The Florida Senate

BILL ANALYSIS AND FISCAL IMPACT STATEMENT

(This document is based on the provisions contained in the legislation as of the latest date listed below.)

Prepared By: The Professional Staff of the Committee on Appropriations

BILL: CS/CS/SB 542

INTRODUCER: Appropriations Committee (Recommended by Appropriations Subcommittee on General Government); Banking and Insurance Committee; and Senator Brandes and others

SUBJECT: Flood Insurance

DATE: February 24, 2014 REVISED:

	ANALYST	STAFF DIRECTOR	REFERENCE	ACTION
1.	Matiyow/Knudson	Knudson	BI	**Fav/CS**
2.	Betta	DeLoach	AGG	**Fav/CS**
3.	Betta	Kynoch	AP	**Fav/CS**

Please see Section IX. for Additional Information:

COMMITTEE SUBSTITUTE - Substantial Changes

I. Summary:

CS/CS/SB 542 creates laws governing the sale of private flood insurance policies, contracts, and endorsements by authorized insurers with the exception of commercial lines risks policies that provide coverage in excess of an underlying policy. The bill requires insurers that write flood coverage to provide coverage for "flood" as currently defined by the National Flood Insurance Program (NFIP). The bill also permits insurers to expand flood coverage to include water intrusion originating from outside the structure.

Flood rates may be established using the existing rate review process in section 627.062, Florida Statutes. For flood rate filings made before July 1, 2024, an insurer may utilize three additional options for the development of flood insurance rates (Flood coverage rates developed under the three additional provisions are subject to section 627.062(1), Florida Statutes, which requires that rates shall not be excessive, inadequate, or unfairly discriminatory):

- A rate filing that is exempt from the filing and review requirements of sections 627.062(2)(a) and (f), Florida Statutes;
- Individual risk rating; and
- If the insurer obtains the written, signed consent of the policyholder, it may use a flood coverage rate that has not been approved by the Office of Insurance Regulation (OIR).

The bill also:

- Allows flood deductibles to be a stated dollar amount or a percentage of coverage, however, insurers must offer the standard deductibles offered by the NFIP.
- Allows flood insurance policies to be offered that adjusts flood claims on a replacement cost basis or actual cash value.
- Allows the policy limit for flood coverage to be any agreed upon amount.
- Makes the following coverages optional: (1) additional living expense coverage; (2) personal property or contents; and (3) law and ordinance coverage. The insurer must offer, however, law and ordinance coverage comparable to such coverage contained in a NFIP policy.
- Authorizes the use of flood loss projection models to establish rates for flood insurance.
- Authorizes the Florida Commission on Hurricane Loss Projection Methodology to evaluate flood models and adopt actuarial methods, principles, standards, models, or output ranges for flood loss by July 1, 2016.
- Requires the declarations page of the policy to disclose clearly all limitations on coverage or policy limits.
- Requires each flood policy, endorsement, or contract to provide notice that flood insurance is available from the NFIP.
- Requires the insurer to give 45 days prior written notice of cancellation or nonrenewal to the insured and any regulated lending institution or federal agency that is a mortgagee.
- Allows an insurer or insured to cancel during the term of the policy or upon renewal if the cancellation is for a valid reason under the NFIP.
- Requires an insurer seeking to provide flood coverage to notify the OIR at least 30 days before writing flood insurance in this state. The insurer must file a plan of operation and financial projections with the OIR unless the insurer maintains at least $35 million in surplus and provides coverage as an endorsement to an existing property insurance form.
- Provides that the provisions of section 627.715, Florida Statutes, supersede any conflicting provisions in the insurance code.
- Requires the insurance commissioner to provide a certification if so required by federal law or federal rule as a condition of qualifying for private flood insurance or disaster relief.

The bill has no fiscal impact to state funds. The Florida Commission on Hurricane Loss projection Methodology estimates a fiscal impact of $350,000 to develop the standards outlined in the bill. The commission is funded by the Florida Hurricane Catastrophe Fund.

II. Present Situation:

The NFIP was created by the passage of the National Flood Insurance Act of 1968.[1] The NFIP is administered by Federal Emergency Management Agency (FEMA) and provides property owners located in flood-prone areas the ability to purchase flood insurance protection from the federal government. Flood insurance through the NFIP is only available in communities that adopt and enforce federal floodplain management criteria.[2]

[1] http://www.fema.gov/media-library/assets/documents/7277?id=2216 (Last accessed by staff on January 2, 2014)
[2] *National Flood Insurance Program: Program Description*, pgs. 2-4., Federal Emergency Management Agency/Federal Insurance and Mitigation Administration (August 1, 2002) http://www.fema.gov/media-library/assets/documents/1150?id=1480 (Last accessed by staff on January 7, 2014).

