, 2015

Jerry Passman
Immediate Past President
Louisiana Home Builders Association

Introduction

Chairman Vitter, and members of the Senate Committee on Small Business and Entrepreneurship, thank you for the opportunity to testify today on the impacts of higher flood insurance rates on home owners, the housing industry and small businesses. My name is Jerry Passman and I am a home builder and small business owner from Baton Rouge, Louisiana, and the Immediate Past President of the Louisiana Home Builders Association (LHBA).

Here in Louisiana, home builders have seen firsthand the integral role that the Federal Emergency Management Agency (FEMA) plays after a major natural disaster. Likewise, the National Flood Insurance Program (NFIP) provides a vital service to home owners across the nation, reducing the impact of flooding on communities and ensuring we can rebuild when catastrophic flooding occurs. Ensuring that the NFIP is predictable, affordable and financially viable is essential to protecting the American Dream.

The National Association of Home Builders (NAHB) has a long history of supporting the NFIP, including fighting for passage of the *Biggert-Waters Flood Insurance Reform Act of 2012* (BW-12). However, dramatic rate increases resulting from the BW-12 reauthorization had a major negative impact on home sales. Congressional leadership from members such as yourselves helped reform the program through the passage of the *Homeowner Flood Insurance Affordability Act of 2014* (HFIAA). Although this law addressed many of the problems created by BW-12, recent actions by FEMA and the administration continue to create uncertainty for home buyers, home owners and small businesses.

Background

Since 1968, Congress has recognized the need to make affordable flood insurance available to home owners and small businesses to protect properties against the potential risk of loss from flooding. Congress also recognized the critical role that state and local governments would play to ensure the NFIP continues to be fiscally sound.

This strong partnership between FEMA and state and local governments require NFIP-participating communities to adopt and enforce strict building code requirements to ensure all new construction located in FEMA-mapped Special Flood Hazard Areas (SFHA) are designed and constructed in a flood-resilient manner.

In 1994, with passage of the *National Flood Insurance Reform Act*, Congress further cemented the direct link between the NFIP, the home building industry and the larger real estate industry. With this law, Congress required home owners to purchase NFIP-backed flood insurance for all properties located within the 100-year floodplain if they had a mortgage or home-equity loan financed by a federally-insured bank or backed by Fannie Mae or Freddie Mac.

In Louisiana, it is difficult to overstate the importance of the NFIP to home owners and home builders. Over 42% of the state's entire land mass is located within the 100-year floodplain, not including our current location, the city of New Orleans.

Unintended Consequences

In 2012, Congress worked to ensure the fiscal soundness of the NFIP through the passage of BW-12. This law mandates that all policyholders eventually pay the full actuarial risk rate for their properties.

While most properties insured by the NFIP, including all new residential construction, already pay full-risk rates, just over 20% of existing NFIP policyholders receive subsidized rates, generally between 40 and 45% of the actuarial premium. Most of these subsidized structures are Pre-Flood Insurance Rate Maps (Pre-FIRM); that is, a property built before 1974 when the first Flood Insurance Rate Maps (FIRMs) were established.

Prior to BW-12, FEMA continued to allow policyholders to pay less than the full actuarial rate if their home was built to meet previous flood risks, even if a more recent flood map placed them in a higher-risk zone. Here in Louisiana, a significant portion of the housing stock enrolled in the NFIP is "grandfathered" under this provision. In fact, according to a 2013 report by the United States Government Accountability Office (GAO), there are over 65,000 grandfathered properties in Louisiana, representing nearly 14% of all NFIP policies in the state.[1]

Shortly after BW-12 was enacted, however, home owners and home builders started to see the unintended consequences of the legislation, especially on grandfathered or pre-FIRM properties.

First, any property that was sold was immediately subject to a full-risk rate, with the premium increasing by 25% each year until it reached the full actuarial rate. The potential buyer would get an unwelcome surprise at settlement, one that could even prevent the sale of the home if the rate increase was high enough to affect the buyer's ability to qualify for financing. In addition, all pre-FIRM and grandfathered policyholders were subject to a similar phase-in to the full-risk rate, but it would occur over five years, with premiums increasing by 20% annually.

Remodelers were also experiencing problems with changes enacted through BW-12. Once renovations on insured pre-FIRM properties exceeded a "substantial improvement" threshold, full-rate premiums would be triggered. Traditionally the substantial improvement threshold of a renovation was 50% or more of the market value of the structure, and was based on a wide range of factors including zoning and building code standards. BW-12 lowered the threshold to 30%. This new threshold, instead of applying only to substantial improvements, now covered very simple remodeling jobs such as installing new appliances or updating bathrooms or kitchens. Once the 30% threshold was met, not only were home owners required to pay an increase of 25% of the full-risk rate per year, but they were also required to bring their property into compliance with their communities' current regulations, which could be extremely expensive.

