CONSIDERATIONS FOR STATE INSURANCE REGULATORS IN BUILDING THE PRIVATE FLOOD INSURANCE MARKET

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BACKGROUND AND PURPOSE

State insurance regulators have first-hand experience with the devastating effects that floods have on the constituents in their states, and they believe it is critical that flood insurance is both available and affordable in order to encourage purchases that thereby protect homes, businesses and personal property. Although private flood insurance is being written largely in the commercial market, this paper will focus on the residential flood insurance market.

For more than a half-century, the federal government's National Flood Insurance Program (NFIP) has been the primary player in the residential flood insurance market, underwriting most policies while private insurers have largely focused on a relatively small residential supplemental market. While the NFIP has done a laudable job in making flood insurance available for millions of residential properties, a significant flood insurance gap exists across the U.S.[1] with flood event after flood event revealing a substantial number of damaged properties being uninsured.[2] A Federal Emergency Management Agency (FEMA) analysis from 2018 indicates that 69% of American homes in high-risk flood zones do not have flood insurance. Concurrently, there has been a heightened interest amongst private carriers to expand their residential flood insurance offerings, greatly assisted by the development of more sophisticated flood mapping and risk modeling technologies.

Funding for continuation of the NFIP expired in September 2017, and since then, the U.S. Congress has passed numerous short-term extensions, and more are expected. The federal Biggert-Waters Flood Insurance Reform Act of 2012 (Biggert-Waters) requires lenders to accept private flood insurance policies meeting certain requirements just as they would an NFIP policy to satisfy the federal mandatory purchase mortgage requirement. The NAIC has been engaged legislatively and with the federal banking regulators on their rulemaking.[3] In February 2019, after six years of deliberation, the federal banking regulators finalized their rule. The final rule provides the requirements[4] for lenders to accept provide flood insurance policies. The rule also provides lenders the option to accept private flood insurance policies that do not meet the mandatory acceptance requirements set forth in Biggert-Waters subject to certain conditions.

State insurance regulators and the NAIC support a long-term NFIP reauthorization, as well as the facilitation of increased private sector involvement in the sale of flood insurance, which can help ensure that consumers have access to multiple options. In 2016, the NAIC developed the "NAIC Principles for National Flood Insurance Program (NFIP) Reauthorization"[5] and has testified in Congress on the importance of ensuring a viable private flood insurance market as an alternative to the NFIP.[6]

[1] *https://riskcenter.wharton.upenn.edu/wp-content/uploads/2019/02/Moving-the-Needle-on-Closing-the-Flood-Insurance-Gap.pdf.*
[2] *www.pciaa.net/docs/default-source/industry-issues/4_lessonslearned.pdf.*
[3] *https://www.naic.org/documents/government_relations_comment_letter_federal_banking_private_flood_insurance.pdf.*
[4] The key conditions in the final rule are: 1) a requirement that the policy provide sufficient protection for a designated loan, consistent with general safety and soundness principles; and 2) a requirement that the regulated lending institution document its conclusion regarding the sufficiency of protection in writing. The final rule also allows regulated lending institutions to exercise their discretion to accept certain plans providing coverage issued by "mutual aid societies."
[5] *https://www.naic.org/documents/government_relations_161019_nfip_guiding_principles.pdf.*
[6] *https://www.naic.org/documents/government_relations_160113_testimony_private_flood_insurance.pdf.*

Following from this NAIC action, the purpose of this document is to provide state insurance regulators with concrete actions that can be and/or have been taken to assist with the development of the burgeoning private insurance market for residential flood insurance.

OVERALL STATE OF THE FLOOD INSURANCE MARKET

According to the most recent data collected by the NAIC (Table 1), approximately $644 million of direct premium was written in the private flood insurance market in 2018 throughout the U.S. In 2018, the private flood insurance market represented 15% of the total flood insurance market ($4.2 billion). The private flood insurance market has been growing over the past few years, with the $644 million in direct premium written in 2018 being an increase of 9% from 2017 direct written premiums, and an increase of 71% since 2016. In 2018, California, Florida, Louisiana, New Jersey, New York, Pennsylvania, Puerto Rico and Texas each had $20 million or more of private flood insurance direct written premium (Table 1), with these eight states/jurisdictions representing nearly 60% of the total private flood insurance market.

It is important to note that the NAIC Annual Statement data used in Table 1 and Table 2 does not differentiate between residential private flood insurance premium and commercial private flood insurance premium. The NAIC is exploring data collection via a supplement and/or data call to collect data for residential private flood insurance and commercial private flood insurance separately.

Beyond this aggregate view of premium being written by state, for a relative sense of market penetration and growth of the private flood market, two other views of the NAIC data are presented: 1) private flood as a percentage of total flood written per state in 2018 (Table 1); and 2) private flood growth by state from 2016 to 2018 (Table 2).

