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TESTIMONY

Association of State Floodplain Managers, Inc.

before the
Subcommittee on Housing and Community Opportunity
House Committee on Financial Services

Bunning-Bereuter-Blumenauer Flood Insurance Reform Act Implementation and Flood Insurance Claims Issues

presented by
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State of Ohio

April 14, 2005

INTRODUCTION

The Association of State Floodplain Managers, Inc., and its 20 State Chapters represent over 7,000 state and local officials and other professionals who are engaged in all aspects of floodplain management and hazard mitigation, including management, engineering, planning, community development, hydrology, forecasting, emergency response, water resources, and insurance. All are concerned with working to reduce our nation's flood-related losses. Our State and local members are the federal government's partners in implementing programs and working to achieve effectiveness to meet our shared objectives. Many of our members are designated by their governors to coordinate the National Flood Insurance Program (NFIP). For more information on the Association, please visit <http://www.floods.org>.

Representatives Bereuter, Blumenauer, and Baker worked extremely hard the last several years to improve the NFIP, culminating in the passage of the Bunning-Bereuter-Blumenauer Flood Insurance Reform Act of 2004 (2004 Reform Act). The ASFPM was pleased to have been a part of effort. From our perspective, the Act contains three critical elements:

1. The creation of a short term, aggressive program to mitigate repetitive loss properties.
2. Changes to existing NFIP-funded mitigation programs and use of insurance claim payments for compliance with planning and land use control measures.
3. Changes to improve insurance claims handling, agent education, and property owner notification.

The Nation's floodplain managers have been anxiously awaiting implementation of the 2004 Reform Act and are disappointed that the Administration's budget request for FY 2006 does little to move in that direction. The ASFPM appreciates that the Subcommittee is holding this hearing to monitor both the implementation of the 2004 Reform Act and ongoing implementation of the NFIP. We thank you for inviting us to offer our views. This testimony addresses:

1. The Repetitive Loss Problem: Summary
2. Repetitive Loss Implementation Issues:
 - Funding Source and Amounts; 2006 Budget Request
 - Basic FMA: State and community Caps and Limitations on Time to Expend
 - Rulemaking for Pilot Program and FMA Individual Program
3. Changes to Existing NFIP & Mitigation Programs:
 - Status of ICC Changes
 - Guidance to Qualify for Reduced Community Match
 - Eligible Activities: Inclusion of the "Demo/Rebuild" Option
4. Adequacy of Flood Insurance Coverage
5. Related NFIP Issues
 - Taxation of Mitigation Benefits
 - Flood Map Modernization
 - FEMA in DHS: Impacts on Programs and Legacy Missions

1. THE REPETITIVE LOSS PROBLEM: SUMMARY

It is important to put the repetitive loss problem in context. While the exact number is not known, it is estimated that over 9 to 11 million buildings are in the areas we call special flood hazard areas that are shown on FEMA's Flood Insurance Rate Maps. About 4.5 million buildings both in and out of the floodplain are insured today (up from only 2 million just 9 years ago). Of those, about 40,000 are on FEMA's list of repetitively flooded properties. Nearly 10,000 have experienced four or more losses, or two or more losses which combine to exceed the building's value as reported on the flood insurance policy. This means that initially we are focusing attention on one-quarter of one percent of the insured buildings. But the impact is huge, since that small fraction accounts for over 25% of the NFIP's losses since 1978.

Why should everybody be concerned about this issue? All current and future NFIP policyholders will benefit because the pressure to raise the rates will be significantly diminished. FEMA reports that properties that have received multiple insurance claim payments account for an average of \$200 million in claims each year. FEMA asserts that this is the most significant factor driving rate increases on all types of policies and all policyholders. Repetitive claims affect the stability of the National Flood Insurance Fund.

FEMA has recognized the repetitive loss problem and in recent years has taken positive steps to help identify issues and to use existing mechanisms to begin to address it. For example, handling of flood insurance policies for certain repetitive loss properties has been consolidated in a special direct facility so targeted outreach and data collection efforts can occur. Also, in recent years Flood Mitigation Assistance Program funds were prioritized for repetitive loss properties, and the first year of FEMA's Pre-Disaster Mitigation program identified mitigation of repetitive loss properties as a national priority.