Were it not for Congressional leadership through the enactment of HFIAA, NAHB estimated that the move from the 50% to the 30% threshold would have placed up to $8.5 billion in annual remodeling activity at risk. This major change to the substantial improvement threshold deterred property owners from making necessary and appropriate renovations and improvements by placing them at the risk of paying exorbitant premium increases. Additionally, home owners who may have been unable or

[1] U.S. General Accounting Office. (2013, July). *Flood Insurance: More Information Needed on Subsidized Properties*. (Publication No. GAO-13-607). Retrieved from U.S. Government Printing office: Retrieved from U.S. Government Printing Office: http://gao.gov/assets/660/655734.pdf

unwilling to maintain or repair their homes would see decreased property values that would have had a negative impact on communities, lenders and neighborhoods.

After BW-12, more and more home owners were not only seeing drastic increases to their flood insurance premiums, they were also seeing major errors in the flood maps. NAHB and LHBA heard from builders across the country who were distraught over the dramatic rate increases. Due to problematic maps and remapping, many of which have expanded the limits of the floodplain, builders have reported associated rate increases that have priced prospective buyers out of their developments and forced the cancellation of sales negatively impacting the local economy.

Some members were seeing rates increase as much as tenfold over what the home owners were previously paying. For example, due to inaccurate maps, a New Orleans couple had to cancel the purchase of their first home due to the flood insurance rates increasing from $2,000 to $6,550 per year. Another builder in Louisiana bought a home and realized the flood insurance rates on his home had increased from $412 to the full-risk rate of over $13,000.

Legislative Fixes

Thankfully, Congress, specifically the leadership here today, acted quickly to address the many unintended consequences of BW-12 by enacting *The Homeowner Flood Insurance Affordability Act of 2014* (HFIAA). This reform bill provided major relief for many of the strains BW-12 placed on the housing industry.

HFIAA reinstated the title of grandfathered properties, and the sale of pre-FIRM properties no longer triggered the immediate increase to full-risk rates. HFIAA also gave home owners a break by providing refunds to the eligible pre-FIRM property owners whose NFIP insurance rate premiums increased.

Thanks to Congressional leadership, FEMA is required to notify communities and their congressional delegations before updating FIRM maps under HFIAA. This is invaluable for pre-FIRM property owners who are selling their homes, who now will be informed if they have been remapped into a new floodplain and will be able to inform the home buyer of any additional NFIP requirements.

Under HFIAA Congress created the Flood Insurance Advocate, an office within FEMA responsible for ensuring NFIP policyholders and property owners understood FEMA's process for appealing a preliminary FIRM maps.

Further, the mapping error concerns have been remedied. Under BW-12, policyholders and communities who had used their own personal funds to challenge FIRM maps. If the FIRM maps were proven to be erroneous, the policyholder or community not able to be refunded the full expense of challenging the FIRM map. Therefore, many FIRM maps went unchallenged. Under HFIAA, FEMA is required to fully reimburse policyholders, or communities by removing a prior reimbursement cap ($250,000 dollars) under BW-12 for successful challenges of erroneous FIRM maps.

To protect grandfathered properties, Congress mandated a surcharge across all NFIP policies, both pre-FIRM and full-risk rates, to offset the cost of continuing to subsidize their premium rates. Although the surcharge increases rates slightly, it is intended to bring the NFIP to a point of solvency until pre-FIRM rates gradually come to full-actuarial rates.

HFIAA also helps remodelers and home owners affected by the change to the substantial improvement threshold in BW-12, which increased NFIP premiums. HFIAA restored the threshold back to its traditional level of 50% or more of the market value of the structure, rather than the BW-12 rate of 30%. This will help to allow existing homeowners to stay in their homes and make the necessary repairs and upgrades without the fear of also triggering unsustainable insurance rate hikes.

Challenges Moving Forward

Although many positive changes were enacted through HFIAA, some challenges with the NFIP remain. Home builders are particularly concerned about potential changes to the NFIP and flood mapping that could result from a recent presidential Executive Order (E.O.) that expands the definition of a floodplain. On Jan. 30, President Obama signed E.O. 13690, updating a 1977 Executive Order on Floodplain Management (E.O. 11988), and created a new Federal Flood Risk Management Standard (FFRMS) for all federally funded or approved projects. As written, the new standard will drastically increase the geographic extent of a floodplain and could harm economic development across the country. Although FEMA has stated the E.O. and the FFRMS will not impact the NFIP because they "do not intend" to change the Special Flood Hazard Area definition, it remains to be seen what safeguards are in place to hold them to their word and keep the mandatory purchase of flood insurance tied to the 100-year floodplain.

In addition to potential effects on the NFIP, NAHB has serious concerns about the impact to private construction, the regulatory uncertainty this will cause, and the lack of oversight and public input sought.

For nearly 40 years the floodplain has been defined as an area with a 1% chance of annual flooding and is otherwise known as the 100-year floodplain. This definition not only governs federal buildings, but is the basis for the NFIP. Now, with only the President's signature, the floodplain definition has been significantly expanded. Under E.O. 13690 and the FFRMS, each agency would be required to independently define floodplains using one of the following criteria:

- the best available climate-informed science;
- the freeboard approach (adding 2 or 3 feet of clearance above the base flood elevation); or
- 500-year floodplain (areas with a 0.2% annual chance of flooding)

Under BW-12, Congress authorized FEMA's Technical Mapping Advisory Council (TMAC) to incorporate the effects of climate change, and to include the "best available science regarding future changes in sea level" into FEMA's National Flood Mapping Program. NAHB questions whether each federal agency has the same capacity and scientific expertise to undertake this effort – map new areas, consider local flood control measures and analyze climate science on a local basis. Additionally, NAHB questions the need for each agency to replicate this process.