Table 1: Private Flood as a Percentage of Total Flood Written per State in 2018

State	Direct Premium Written – Private	Direct Written Premium – NFIP	Total	Private Flood Percentage
AK	$ 726,128	$ 2,173,734	$ 2,899,862	25%
AL	$ 4,717,310	$ 37,369,849	$ 42,087,159	11%
AR	$ 2,918,840	$ 13,387,226	$ 16,306,066	18%
AS	$ 17	$ 38,356	$ 38,373	0%
AZ	$ 13,616,250	$ 20,785,412	$ 34,401,662	40%
CA	$ 83,598,726	$ 184,728,154	$ 268,326,880	31%
CO	$ 6,815,467	$ 17,996,733	$ 24,812,200	27%
CT	$ 8,554,006	$ 52,057,947	$ 60,611,953	14%
DC	$ 2,023,055	$ 1,481,959	$ 3,505,014	58%
DE	$ 1,870,439	$ 19,394,560	$ 21,264,999	9%
FL	$ 79,664,174	$ 974,338,089	$ 1,054,002,263	8%
GA	$ 13,822,654	$ 59,793,148	$ 73,615,802	19%
GU	$ 23,475	$ 348,208	$ 371,683	6%
HI	$ 3,511,428	$ 40,778,877	$ 44,290,305	8%
IA	$ 9,261,662	$ 12,894,876	$ 22,156,538	42%
ID	$ 1,685,637	$ 4,443,509	$ 6,129,146	28%
IL	$ 15,571,396	$ 41,782,653	$ 57,354,049	27%
IN	$ 9,754,263	$ 22,122,449	$ 31,876,712	31%
KS	$ 5,619,810	$ 8,096,167	$ 13,715,977	41%

Table 1: Private Flood as a Percentage of Total Flood Written Per State in 2018 (cont'd)				
State	**Direct Premium Written – Private**	**Direct Written Premium – NFIP**	**Total**	**Private Flood Percentage**
KY	$ 5,562,791	$ 19,859,236	$ 25,422,027	22%
LA	$ 20,518,942	$ 332,451,130	$ 352,970,072	6%
MA	$ 17,035,775	$ 77,215,928	$ 94,251,703	18%
MD	$ 6,161,138	$ 38,179,561	$ 44,340,699	14%
ME	$ 1,826,143	$ 8,778,305	$ 10,604,448	17%
MI	$ 7,287,062	$ 20,395,079	$ 27,682,141	26%
MN	$ 6,072,364	$ 7,828,757	$ 13,901,121	44%
MO	$ 10,054,439	$ 21,828,499	$ 31,882,938	32%
MP	$ 1,406	$ -	$ 1,406	100%
MS	$ 5,401,764	$ 43,786,173	$ 49,187,937	11%
MT	$ 1,107,818	$ 3,679,000	$ 4,786,818	23%
NC	$ 10,477,327	$ 109,932,602	$ 120,409,929	9%
ND	$ 1,808,961	$ 6,508,148	$ 8,317,109	22%
NE	$ 3,426,045	$ 8,737,796	$ 12,163,841	28%
NH	$ 1,579,406	$ 8,531,507	$ 10,110,913	16%
NJ	$ 33,570,528	$ 215,735,820	$ 249,306,348	13%
NM	$ 2,025,523	$ 10,462,171	$ 12,487,694	16%
NV	$ 4,598,626	$ 8,083,596	$ 12,682,222	36%
NY	$ 47,243,273	$ 205,299,097	$ 252,542,370	19%
OH	$ 15,400,298	$ 33,185,859	$ 48,586,157	32%
OK	$ 3,076,462	$ 11,092,205	$ 14,168,667	22%
OR	$ 6,248,012	$ 23,928,017	$ 30,176,029	21%
PA	$ 22,141,354	$ 65,301,183	$ 87,442,537	25%
PR	$ 21,658,142	$ 7,645,531	$ 29,303,673	74%
RI	$ 2,317,465	$ 18,409,898	$ 20,727,363	11%
SC	$ 13,703,417	$ 137,792,886	$ 151,496,303	9%
SD	$ 834,247	$ 3,115,261	$ 3,949,508	21%
TN	$ 12,179,549	$ 24,574,361	$ 36,753,910	33%
TX	$ 63,221,041	$ 435,173,125	$ 498,394,166	13%
UT	$ 2,712,200	$ 2,509,861	$ 5,222,061	52%
VA	$ 9,475,832	$ 78,057,383	$ 87,533,215	11%
VI	$ 37,329	$ 2,185,181	$ 2,222,510	2%
VT	$ 698,550	$ 4,937,502	$ 5,636,052	12%
WA	$ 12,061,004	$ 31,765,783	$ 43,826,787	28%
WI	$ 5,896,222	$ 11,790,299	$ 17,686,521	33%
WV	$ 1,804,872	$ 16,683,897	$ 18,488,769	10%
WY	$ 899,933	$ 1,580,170	$ 2,480,103	36%
Total	**$ 643,879,997**	**$ 3,571,032,713**	**$ 4,214,912,710**	**15%**

