

HOUSE OF REPRESENTATIVES STAFF ANALYSIS

BILL #: CS/HB 929 Peril of Flood
SPONSOR(S): Insurance & Banking; Ahern
TIED BILLS: **IDEN./SIM. BILLS:** CS/SB 584

REFERENCE	ACTION	ANALYST	STAFF DIRECTOR or BUDGET/POLICY CHIEF
1) Insurance & Banking Subcommittee	10 Y, 0 N, As CS	Peterson	Luczynski
2) Economic Affairs Committee	14 Y, 0 N	Johnson	Pitts

SUMMARY ANALYSIS

The National Flood Insurance Program (NFIP) is a federal program that offers federally-subsidized flood insurance to property owners and promotes land-use controls in floodplains. The Federal Emergency Management Agency (FEMA) administers the NFIP. The Biggert-Waters Flood Insurance Reform Act of 2012 (Biggert-Waters Act) made major changes to the NFIP, including an increase in rates charged by the NFIP for flood insurance, starting in 2013. However, starting October 1, 2013, some NFIP policies that were subsidized moved directly to full-risk rates, resulting in dramatic flood insurance rate increases for some homeowners. In March 2014, federal legislation was enacted to moderate some of the rate increases resulting from the Biggert-Waters Act.

Anticipating substantial rate increases in the NFIP, the 2014 Legislature enacted s. 627.715, F.S., to provide a framework for a private, personal lines flood insurance market in Florida. The section originally provided for four types of flood insurance: *standard flood insurance* (which is equivalent to a standard policy under the NFIP), *preferred flood insurance*, *customized flood insurance*, and *supplemental flood insurance*. In 2015, the Legislature amended the state-authorized flood insurance program to include a fifth category of insurance, "flexible flood insurance." Insurers who wish to provide Florida-authorized coverage may develop rates for flood coverage, by either filing the rate with the Office of Insurance Regulation (OIR) and obtaining approval, or, until October 1, 2019, using a rate without the OIR's approval, so long as the rate is not excessive, inadequate, or unfairly discriminatory. In addition, current law authorizes a surplus lines agent to export a policy without having to determine that coverage is unavailable from an admitted carrier. This exemption is scheduled for repeal July 1, 2017.

The bill extends to October 1, 2025 the period in which insurers may develop and use rates without first obtaining approval from the OIR. It also extends and broadens the exemption permitting the export of coverage to a surplus lines carrier without meeting statutory conditions. The exemption is extended to July 1, 2020. The exemption is broadened to eliminate the conditions related to comparability of premiums, policy contents, and deductibles, and the condition related to notifying a policyholder of the availability of coverage from Citizens Property Insurance Corporation (Citizens) (Citizens is prohibited by law from offering flood coverage).

The bill has no fiscal impact on state government revenues and an indeterminate fiscal impact on state and local expenditures. The bill may have a positive impact on the private sector.

The bill provides an effective date of July 1, 2016.

I. SUBSTANTIVE ANALYSIS

A. EFFECT OF PROPOSED CHANGES:

Current Situation

National Flood Insurance Program

The National Flood Insurance Program (NFIP or program) was created by the passage of the National Flood Insurance Act of 1968 to offer federally-subsidized flood insurance to property owners and to promote land-use controls in floodplains. The NFIP is administered by the Federal Emergency Management Agency (FEMA). The federal government will make flood insurance available within a community, if that community adopts and enforces a floodplain management ordinance to reduce future flood risk to new construction in floodplains.¹

Nationally, the NFIP insured almost \$1.3 trillion in assets in 2014. Total earned premium for NFIP coverage for 2014 was \$3.56 billion.²

The Biggert-Waters Flood Insurance Reform Act of 2012

Following flood losses from the 2005 hurricanes Katrina, Rita, and Wilma, the NFIP borrowed \$21 billion from the U.S. Treasury in order to remain solvent. However, flood losses in 2012 from Super-storm Sandy increased the NFIP's deficit. In 2012, the United States Congress passed the Biggert-Waters Flood Insurance Reform Act (Biggert-Waters Act).³ The Biggert-Waters Act reauthorized the National Flood Insurance Program for five years. Key provisions of the legislation require the NFIP to raise rates to reflect true flood risk, make the program more financially stable, and change how Flood Insurance Rate Map updates impact policyholders. These changes by Congress have resulted in premium rate increases for approximately 20 percent of NFIP policyholders nationwide.

