Testimony of

America's Community Bankers

on

National Flood Insurance Program, and
FEMA's Repetitive Loss Mitigation Strategy

H.R. 253 and H.R. 670

before the

Subcommittee on Housing and Community Opportunity

of the

Financial Services Committee

of the

United States House of Representatives

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Good afternoon. Chairman Ney, Ranking Member Waters, and Distinguished Members of the Committee, thank you for the opportunity to testify at today's hearing on the National Flood Insurance Program (NFIP) and specifically on the Federal Emergency Management Agency's (FEMA) repetitive loss mitigation strategy and multi-year reauthorization of the NFIP.

My name is Frederick Willetts III. I am President and CEO of Cooperative Bank in Wilmington, North Carolina. Cooperative Bank is a state chartered commercial bank with total assets of $500 million. The bank and it's subsidiary operate 20 offices from Virginia Beach, Virginia to Myrtle Beach, South Carolina. I am testifying today as a member of America's Community Bankers (ACB). ACB's member banks originate more than 25 percent of all mortgages in the United States, and significantly more than half of all mortgages originated by depository institutions. In addition, our members operate a large number of mortgage banking affiliates that originate a substantial part of the business from that segment of the industry.

The NFIP is important to every mortgage lender in the United States whose lending territory includes properties in areas of high flood risk. ACB members and their customers have come to rely on the NFIP as a primary source of affordable flood insurance. As a result, we would like to focus our remarks on the impact of these bills on our members and their customers.

Thank you for the opportunity to testify today on this important program.

ACB's Positions

We support attempts by FEMA, the Administration, and Congress to begin to stem the costs to taxpayers associated with repetitive loss properties. However, it is vital that any such efforts protect mortgage lenders to the extend possible by giving them advance notice of any actions that would impair the ability of the homeowner to repay the mortgage or recoup the value of the property. Also, Congress must clarify that it does not intend to treat as repetitive loss properties those that have experienced losses not expected to be recurrent.

Additionally, ACB believes that any bill to revise the NFIP must include a multi-year extension of NFIP authorization.

Explanation

H.R. 253—"Two Floods and You are Out of the Taxpayer's Pocket Act" and H.R. 670—"Flood Loss Mitigation Act"

Repetitive Loss Properties

H.R. 253 and H.R. 670 propose a two-pronged approach to curtail excessive government subsidies on repetitive loss properties. First, the bills would increase funding and improve procedures for mitigating losses under the NFIP. For many years, FEMA has endeavored to mitigate repetitive losses through various strategies, including the purchase, relocation, and elevation of properties that have experienced repetitive losses. The funds available for such mitigation efforts have been limited. Both bills would provide additional financing for FEMA's loss mitigation strategy.

Second, each bill would put some responsibility on property owners to bear the cost of not accepting the government's buyout or mitigation offers. The bills impose these responsibilities in different ways. H.R. 253 would require property owners to pay actuarial rates for their flood insurance and would make repetitive loss policyholders ineligible for federal disaster relief assistance if they refuse mitigation measures. H.R. 670 provides that policyholders who refuse mitigation assistance could face higher premiums or cancellation of NFIP policies.

ACB supports increased flood insurance premiums under the circumstances identified in the bills as a way of making property owners take additional responsibility to prevent multiple claims. However, we think the bills should take into account circumstances that might unduly imperil the homeowner, the lender, or other affected parties.

Specific Policy Concerns Regarding Mortgage Lender Protection

Termination of flood insurance or large increases in premiums will have significant consequences for homeowners and lenders that have financed their home purchases. It has been estimated that the average annual flood insurance premium assessed for targeted properties would increase from approximately $600 per year to $10,000 per year. Such an increase would not only represent a financial hardship on the property owner (perhaps beyond his or her capacity to pay), it also likely would affect the value and marketability of the property.

The mortgage lender who extended credit based upon the borrower's ability to pay and the property's market value should be notified formally of the planned premium increase in advance and at a time when intervention might still be possible. For similar reasons, prospective purchasers and mortgage lenders should also be made aware of the proposed premium increase.