Standard NFIP Flood Insurance

The standard flood insurance policy dwelling form offered by the NFIP[3] is a single peril flood policy that pays for direct physical damage to the insured residential property up to the replacement cost[4] (RCV) or actual cash value (ACV) or the policy limit.[5] The maximum coverage limit for a NFIP standard flood insurance policy is $250,000. The NFIP also offers up to $100,000 in personal property (contents) coverage, which is always valued at ACV.[6] Most NFIP policies also include Increased Cost of Compliance (ICC) coverage of up to $30,000 of the cost to comply with state or community floodplain management laws or ordinances after a flood in which a building has been declared substantially damaged or repetitively damaged.[7] The maximum coverage available to a condominium association is $250,000 per unit multiplied by the total number of units.[8] The limits of coverage for NFIP flood insurance on non-residential buildings are $500,000 in coverage to the building and $500,000 in contents coverage.[9]

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.[10]

The minimum deductibles for NFIP flood coverage are:

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[3] The standard form insures one-to-four family residential buildings and single-family dwelling units in a condominium building. The NFIP also offers (a) a general property form that is used to insure five-or-more-family residential buildings and non-residential buildings and (b) a residential condominium building association policy form that insures residential condominium association buildings.

[4] To obtain RCV coverage under the NFIP dwelling form, the building must be a single-family dwelling, be the principal residence of the insured at the time of loss (the insured lives there at least 80 percent of the year), and the building coverage of at least 80 percent of the full replacement cost of the building or its the maximum available for the property under the NFIP.

[5] *National Flood Insurance Program: Summary of Coverage*, Federal Emergency Management Agency (FEMA F-679/November 2012) http://www.fema.gov/media-library-data/20130726-1620-20490-4648/f_679_summaryofcoverage_11_2012.pdf (Last accessed by staff on January 7, 2014).

[6] See footnote 4.

[7] The total amount of a building claim and ICC claim cannot exceed the maximum limit for building property coverage. For a single-family home, this is the $250,000 maximum limit on coverage to the building. See footnote 4 and footnote 5 at page 26.

[8] *FDIC Compliance Manual*, V – 6.8. http://www.fdic.gov/regulations/compliance/manual/index.html (Last accessed by staff on January 7, 2014).

[9] *Reducing Damage from Localized Flooding: A Guide for Communities*, 11-2. http://www.fema.gov/media-library/assets/documents/1012 (Last accessed by staff on January 7, 2014).

[10] http://www.fema.gov/national-flood-insurance-program/definitions (Last accessed by staff on January 2, 2014)

- For properties built before the effective date of the first Flood Insurance Rate Map[11] (FIRM) for a community, the minimum deductible is:
  - $1,500 if the property is insured for $100,000 or less.
  - $2,000 if the property is insured for over $100,000.
- For properties built after the effective date of the first Flood Insurance Rate Map (FIRM) for a community, the minimum deductible is:
  - $1,000 if the property is insured for $100,000 or less.
  - $1,250 if the property is insured for over $100,000.

Federal Requirements to Obtain Flood Insurance

The U.S. Congress passed the Flood Disaster Protection Act in 1973[12]. The Act mandated property owners with mortgages issued by federally regulated or insured lenders must purchase flood insurance if their properties are located in Special Flood Hazard Areas. Special Flood Hazard Areas are defined by FEMA as high-risk areas where there is at least a one in four chance of flooding during a 30-year mortgage.[13]

The National Flood Insurance Reform Act of 1994[14] (1994 Reform Act) required federal financial regulatory agencies[15] to revise their flood insurance regulations. The 1994 Reform Act applied flood insurance requirements to loans purchased by the Federal National Mortgage Association (Fannie Mae) and the Federal Home Loan Mortgage Corporation (Freddie Mac) and to agencies that provide government insurance or guarantees such as the Small Business Administration, the Federal Housing Administration, and the Veterans Administration. Lending institutions regulated by federal agencies are prohibited from offering loans on properties located in a Special Flood Hazard Area (SFHA) of a community participating in the NFIP unless the property is covered by flood insurance.[16] The amount of flood insurance required by lending institutions must be at least equal to the outstanding principal balance of the loan, or the maximum amount available under the NFIP, whichever is less.

