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NATIONAL FLOOD INSURANCE PROGRAM

Continued Attention Needed to Address Challenges

Statement of Alicia Puente Cackley, Director
Financial Markets and Community Investment Team

GAO-13-858T

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Continued Attention Needed to Address Challenges

GAO Highlights

Highlights of GAO-13-858T, a testimony before the Subcommittee on Economic Policy, Committee on Banking, Housing, and Urban Affairs, U.S. Senate

Why GAO Did This Study

NFIP, established in 1968, provides policyholders with insurance coverage for flood damage. FEMA, within the Department of Homeland Security, is responsible for managing the program. NFIP offers two types of flood insurance premiums to property owners: subsidized and full-risk. The subsidized rates are not based on flood risk and, according to FEMA, represent only about 40-45 percent of the full flood risk. GAO placed NFIP on its high-risk list in 2006 because of concerns about its long-term solvency and related operational issues.

GAO was asked to testify about NFIP issues and its recent work on NFIP. This statement discusses (1) the reasons that NFIP is considered high-risk, (2) changes to subsidized policies and implications of potential additional program changes, and (3) additional challenges for FEMA to address. In preparing this statement, GAO relied on its past work on NFIP, including GAO-13-607, GAO-13-568, and GAO-13-283.

What GAO Recommends

GAO continues to support its previous recommendations made to FEMA that focus on the need to address management and operational challenges, ensure that the methods and data used to set NFIP rates accurately reflect the risk of losses from flooding, and that oversight of NFIP and insurance companies responsible for selling and servicing flood policies is strengthened. FEMA agreed with these recommendations and is taking steps to address them.

View GAO-13-858T. For more information, contact Alicia Puente Cackley at (202) 512-8678 or cackleya@gao.gov.

What GAO Found

The National Flood Insurance Program (NFIP) was added to GAO's high-risk list in 2006 and remains high risk due to losses incurred from the 2005 hurricanes and subsequent losses, the financial exposure the program represents for the federal government, and ongoing management and operational challenges. As of July 31, 2013, the program owed approximately $24 billion to the U.S. Treasury (Treasury). NFIP's financial condition highlights structural weaknesses in how the program has been funded—primarily its rate structure. The annual amount that NFIP collects in both full-risk and subsidized premiums is generally not enough to cover its operating costs, claim payments, and principal and interest payments for the debt owed to Treasury, especially in years of catastrophic flooding, such as 2005. This arrangement results in much of the financial risk of flooding being transferred to the federal government and ultimately the taxpayer. Furthermore, weaknesses in NFIP management and operations, including financial reporting processes and internal controls, strategic and human capital planning, and oversight of contractors have placed the program at risk.

The Biggert-Waters Flood Insurance Reform Act of 2012 (Biggert-Waters Act) mandated that GAO conduct a number of studies related to actual and potential changes to NFIP, including analyses of remaining subsidies and the effect of increasing coverage limits or adding coverage options. In a study of remaining subsidies, GAO estimated that with the changes in the Biggert-Waters Act approximately 438,000 policies no longer are eligible for subsidies, including about 345,000 policies for nonprimary residences, about 87,000 business policies, and about 9,000 policies for single-family properties that had severe-repetitive losses. Subsidies on most of the approximately 715,000 remaining subsidized policies are expected to be eliminated over time as properties are sold or coverage lapses, as are previous exemptions from rate increases after flood zone map revisions. Reducing the financial impact of remaining subsidized policies on NFIP generally could involve accelerating elimination of subsidies, targeting assistance for subsidies, or expanding mitigation efforts, or some combination. Each approach has advantages and disadvantages. In GAO's 2008 study about rate-setting, GAO noted that the losses generated by NFIP have created substantial financial exposure for the federal government and U.S. taxpayers—due in part to its rate-setting process. Partly because of these rate-setting issues, GAO concluded in a July 2013 report that the advantages and disadvantages to additional changes to the program, such as raising coverage limits or adding optional coverage types, would need to be carefully weighed.