In December 2003, FEMA convened a meeting of stakeholders to obtain input into a Repetitive Loss Action Plan. A draft plan was produced, but as of early 2005 ASFPM has not been advised of the status or steps taken towards finalizing the plan and its implementation.

2. REPETITIVE LOSS PROGRAM IMPLEMENTATION ISSUES

FUNDING SOURCE AND AMOUNTS; FY2006 BUDGET REQUEST

The Flood Insurance Reform Act of 2004 authorizes additional funding and mechanisms to focus mitigation efforts on "severe" repetitive loss structures that result in disproportionate claims on the National Flood Insurance Fund (the Fund). Importantly, the additional mitigation funding is to be derived from that Fund, which recognizes that the NFIP and policyholders, rather than taxpayers as a whole, will benefit from the added mitigation elements. A primary focus of the Act is to augment the existing Flood Mitigation Assistance Program in three ways:

- **Basic Flood Mitigation Assistance Program:** Increases the authorized limit of funding for the Basic FMA to \$40 million per year; the funds are to be transferred from the National Flood Insurance Fund and are to remain available until expended. As authorized in 1994, Basic FMA had an annual ceiling of \$20 million and FEMA imposes a 2-year limitation on availability, causing difficulties for many communities and property owners.

- **Pilot Program:** Authorizes the Pilot Program, which essentially is an adjunct to the Basic FMA program with particular focus on “severe repetitive loss properties” as defined by the Act. The Pilot Program, authorized for just five years, has an authorized limit of funding of \$40 million per year. These funds are to be transferred from the National Flood Insurance Fund and they are time-limited; the Act specifies that assistance may not be provided after September 30, 2009. The Act states that the transfer of funds shall not be subject to offsetting collections through premium rates, and S. Report 108-262 clarifies that the policy service fee shall not be increased because of the transfer.
- **FMA Individual Program:** Authorizes a program, with an annual funding limit of \$10 million, under which FEMA may work directly with individual property owners of severe repetitive loss properties if a state or community do not meet the requirements.

With respect to these programs and the President’s Budget for FY2006, the budget request includes only \$28 million to be transferred from the National Flood Insurance Fund for the Basic FMA program and which are to be available for only two years (the request does not include funds for the Pilot Program or the Individual Program). The Basic FMA program is a fully functioning, mature program. Therefore, ASFPM is puzzled why the budget requested only an additional \$8 million. Given FEMA’s long-standing and repeated emphasis on the long-term benefits of mitigation of repetitive loss properties, ASFPM does not understand the Administration’s reluctance to move more aggressively. We recognize the need for rulemaking for the Pilot Program and the FMA Individual Program. However, at this rate two years of the 5-year Pilot Program will be lost. This points out the urgency of moving to implementation as quickly as possible.

Undersecretary Brown testified last month that FEMA was still analyzing exactly from where the funds to implement the 2004 Reform Act would be derived. He differentiated between premium income and policy service fee income. During that testimony, it was clear that the requested increase of \$8 million will come from policy service fee income (the traditional source of FMA funds). The 2004 Reform Act does not specify which part of the NFIF the funds should come from, although transfers for both the Pilot Program and the Individual Program are not to be subject to offsetting collections through premium rates for flood insurance coverage and Senate Report 108-262 clarifies that the policy service fee is not to be increased because of the transfer.

The ASFPM asserts that it should not matter whether the transfers come from flood insurance premium income or policy service fee income, and that both sources are acceptable. Although there may be some trepidation about transferring premium dollars because it is a nontraditional use, there is a precedent. Prior to the National Flood Insurance Reform Act of 1994 the NFIP contained a provision in Section 1362 under which certain properties were purchased using NFIP funds; this mitigation provision was repealed and replaced with the FMA program. We submit that mitigation of repetitive losses is a direct investment in stabilizing the National Flood Insurance Fund since future repetitive claims will be reduced or eliminated.