Regulatory Uncertainty

According to FEMA, each agency may use a different floodplain definition, based on any of the criteria previously mentioned. Home builders and developers rely on permitting programs and regulations that are consistent, timely and predictable. When one agency defines the floodplain according to "climate-informed science," another uses the "freeboard" approach, and yet a third adopts the 500-year floodplain, permit, loan, and grant applicants are left wondering where the requirements of the E.O. apply. To make matters worse, agencies are not required to use only one definition, but instead can apply different definitions on a project-by-project basis.

Private Development

While the E.O. states that it will apply to "federally-funded projects," the original Executive Order and the FFRMS refer to "all federal actions." This is defined as "(1) acquiring, managing, and disposing of Federal lands, and facilities; (2) providing Federally undertaken, financed, or assisted construction and improvements; and (3) conducting Federal activities and programs affecting land use, including but not limited to water and related land resources planning, regulating and licensing activities." Putting aside the questions about the necessity for this E.O. and the ability of each agency to make such determinations, home builders are very concerned that these new definitions will be applied to projects well-beyond government buildings, directly impacting many private construction projects and indirectly impacting the NFIP.

While FEMA stresses that the new floodplain definitions will not impact NFIP rates or FIRMs, home builders and property owners are left wondering if structures in the 500-year floodplain or the ambiguously defined "climate-informed science" floodplain will soon require mandatory purchase of flood insurance. This uncertainty will devalue land and existing homes and businesses well beyond the long-accepted 100-year floodplain to which the NFIP, and indeed many other federal, state and local regulations, are tied according the definition of *special flood hazard area* (SFHA).

NAHB is also concerned about the impact of the E.O. and the FFRMS on development that receives federal grant funding (e.g. rural development grants, community development block grants, etc.), financing (e.g. FHA new construction) and permitting (e.g. Section 7 consultation under the Endangered Species Act, 402 and 404 permits under Clean Water Act, etc.), as the definition of "federal actions" clearly includes these types of activities.

Oversight

This E.O. was put into place without any congressional oversight or public input. While some agencies may need to go through a public rulemaking to effectuate the new definition of floodplain, some will be able to change their internal policies without any outside input. The FY 2015 Omnibus Legislation required FEMA to seek input from state and local governments. While FEMA hosted a series of listening sessions, all were completed after the draft implementation guidelines were released. Further, the administration has not made public any scientific or technical data to substantiate the basis for the new definition, a cost/benefit analysis to justify the definition, or even maps for regulators or the regulated community to review that show the extent of the floodplain according to the climate-informed science and freeboard approaches. And, in many locations, the 500-year floodplain is not mapped.

This new policy will drastically impact economic development across this country. Should the 500-year definition be adopted, the expansion of the floodplain could result in as much as a 20% increase in the floodplain area beyond the 100-year floodplain. No one knows the significance of the "climate-informed science approach." The Administration is putting the "cart-before-the-horse" in its attempt to implement the FFRMS before providing the necessary floodplain maps.

Home builders across the country hope that just as Congress helped to alleviate the problems stemming from BW-12, they will help rein in this overreaching E.O. and the many unintended consequences that will result.

Conclusion

I would like to thank the Committee for the opportunity to testify today, and specifically Chairman Vitter for his leadership on this issue. Forums like this one provide an important opportunity for members of the community to engage in the issues that impact our neighbors and local economy. Home builders have supported common sense changes to the NFIP through BW-12 and HFIAA, and we urge Congress to continue to support and protect Louisiana's small business owners and home owners from the exorbitant rate hikes and inaccurate mapping we have seen in the past.

Chairman VITTER. Great. Thank you very much, Jerry. And now we move on to David McKey. David, welcome.

STATEMENT OF DAVID McKEY, MANAGING BROKER, COLDWELL BANKER ONE, BATON ROUGE, LA

Mr. MCKEY. Thank you, Chairman Vitter, and thank you, Senator Cassidy. You have been friends of realtors for many years, and also, you have been great supporters of home ownership and business property ownership, in Louisiana, and we appreciate that.

Chairman VITTER. Thank you.

Mr. MCKEY. My name is David McKey. I am a managing broker and owner of Coldwell Banker One, in Baton Rouge, Louisiana. I've been a realtor for 23 years, and I am speaking to you on behalf of 11,350 realtors across the state of Louisiana that are members of Louisiana Realtors. I'm also one of over a million realtors that are members of the National Association of Realtors across the country, one of the largest trade associations in the country.

Every community across the Nation, realtors help citizens from all walks of life to achieve their dream of home ownership. We also help small businesses find locations and open their doors to business.

One of the inalienable truths of working in real estate is the big surprises just before a closing or at the closing table, and it's rarely good news. Transparency and certainty are vital to running a good business and not the fear of uncertainty.