Table 2: Private Flood Growth by State from 2016 to 2018					
State	Direct Premium Written – 2018	Direct Premium Written – 2017	Direct Premium Written – 2016	Percentage of Change Premium Written from 2017 to 2018	Percentage of Change Premium from 2016 to 2018
AK	$ 726,128	$ 957,063	$ 555,129	-24%	31%
AL	$ 4,717,310	$ 4,799,724	$ 3,005,135	-2%	57%
AR	$ 2,918,840	$ 2,826,120	$ 1,607,656	3%	82%
AS	$ 17	$ -	$ -	N/A	N/A
AZ	$ 13,616,250	$ 11,068,965	$ 6,260,448	23%	117%
CA	$ 83,598,726	$ 71,951,648	$ 48,786,070	16%	71%
CO	$ 6,815,467	$ 6,097,813	$ 4,735,996	12%	44%
CT	$ 8,554,006	$ 9,810,824	$ 6,787,613	-13%	26%
DC	$ 2,023,055	$ 2,838,882	$ 1,829,183	-29%	11%
DE	$ 1,870,439	$ 1,669,426	$ 740,005	12%	153%
FL	$ 79,664,174	$ 84,491,040	$ 47,796,186	-6%	67%
GA	$ 13,822,654	$ 12,154,732	$ 6,953,126	14%	99%
GU	$ 23,475	$ 61,491	$ 9,396	-62%	150%
HI	$ 3,511,428	$ 4,707,292	$ 3,149,891	-25%	11%
IA	$ 9,261,662	$ 7,973,218	$ 6,739,156	16%	37%
ID	$ 1,685,637	$ 1,246,073	$ 842,501	35%	100%
IL	$ 15,571,396	$ 14,022,683	$ 9,770,834	11%	59%
IN	$ 9,754,263	$ 9,359,454	$ 5,834,525	4%	67%
KS	$ 5,619,810	$ 5,187,276	$ 3,519,857	8%	60%
KY	$ 5,562,791	$ 5,184,777	$ 3,636,333	7%	53%
LA	$ 20,518,942	$ 17,883,168	$ 11,495,497	15%	78%
MA	$ 17,035,775	$ 15,255,682	$ 8,980,394	12%	90%
MD	$ 6,161,138	$ 4,881,020	$ 3,004,956	26%	105%
ME	$ 1,826,143	$ 1,393,303	$ 1,449,308	31%	26%
MI	$ 7,287,062	$ 5,784,426	$ 3,112,100	26%	134%
MN	$ 6,072,364	$ 6,034,414	$ 4,382,496	1%	39%
MO	$ 10,054,439	$ 8,579,964	$ 5,611,173	17%	79%
MP	$ 1,406	$ 673	$ -	109%	N/A
MS	$ 5,401,764	$ 4,954,089	$ 3,545,564	9%	52%
MT	$ 1,107,818	$ 965,222	$ 546,157	15%	103%
NC	$ 10,477,327	$ 9,385,350	$ 5,916,463	12%	77%

Table 2: Private Flood Growth by State from 2016 to 2018 (cont'd)					
State	**Direct Premium Written – 2018**	**Direct Premium Written – 2017**	**Direct Premium Written – 2016**	**Percentage of Change Premium Written from 2017 to 2018**	**Percentage of Change Premium from 2016 to 2018**
ND	$ 1,808,961	$ 1,518,138	$ 1,033,168	19%	75%
NE	$ 3,426,045	$ 2,733,969	$ 1,819,577	25%	88%
NH	$ 1,579,406	$ 1,773,337	$ 1,516,804	-11%	4%
NJ	$ 33,570,528	$ 28,862,467	$ 17,035,409	16%	97%
NM	$ 2,025,523	$ 1,735,136	$ 662,921	17%	206%
NV	$ 4,598,626	$ 4,574,608	$ 2,440,079	1%	88%
NY	$ 47,243,273	$ 47,674,483	$ 27,419,308	-1%	72%
OH	$ 15,400,298	$ 14,202,904	$ 5,628,305	8%	174%
OK	$ 3,076,462	$ 3,507,498	$ 1,746,619	-12%	76%
OR	$ 6,248,012	$ 4,730,473	$ 2,910,035	32%	115%
PA	$ 22,141,354	$ 18,832,760	$ 13,240,946	18%	67%
PR	$ 21,658,142	$ 19,554,982	$ 19,436,229	11%	11%
RI	$ 2,317,465	$ 2,623,963	$ 1,286,538	-12%	80%
SC	$ 13,703,417	$ 12,726,603	$ 10,633,358	8%	29%
SD	$ 834,247	$ 770,092	$ 572,506	8%	46%
TN	$ 12,179,549	$ 8,584,856	$ 5,939,417	42%	105%
TX	$ 63,221,041	$ 53,512,832	$ 31,771,120	18%	99%
UT	$ 2,712,200	$ 1,958,666	$ 1,050,341	38%	158%
VA	$ 9,475,832	$ 8,527,381	$ 4,727,129	11%	100%
VI	$ 37,329	$ 43,449	$ 122,459	-14%	-70%
VT	$ 698,550	$ 520,374	$ 297,124	34%	135%
WA	$ 12,061,004	$ 11,566,163	$ 9,609,189	4%	26%
WI	$ 5,896,222	$ 4,140,377	$ 2,300,499	42%	156%
WV	$ 1,804,872	$ 1,986,325	$ 1,614,061	-9%	12%
WY	$ 899,933	$ 959,541	$ 713,965	-6%	26%
Total	**$ 643,879,997**	**$ 589,147,189**	**$ 376,130,254**	**9%**	**71%**

Clearly, this data suggests that there are considerable opportunities for private flood insurance placement and market development. However, it is important to note that in 2018, the majority of growth occurred in the private commercial flood insurance market. The residential private flood insurance market showed a slight decline from 2017.[7]

As insurers' familiarity with flood catastrophe models grows, as underwriting experience develops and as state regulatory structures evolve, the number of private flood insurance policies in force could continue to grow, including among admitted carriers. Therefore, it is important to understand what the states have done (or not done) to enhance this growth.