- ▶▶ **ASFPM urges the Subcommittee to clarify that the funds to implement repetitive loss mitigation programs authorized by the 2004 Reform Act may be transferred from premium income and/or policy service fee income.**

BASIC FMA: STATE AND COMMUNITY CAPS; LIMITATION ON TIME TO EXPEND

An issue not addressed in the 2004 Reform Act is the existing per state and per community limitation under the Basic FMA program. The statute imposes a per state limit of \$10 million and a per community limit of \$3.3 million in any 5-year period. Many of the active states and communities are approaching those limits, especially those with large numbers of repetitive loss properties. For example, two communities with the greatest number of repetitively-flooded homes have aggressive and active mitigation programs – and both are poised to pursue the additional Basic FMA funds and Pilot Program funds. However, since the funding amount was doubled, implementation in these communities and others may be hampered if FEMA does not request changes to those limits.

The 2004 Reform Act explicitly makes Basic FMA funding "available until expended" yet the Administration's request for FY 2006 continues to impose a 2-year limitation. Mitigation projects can take a long time because of the importance of working with property owners to encourage participation and, sometimes, because qualified contractors are difficult to find especially in disaster areas where there is a lot of repair activity. ASFPM understands the need for States and communities to make progress when scarce funds are obligated. However, that can be accomplished without imposing an artificial limit on the availability of the funds.

- ▶▶ **ASFPM urges the Subcommittee to request that FEMA, as part of its FY 2006 budget request, eliminate the per state and per community limits and clarify that the Basic FMA funds are to remain available until expended.**

RULEMAKING FOR PILOT PROGRAM AND INDIVIDUAL PROPERTY PROGRAM

The 2004 Reform Act directed FEMA to consult with state and local officials regarding these programs within 90 days of enactment. FEMA electronically solicited comments on 10 questions and conducted the consultation session in November 2004. It is our understanding that FEMA is engaged in the rulemaking process. Because the Pilot Program is scheduled to expire in 2009 and two years have already been lost, it is critical that the program rules be available as soon as possible.

The fact that the Individual Program does not expire should not lessen the importance of implementation as quickly as possible. ASFPM expects the Individual Property Program to be most effective for non-residential buildings which represent a disproportionately large percentage of the repetitive loss problem. Many communities are reluctant to expend scarce staff resources on projects that do not mitigate losses on primary residences even though flooded businesses and industries can adversely affect local economies.

- ▶▶ **ASFPM suggests that the Subcommittee request that FEMA report on the status and schedule for publication of implementation rules for both the Pilot Program and the Individual Property Program.**

3. CHANGES TO EXISTING NFIP & MITIGATION PROGRAMS

The 2004 Reform Act contains several provisions that are intended to make existing NFIP and Mitigation programs more effective.

STATUS OF ICC CHANGES

The National Flood Insurance Reform Act of 1994 authorized a powerful new mitigation tool – mitigation coverage as part of the standard flood insurance policy. Called ICC or “Increased Cost of Compliance,” it was touted by FEMA – and expected by others – to be one of the best tools to effect more post-flood mitigation, in part because it is funded by a separate premium included in all flood insurance policies. Although FEMA announced an increase of the benefit under ICC to \$30,000 (effective May 1, 2003), as currently administered this increase has not increased the size of claim payments made for most eligible mitigation activities. The average ICC payment to support an acquisition project is on the order of \$7,000 and the average payment for elevation projects averages about \$16,000.

Currently, ICC premiums account for over \$80 million in income, but most of that is not utilized for ICC claim payments. It appears that ICC income cross-subsidizes the National Flood Insurance Fund and is not being used for its intended purposes.

Because of the under-utilization of ICC, the ASFPM supported the ICC reforms in the 2004 Reform Act. Importantly, the change allows ICC claims to be triggered as part of an offer of mitigation through one of FEMA’s mitigation programs and modifies the definition of substantial damage to recognize community efforts that go beyond the minimum standards of the NFIP.

One of the more difficult parts of many mitigation projects is finding the non-federal match. ICC claim payments are considered non-federal funds because they are from flood insurance premiums (not taxpayer dollars). For insured property owners, this makes ICC a readily-available, valuable source of the match and thus can help property owners recover. As a result of the large number of floods and hurricane disasters last year, significant post-disaster mitigation funds have been made available. The 2004 Reform Act changes to ICC must be implemented as quickly as possible in order to bring about the anticipated benefits in the coming flood and hurricane season.