We appreciate your continued support and your leadership on the flood insurance, especially your hard work last year, in Congress. One year later, we believe the Flood Insurance Affordability Act has succeeded in reining in most of the excessive and inaccurate rates across Louisiana, but as you know, we still have work to do.

Small businesses employ over half of the state's private work force. At the same time, flood insurance has become a significant expense for many property owners, especially small business owners who tend to have smaller production lines over which to spread costs relative to their larger competitors.

For this reason, it is especially important to phase in gradual increases in flood insurance so that there's a transition period, a planning period, and an adoptability period for small businesses. In our state, however, that's not always been the case.

Let me give you a practical example. Before the Affordability Act, there were news reports of surprise increases in flood insurance premiums, up to $30,000 or more, for some businesses, businesses that had never flooded or had flood issues in the past. It didn't matter if the information was factual, misleading, and in some cases, not factual. Buyers feared the worst. They were scared that they would wake up with a $30,000 flood insurance bill in their mailbox, and that's a death for a small business. Perception is reality, and in real estate, that's why we need certainty in the flood insurance program.

Our realtors have told us that often clients' first words are not to show them properties in an area that would require them to carry flood insurance for their mortgage. This certainly rules out a number of properties being marketed, and as a result, many owners find their property unsalable or hard to sell.

It also creates a rippling effect throughout the communities. As values decline on these properties, it also affects surrounding properties, as we just talked about, and in turn, the community tax base. It costs our citizens income, loss of equity in their real estate, and in some cases, jobs were lost.

So while the Affordability Act has been a success, there are still some issues, and I'll discuss five with you.

First and foremost, we need long-term reauthorization. The National Flood Insurance Program will sunset in 2017. We urge Congress to reauthorize a program for a minimum of another five years.

Second, it's important to have rate accuracy. There's too much confusion over rates and fees. Clarity on something like the 25 percent increase, for example. We'd also like to see a strengthening of training for our insurance agents so everybody's on the same page, and consider other incentives for accurate rates.

Third, let's identify programs and funding opportunities for additional investments in strengthening older, pre-FIRM properties against flooding.

Fourth, the Office of Flood Insurance Advocate, created by the Affordability Act, needs additional authority and staffing to be a full-fledged advocate for homeowners when the insurance companies—there's clarity or flaws in the insurance rates that the insurance companies are quoting. The office should also report on these issues it is not able to resolve, under existing NFIP authorities.

And, finally, we absolutely must fix the flood map appeals process. Right now FEMA must first issue regulations before it can begin reimbursing property owners. This could take a while. Many property owners might succeed if they appeal the flood map, but could be discouraged from doing so because they are outside the formal window of 90 days to appeal, or the cost to appeal may be too high. Let's expedite reimbursement of successful appeals by allowing FEMA to issue guidance.

In closing, let me say that I hope we continue down the path of increased certainty and accuracy. Most people are afraid of the unknown, and this holds true in the case of future affordability of flood insurance.

We look forward to working with you in the future to try and keep the current flood insurance in place past that September 30th date, and I thank you for your time and allowing me to be here today.

[The prepared statement of Mr. McKey follows:]

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STATEMENT OF

DAVID McKEY

LOUISIANA REALTORS 2013 PRESIDENT

TO THE

UNITED STATES SENATE COMMITTEE ON SMALL BUSINESS AND ENTREPRENEURSHIP

HEARING TITLED

HOW FLOOD INSURANCE RATE INCREASES AND FLOOD MAPPING POLICY CHANGES WILL IMPACT SMALL BUSINESSES AND ECONOMIC GROWTH

May 1, 2015

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Introduction

Chairman Vitter, thank you for the opportunity to testify. My name is David McKey, and I am the Managing Broker/Owner of Coldwell Banker One in Baton Rouge. I am here today representing the views of 11,350 members of the Louisiana REALTORS®. I have served the Louisiana REALTORS® most recently as State President in 2013. I also currently chair the Flood Insurance Working Group for the National Association of REALTORS®.

The REALTORS® appreciate your continued leadership on flood insurance and especially your hard work last Congress. We note that you were one of the original "Gang of Eight" that drafted the "Flood Insurance Affordability Act" which became Public Law #113-89. One year later, I'm pleased to report the Affordability Act has succeeded in reigning in the most excessive and inaccurate rate increases across Louisiana. We outline a few remaining issues below, but for the most part, the Affordability Act has addressed the most pressing and immediate concerns under the National Flood Insurance Program (NFIP). We look forward to continuing to work with you and the Senate on these and other issues before the current authority for the NFIP expires on September 30, 2017.

Importance of Small Businesses

Small businesses are the engine of economic growth in Louisiana. Small businesses provide the very competition which keeps prices down and spurs market innovations. They are responsible for most job creation within our great state. According to the latest statistics from the U.S. Small Business Administration, Louisiana's small businesses created nearly 25,000 jobs in 2012 alone and employed over half of the state's private workforce.[1] At the same time, flood insurance has become a significant expense for many property owners especially the small business owners who tend to have smaller production lines over which to spread the cost relative to their large competitors. For this reason, it is especially important that any flood insurance rate increases be spread out and gradually phased-in over time so that the small business owners has some time to transition, plan and adapt accordingly.