The Federal Emergency Management Agency (FEMA) will require several years to fully implement the Biggert-Waters Act. FEMA officials acknowledged that they have challenges to resolve. These include updating and correcting information on whether a policy is for a primary or secondary residence, determining the fair market value of insured properties, and developing a definition of severe repetitive loss for multifamily properties. Further, FEMA must establish full-risk rates that reflect flood risk for active policies that no longer are eligible for subsidies; but it does not have a plan to do so. In an effort to update payment formulas to insurance companies, as GAO recommended, FEMA has begun receiving actual flood-related information from some insurance companies but all companies are not reporting the information consistently.

Chairman Merkley, Ranking Member Heller, and Members of the Subcommittee:

I am pleased to be here today to testify on the National Flood Insurance Program (NFIP). As you know, the flood insurance program is a key component of the federal government's efforts to minimize the damage and financial impact of floods. Created in 1968, it is administered by the Federal Emergency Management Agency (FEMA) within the Department of Homeland Security. As of the end of fiscal year 2012, the program had more than 5.5 million policies with an insured value of about $1.3 trillion and collected about $3.5 billion in annual premiums.

My statement today will discuss (1) the reasons that NFIP is considered high risk, (2) changes to subsidized policies and implications of potential additional program changes, and (3) additional challenges for FEMA to address. This testimony is based on two reports we recently issued in July 2013 on NFIP coverage limits and subsidized properties and other prior GAO reports on various issues related to NFIP.[1] In conducting work for our July 2013 reports, we analyzed FEMA data on flood insurance policies, claims, and repetitive losses, as well as historic data on claims and premiums for policies with subsidized and full-risk rates. We also interviewed industry experts, including representatives from FEMA, insurance industry organizations, brokers, insurance companies, and consumer advocacy organizations. Finally, we reviewed prior GAO reports and testimonies and relevant studies conducted by RAND, the Wharton Risk Management and Decision Processes Center, Deloitte Consulting LLP, the Congressional Research Service, and academics.

We conducted the work on which this statement is largely based in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that

[1]GAO, *Flood Insurance: More Information Needed on Subsidized Properties,* GAO-13-607 (Washington, D.C.: July 3, 2013); *Flood Insurance: Implications of Changing Coverage Limits and Expanding Coverage,* GAO-13-568 (Washington, D.C.: July 3, 2013);*High-Risk Series: An Update*, GAO-13-283 (Washington, D.C.: February 2013); *Flood Insurance: Options for Addressing the Financial Impact of Subsidized Premium Rates on the National Flood Insurance Program,* GAO-09-20 (Washington, D.C.: Nov. 14, 2008); and *Flood Insurance: FEMA's Rate-Setting Process Warrants Attention,* GAO-09-12 (Washington, D.C.: Oct. 31, 2008).

the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Background

The National Flood Insurance Act of 1968 established NFIP as an alternative to providing direct disaster relief after floods.[2] NFIP, which makes federally backed flood insurance available to residential property owners and businesses, was intended to reduce the government's escalating costs for repairing flood damage. Floods are the most common and destructive natural disaster in the United States; however, homeowners' insurance generally excludes flooding. Because of the catastrophic nature of flooding and the inability to adequately predict flood risks, private insurance companies historically have been largely unwilling to underwrite and bear the risk resulting from providing primary flood insurance coverage. Under NFIP, the federal government assumes the liability for the insurance coverage and sets rates and coverage limitations, while the private insurance industry sells the policies and administers the claims.

NFIP offers two types of flood insurance premiums to property owners who live in participating communities: subsidized and full-risk. The National Flood Insurance Act of 1968 authorized NFIP to offer subsidized premiums to owners of certain properties. These subsidized rates are not based on flood risk and, according to FEMA, represent only about 40-45 percent of the full flood risk. Congress originally mandated the use of subsidized premiums to encourage communities to join the program and mitigate concerns that charging rates that fully and accurately reflected flood risk would be burdensome to some property owners. Even with highly discounted rates, subsidized premiums are, on average, higher than full-risk premiums. The premiums are higher because subsidized structures built before Flood Insurance Rate Maps (FIRM) became available generally are more prone to flooding (that is, riskier) than other structures. In general, pre-FIRM properties were not constructed according to the program's building standards or were built without regard to base flood elevation—the level relative to mean sea level at which there is a 1 percent or greater chance of flooding in a given year.