ASFPM has met with FEMA on a number of occasions in the past three years to discuss administrative adjustments to how ICC is administered and how insurance adjusters handle ICC claims, especially when the recipient of ICC payment is also participating in a FEMA. The ASFPM urges that there be ONE process, and that the ICC process cede to the FEMA grant process. Otherwise homeowners, community officials, and states will have twice the number of requirements to satisfy and the complexity and frustration will be overwhelming. To date, the changes that were indicated as workable have not been implemented, specifically:

1. When paired with a mitigation grant for buyout, the ICC payment for demolition must be expanded to include all elements of demolition and lot restoration. Currently only certain costs associated with the primary structure are eligible.

2. FEMA must direct adjusters to handle ICC claims congruent with the timeframe of mitigation grants to the maximum extent possible. This will be even more important as a result of the 2004 Reform Act which will increase the number of insured property owners undertaking mitigation who will be eligible for the ICC payment.
3. FEMA must not allow conflicts in determining which parts of mitigation projects are eligible under ICC and which are eligible under FEMA's grant programs. The two components must be made to work together and the claims adjuster and the mitigation manager must be in partnership focused on getting the funding invested in cost-effective mitigation measures.

►► **ASFPM suggests that the Subcommittee urge FEMA to make the necessary administrative changes promptly. This is absolutely necessary so that ICC can function effectively under all circumstances and specifically as directed by the 2004 Reform Act.**

GUIDANCE TO QUALIFY FOR REDUCED COMMUNITY MATCH

The 2004 Reform Act authorizes a reduced non-federal match for FMA grants if a State's Hazard Mitigation Plan indicates how the State intends to reduce the number of severe repetitive loss properties and if FEMA determines that the State has taken such actions. FEMA reports that 43 states have FEMA-approved State Mitigation Plans. ASFPM acknowledges the diligent and hard work that FEMA has contributed to this effort. However, guidance related to qualifying for the reduced match has not been issued. Interested State have no option but to proceed on their own.

ELIGIBLE ACTIVITIES: INCLUSION OF THE "DEMO/REBUILD" OPTION

The 2004 Reform Act recognizes, for the first time officially, the mitigation alternative that involves demolition of substandard buildings and rebuilding fully-compliant buildings. This alternative, called "modified elevation" by FEMA and referred to as "demo/rebuild" by many, offers an option for property owners and communities in cases where mitigation is cost-effective, but elevation-in-place is not be feasible. This occurs most commonly when older homes are structurally unsound and also do not meet other health and safety codes.

Under all of its mitigation programs FEMA has approved use of grant funds "on a pilot basis" for demo/rebuild in several states over the past five years. Although States and communities report that the process has been made more complicated and difficult than necessary, the results are soundly endorsed. Elevation is effective in many cases, but it cannot be applied to many older homes. Without demo/rebuild as an option, many at-risk, flood-prone, low income homeowners will not benefit from mitigation. Jefferson Parish, LA, one of the most repetitively-flooded communities, has used demo/rebuild with five homeowners. The results, reported by Emergency Preparedness Director Walter Maestri, are "extremely successful." Unfortunately, Dr. Maestri and others report that FEMA has suddenly withdrawn support for demo/rebuild without explanation.

The 2004 Reform Act explicitly includes demolish and rebuild as an eligible mitigation activity under the Pilot Program. This was included in response to concerns that many

communities need options that keep neighborhoods intact and allow property owners to retain ownership of their land. ASFPM acknowledges that demo/rebuild requires careful and thoughtful application and we appreciate FEMA's undertaking pilot projects in order to evaluate effectiveness. However, we remain concerned that FEMA may interpret the Act to allow use of this viable option only under the Pilot Program and disallow it for all other grant programs.