The Biggert-Waters Act increases flood insurance premiums purchased through the program for second homes, business properties, severe repetitive loss properties, and substantially improved damaged properties by requiring premium increases of 25 percent per year until premiums meet the full actuarial cost of flood coverage. Most residences immediately lose their subsidized rates if the property is sold, the policy lapses, repeated and severe flood losses occur, or a new policy is purchased. Some flood maps used by FEMA have not been updated since the 1980s. Policyholders whose communities adopt a new, updated Flood Insurance Rate Map (FIRM) that results in higher rates will experience a five year phase in of rate increases to achieve rates that incorporate the full actuarial cost of coverage.

The Biggert-Waters Act also requires most NFIP policyholders to pay a 5 percent assessment on their policy to create a reserve fund for catastrophic losses.⁴ Additional changes to premium rates, including those paid by the 80 percent of NFIP policyholders with non-subsidized rates, can occur upon remapping. Current law limits rate increases due to remapping to 10 percent per year; the Biggert-Waters Act allows a larger annual rate increase for remapped properties. However, federal action in the 2014 federal omnibus spending bill has delayed rate increases associated with remapping for 12-18 months, as described below.

2014 Federal Flood Reform Bills

¹ FEMA, *National Flood Insurance Program, Program Description*, (Aug. 1, 2002), <https://www.fema.gov/media-library/assets/documents/1150?id=1480> (last visited Jan. 14, 2016).

² FEMA, *Total Coverage by Calendar Year*, <http://www.fema.gov/statistics-calendar-year> (last visited Jan. 14, 2016).

³ FEMA, *Flood Insurance Reform*, <https://www.fema.gov/national-flood-insurance-program/flood-insurance-reform> (last visited Jan. 14, 2016).

⁴ For those NFIP policies with a 25 percent rate increase, the 5 percent assessment is not on top of the 25 percent rate increase. In other words, 5 percent of the 25 percent increase will be allocated to the Reserve Fund.

The Consolidated Appropriations Act of 2014 and the Homeowner Flood Insurance Affordability Act of 2014⁵ repealed or modified some provisions of the Biggert-Waters Act. The new law reduced the mandatory rate increases for subsidized properties from 25 percent annually to no less than 5 percent, generally not to increase more than 18 percent annually.⁶ Properties that remain subject to the 25 percent annual increase include older business properties, older non-primary residences, severe repetitive loss properties, and pre-FIRM properties. The 20 percent annual phase-in of premium increases after adoption of a new or updated flood insurance rate map was reduced to a maximum of no more than an 18 percent annual premium increase. For property not currently at a full-risk rate, a minimum increase of 5 percent per year is required for flood policies on primary residences built on or before December 31, 1994, or before the effective date of the initial flood insurance rate map for the community was adopted.⁷

Private Market Flood Insurance in Florida

In response to the changes to the NFIP, the 2014 Legislature enacted s. 627.715, F.S., governing the sale of personal lines residential flood insurance.⁸ Flood is defined in the standard NFIP policy as a general and temporary condition of partial or complete inundation of two or more acres of normally dry land area or of two or more properties from:

- Overflow of inland or tidal waters;
- Unusual and rapid accumulation or runoff of surface waters from any source;
- Mudflow; or
- Collapse or subsidence of land along the shore of a lake or similar body of water as a result of erosion or undermining caused by waves or currents of water exceeding anticipated cyclical levels that result in a flood as defined above.

Under the 2014 law, authorized insurers could sell four different types of flood insurance products:

- Standard coverage, which covers only losses from the peril of flood as defined in the bill, which is the definition used by the NFIP. The policy must be the same as coverage offered from the NFIP regarding the definition of flood, coverage, deductibles, and loss adjustment.
- Preferred coverage, which includes the same coverage as standard flood insurance and also must cover flood losses caused by water intrusion from outside the structure that are not otherwise covered under the definition of flood in the bill.
- Customized coverage, which is coverage that is broader than standard flood coverage.
- Supplemental coverage, which supplements an NFIP flood policy or a standard or preferred policy from a private market insurer. Supplemental coverage may provide coverage for jewelry, art, deductibles, and additional living expenses. It does not include excess flood coverage over other flood policies.

The 2015 Legislature amended the program to add a fifth category, “flexible flood coverage.”⁹ “Flexible flood coverage” is defined as the coverage for the peril of flood that may include water intrusion coverage, and includes or excludes specified provisions, including the authority to limit coverage to only the outstanding mortgage on the property and to allow dwelling loss to be adjusted only on the actual cash value of the property.

An insurer may establish flood rates through the standard process in s. 627.062, F.S. Alternatively, rates filed before October 1, 2019, may be established through a rate filing with the OIR that is not required to be reviewed by the OIR before implementation of the rate (“file and use” review) or shortly after implementation of the rate (“use and file” review). Specifically, the flood rate is exempt from the “file and use” and “use and file” requirements of s. 627.062(2)(a), F.S. Such filings are also exempt from the requirement to provide information necessary to evaluate the company and the reasonableness of the rate. The OIR may, however, examine a rate filing at its discretion. To enable the office to conduct such examinations, insurers must

⁵ Homeowner Flood Insurance Affordability Act of 2014, H.R. 3370, 113th Cong. (2014) (Pub. L. No. 113-89).