Implementation of the Biggert-Waters Law

Before the Affordability Act, thousands of small business owners in Louisiana were facing immediate and excessive rate increases under the Federal Emergency Management Agency's (FEMA) implementation the "Biggert Waters" Law. While most of the state's policyholders (83%) were already paying full cost for flood insurance, the 4% that weren't could see rate increases <u>in excess</u> of 25% when the property was purchased[2].

The crux of the problem was FEMA's implementation of Section 205. Under Biggert Waters, property owners including the small businesses were not supposed to see more than a 25% increase in any given year – regardless of whether the property had been sold or not. However, there was a separate provision in the law pertaining to home sales that prohibited the owners of "any property purchased" from paying less than full cost for flood insurance. This home purchase provision was not intended to apply to business property owners, but this was not technically reflected when the House and Senate versions of the law were reconciled and added to a 600-page transportation bill the night before the vote. It was the kind of legislative drafting issue that FEMA could have used its administrative discretion to clarify, but didn't.

To make matters worse, it took more than a year for FEMA to provide the necessary instructions for insurance companies to begin complying with the new law. As a result of this, as well as the lack of clarity on whether the home purchase provision applied to the business properties, insurers filled the vacuum by raising rates by 25% or more if the property sold and the insurer needed to close the gap between the subsidized rate and the full cost for flood insurance. For many business owners, the insurance renewal notice a year after the property's purchase was the first time they were informed of a substantial rate increase under "Biggert Waters."

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[1] For SBA's state profile of Louisiana, see: https://www.sba.gov/sites/default/files/advocacy/LA_0.pdf

[2] See NFIP's analysis of the impacts on the state of Louisiana: http://www.fema.gov/media-library-data/20130726-1912-25045-2652/bw12_impact_fs_04092013_louisiana_508.pdf

Real Estate Market Impacts

News reports of surprise "$30,000 flood insurance" notices drove buyers away from the floodplain and had a chilling effect on real estate markets everywhere. In addition, implementation of Section 207 loomed, which had not taken effect at the time but would have phased out "grandfathering" as well. Most property sellers did not know if their property had been grandfathered under lower risk rate tables at some point in the past. It did not matter that this information was included in the rate quote. All buyers knew was what they heard or read in the news and worried that they too could one day wake up to find a $30,000 bill in the mail. REALTORS® anecdotally reported that often their client's first words were not to show them any listings in the floodplain. As a result, many property owners were left with a property which could not be sold. Others began marketing their property as "does not require flood insurance." Also, according to RAND, a $500 premium increase is associated with a $10,000 decrease in property value based on previous research.[3] Not only were the increases affecting the sellers but also entire neighborhoods as winners and losers were picked. It was costing jobs and income in related industries and rippling throughout the local economy and community tax base.

REALTORS® help others buy and sell their properties. What differentiates the REALTOR® from other real estate agents is they conduct themselves by a higher code of standards governing their interactions with clients. They are the pillars of their communities. Much of their business comes from word-of-mouth referrals so it is especially important to the REALTOR® that they build and maintain working relationships with their former clients. How you get ahead in this business is by managing client expectations every step of way in the property buying process. Big surprises at the closing table are rarely good for business.

Biggert-Waters made an already difficult job more complicated. REALTORS® are a resource, but not the source of the information they provide their clients. It is hard enough for them to advise clients when the flood maps, where flood insurance is required for a mortgage, are not updated and usually inaccurate. Like the buyer, REALTORS® also rely on the insurance agent to quote accurate flood insurance rates.

With FEMA not immediately issuing instructions for insurance agents as to how to raise rates and applying the increases retroactively, insurance agents were not able to quote accurate flood insurance rates that reflected the law of the land. During the period when FEMA failed to act, thousands of properties were sold based on substantially inaccurate flood insurance rates. Worse, until only recently, the property owners did not even know whether their properties' insurance rates were subsidized or not. That information was not included with the flood insurance rate information until after the Affordability Act had passed.

When they received an insurance renewal notice with a large increase after the property's purchase, often one of the first calls from the property owner was to their REALTOR® demanding to know why this information was not disclosed sooner. The truth is the REALTOR® could not have known what the insurance agent did not quote them. Yet, trying to explain this to the client often did not help: At worst, the REALTOR® might be perceived as avoiding responsibility and at best, as someone who did not have the necessary information to sell the property.

Many REALTORS® tried to help their past clients by contacting FEMA directly, but typically, no one there seemed able or willing to verify the accuracy of the rate increases. Eventually, many turned to independent contractors who were hired to find and document mistakes in the rate quotes to try and bring down the rates. Most of the time, the contractor was able to find at least one mistake, but the insurance company often refused to make the rate changes until FEMA weighed in. In one case documented in NAR's earlier Congressional testimony, the contractor succeeded in reducing the rate from over $10,000 down to $500 per year because the insurance agents did not input the correct property information and did not check to see if the property was eligible for grandfathering.[4]

Flood Insurance Affordability Amendments

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[3] RAND. "Flood Insurance in New York City Following Hurricane Sandy," Pre-published report, 2013, page xxi.