▶▶ **ASFPM requests that the Subcommittee clarify that demo/rebuild is a viable mitigation activity under all mitigation grant programs.**

4. ADEQUACY OF FLOOD INSURANCE COVERAGE

The 2004 Reform Act calls for a GAO study and report regarding the adequacy of coverage provided under the National Flood Insurance Program's flood insurance policies and payments made to policyholders who file claims for eligible damage. We wish to express concern with the statement in the Act that it is a goal of the NFIP to restore flood victims to pre-flood conditions.

Many ASFPM members work with flood victims as they attempt to repair and rebuild. We appreciate the dilemma that flood victims face when insurance claims fall short of amounts needed to fully restore them to their pre-flood conditions. We believe a significant part of the problem is in the adjustment process, and we note that the 2004 Reform Act should lead to improvements in this arena. We submit that rather than assume the solution is to raise the rates sufficient to make payments large enough to restore claimants to pre-flood condition, it is more important to focus on mitigation measures to reduce damage, thus reducing claims against the program. By aggressively implementing the mitigation programs authorized by the 2004 Reform Act, the pressure to raise the rates can be reduced and, eventually, it may be feasible for coverage to expand to address more of the concerns raised by flood victims.

We must be mindful that since the inception of the NFIP, there has been a struggle between what should be covered under a flood insurance policy and affordability. One of the most common complaints that floodplain managers receive is that flood insurance policy "costs too much." FEMA has the difficult challenge of optimizing the coverage limits while keeping flood insurance premiums low. We wish to point out that if coverage was changed to provide payments sufficient to flood victims wholly restored to pre-flood conditions that the policy would cost much more – more than most policyholders could either afford or be willing to pay.

5. RELATED NFIP ISSUES

ASFPM respectfully brings to the Subcommittee's attention a number of issues that have bearing on the success of the 2004 Reform Act.

TAXATION OF MITIGATION BENEFITS

Currently, all of the NFIP-funded mitigation programs (Basic FMA, Pilot Program, and Individual Program) and all of FEMA's other mitigation programs, are subject to a June 28, 2004 ruling by the Internal Revenue Service that mitigation payments are taxable as personal income when the property remains in private ownership. Our members are reporting that this ruling is directly responsible for flood-damaged property owners and communities declining to

participate. Importantly, many property owners accepted mitigation offers before the ruling and without knowledge of the tax implications – now they are receiving form 1099s for the 2004 tax year and many are struggling with the financial implications.

The White House and the Department of the Treasury have indicated support for legislation to make clear that mitigation funds should not be considered income for tax purposes. In response, the House has passed H.R. 1134, which states that mitigation funds are not taxable, but only prospectively. Apparently the Department of the Treasury has indicated that the IRS would not take any steps to enforce the Ruling for 2004 or any earlier year. To our knowledge this position has not been formalized and it is unclear how it will be communicated to affected states, communities and property owners. Representative Baker of this Subcommittee has introduced H.R. 804 which would clarify that NFIP mitigation programs should not be considered as income for the purposes of means tested federal programs, such as Medicaid or Pell Grants. The ASFPM strongly supports both bills – and the clarification by Treasury – and hopes that action is taken soon.

FLOOD MAP MODERNIZATION

The President's budget request for the past two years has included FEMA's Flood Map Modernization as a Presidential Initiative. FEMA, in partnership with States and communities, is working to revise and update the Nation's flood maps. The maps are not only important for flood zone determinations for flood insurance and for land use/development decisions, but are also important for the NFIP mitigation programs. For example, the ICC mitigation insurance claim payment is almost never used in areas outside of FEMA mapped flood zones because there is no provision for regulatory compliance. In addition, fully one-third of flood insurance claims are in areas not shown on FEMA maps. With respect to repetitive flood claims, approximately 25% of properties that have received multiple claims are located outside of areas mapped as flood-prone. This clearly points to the need for good quality flood maps not only for land management purposes but also to reduce the NFIP's repetitive loss problem.

The Administration's FY 2006 proposed budget for FEMA contains \$200 million for Map Modernization (Map Mod). The ASFPM is appreciative of the Administration's support of this initiative and hopes the Congressional support will continue throughout the entire effort.