⁶ FEMA, *Changes to the National Flood Insurance Program – What to Expect*, available at <https://www.fema.gov/media-library/assets/documents/96449>, (last visited Jan. 14, 2016).

⁷ Homeowner Flood Insurance Affordability Act of 2014, at s. 5, H.R. 3370, 113th Cong. (2014).

⁸ Ch. 2014-80, Laws of Fla.

⁹ Ch. 2015-69, Laws of Fla.

maintain actuarial data related to flood coverage for two years after the effective date of the rate change. Upon examination, the OIR will use actuarial techniques and the standards of the rating law to determine if the rate is excessive, inadequate or unfairly discriminatory. The law allows projected flood losses for personal residential property insurance to be a rating factor. Flood losses may be estimated using a model or straight average of models found reliable by the Florida Commission on Hurricane Loss Projection Methodology.

A surplus lines agent can export a contract or endorsement for flood insurance without the obligation to conduct the due diligence required in s. 626.916(1)(a), F.S. That paragraph requires an agent to determine that the insurance is not available from a company currently writing in the state and limits any amount that may be exported to the amount in excess of the amount that can be procured in the state. The agent must document that he or she has made a diligent effort to procure the coverage from an admitted insurer.¹⁰ This is one of five conditions currently applicable to agents who seek to export other lines of insurance. The four others relate to premium, the policy form, deductible amounts, and notice to an applicant of the availability of coverage from Citizens.¹¹ In general, the conditions prevent a surplus lines insurer, which is subject to substantially less regulation than an admitted carrier, from offering policies with terms and conditions that are more favorable than can be offered by an admitted insurer. This exemption is scheduled for repeal July 1, 2017.

Effect of the Bill

The bill extends to October 1, 2025 the period in which insurers may develop and use rates without first obtaining approval from the OIR. It also extends and broadens the exemption permitting the export of coverage to a surplus lines carrier without meeting statutory conditions. The exemption is extended to July 1, 2020. The exemption is broadened to eliminate the conditions related to comparability of premiums, policy contents, and deductibles, and the condition related to notifying a policyholder of the availability of coverage from Citizens. In addition, the bill makes a technical correction, adding the word “flexible,” to the introductory language in s. 627.715, F.S.

B. SECTION DIRECTORY:

Section 1: Amends s. 627.715, F.S., relating to flood insurance.

Section 2: Provides an effective date of July 1, 2016.

II. FISCAL ANALYSIS & ECONOMIC IMPACT STATEMENT

A. FISCAL IMPACT ON STATE GOVERNMENT:

1. Revenues:

None.

2. Expenditures:

None.

B. FISCAL IMPACT ON LOCAL GOVERNMENTS:

1. Revenues:

None.

2. Expenditures:

Indeterminate.

¹⁰ Section 626.914, F.S., defines “diligent effort” as seeking and being denied coverage from at least three authorized insurers in the admitted market, unless the cost to replace the property insured is \$1 million or more. In that case, diligent effort is seeking and being denied coverage from at least one authorized insurer in the admitted market.

¹¹ Current law prohibits Citizens from offering flood coverage. s. 626.916(6), F.S.

C. DIRECT ECONOMIC IMPACT ON PRIVATE SECTOR:

To the extent that the bill encourages more private insurers to provide coverage for flood loss, consumers may ultimately benefit from increased competition. Relaxing the standards for placing flood insurance coverage in the surplus lines market may increase access to coverage for property owners, but could negatively affect the development of the Florida flood insurance market by creating an unlevel playing field for competition.

D. FISCAL COMMENTS:

None.

III. COMMENTS

A. CONSTITUTIONAL ISSUES:

1. Applicability of Municipality/County Mandates Provision:

Not applicable. This bill does not appear to affect county or municipal governments.

2. Other:

None.

B. RULE-MAKING AUTHORITY:

None provided by the bill.

C. DRAFTING ISSUES OR OTHER COMMENTS:

None.

IV. AMENDMENTS/ COMMITTEE SUBSTITUTE CHANGES

On January 25, 2016, the Insurance & Banking Subcommittee adopted a proposed committee substitute (PCS) and reported the bill favorably as a committee substitute. The PCS removed all of the provisions of the bill which did not relate to insurance, clarified the language related to the exemption permitting the export of coverage to a surplus lines carrier, and revised the extension of exemption expiration from 2025 to 2020.

The staff analysis is drafted to reflect the committee substitute.