[2] Pub. L. No. 90-448, Title XIII, § 1302, 82 Stat. 476, 572 (1968).

Potential policyholders can purchase flood insurance to cover both buildings and contents for residential and commercial properties. NFIP's maximum coverage for residential policyholders is $250,000 for building property and $100,000 for contents. This coverage includes replacement value of the building and its foundation, electrical and plumbing systems, central air and heating, furnaces and water heater, and equipment considered part of the overall structure of the building. Personal property coverage includes clothing, furniture, and portable electronic equipment. For commercial policyholders, the maximum coverage is $500,000 per unit for buildings and $500,000 for contents (for items similar to those covered under residential policies).

NFIP largely has relied on the private insurance industry to sell and service policies. In 1983, FEMA established the Write-Your-Own (WYO) program.[3] Private insurers become WYOs by entering into an arrangement with FEMA to issue flood policies in their own name. WYOs adjust flood claims and settle, pay, and defend claims but assume no flood risk. Insurance agents from these companies are the main point of contact for most policyholders. WYOs issue policies, collect premiums, deduct an allowance for commission and operating expenses from the premiums, and remit the balance to NFIP. In most cases, insurance companies hire subcontractors—flood insurance vendors—to conduct some or all of the day-to-day processing and management of flood insurance policies. When flood losses occur, policyholders report them to their insurance agents, who notify the WYOs. The companies review the claims and process approved claims for payment. FEMA reimburses the WYOs for the amount of the claims plus expenses for adjusting and processing the claims, using rates that FEMA establishes. As of September 2012, about 85 WYOs accounted for about 85 percent of the more than 5.5 million policies in force.[4]

[3]From 1969 through 1977, the Department of Housing and Urban Development (HUD), which administered NFIP at the time, had an agreement with a consortium of private insurers known as the National Flood Insurers Association. Under this agreement, HUD reimbursed the association for operating costs and provided an annual operating allowance equal to 5 percent of policyholders' premiums. From 1978 through 1983, a federal contractor (not an insurance company) sold and serviced policies.

[4]Although WYOs handle most flood policies, FEMA still contracts with a company that serves as the insurer of last resort when an eligible customer cannot purchase insurance from a WYO.

NFIP Remains on GAO's High-Risk List Due to Financial Instability and Other Challenges

NFIP was added to GAO's High-Risk List in 2006 due to losses from the 2005 hurricanes and the financial exposure the program created for the federal government.[5] Until 2004, NFIP was able to cover most of its claims with premiums it collected and occasional loans from the U.S. Treasury (Treasury) that it repaid. However, after the 2005 hurricanes—primarily Hurricane Katrina—the program borrowed $16.8 billion from Treasury to cover the unprecedented number of claims. In prior work we found that NFIP, as it was then structured, was not likely to generate sufficient revenues to repay this amount.[6] NFIP since has received additional borrowing authority in the amount of $9.7 billion to cover claims for Superstorm Sandy. As of July 31, 2013, the program owed Treasury approximately $24 billion.

NFIP's financial condition highlights structural weaknesses in program funding—primarily its rate structure. By design, NFIP does not operate for profit. Instead, the program must meet a public policy goal—to provide flood insurance in flood-prone areas to property owners who otherwise would not be able to obtain it. NFIP generally is expected to cover its claim payments and operating expenses with the premiums it collects. However, subsidized policies have been a financial burden on the program because of their relatively high losses and premium rates that are not actuarially based. As discussed previously, subsidized policies are associated with structures more prone to flood damage (either because of the way they were built or their location). As a result, the annual amount that NFIP collects in both full-risk and subsidized premiums is generally not enough to cover its operating costs, claim payments, and principal and interest payments to Treasury, especially in years of catastrophic flooding. This arrangement results in much of the financial risk of flooding being transferred to the federal government and ultimately the taxpayer.

The Biggert-Waters Flood Insurance Reform Act of 2012 (Biggert-Waters Act) addressed some of the structural challenges that have contributed to the program's financial instability.[7] For example, new flood insurance policies will not receive subsidized premium rates, subsidies on existing

[5]GAO, *GAO's High-Risk Program,* GAO-06-497T (Washington, D.C.: Mar. 15, 2006).