[7] *https://www.insurancejournal.com/research/app/uploads/2019/06/FINAL-Private-Flood-Insurance-Report-2019.pdf.*

STATE ACTION

During the six years of uncertainty regarding the federal banking rules for private flood insurance, a number of states began undertaking efforts to encourage the growth of a private flood insurance market in their state. Florida's efforts to establish a private flood insurance market have been applauded as a potential model to be used in other states looking to expand their residential private flood insurance offerings. Florida has the largest flood insurance market in the country; approximately 35% of NFIP policies are written there.[8] Florida has enacted legislation to create a statutory framework, allowing private insurers to offer multiple types of flood coverage ranging from standard coverage, which mirrors the NFIP, to other enhanced coverages. This legislation includes: 1) streamlining the rate filing process for private flood insurers; 2) eliminating the diligent search requirement for flood policies issued by surplus lines carriers until July 2019; and 3) providing a process by which the Office of Insurance Regulation (OIR) will certify that a private insurer's policy equals or exceeds coverage provided by the NFIP. Florida's OIR issued an informational memorandum providing guidance on how private insurers will need to demonstrate the financial capacity to assume this risk, as well as options for developing private flood rates and policy forms.

In addition to Florida, we can draw upon the existing experiences from other states in developing a robust flood insurance market along the key aspects of insurance regulation.

The NAIC reached out to the states on the drafting group to provide information that was not readily available on the states' websites, as well as to gather information from other resources, including: 1) the Wharton School of the University of Pennsylvania study *The Emerging Private Residential Flood Insurance Market in the United States*; 2) Government Accountability Office (GAO) reports; and 3) a recently updated Congressional Research Service (CRS) report regarding private flood insurance and the NFIP. In the future, the NAIC might want to consider sending a more detailed questionnaire to the states to gather more information regarding the developing private flood insurance market.

State efforts to grow a viable private flood insurance market include:

Legislative and Regulatory Changes

- Supporting private flood insurance legislation.
- Approving private flood insurance products.
- Tailoring rate and form requirements for private flood insurance coverage.
- Allowing private flood insurers to submit rates on an informational basis.
- Removing diligent search requirements.

Consumer Information

- Conducting consumer outreach.
- Listing private flood insurance products on a department of insurance's (DOI) website.
- Collecting residential private flood insurance data.

Agent and Lender Actions

- Implementing specific continuing education (CE) requirements for producers.
- Increasing the weighting of flood insurance questions on producer licensing exams.
- Conducting agent education.
- Conducting lender education.

[8] *www.floods.org/ace-files/documentlibrary/committees/Insurance/Emerging_Flood_Insurance_Market_Report-Wharton-07-13-18.pdf.*

LEGISLATIVE AND REGULATORY CHANGES

Supporting Private Flood Insurance Legislation

In addition to Florida's legislation, West Virginia has passed legislation requiring insurers to file their private flood insurance plan of operation with the insurance commissioner and authorizing expedited processing of surplus lines policies for flood insurance.

Approving Private Flood Insurance Products

Personal lines private flood insurance products are being approved by a number of states. Currently, Alabama, California, Mississippi and Pennsylvania are among states approving new personal lines private flood insurance products for entry into the market.

In January 2018, the Insurance Services Office (ISO) developed a new private flood insurance form, for both personal and commercial flood insurance. The ISO forms are similar to a homeowner's policy form. However, the damage to the property must be caused by flooding. As of March 2018, ISO personal flood insurance forms have been filed in 43 jurisdictions, and commercial flood insurance forms have been filed in 45 jurisdictions. The states with independent rating bureaus are not reflected in these numbers.

TAILORING RATE AND FORM REQUIREMENTS FOR PRIVATE FLOOD INSURANCE COVERAGE

The states might want to consider permitting insurers to file private flood insurance products without a prior approval requirement. For example, Florida law permits private flood insurance rates to be implemented without prior approval at the time of filing. However, insurers are required to keep supporting actuarial data for two years. Furthermore, Florida law allows insurers to request the state to certify that a private policy provides flood coverage that equals or exceeds that offered by NFIP. (See Appendix I for information on Florida's process.)

Maryland, South Carolina and Pennsylvania have not relaxed the rate and form filing requirements. However, they are committed to an efficient and swift overview of private flood insurance filings, and they will work with insurers to make the filing and approval process as smooth as possible.

EXPORT LIST / WAIVING DILIGENT SEARCH REQUIREMENTS

Insurance generally must be sold in the admitted market. Only after a "diligent search" of the admitted market is performed and coverage is denied can insurance be placed in the surplus lines market. However, states make exceptions for those types of insurance that are known to not be available in the admitted market. These insurance products are listed on what is known as an "Export list." When a type of insurance is listed on an Export list, the applicant can go straight to the surplus lines market without the need for the diligent search, thereby obtaining coverage more easily and quickly. At least 14 states have placed flood insurance on their "Export list," including: Alaska, Arizona, Connecticut, Idaho, Louisiana, New Jersey, Oklahoma, Oregon, Pennsylvania, Rhode Island, Texas, Virginia, West Virginia and Wisconsin.

Allowing Private Flood Insurers to Submit Rates on an Informational Basis

Allowing insurers to submit rates on an informational basis in states with prior approval rate filing laws is another way to encourage the growth of the private flood insurance market. Two states that have

taken this approach include Florida and New Jersey.[9] (See Appendix I for information on Florida's process.)

CONSUMER INFORMATION

Consumer Outreach

It is important to understand that everyone lives in a flood zone. Some people live in higher-risk flood zones than others, but we all live in a flood zone.

When people say they live or do not live in a flood zone, they typically mean what is known as a "special flood hazard area". A "special flood hazard area" is an area within FEMA's 100-year flood plain. This is where flood insurance is typically mandatory as a condition of obtaining a property loan. But there are flood zones outside of the 100-year flood plain as well. For example, there is also what FEMA classifies as moderate risk flood zones. These are the properties in the 500-year flood plain. By definition, and according to FEMA, these properties have between a 0.2% and a 1% chance of flooding in any given year. That might sound small, but over the course of a 30-year mortgage, these properties, according to FEMA, have between a 6% and 26% chance of being inundated by a flood. And flood insurance is not mandatory as a condition of obtaining a property loan in these moderate-risk flood zones.