[4] For more information about this, see example #3 in the appendix of NAR's November-2013 testimony before a House Financial Services Subcommittee: http://www.ksefocus.com/billdatabase/clientfiles/172/1/1914.pdf

The Flood Insurance Affordability Act addressed the most pressing issues facing newly-purchased business properties by repealing Sections 205 and 207. The bill required FEMA to re-set the rates back to pre-Biggert Waters levels for all properties, including those newly purchased, and cap their insurance rate increases going forward at no more than 25%. Within a few short months of passage, FEMA had re-set the rates. Within a year, FEMA had refunded most policy holders the difference between what they had actually paid versus what they should have paid – something that wouldn't have been necessary had FEMA implemented congressional intent all along.

The latest development in the implementation of the Affordability Act came about a month ago, when FEMA announced the 2015 insurance rates. Increases for 2015 amounted to about a 10% increase for the average policy holder. These increases were largely consistent with those prior to Biggert-Waters. In addition, policy holders were informed of a new surcharge – from $25 to $250 depending on the building. This surcharge paid for the recent rate changes under the Affordability Act. FEMA also established the new Office of the Flood Insurance Advocate to assist property owners when they have questions about the accuracy of their flood insurance rates and flood maps. Property owners should not have to hire outside contractors when it's FEMA's responsibility to instruct its own insurance contractors on how to implement FEMA's own rules. FEMA's office of the Advocate is intended to serve this function. FEMA is now in the process of transitioning the office from an interim to a permanent basis, and we are working with the Agency and Congress to find way to strengthen the office so it will become a "full-fledged" advocate for the property owner.

Recommendations on Remaining Issues

While the Affordability Act addressed the most excessive and inaccurate rate increases, there are still some remaining issues which we would like to bring to your attention:

1) **Long-term Reauthorization.** The National Flood Insurance Program will sunset in 2017 unless Congress renews program authority to provide flood insurance. We would urge the Congress to reauthorize the program for a minimum of another 5 years. Shorter term extensions only exacerbate market uncertainty and disrupt property sales where flood insurance is required for a federally related mortgage.

2) **Flood Insurance Rate Accuracy.**

   a) **25% Increases into Perpetuity**. Currently, the 25% increases for older ("pre-FIRM") properties do not end until the property owner (including business properties) is paying the full cost for flood insurance. The only way for an owner to demonstrate that they are paying the full cost is to obtain an elevation certificate which can cost anywhere from $500 into the thousands of dollars. If the elevation certificate shows the property owner is paying too much, the owner may request an optional "full-risk" rating under FEMA's guidelines to end the 25% increases. Yet, many of these owners are not aware of this option, which means that some could be paying a 25% increase that is not appropriate. There also seems to be some confusion over the $250 surcharge and its application to every building, including condos and detached structures, unless the owner declares that it is their primary residence. Recommendation: Clarify the 25% increases and provide for reimbursement for those who obtain an elevation certificate.

   b) **Elevation-Based Rating Errors**. The Affordability Act slowed the rate of increase but subsidized rates will keep increasing until they reach their full actuarial level as determined by an elevation certificate. If the procedures used to eventually rate these properties are not accurate, then the property owner could end up being over charged for flood insurance in the future. Most of the inaccurate rate increases we reviewed were for pre-FIRM properties located 2 or more feet below the Base Flood Elevation and mis-rated under special "Submit-to-Rate" procedures. We seek a full and thorough review of these procedures to ensure the accuracy of the flood insurance rates before subsidized properties begin paying too much for flood insurance. Recommendation: Request an independent actuarial review of FEMA's "Submit-to-Rate" procedures, strengthen insurance company training, and consider other incentives for accurate rates.

3) **Property Mitigation.** NFIP currently owes $23 billion on Treasury loans and one million properties are paying a "subsidized" rate. The more of these properties that are flood proofed, elevated, relocated or otherwise

strengthened against the risk of flooding, the lower the overall risk exposure of the NFIP and therefore taxpayers will be. Recommendation: Think outside the box and across the federal government to identify programs and funding opportunities for additional investments in mitigating pre-FIRM properties.

4) **Flood Insurance Advocate.** The Affordability Act established the office which was recently funded with appropriations. But the Office has not fulfilled its advocacy function of ensuring insurance rate accuracy. We understand that the Office is informally coaching some property owners on what questions to ask their insurance agent, but some are simply being referred back to the agent because the Office does not have the staff, resources and authority to directly contact every insurance company on every issue that arises with their insurance rate quotes. Recommendation: Clarify and provide additional authority and staffing for the Office to directly instruct insurance agents and companies when insurance rates are flawed and report on those issues it is not able to resolve under existing NFIP authorities.