However, there are some significant issues that, if not addressed, could be detrimental. The metrics (key performance indicators) that drive Map Mod may well result in maps that don't satisfy the quality objectives unless some modifications are made. FEMA's current metrics: (1) map 100% of the Nation in 5 years; (2) \$750 million to a billion (based on an estimate prepared in 1996-97); and (3) ensure a basic (or foundational) level of quality, i.e., all floodplains identified will match best available (existing) topography. ASFPM recognizes FEMA's move to adopt this quality standard, which is essential to a successful flood mapping program.

Unfortunately, those three metrics cannot be met simultaneously. A number of the assumptions made in 1996, such as the time and effort required to translate existing studies from the old cartographic base onto a GIS base, are not as simple as we thought. In order to make the maps accurate and to remap waterways and coastal areas that need new studies, we are finding that more time and effort is necessary as the process gets underway.

Most floodplain managers agree: Every map that is produced must be an accurate map – even if it means that not all communities get studied in next 5 years. As we stick to the metrics described above, too often it results in simply digitizing existing data without matching topography, so an old inaccurate map is still an inaccurate map, only it is on a digital (GIS) base instead of a cartographic (paper) base. That happens because when the metric of mapping 100% of the nation in 5 years is matched with the money allocated and time, the quality metric often is sacrificed.

Communities will balk at adopting these as “new” maps without the quality match or limited studies in critical areas, since it does not solve their flood map problems, nor will it improve the mapping they currently use. Without good maps we will erode the ability of communities, and collectively, the Nation, to reduce flood losses, damages and loss of life from flooding.

The ASFPM feels strongly that the first five years of Map Mod will be successful if we focus on producing quality flood maps for the highest priority communities. Mapping 100% of the nation is an appropriate goal, but the timeframe to develop “adequate” maps needs to be extended. In future years there will be a need to extend the program on to the next tier of communities.

Furthermore, under the current scenario, not all stream miles in all communities will be studied, nor will all areas that need detailed study areas have them, nor will out-of-date hydrologic/hydraulic data be updated. The process needs to identify the priority of these additional parameters that go into making quality flood maps: developing flood risk information for those unstudied stream miles, identifying existing and future growth areas where detailed flood study data is needed, and updating those areas where existing hydrologic and hydraulic data are no longer accurate. This will allow communities to have good data for critical areas now, and help them plan for future development so they do not create tomorrow's flood disasters.

FEMA IN DHS: IMPACTS ON PROGRAMS AND LEGACY MISSIONS

FEMA has several critical missions that are vital to nearly every community and state in the country. Its legacy missions, those that pre-date becoming a part of the Department of Homeland Security, were to prepare for, respond to, recover from, and mitigate against all hazards. Since nearly the entire nation is at risk from and vulnerable to natural hazards, FEMA's focus tended to be on natural hazards. Now that FEMA is part of the Department of Homeland Security, we have been witness to the systematic dismantling of FEMA – funds have been transferred and staff positions have been lost.

FEMA has borne a large share of the DHS organizational costs and administrative realignment of staff, and, if something isn't done soon, FEMA will bear little resemblance to the agency it once was. Mitigation and long-term cost containment are particularly at-risk. Many are concerned that it will be difficult, if not impossible, to implement the repetitive loss programs envisioned in the 2004 Reform Act if FEMA does not have sufficient staff to administer the Flood Mitigation Assistance programs and other pre- and post-disaster mitigation programs. Ultimately the Members of Congress in every district will have to respond to constituents when FEMA can no longer implement its programs and missions. We urge the

Subcommittee to pay close attention to such issues and take action to ensure that FEMA and the National Flood Insurance Program have the capacity to carry out their legacy missions.

CONCLUSION

We appreciate that in the past Congress has provided an array of flood mitigation tools which increase the prospect that communities, states, and businesses and families can become more resistant to future flood disasters. The repetitive loss programs established in the 2004 Reform Act build on the Congress' work in this area. This Subcommittee's support of the new authorities and funding to allow us to mitigate repetitive loss properties are vital next steps.

Thank you for the opportunity to provide our thoughts and recommendations on these important issues. The ASFPM and its members look forward to working with you as we move towards a common goal of reducing flood losses.

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