Consumers need to understand that their property may still be at risk for flooding even if they do not live in a special flood hazard area and are not required to purchase it. They also need to understand that flood insurance can be relatively inexpensive, especially when the property is not in the highest-risk flood zones. There are options available to them, from both the NFIP and the private flood insurance market. And they can purchase lower limits of coverage; they do not need to insure the full replacement cost of their home if they do not wish to do so. Purchasing just $20,000 of coverage, for example, might go a long way in the event of a flood and may be cheaper to purchase than believed. Further, renters can buy policies that cover only their personal property and not the dwelling that they rent.

There are also many consumers under the misconception that flood damage will be covered by their homeowners insurance policy or rental insurance policy. Therefore, they are unaware of their actual flood risk, and they learn that they are uninsured for this catastrophic peril only after a flood event for which they have no coverage.

State DOIs, as well as the NAIC, are launching consumer outreach programs to help address this coverage gap.

Some states now require a flood disclosure with homeowners policies. For example, Texas recently passed a law requiring a conspicuous disclosure when homeowners policies do not include flood coverage.

The NAIC Communications Department has also launched a flood campaign this year to inform consumers of the importance of purchasing flood insurance, either private flood insurance or flood insurance provided by the NFIP. Additionally, the NAIC recently released a special section of its website dedicated to educating consumers about the risks of flooding and what kinds of coverage options are available to protect against those risks.

Finally, the NAIC's Transparency and Readability of Consumer Information (C) Working Group has created both a basic flood insurance document and several graphic materials containing flood facts, to be used by DOIs for consumer outreach via social media.

[9] *https://riskcenter.wharton.upenn.edu/wp-content/uploads/2018/07/Emerging-Flood-Insurance-Market-Report.pdf* and state DOIs.

Listing Private Flood Insurance Writers on a DOI Website

While many DOIs include information regarding NFIP policies on their websites, some states, including Florida, Louisiana, New Jersey and Pennsylvania, provide a list of private flood insurance writers and their contact information on their websites.

It is worthwhile to note that surplus lines writers are generally not listed by the line of business they write. However, it has been suggested that there would be value for the states to provide information regarding which surplus lines writers are writing residential private flood insurance. Pennsylvania lists the surplus lines producers placing residential flood insurance on its website.

Collecting Residential Private Flood Insurance Data

Florida and Texas both collect comprehensive data regarding residential private flood insurance.[10] As described previously, the NAIC has been collecting private flood insurance data since the data year 2016. Before that, the private flood insurance line was not a separate entry in the annual statement. While residential and commercial private flood insurance are not separated in the property/casualty (P/C) annual statement blank, the NAIC, through its Property and Casualty Insurance (C) Committee, is considering enhancements to the annual statement that would require insurers to report the residential private flood insurance premiums and commercial private flood insurance premiums independently. The Surplus Lines (C) Task Force is considering similar changes to alien surplus lines private flood insurance data that is reported to the International Insurers Department (IID).

The Wholesale & Specialty Insurance Association (WSIA) is also providing the Reinsurance Association of America (RAA) with data regarding surplus lines insurance. The RAA is working on an open source database that provides information regarding private flood insurance.

These changes would allow state insurance regulators and FEMA to better measure the growth of the private residential flood insurance market.

AGENT AND LENDER ACTIONS

Continuing Education and Producer Licensing Requirements

FEMA requires all insurance producers licensed in property, casualty or personal lines of authority who sell flood insurance through the NFIP to complete a one-time course, as required by the federal Flood Insurance Reform Act of 2004. This is also the only educational requirement in many states.

At least one state has increased the weighting of the flood insurance questions on their producer licensing exam.

Agent Education

Selling flood insurance requires an agent to understand the intricacies of NFIP and private flood insurance policies.[11]

When purchasing insurance, many times the insurance agent is the consumer's first point of contact. Therefore, it would be valuable if an agent could explain the risks of flooding, even if a consumer does not own or rent property in a high-risk flood zone. Recent flood events remind us that where it can rain, it can flood, and many floods occur outside of a high-risk flood zone. If agents help to educate the consumer, it will help eliminate the cost of inaction, as the occurrence of a flood event could be financially unbearable for homeowners or renters if they are not insured or are underinsured. It is critical

[10] *https://riskcenter.wharton.upenn.edu/wp-content/uploads/2018/07/Emerging-Flood-Insurance-Market-Report.pdf.*

[11] www.floods.org/ace-files/documentlibrary/committees */Insurance/Emerging_Flood_Insurance_Market_Report-Wharton-07-13-18.pdf.*

for agents to make a special effort to educate homeowners regarding the need for flood insurance, even if a business or home is not located in a high-risk flood zone.

DOIs can provide agents with information that they have learned as a result of a flood event, and they can foster agent education by requiring CE requirements to improve an agent's knowledge of flood insurance.

Other states' adoption of such practices would likely improve agents' knowledge of flood insurance, therefore helping their clients to obtain more effective flood coverage, whether through the NFIP or the private market.