5) **Flood Map Appeals.** FEMA must first issue regulations before it can begin reimbursing property owners when they successfully appeal flood maps. FEMA reports that such a rule could take several years to complete. At the same time, however, property owners have just 90 days to appeal in order to be eligible for reimbursement once those regulations are issued. Many property owners might succeed if they appeal the flood map but could be discouraged from doing so because they're outside the 90-day formal window or out-of-pocket on the cost to appeals. It is not clear why some should be reimbursed but not everyone who wins an appeal. In both cases, the map has been found to be inaccurate. As long as reimbursement is tied to a successful challenge, this should discourage appeals except when a property owner believes they have a sound basis to do so. Recommendation: Expedite reimbursement of successful appeals by allowing FEMA to issue guidance, instead of requiring a formal notice-and-comment rulemaking. Clarify that homeowners may appeal at any time and get reimbursed whenever they win.

Conclusion

Thank you for the opportunity to testify about flood insurance. We greatly appreciate the Committee's work in this area. We look forward to working with you and the Senate on these and other issues before the current authority for the NFIP expires on September 30, 2017.

Chairman VITTER. Great, David. Thank you very, very much. Thanks to all of you. And now I'm going to turn it over to Senator Cassidy for comments and questions, to begin.

Senator CASSIDY. Mr. Bourgeois, I really liked your comments, but I think it's also important to understand that, one, we've got to have a five-year reauthorization, at least, and we have to put in those reforms that will actually lower the premium for those of us who are purchasing insurance, absolutely.

But we would not be totally kind of in the right context to understand, this is going to be a political battle. It really is. Because if there's somebody on a mountaintop in New Mexico, they may wonder why they, quote/unquote, are subsidizing us. Now, that is, until they have a flash flood and they are now rated—since they live next to a stream—as in a 500-year flood zone.

Now, I say that not tongue in cheek, but accurately describing what takes place. Because once you start talking 500 years, there is no place in the Nation, including mountaintops in Colorado, that are not at risk.

So just to say, in a political context, what Senator Vitter and Congressman Scalise and the others do is going to be tough because people do not yet understand their own community's risk.

Let me point out a couple other things just in comment to what you all said. You are right. A minority of people who should have flood insurance have it. But that's actually not FEMA's fault—although it's always wonderful to blame FEMA—it's actually the banking, the judiciary. It's another government department that should require that.

And there is some reticence when we have a program that has been broken, charging rates that are too high, to go start tracking down a middle-income homeowner to pay a rate that is not actuarially sound. Do you follow what I'm saying?

So if you are in the middle of Kansas and all of a sudden you're rated because you live near a river, for a high premium, but your premium is too high because the flood map is wrong, are you really going to take them to court because they're not doing it?

Now, I say all of this to give a context of what Senator Vitter and I will be working with in the Senate and our Congressmen and women will be doing on the House side, and that is, all your ideas are good. It's going to be tough.

Let me finish by something optimistic before I turn it over to David. The way it worked last time is you all got involved. The way it worked last time is that people got on their Facebook page, reconnected with someone they went to high school with and who lived in Wisconsin, and said, "By the way, do you know what's about to happen to your rate," and when she got involved, she contacted her Congresswoman, and all of a sudden it began to work. Realtors, bankers, home builders, insurance brokers all began to contact——

The best example I can give, I was on the House side. We were setting up a caucus, a homeowners' caucus, to advocate for this, and I went up to a fellow from southern Florida and I said, "Are you familiar with Biggert-Waters, the rate increases? We need your help on this caucus." He goes, "I haven't heard from my constituents about this." So I walked out, I called up some realtors in Louisiana and I said, “Light up south Florida.” They lit it up, and he got on the caucus and became one of our biggest advocates.

Now, this is something where y’all being involved will make a difference on a national level. David.

Chairman VITTER. Great. Thank you, Bill. I want to start by going to Jerry Passman. Jerry, we’re all concerned about this new Executive Order related to climate science and floodplain management.

You heard what Roy Wright said. Based on that, if all of that were truly nailed down, if all of that were accurate, would that affect your new construction activity still or not?

Mr. PASSMAN. Well, we think, if you go to the preamble, the intent is for Federal buildings, Federal highways and that sort of thing.

As a home builder, if the Federal government wants to apply it to buildings they are building or highways they are building, we’re fine with it, but the EEO clearly states that it applies to all federal actions, and we can see where that would go to private construction, because as I had mentioned in my testimony, many of the houses I sell are bought with a mortgage that is backed by the Federal government, like Fannie Mae and Freddie Mac, so that’s a federal action.

Also, there could be a 404 Wetlands Permit. There’s definitely a 402 Clean Water Permit on those. Again, those are federal actions.

And my experience is, and from what I’ve seen from being active in my trade association, if you give a Federal regulator an inch, they will take a mile. And you can just look how convoluted the word Navigable Waters has become. They’ve tortured, twisted it, and then everyone in this room would probably come up with a definition of Navigable Water that’s definitely not the definition of Navigable Water in Washington, DC.

Chairman VITTER. Right. Okay. And following on from that, even in the areas that it’s clearly meant to be about, like a federal highway project or a Federal building, certainly that’s going to impact us and the economy here, right?