The Biggert-Waters Flood Insurance Reform Act

In 2012[17] the United States Congress passed the Biggert-Waters Flood Insurance Reform Act (Biggert-Waters Act). 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

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[11] The effective date of the first FIRM for Florida communities can be found at http://www.fema.gov/cis/FL.pdf (Last accessed by staff on January 10, 2014).
[12] http://www.fema.gov/media-library-data/20130726-1545-20490-9247/frm_acts.pdf (Last accessed by staff on January 2, 2014).
[13] http://www.floodsmart.gov/floodsmart/pages/flooding_flood_risks/defining_flood_risks.jsp (Last accessed by staff on January 2, 2014).
[14] Title V of the Riegle Community Development and Regulatory Improvement Act of 1994. Pub. L. 103-325, Title V, 108 Stat. 2160, 2255-87 (September 23, 1994).
[15] Office of Comptroller of Currency, Federal Deposit Insurance Corporation, Office of Thrift Supervision, National Credit Union Administration, Farm Credit Administration and Federal Reserve.
[16] *FDIC Compliance Manual*, V – 6.1. http://www.fdic.gov/regulations/compliance/manual/index.html (Last accessed by staff on January 7, 2014).
[17] http://www.fema.gov/flood-insurance-reform-act-2012 (Last accessed by staff on January 2, 2014).

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. 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.

NFIP Flood Insurance in Florida

Over two million NFIP policies are written on Florida properties, with approximately 268,500 policies receiving subsidized rates.[18] This accounts for approximately 37 percent of the total policies written by the NFIP.

Historically, properties insured in Florida have paid approximately $3.60 in premium for NFIP flood coverage for every $1 received in claims payments.[19] The rate impact of the Biggert-Waters Act on subsidized policies in Florida is approximately as follows:

- Approximately 50,000 secondary residences, businesses, and severe repetitive loss properties are subject to immediate, annual 25 percent increases until their premiums are full risk premiums.
- Approximately 103,000 primary residences will lose their subsidy if the property is sold, the policy lapses, the property suffers severe, repeated flood losses, or a new policy is purchased.
- Approximately 115,000 non-primary residences, business properties, and severe repetitive loss properties are subject to the elimination of subsidies once FEMA develops guidance for their removal.

III. Effect of Proposed Changes:

The bill creates laws governing the sale of flood insurance policies, contracts, and endorsements by authorized insurers.

Condition Covered by Private Market Flood Coverage [s. 627.715(2) and (3), F.S.]

The bill requires insurers that write flood coverage to provide coverage for “flood” as currently defined by the NFIP. The bill also permits insurers to expand flood coverage to include water intrusion originating from outside the structure which is not otherwise covered within the

[18] Office of Insurance Regulation, *The Biggert-Waters Flood Insurance Reform Act of 2012*, (Presentation to the Florida Senate Banking and Insurance Committee on October 8, 2013). http://flsenate.gov/PublishedContent/Committees/2012-2014/BI/MeetingRecords/MeetingPacket_2346.pdf.

[19] Wharton Center for Risk Management and Decision Processes, *Who's Paying and Who's Benefiting Most From Flood Insurance Under the NFIP? A Financial Analysis of the U.S. National Flood Insurance Program (NFIP)*, (Issue Brief, Fall 2011).

definition of flood provided in the bill and as also defined by the NFIP. Water intrusion, if offered, is defined by the insurance policy.

The bill defines "flood" in the same way as the NFIP: a general and temporary condition of partial or complete inundation of two acres or more of normally dry land area or of two or more properties, at least one of which is the policyholder's property. The NFIP definition includes four causes of inundation of normally dry land that constitute flood: (1) overflow of inland or tidal waters; (2) unusual or rapid accumulation or runoff of surface waters from any source; (3) mudflow; or (4) 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 which results in flood.

Deductibles [s. 627.715(4)(a), F.S.]

Flood deductibles may be a stated dollar amount or a percentage of coverage. Insurers, however, must offer deductible amounts for flood losses that equal the standard deductibles offered by the NFIP.

Adjustment of Flood Claims [s. 627.715(4)(b), F.S.]

The bill authorizes the sale of flood insurance that adjusts claims on a replacement cost basis or actual cash value.

Option to Restrict Flood Coverage Principal Building [s. 627.415(4)(c), F.S.]

The bill allows, but does not require, the restriction of flood coverage to the principal building, as defined in the insurance policy.

Policy Limits [s. 627.715(4)(d), F.S.]

The policy limit for flood coverage may be any agreed upon amount. This includes the full replacement cost of the property, a set dollar amount, or the amount of the outstanding mortgages on the property.

Optional Coverage [s. 627.715(4)(e), F.S.]

Flood insurance is not required to include any of the following coverages: (1) additional living expense coverage; (2) personal property or contents; and (3) law and ordinance coverage.