Lender Education

A large percentage of Americans have a mortgage on their home. Therefore, lender education is another opportunity for consumer flood insurance education. Recent catastrophic flooding events have illustrated that floods can happen anywhere. Therefore, it may be in the best interest of homeowners to purchase flood insurance even if they do not live in a high-risk flood zone.

While state insurance regulators do not have the authority to regulate lenders, lenders should still be educated regarding the importance of flood insurance. When navigating the loan process, lenders do not always discuss purchasing flood insurance unless the borrower's home is in a high-risk flood zone. A discussion about purchasing flood insurance even if the homeowner does not live in a high-risk flood zone should ideally be addressed with the borrower.

DOIs can raise awareness regarding flood insurance by bringing agents, consumers, lenders, FEMA, private flood insurance writers, etc. together in communities to discuss the importance of a homeowner purchasing flood insurance.

MARKET UNCERTAINTY AND THE DEVELOPMENT OF A PRIVATE FLOOD INSURANCE MARKET

The May 2019 CRS report, "Private Flood Insurance and the National Flood Insurance Program," identified some of the barriers to the development of a private flood insurance market. Some of the barriers identified in the report include: 1) regulatory uncertainty; and 2) continuous coverage.

Most directly relevant for the NAIC members is the notion of regulatory uncertainty, which is covered below. The remaining topics will be addressed in Appendix II.

In 2016, the U.S. experienced several major flood catastrophes, causing billions of dollars in property losses.[12] Following these storms, it was found that somewhere between 50% and 80% of these losses were not insured, which implies that communities are unable to bounce back quickly following large catastrophic events.

Floods are expected to cost U.S. households $20 billion each year[13]. An Insurance Information Institute (I.I.I.) survey indicated that 15% of American homeowners had a flood insurance policy in 2018[14] and that there were approximately 5.18 million flood insurance policies held by the NFIP.[15] Milliman estimates the potential private residential flood insurance market to represent between $34 billion and

[12] https://www.pewtrusts.org/en/research-and-analysis/articles/2017/02/01/flooding-disasters-cost-billions-in-2016
[13] Milliman
[14] https://www.iii.org/fact-statistic/facts-statistics-flood-insurance
[15] https://www.fema.gov/total-policies-force-calendar-year

$48 billion in direct written premium.[16] This data clearly indicates an opportunity for growth in the residential private flood insurance market in the U.S.

Recently, comments have surfaced regarding the possibility of the residential private flood insurance market cherry-picking their risks. It is important to remember the NFIP was meant to be a temporary solution that was put into place 50 years ago due to private insurers not insuring flood. While the NFIP is important, every state has some type of residual market that aids in insuring and providing flood insurance coverage for those who are unable to obtain flood insurance coverage available in the market. While not directly related to flood insurance, two good examples of successful residual markets are Florida Citizens and Louisiana Citizens. As the market has grown and shrunk in both Florida and Louisiana, both Florida Citizens and Louisiana Citizens needed to and provided a safe and reliable source of insurance for consumers. The NFIP can continue to evolve and do the same thing. Milliman believes Risk Rating 2.0 will help the NFIP and provide helpful information regarding the actual risk of a flood insurance policy; however, it was recently announced that the implementation of Risk Rating 2.0 will be delayed until Oct. 1, 2021 to allow for more analysis of its impact.

Milliman is of the opinion that a private market can coexist alongside the NFIP. Private flood insurance can be written in the admitted and non-admitted market. However, it needs to be determined if the guaranty funds will cover flood insurance in the admitted market, as flood may be excluded in many states.

Many private insurers have not serviced or written flood insurance policies. Additionally, private insurers do not have access to historical data; this poses a problem. It will be important to balance the need to protect consumers against the need to promote the private flood insurance market.

New entrants to the private flood insurance market are likely to purchase significant amounts of reinsurance. Flood insurance is inherently high-risk and volatile, so insurers may require higher amounts of profit and contingencies built into rates than for a typical homeowner's insurance product. States allowing these options might make it easier for an insurer to offer private flood insurance. For example, Wisconsin has no limitations or requirements for reinsurance cost and profit provision assumptions.

The issue of continuous coverage is problematic. In order for an NFIP policyholder to preserve any subsidies provided by the NFIP, a policyholder is required to have continuous flood insurance coverage. Currently, a policyholder loses subsidies or cross-subsidies when private flood insurance is purchased, if the policyholder chooses to return to the NFIP.

Unless there is legislation in place allowing private flood insurance to be deemed as continuous coverage, homeowners may be averse to purchasing private flood insurance. Homeowners do not want to find themselves in a situation causing them to lose their subsidy should they elect to return to the NFIP for flood insurance coverage. While legislation has been introduced in the U.S. House of Representatives allowing private flood insurance to count towards continuous coverage, legislation has yet to be passed.

The availability of private flood insurance provides the added benefit of increasing consumer choice. As private insurers are entering the flood insurance market, some of the policies offered are providing broader coverage than that provided by the NFIP. Additionally, some policyholders are finding private flood insurance policies to be less expensive than those offered by the NFIP.[17]

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[16] Milliman

[17] Congressional Research Service report, "Private Flood Insurance and the National Flood Insurance Program, May 7, 2019

SUMMARY

In the past few years, many states have experienced catastrophic flooding. Following the flood events, it has become even more apparent that a significant number of consumers are either uninsured or underinsured for the flood peril.

While the NFIP still writes a majority of the residential flood insurance policies, there are considerable opportunities for the development of the residential private flood insurance market.

This document provides details about how a few states have put procedures in place to enhance the private flood insurance market in a state. These procedures include: 1) supporting private flood insurance legislation and initiatives; 2) tailoring rate and form requirements for residential private flood insurance products; and 3) consumer, agent and lender education.

