

NATIONAL FLOOD INSURANCE: THE BIGGERT-WATERS ACT

By

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Background. The National Flood Insurance Program (“the Program”) was created by Congress in 1968 to mitigate the financial impact of floods on residents and communities. It also encouraged smarter planning choices *[and discouraged some development]* in areas with an unacceptable risk of flooding. The NFIP is controlled by the Federal Emergency Management Agency (“FEMA”).

The Financial History of the Program. Historically the Program has not been run in a prudent financial manner. From its inception in 1968 to the present, Congress has failed to pass legislation to address problems within the program, instead choosing to pass multiple extensions. With losses estimated in the billions of dollars after severe flooding events such as Hurricanes Katrina, Rita, Irene, and more recently, Sandy, the Program’s resources have become depleted. According to the Government Accounting Office (“GAO”):

"The potential losses generated by NFIP have created substantial financial exposure for the federal government and U.S. taxpayers. While Congress and FEMA intended that NFIP be funded with premiums collected from policyholders and not with tax dollars, the program was, by design, not actuarially sound. As of November 2012, FEMA owes the Treasury approximately \$20 billion, up from \$17.8 billion pre-Sandy, and had not repaid any principal on the loan since 2010."

In January 2013, Congress, passed legislation to temporarily increase NFIP’s borrowing authority to \$30.4 billion.

Biggert-Waters Flood Insurance Reform Act of 2012 (“the Act”). Although the Act became effective on July 6, 2012, there has been relatively little attention given to the new law until now.

The Act implemented a number of changes, but the most significant for sellers, buyers and their real estate agents is the phase-out of flood insurance subsidies for certain property owners. The rationale for the phase-out is twofold: (a) To bring in more revenue for FEMA; and (b) To make the cost of flood insurance more accurately reflect the actuarial risk.

The result, not surprisingly, is that many property owners are now finding themselves facing the prospect of unaffordable coverage and/or properties they are unable to sell due to unexpectedly high flood insurance premiums. In addition, FEMA has been redrawing the flood maps for communities across the US. As a result, some properties not previously required to obtain flood insurance have now been classified as high-risk.

Coverage and Rates. Under the Act, homeowners, renters, and business owners may purchase federally-backed flood insurance through private brokers. Rates and coverage is federally determined

and is identical regardless of insurer; rates are set in compliance with the Program. Here is a summary of coverage:

- Homeowners may insure for up to \$250,000 in property damage plus \$100,000 for the contents of the property;
- Renters may insure for up to \$100,000 for the contents of their rental unit;
- Business owners may insure for up to \$500,000 for the premises and contents of their business in total.
- Owners of multi-family housing (5+ units) are entitled to a full \$500,000 coverage policy and unit occupiers may insure the contents of their dwellings separately for up to \$100,000.

High-Risk Areas. Insurance is available for homeowners and business owners in high-risk areas, called Special Flood Hazard Areas (“SFHAs”). They are defined as “any land that would be inundated by a flood having a 1-percent chance of occurring in a given year.” These areas are identified and mapped by FEMA. Home or business owners in SFHAs who acquire a loan from a federally regulated and insured lender must carry insurance for the life of the loan. This constitutes just about every residential loan program in the marketplace, i.e. conventional, FHA, VA, USDA, etc. - except private loans. Just the same as with fire insurance, if coverage lapses, lenders may “force-place” a flood insurance policy on the property. Homeowners, renters, and business owners in low-to-moderate risk areas may also purchase flood insurance, although it is not mandatory.

The Subsidy Phase-Out. The phase-out is expected to affect roughly 20% of properties under the Plan, or about 1.12 million of the 5.6 million flood insurance policies in effect. Initially, structures built before a community adopted a “Flood Insurance Rate Map” (“FIRM”) were allowed to purchase flood insurance coverage with subsidized rates. [These are referred to as “Pre-FIRM” properties.] Now, under the Act, the Pre-FIRM Properties, estimated to be about 5% of the 1.12 million flood-insured properties, will see increases phased-in *immediately*. Additionally, the following properties – formerly subsidized – will also see their premiums increase:

1. Second homes;
2. Businesses;
3. Severe repetitive loss properties – properties with 1-4 residences making multiple claims under flood insurance policies;
4. Substantially improved or damaged properties.

Subsidies will be phased out at a rate of 25% per year until the property owner is paying premiums commensurate to the property’s risk level. This will apply to: (a) Any property purchased after the effective date of July 6, 2012; and (b) Any property not previously covered by flood insurance. Any property that was covered by a lapsed policy, including primary residences, will *not* be eligible for any subsidy going forward.

Primary Residences. FEMA reports that subsidies are not being phased out for existing policies covering primary residences. However, owners may see rate increases similar to non-subsidized policies due to FEMA’s redrawing of its flood maps.