The insurer is required to offer law and ordinance coverage for flood comparable to the law and ordinance coverage contained in the standard NFIP policy. Such coverage is called increased cost of compliance (ICC) coverage under the NFIP and, for the NFIP standard policy, provides up to $30,000 to elevate, demolish, or relocate the insured dwelling if such action is required because a floodplain management ordinance finds the structure is substantially damaged or repetitively damaged by flood. Under the NFIP, ICC coverage cannot increase the maximum limit for coverage to the structure ($250,000 for a dwelling or $500,000 for a business). The insurer must include the following written disclosure with flood insurance that includes NFIP-type law and ordinance coverage: "Law and ordinance coverage under this policy might have limitations on what is covered in the event of a loss. You should consult with your agent if you have questions about the coverage offered under this policy."

Notice Provisions [s. 627.715(5), (7) and (9), F.S.]

The declarations page of the policy must disclose prominently, in at least 12-point type, and clearly all limitations on coverage or policy limits on the declarations page. Limitations requiring disclosure include, but are not limited to, deductibles and coverage limited to the amount of outstanding mortgages. The following specific disclosures are required:

- If the dwelling is insured for less than the full replacement cost: "This policy limits flood coverage to less than the full cost of replacement for the property, which may result in high out-of-pocket expenses to you and may put your equity in this property at risk."
- If the dwelling is insured on an actual cash value basis: "This policy pays you the depreciated value of your property that is damaged by flood, which may result in high out-of-pocket expenses to you if your property needs to be repaired or replaced."

Each flood policy, endorsement, or contract must provide notice that flood insurance is available from the NFIP.

The insurer must give 45 days prior written notice of cancellation or nonrenewal to the insured and any regulated lending institution or federal agency that is a mortgagee. An insurer or insured may cancel during the term of the policy or upon renewal if the cancellation is for a valid reason under the NFIP.

Rate Standards for Flood Coverage [s. 627.715(6), F.S.]

The bill allows insurers to develop flood insurance rates under the full rate review process provided for in s. 627.062, F.S. Flood insurance rates may be developed using three additional options in any flood insurance rate filing submitted to the OIR before July 1, 2024:

Rate Filing Exempt from the File and Use and Use and File Requirements

A flood insurance rate filing is exempt from the filing and review requirements of s. 627.062(2)(a) and (f), F.S., and instead requires an informational filing by the insurer. The rates are not subject to the "file and use" or "use and file" process under s. 627.062(2)(a), F.S.

An insurer must notify the OIR of any change to its flood insurance rates, including the average statewide percentage change in rates, no later than 30 days after the effective date of the change in rates. Insurers that utilize this option must maintain actual data regarding its flood insurance rates for two years after the effective date of those rates.

Individual Risk Rating

Insurers may individually rate a flood risk, under the procedure provided under current law in s. 627.062(3)(a) and (b), F.S. The insurer must maintain documentation on each individually rated risk that specifies the characteristics and classification of the risk supporting the reason for the risk being individually rated and also maintain modifications to existing forms. Modifications to flood insurance forms are subject to the provisions of this section and provisions of the insurance code that do not conflict with the bill.

Consent to Rate

If the insurer obtains the written, signed consent of the policyholder, the insurer may use a flood coverage rate that has not been approved by the OIR. The signed consent form must notify the insured that the rate is not subject to OIR approval. Upon policy renewal, the insurer must provide notice that the rate is not subject to OIR approval. The insurer must maintain a copy of the signed consent form for three years and make it available for OIR review. The consent to rate provision in current law under s. 627.171, F.S., contains the same requirements to authorize insurers to use rates in excess of the insurer's approved rate but limits the practice to ten percent of the insurer's commercial lines policies and five percent of its personal lines (homeowners, auto; etc.) policies.

For all three of the options, the OIR is authorized to require the insurer to submit to an examination under which the OIR may determine whether the rate is excessive, inadequate, or unfairly discriminatory.

Authorization of Flood Loss Projection Models to Establish Flood Rates [s. 627.062, F.S., and s. 627.0628, F.S.]

The bill authorizes the use of flood models as a factor in rate filings under s. 627.062, F.S. The insurer may project flood losses using a model, method, or an average of models or methods found acceptable or reliable by the Florida Commission on Hurricane Loss Projection Methodology, and as further provided in the statute governing the commission, s. 627.0628, F.S.

To assist the methodology commission in evaluating flood models, the bill expands the membership of the commission to include a licensed professional engineer who is an expert in floodplain management and not regularly retained by a property and casualty insurer and a meteorologist who specializes in flood. The commission is authorized to consider the accuracy and reliability of flood loss projection models. The commission must adopt actuarial methods, principles, standards, models, or output ranges for flood loss by July 1, 2016.