[6]GAO-13-283.

[7]Biggert-Waters Flood Insurance Reform Act of 2012, Pub. L. No. 112-141, 126 Stat. 405, 916 (2012).

policies for many other properties will be phased out, and policies for properties that are remapped to a higher risk level will be subject to higher premium rates. In addition the Biggert-Waters Act requires FEMA to implement other changes to its rate-setting process, including building a reserve fund and updating maps used to set rates to reflect relevant information on topography, long-term erosion of shorelines, future changes in sea levels, and the intensity of hurricanes.[8] While these changes may help increase NFIP's long-term financial stability, the program still faces challenges in implementing the changes and their ultimate effect is not yet known.

Furthermore, weaknesses in NFIP management and operations, including financial reporting processes and internal controls, strategic and human capital planning, and oversight of contractors, also have placed the program at risk. For example, in 2011 we found that FEMA had not developed goals, objectives, or performance measures for NFIP. In addition, FEMA faces challenges modernizing NFIP's insurance policy and claims management system. As a result, we made recommendations to improve the effectiveness of FEMA's planning and oversight efforts for NFIP; improve FEMA's policies and procedures for achieving NFIP's goals; and increase the usefulness and reliability of NFIP's flood insurance policy and claims processing system. While FEMA agreed with our recommendations and has taken some steps to address them, continued attention to these issues is vital and additional steps are needed to address the concerns we have identified in the past.[9]

Change to Subsidized Policies and Implications of Additional Program Changes

The Biggert-Waters Act mandates that GAO conduct a number of studies related to actual and potential changes to NFIP, including analyses of remaining subsidized properties, and the effect of increasing coverage limits or adding coverage options. In one of our studies responding to these mandates, of remaining subsidized properties, we estimated that with the changes in the Biggert-Waters Act approximately 438,000 policies are no longer eligible for subsidies, including about 345,000 nonprimary residential policies, about 87,000 business policies, and about

[8] Pub. L. No. 112-141, §§ 100212, 100216, 126 Stat. 405,922,927 (2012).

[9] GAO, *FEMA: Action Needed to Improve Administration of the National Flood Insurance Program,* GAO-11-297 (Washington, D.C.: June 9, 2011).

9,000 single-family, severe-repetitive-loss policies.[10] Subsidies on most of the approximately 715,000 remaining subsidized policies are expected to be eliminated over time. Under the act, most remaining subsidized policies no longer would be eligible for subsidies if NFIP coverage lapsed or the properties were sold or substantially damaged. We estimated that with implementation of the provisions addressing sales and coverage lapses, the number of subsidized policies could decline by almost 14 percent per year. At that rate, the number of subsidized policies would be reduced by 50 percent in approximately 5 years. After about 14 years, fewer than 100,000 subsidized policies would remain. However, the actual outcomes and time required for subsidies to be reduced could vary depending on the behavior of policyholders and the actual rate of sales and coverage lapses. In terms of characteristics, we found that the geographic distribution of remaining subsidized policies was similar to the distribution of all NFIP policies. Other characteristics we analyzed—indicators of home value and owner income—were different for the policies that continue to be eligible for subsidized premium rates compared to those with full-risk rates. In particular, counties with higher home values and income levels tended to have larger percentages of remaining subsidized policies than policies with full-risk rates.

In our July 2013 report on subsidized policies, we identified three broad options that could help address the financial impact of remaining subsidized policies on the program, but the advantages and disadvantages of each would need to be considered and action would be required from both Congress and FEMA. These options are not mutually exclusive and may be used together to reduce the financial impact of subsidized policies on NFIP. The way in which an option is implemented (such as more aggressively or gradually) also can produce different effects in terms of policy goals and thus change the advantages and disadvantages.

- *Adjust the pace of eliminating subsidies*. Accelerating the elimination of subsidies could improve NFIP's financial stability by more quickly increasing the number of policies with premium rates that more accurately reflect the full risk of flooding, but could exacerbate the difficulty some policyholders may have in adjusting to new rates. In contrast, delaying the elimination of subsidized policies or lengthening

[10] GAO-13-607.

the phase-in period would continue to expose the federal government to increased financial risk over a longer time. Moreover, delaying the elimination of subsidies would not represent a long-term fix for those policyholders who could not afford the new premium rates, whenever they came into effect.