Miscellaneous. Additionally the Act also makes major changes to insurance for all holders of a Plan policy: insurance may now be paid in installments, and rate changes are capped at 20% annually, up from 10% in previous years. However, the rate increase cap does not apply to those in a subsidy phase-out program. Most policy-holders will see increased cost as the Act requires FEMA to maintain a reserve fund.

The Biggert-Waters Act also makes a number of less controversial changes to the technical aspects of flood insurance and mapping, including but not limited to: setting the lower limit on deductibles; setting civil penalties for lenders who do not require flood insurance under a federally funded program; providing direction to FEMA in setting premiums; creating a technical advisory board to oversee flood mapping; creating an appeals board for property owners disputing mapping decisions; providing direction to private insurance companies in creating their own flood insurance policies [*known as "Write-Your-Own" policies*]; allowing the Plan to take over policies from private insurers, etc.

Realtor® Tips

- ***For any property that is located near waterways, including the ocean, flood insurance must be considered.***
- ***Lenders will require a flood certification stating the flood zone status. Know how the "flood certs" are performed. [E.g. if they are entirely computerized they may indicate the property is in a flood zone, when it is not.]***
- ***The Oregon Seller's Property Disclosure Statements does ask if the property is in a flood zone. If in doubt, do not accept "No" as the final answer. Always beware of "Unknown" answers. Encourage your buyer-client to secure expert help.***
- ***Sellers and their listing agents should consider vetting the flood zone issue before placing the property on the market.***
- ***The OREF Sale Agreement does not address flood zones or flood insurance at the present time. This likely will change, but perhaps not until next year.***
 - ***The National Association of Realtors® has a sample Disclosure form that [depending on company policy] you may wish to use. It can be found [here](#).***
 - ***Buyer brokers should consider making the flood insurance issue a contingency in the offer, whereby the existence and cost of flood insurance becomes a condition of buyer's obligation to purchase the property.***
- ***While it is true that Realtors® are not expected to be "experts" or to research whether a property is located in a flood zone, it is also true that they should not ignore the issue if all of the signs point to the property being in or near a floodplain.***

- *Here are some risk management reminders:*
 - *Sellers in high risk areas will likely experience an increase in premiums, either because of the phase-out of premium subsidies, or because of FEMA's remapping of flood zones;*
 - *If the property is going to experience a phase-out of the premium subsidy, it is important that the seller know this before putting the property on the market;*
 - *If the property is not going to experience an immediate phase-out [e.g. it is a primary residence], it may still experience some increases due to FEMA remapping, although under the Act, there are premium caps in the new law.*
 - *Instruct your clients to secure expert help. This may be one or more persons in the insurance industry, familiar with the new law, likely premium increases, and how best to reduce rates with good flood protection tips. If you have one or more names of experts, provide them – but don't "endorse" them.*
 - *Never, never, never, hold yourself out as an "expert." The law does not hold you to that standard. You don't have to say you're an "expert" – it is sufficient if you act as one. Don't act as one. Encourage your client to secure their own expert.*

Realtor® Resources

- NAR, LEGAL GUIDANCE ON DISCLOSURES:
<http://www.ksefocus.com/billdatabase/clientfiles/172/4/1816.pdf>
- FEMA, QUESTIONS ABOUT THE BIGGER-WATERS FLOOD INSURANCE REFORM ACT OF 2012:
http://www.fema.gov/media-library-data/20130726-1912-25045-9380/bw12_qa_04_2013.pdf
- FEMA, FLOOD INSURANCE: HOW IT WORKS, (Sept. 2013):
http://www.floodsmart.gov/toolkits/flood/downloads/FloodInsuranceHowWorks_11%2019%2010.pdf
- FEMA, ANSWERS TO QUESTIONS ABOUT THE NFIP, 3 (March 2011): http://www.fema.gov/media-library-data/20130726-1438-20490-1905/f084_atq_11aug11.pdf
- NATIONAL ASSOCIATION OF REALTORS, FLOOD INSURANCE REFORM ACT OF 2012: SECTION BY SECTION HIGHLIGHTS, (Nov. 7, 2012): <http://www.realtor.org/articles/flood-insurance-reform-act-of-2012-section-by-section-highlights>
- Les Christie, *Flood Insurance Costs Soaring for Thousands of Homeowners*, CNN MONEY (Oct. 21, 2013): http://money.cnn.com/2013/10/21/real_estate/flood-insurance/index.html

- Insurance Journal, *Rep. Waters, Author of Flood Reform Act, Calls for Delay in Implementation*, (Sept. 30 2013):
<http://www.insurancejournal.com/news/national/2013/09/30/306602.htm>
- Arthur D. Postal, *FEMA Reps Bracing for Consumer Backlash When NFIP Actuarial Rates Phased In*. Property Casualty 360 (Dec. 3, 2012):
<http://www.propertycasualty360.com/2012/12/03/fema-reps-bracing-for-consumer-backlash-when-nfip>

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