I mean, building these things to a much, much higher standard often means they never get built. I mean, we’ve sort of dealt with that, Dwayne, with some of the demands post-Katrina in terms of levee standards, correct? Can you expand on that?

Mr. BOURGEOIS. Well, in the guidance, in the Federal Flood Risk Management Standard gives an example of a post office, and suggests that just placing a post office somewhere within this floodplain encourages other people to be there. Because you’ve got the construction of the post office and the roads, the highways and the infrastructure leading to it, and then the fact that you’ve got a post office, it suggests that that’s going to bring people to the area because of the Federal services.

So, you know, it’s clearly stated to try to avoid, directly or indirectly, encouraging development inside, and that’s inside the guidance more than the Executive Order itself, that modifies the things, but yes, we definitely had similar problems.

You know, if it’s going to be more costly to be constructed, with the limited availability of funds across the board, it’s just not going to get selected. And it’s also a good opportunity for an agency to make a determination not to select something. That's another reason to check off not doing it.

Chairman VITTER. Okay. And, also, Dwayne, to you, as a follow-up on the FEMA flood mapping side, how would you grade how FEMA is doing in that regard, including this so-called LAMP process that has a lot of applications in Louisiana?

Mr. BOURGEOIS. Well, the LAMP process, the Levee Analysis Mapping Procedure, has to do with getting some credit in the flood insurance study for noncertified levees, okay. You guys did a great job convincing FEMA to include this legislation, in the first place, so that the Without Levees Policy, which was quite archaic, was removed.

Currently there's 25 communities throughout the United States that are doing a pilot of this LAMP, with five of them in Louisiana.

The biggest issue about that, to me, that we need is flexibility, because in all of the documentation and all of the processes they created in LAMP, they were more riverine-oriented, and we did get the folks that were developing this to eventually say that they realize that most of the processes they've looked at there weren't suitable for coastal levees. The flood source is opposite. The time of the flood source is much, much shorter, and you just have to hang on for the length of the storm versus a riverine flood that could last for weeks.

To that, they purposely made some of the coastal issues vague. My biggest concern is that we have flexibility. So far it looks like we are getting that, but, again, when you get into the realm of guidance as compared to something that's truly codified, it's difficult to be assured that they're going to let the regional offices and their mapping partners aware that they have the flexibility to look at alternatives to determining the still-water elevations and the wave run-offs and other things of that nature.

Overall, it seems like they are, but I would have loved to have seen something in writing that tells those good-intended FEMA partners that they have that authority.

Chairman VITTER. Right, okay.

Senator CASSIDY. David, can I?

Chairman VITTER. Sure.

Senator CASSIDY. Jerry, how much more will it cost to build a home compliant with these recommendations, two to three feet higher than currently being elevated?

Mr. PASSMAN. Well, when we build in a flood area and we have to build a pad for it, we typically figure about 10—and it depends on the size of the home. I mean, you know, obviously a 2,000 square foot house is going to cost less than a 3,000, but say the average house I build is 22-, 2300 square foot. We generally figure $10- to $12,000 feet per foot higher that we have to build the house.

Senator CASSIDY. So if you have to build it three feet higher, it will be $36,000 more for the same square footage?

Mr. PASSMAN. That is correct, yes.

Senator CASSIDY. And, David, if you're reselling your home, and people rode down the block, and this one's three feet higher than yours, at least, in my mind, it makes me think that the one that's not elevated is at greater risk. Will that affect the resale, if there is a patchwork of homes elevated and homes not?

Mr. McKEY. I don't think it's any doubt that it will. And, again, as I mentioned earlier, perception is reality, so when they do see that elevated home and they see that one that's built on a slab, I think—the first thing, in their mind, is how much in flood insurance am I going to have to pay for the one that's just a slab house, and it makes it less appealing, No. 1.

And No. 2, again, the likeliness of that house selling is going to be reduced pretty dramatically, and it's going to have an impact not only on that house, but it's also going to have an impact on that house that you just put 35,000 additional dollars in.

Senator CASSIDY. I see. So it drags down that value because of the surrounding property. And by the way, my point with Roy, who was here, of course, we want higher and better, but you could, you know, build a castle, and it's not practical, but at some point there's a cost-benefit ratio.

Mr. McKEY. That's correct, yes.

Senator CASSIDY. Okay. David.

Chairman VITTER. Great, okay. We're going to wrap up. Thanks to all of our witnesses on the second panel who have given a great Louisiana real-world perspective. Let's give them a round of applause.

[Applause].

And thanks to all of you. Obviously, the Flood Insurance Program, flood mapping, all of those related issues are critically important to south Louisiana. They're important to small businesses, they're important to economic growth, and that's why we had this town hall meeting and hearing, and that's why Bill and I, with the rest of our delegation, will continue to work on these crucial issues, and we certainly don't want this exchange to be an isolated visit.

I believe each of you walking in got a hand-out. On the left-hand side of the hand-out, in that blue column, is all of my contact information, so please keep that handy, and please don't hesitate to call, write, email about these and other related issues, whenever it's appropriate. Thank you all very much.

Thank you for being here today.

[Whereupon, at 11:04 a.m., the hearing was adjourned.]

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