There are also situations where a lender's collateral would be put at great risk by a mitigation buy-out offer. A key objective of H.R. 670 and H.R. 253 is to dramatically expand FEMA's current efforts to acquire properties and relocate families out of areas prone to repeat flooding. Unlike a traditional property sale, however, FEMA's goal is not to preserve the structure, but to demolish it. As a result, lenders' collateral is put at risk. Lenders' deserve some assurances that any loan secured by a property targeted for demolition will be repaid with the proceeds of the buyout. As a result of this concern, we recommend that the bills provide for notice to the mortgage lender or servicer of a buyout offer made under the mitigation program.

We believe there are circumstances in which homeowners should not be required to accept a buyout offer under the mitigation program. H.R.670 makes this exclusion in the following instances: (1) the homeowner would be unable to purchase a replacement structure; (2) flood damage was caused by a third party; (3) the property was historically significant; or (4) the property was not located in a Special Flood Hazard Area at the time of purchase. H.R. 670 further grants the Director of FEMA the authority to provide other exemptions.

ACB supports these exemptions and would like to recommend that an additional exemption be added. We request that consideration be given to excluding purchase offers that are insufficient to pay off the outstanding balance on mortgages secured by these properties. We do not believe homeowners should be penalized for refusing buyout offers when the mortgage balance exceeds the purchase offer. Homeowners should not have their flood insurance cancelled, premiums significantly raised, or be made ineligible for disaster relief because the property value has declined significantly since it was purchased.

Again, we believe there are numerous reasons why a buyout or mitigation offer is not the best solution in all instances. Therefore, we support the appeals concept found in H.R. 670, which allows homeowners to appeal a decision to cancel flood insurance or increase the insurance rates.

In addition, ACB believes it is essential for Congress to clarify that it does not intend flood insurance coverage be denied to properties in broad geographic areas that might experience large number of losses as an aberration. For instance, under the bills, specific property owners and those in limited, designated areas might be denied flood insurance coverage, or charged higher premiums, if they have multiple claims in certain time periods and have refused mitigation assistance. Such denials might occur for a property on a point of land on a coastal bay, or a neighborhood at the confluence of two rivers.

ACB does not view the bills as applicable to potential denials of coverage in broad geographic regions. For instance, the region in which I live, coastal Carolina, has recently experienced an unusually large number of hurricanes, one of which resulted in a 500-year flood. It would not be practicable for FEMA to respond to such circumstances by seeking extensive mitigation or relocation. Such actions would be neither practicable nor warranted, be they for coastal Carolina, Louisiana, or Texas, or perhaps for entire river systems. It is essential that Congress clarify the expected scope of circumstances under which FEMA might deny, cancel or otherwise change the availability of flood insurance under the bills as proposed to avoid such unintended applications of any statutory change.

Implications for Lapse in NFIP Statutory Authority

H.R. 253 also would extend the authorization of the NFIP until 2007, which ACB strongly supports. Under the NFIP, financial institutions are prohibited from originating or refinancing loans secured by property in Special Flood Hazard Areas unless covered by flood insurance. Federal financial institutions, agencies, and FEMA each have adopted regulations requiring lenders to compel compliance with mandatory flood insurance purchase requirements for residential properties in NFIP participating communities. Lenders must first determine if the structure is located in a Special Flood Hazard Area, and then must provide written notice to property owners requiring flood insurance.

The lack of NFIP authorization at the beginning of the 108th Congress could have caused significant disruption to property owners whose policies were not issued or renewed before December 31, 2002. During the lapse in authorization, FEMA estimates that approximately 400,000 households may have been prevented from obtaining or maintaining insurance, and those seeking home loans or mortgage refinancings that require flood insurance as a precondition to settlement might have been delayed or prevented from completing their transactions.

To avoid such problems in the future, ACB advocates a multi-year extension of NFIP authority for a period of at least four or five years.

Conclusion

ACB looks forward to working with FEMA on solutions to make the NFIP a beneficial program to all entities.