It is noteworthy to say that the states experiencing large flooding events have seen growth in the private flood insurance market regardless of any other actions. For example, following Hurricane Harvey, Texas saw growth in its residential private flood insurance market. Catastrophic events are a reminder to consumers of the devastation caused by flooding.

While there are several barriers for the residential private flood insurance market, the most significant barrier for private insurers may be uncertainty about the state regulatory environment.

The attached appendices discuss steps that Florida has taken in its approach to cultivate the private residential flood insurance market and discussion of other barriers to the entrance of residential private flood insurers.

Appendix I – Actions Florida Has Taken

FLORIDA'S FORM FILING PROCESS EXAMPLE

Florida reviews form filings, providing flood coverage differently based on the type of flood coverage being provided.

Subject to the Requirements of Florida's Flood Statute

The coverage provided under the policy must meet one of the definitions of type of flood coverage, as defined by S. 627.715, F.S. Of the five defined types, "standard," "preferred" and "customized" are defined to meet or exceed the coverage provided by the standard NFIP policy. "Flexible" flood insurance must cover losses from the peril of "flood" as defined by the statute, but it does not have to provide coverage comparable to the entire NFIP policy. "Supplemental" flood coverage is meant to supplement an NFIP or private flood policy. Policies that fall under these definitions may have certain provisions that differ from that which would otherwise be required if not written under the flood statute.

Items Not Subject to the Requirements of Florida's Flood Statute

The coverage does not have to meet or exceed the coverage provided by the standard NFIP policy. However, the provisions of the flood statute that allow changes to the form and rate requirements, as well as allowing for a certification provided by the Florida OIR, do not apply. This means that forms and rates would be subject to all the requirements of Florida law, and the coverage does not have to meet the definition of "flood" under the statute.

Florida's private flood insurance statute, S. 627.715 F.S., does not apply to the commercial lines market. Forms providing commercial flood coverage must comply with all applicable Florida laws.

REVIEW OF FLORIDA'S FORM FILING PROCESS

How the Florida OIR Reviews Form Filings Subject to its Flood Statute

The Florida OIR coordinates with FEMA about training to educate forms analysts about the details and nuances of a federal NFIP policy. Forms analysts:

- Review the policy or endorsement and compare it to the NFIP policy.
- Review the provisions of the underlying policy that are not superseded by changes made in the endorsement.
- Make sure that the flood coverage in total (including definitions, deductibles, limits, conditions, property not covered, exclusions, etc.) are as broad as that provided under the NFIP policy.
- Exclude provisions, specific to the NFIP, that would not make sense to be in a private company's policy.

State Law Conflict

There are certain provisions in the federal private flood definition that may conflict with a state's law.

For example, the statute of limitations under the standard NFIP policy is one year after the date of denial. In Florida, the statute of limitations for most claims is five years from the date of loss. The insurer could use the standard NFIP provision, or the insurer could use a provision such as one year after the date of denial of a claim or five years from the date of the loss, whichever is greater. The modified provision would be considered as providing better coverage.

Another potential area in which there could be conflict between the standard NFIP policy and state law is the requirement for notice of cancellation. The NFIP requires 45 days, which may be more or less than state provisions.

In Florida, the statute requires a 10-day cancellation for non-payment of premium. In Florida, to comply with the flood statute, the insurer would have to give at least 45 days.

The general filing requirement for forms is found in S. 627.410, F.S., which requires the Florida OIR to approve forms before use.

For commercial flood coverage, the insurer has the option to file the forms as informational pursuant to S. 627.4102, F.S.

FLORIDA RATE PROCESS EXAMPLE

Florida allows insurers to offer personal residential flood insurance coverage that meets the requirements of the flood statute. Insurers may decide to either submit the rate filings subject to the normal filing requirements of review and approval or (until Oct. 1, 2025) submit the filing for informational purposes.

Personal residential flood insurance rates submitted for informational purposes are subject to examination by the Florida OIR for a period of two years from the effective date to determine if the rates are excessive, inadequate or unfairly discriminatory.

If the coverage does not meet the requirements of the "flood statute," the rate filing is subject to the normal filing requirements of review and approval. Commercial non-residential property rates (including that for flood coverage) are informational due to a separate provision of Florida laws, and they are an exception to these filing requirements.

FLORIDA FLOOD STATUTE – FLOOD POLICY TYPES

Florida's flood statute (S. 627.715, F.S.) sets up five types of flood coverage that may be written using the special deviations allowed for flood insurance.

- *Standard flood insurance (equivalent to coverage provided under the standard flood policy under the NFIP).*
- *Preferred flood insurance.*
- *Customized flood insurance.*
- *Flexible flood insurance.*
- *Supplemental flood insurance.*

Flexible and supplemental coverage are the only flood coverage types under the statute that do not require flood insurance coverage to meet or exceed what is provided under the standard NIFP policy. Flexible coverage must provide coverage for the peril of flood as defined by the statute (which mirrors that of the NFIP). However, there are ancillary coverages that are not required to be provided.