Placement of Flood Insurance with Surplus Lines Insurers [s. 627.715(8), F.S.]

A surplus lines agent may export flood coverage to an eligible surplus lines insurer without making a diligent effort to seek such coverage from three or more authorized insurers as generally required by s. 626.916(1)(a), F.S. This provision expires July 1, 2017.

Authorization to Write Flood Insurance [s. 627.715(10), F.S.]

An insurer seeking to provide flood coverage must notify the OIR at least 30 days before writing flood insurance in this state. The insurer must file a plan of operation and financial projections with the OIR unless the insurer maintains at least $35 million in surplus and provides coverage as an endorsement to an existing property insurance form. The insurer must also comply with all other applicable requirements contained in the insurance code.

Conflict of Laws [s. 627.715(11), F.S.]

The provisions of s. 627.715, F.S., supersede any conflicting provisions in the rest of the insurance code.

Certification That Private Flood Insurance Complies With Federal Law and Requirements

The bill requires the insurance commissioner to provide a certification if so required by federal law or federal rule as a condition of qualifying for private flood insurance or disaster relief. The certification is not subject to review under ch. 120, F.S.

Citizens Property Insurance Corporation

The bill prohibits Citizens Property Insurance Corporation from providing insurance for the peril of flood.

Florida Hurricane Catastrophe Fund

The bill prohibits the Florida Hurricane Catastrophe Fund from providing reimbursement for losses caused by the peril of flood.

Effective Date

The bill is effective upon becoming a law.

IV. Constitutional Issues:

A. Municipality/County Mandates Restrictions:

None.

B. Public Records/Open Meetings Issues:

None.

C. Trust Funds Restrictions:

None.

V. Fiscal Impact Statement:

A. Tax/Fee Issues:

None.

B. Private Sector Impact:

It is anticipated that the implementation of CS/CS/SB 542 will result in additional private insurers offering flood insurance which may increase competition in the marketplace and provide consumers with more coverage options.

C. Government Sector Impact:

The bill requires the Florida Commission on Hurricane Loss Projection Methodology to develop standards for the review of flood models. The commission estimates the fiscal impact of the bill is $350,000. The commission is funded by the Florida Hurricane Catastrophe Fund. The development of such standards will require the commission to incur costs associated with additional commission meetings, research, workshops, consultants, and possible meetings at the location of each modeler.

According to the OIR, the bill will be implemented within existing resources.

VI. Technical Deficiencies:

None.

VII. Related Issues:

None.

VIII. Statutes Affected:

This bill substantially amends the following sections of the Florida Statutes: 627.062 and 627.0628.

This bill creates section 627.715 of the Florida Statutes.

IX. Additional Information:

A. Committee Substitute – Statement of Substantial Changes:

(Summarizing differences between the Committee Substitute and the prior version of the bill.)

CS/CS by Appropriations on February 20, 2014:

- Changes the sunset that limits the use of alternative rate filing options for flood insurance to filings submitted to the OIR from July 1, 2017, to July 1, 2024.
- Eliminates the provision restricting surplus lines insurers from providing flood coverage only valued at $1 million or more.
- Deletes the provision of the bill which added two members to the Florida Commission on Hurricane Loss Projection Methodology thereby keeping the commission membership the same as in current law.

- Changes the date by which the Florida Commission on Hurricane Loss Projection Methodology must adopt actuarial methods, principles, standards, models, or output ranges for flood loss from July 1, 2015, to July 1, 2016.
- Authorizes the OIR to require insurers offering flood insurance coverage submit to an examination under which the OIR may determine whether the rates charged are excessive, inadequate, or unfairly discriminatory when the rates charged are based on an “individual risk rating” or a “written consent rating”.
- Prohibits Citizens Property Insurance Corporation from providing insurance for the peril of flood.
- Prohibits the Florida Hurricane Catastrophe Fund from providing reimbursement for losses caused by the peril of flood.

CS by Banking and Insurance on January 8, 2014:

- Limits the use of alternative rate filing options for flood insurance to filings submitted to the OIR before July 1, 2017.
- Limits the ability of a surplus lines agent to export flood insurance to a surplus lines insurer without making a diligent effort to place coverage with authorized insurers to coverage of $1 million or more. The provision expires July 1, 2017.
- Requires the insurance commissioner to provide a certification if so required by federal law or federal rule as a condition of qualifying for private flood insurance or disaster relief.
- Requires insurers to offer law and ordinance coverage for flood equivalent to NFIP law and ordinance coverage.

B. Amendments:

None.