APPENDIX II – BARRIERS TO THE RESIDENTIAL PRIVATE FLOOD INSURANCE MARKET

Flood Coverage Being "At Least as Broad as" the NFIP

Biggert-Waters specifies that private flood insurance satisfies the mandatory purchase mortgage requirement when a private flood insurance policy affords coverage that is "at least as broad as" the coverage offered by an NFIP flood insurance policy.[18]

Many property owners are not required to purchase flood insurance because their home is outside of a Special Flood Hazard Area (SFHA) or because they do not have a federally backed mortgage. Lenders may accept private flood insurance that meets the "discretionary acceptance" definition, which states that lending institutions may accept private flood insurance policies that do not meet the "mandatory acceptance" requirements, provided that certain conditions are met, such as that the policy provides sufficient protection of the loan, consistent with general safety and soundness principles.[19] This distinction may be important for insurers with a product designed with higher-deductible options and/or a shorter cancellation notice for nonpayment of premiums.

Since there was not a federal banking rule in place regarding private flood insurance following the passage of Biggert-Waters, it was challenging to implement the use of private flood insurance for the mandatory purchase mortgage requirement. Some lending institutions thought that they did not have the knowledge necessary to assess whether a flood insurance policy met the definition of private flood insurance set forth in Biggert-Waters.

The federal banking rule became effective July 1, 2019. The rule fulfills the condition in Biggert-Waters that regulated lending institutions accept private flood insurance policies satisfying the conditions specified in the Act. Furthermore, the federal banking rule allows lending institutions to accept an insurer's written assurances stated in a private flood insurance policy that the appropriate criteria is met. The rule also permits lending institutions to accept some flood insurance coverage plans provided by mutual aid societies.

Theoretically, the federal banking rule removes the acceptance of private flood insurance as a barrier to the private flood insurance market. However, educating the banking industry is clearly still needed as state insurance regulators are still hearing that lenders are telling borrowers that the only flood insurance policy that is acceptable is an NFIP flood policy. Thus, further education regarding the federal banking rule needs to be done. States may want to consider drafting a bulletin that can be used for these purposes.

Continuous Coverage

If an NFIP policy holder lets an NFIP policy lapse, by either not paying premium or going to a private flood insurer, any subsidy the NFIP policy holder would have received is immediately eliminated.[20] Legislation currently being considered by Congress to reauthorize the NFIP includes the ability of policyholders to leave the NFIP in order to purchase a private flood insurance policy and then return to the NFIP without penalty.

[18] 42 U.S.C §4012a(b).
[19] Ibid
[20] As required by §100205(a)(1)(B) of Biggert-Waters (P.L. 112-141, 126 Stat. 917), only for NFIP policies that lapsed in coverage as a result of the deliberate choice of the policyholder.

Non-Compete Clause

FEMA dropped its non-compete clause in 2018. FEMA now allows Write Your Own (WYO) companies to sell NFIP policies. Therefore, this is no longer a barrier.

NFIP Subsidized Rates

One of the hurdles facing private flood insurance growth involves the NFIP's subsidized rates, as NFIP premiums do not always reflect the full risk of flooding. NFIP rates allow certain policyholders to have more affordable premiums. Additionally, NFIP rates do not incorporate profit, which is an important element for private flood insurers.[21] Private flood insurers need to charge rates that represent the full risk of the peril.[22]

If the NFIP were to reform its rate structure to collect full-risk rates, it might result in the encouragement of more private insurers to write policies in the private flood insurance market. Full-risk NFIP rates would fall closer to what a private insurer would charge. It is important to note that full-risk rates would likely lead to higher rates than those that currently exist.[23]

Presently, FEMA is in the process of redesigning its rating system. The new NFIP rating system will be known as Risk Rating 2.0. This new rating structure will add replacement cost value and consider the distance between a property and a source of water. Additionally, Risk Rating 2.0 takes into consideration things that are not reflected in the current rating structure, such as intense rainfall.[24] As stated previously it was recently announced that Risk Rating 2.0 will be delayed until Oct. 1, 2021 to allow for more analysis on its impact.

Ability to Assess Flood Risk Accurately

On June 11, 2019, the NFIP released data on flood losses and claims. Prior to the release of this data, insurers viewed the lack of access to NFIP data on flood losses and claims as a barrier for private companies offering flood insurance.

For private flood insurers to manage and diversify their risk exposure, consumer participation to manage and diversify their risk exposure is required. Many private insurers have expressed the view that broader participation in the flood insurance market would be necessary to address adverse selection and maintain a sufficiently large risk pool.[25]

An established goal of the NFIP is to increase the number of flood insurance policies in force. Even though there is a mandatory purchase requirement for homeowners to purchase flood insurance in certain flood zones, this does not always occur.

As more insurers begin to write private flood insurance, it is likely that consumers will be offered more choices. Private flood insurers may also offer coverages not available through the NFIP. These coverages might include coverage such as basement coverage, business interruption, additional living expenses, etc. Private insurers might also be able to offer higher coverage limits than those offered by the NFIP.

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[21] *www.floods.org/ace-files/documentlibrary/committees/Insurance/Emerging_Flood_Insurance_Market_Report-Wharton-07-13-18.pdf.*
[22] Ibid.
[23] Ibid.
[24] Ibid.
[25] GAO, Jan. 22, 2014. "Flood Insurance: Strategies for Increasing Private Sector Involvement," 14–127, accessed online at *https://www.gao.gov/products/GAO-14-127.*

Private flood insurance offered as an endorsement to a standard homeowners insurance policy could possibly eliminate instances where it is necessary to differentiate between flood and wind damage.[26]

[26] CRS, May 7, 2019. "Private Flood Insurance and the National Flood Insurance Program," accessed online at *https://www.everycrsreport.com/files/20190507_ R45242_968aced5ccda33b36e57f26022e80552ffa6f32d.pdf.*