- *Target assistance for remaining subsidies*. Assistance or a subsidy could be based on the financial need of the property owners, which could help ensure that only those policyholders needing the subsidy would have access to it and retain their coverage, with the rest paying full-risk rates. Targeting subsidies based on need—through a means test, for example—is an approach other federal programs use. However, NFIP does not currently collect the policyholder data required to assess need and determine eligibility and it could be difficult for FEMA to develop and administer such an assistance program in the midst of ongoing management challenges. Moreover, unlike other agencies that provide—and are allocated funds for—traditional subsidies, NFIP does not receive an appropriation to pay for shortfalls in collected premiums caused by its subsidized rates. One approach to maintain subsidies but improve NFIP's financial stability would be to rate all policies at the full-risk rate and appropriate subsidies for eligible policyholders.
- *Expand mitigation efforts such as elevation, relocation, and demolition of properties*. This would include making mitigation mandatory to ensure that more homes were better protected. Mitigation efforts could be used to help reduce or eliminate the long-term risk of flood damage; especially if FEMA targeted the properties that were most costly to the program, such as those with repetitive losses. However, mitigation is expensive for NFIP, taxpayers, and communities.

In our October 2008 study of NFIP's rate-setting, we found that the losses generated by NFIP have created substantial financial exposure for the federal government and U.S. taxpayers—due in part to the program's rate-setting process.[11] We also found that FEMA's rate-setting methods, even for full-risk rates, do not result in rates that accurately reflect flood risks. For example, FEMA's rate-setting process does not fully take into account ongoing and planned development, long-term trends in erosion, or the effects of global climate change.[12] Furthermore, FEMA sets rates

[11]GAO-09-12.

[12]The Biggert-Waters Act requires FEMA to include, among other things, relevant information on topography, coastal erosion areas, changing lake levels, future changes in sea levels, and intensity of hurricanes.

on a nationwide basis, combining and averaging many topographic factors that are relevant to flood risks, and does not specifically account for these factors when setting rates for individual properties.

Partly because of the rate-setting issues, in our July 2013 report on raising coverage limits or adding optional coverage types, we found that the advantages and disadvantages to making more changes to the program, such as these, would need to be carefully weighed.[13] To determine the financial impact on NFIP of increasing coverage limits, we estimated the potential financial effect on NFIP if coverage limits had been raised in 2002–2011. Higher coverage limits would have been associated with increased net revenue in all fiscal years from 2002 through 2011, except for fiscal years 2004 and 2005 when the program experienced catastrophic losses. The overall results were the same when we conducted the analyses using variations in our assumptions to (1) decrease the premiums by 20 percent below the baseline estimate; (2) decrease the claims by 20 percent below the baseline estimate; and (3) estimate that only 25 percent, 50 percent, or 75 percent of all policyholders increased their coverage. Overall, the financial impact on the program of raising coverage limits would depend on the adequacy of the rates charged for the additional coverage. We also found that adding business interruption coverage to NFIP could be particularly challenging. For example, properly pricing risk, underwriting, and claim processing can be complex. Similarly, offering optional coverage for additional living expenses would have many of the same potential effects on NFIP, although this coverage generally is less complex to administer.

Additional Challenges for FEMA to Address

In July 2013, we reported that FEMA will require several years to fully implement the Biggert-Waters Act and FEMA officials acknowledged that they have data limitations and other challenges to resolve before eliminating some subsidies as required in the act. The following points highlight some of the challenges we identified:

- The act eliminated subsidies for residential policies that covered nonprimary residences and business policies. FEMA has data on whether a policy covers a primary residence, but officials stated that the data may be outdated or incorrect. In addition, FEMA categorizes

[13] GAO-13-568.

policies as residential and nonresidential rather than residential and business. As a result, FEMA does not have the information to identify nonresidential properties such as schools or churches that are not businesses and continue to be eligible for a subsidy. Beginning in October 2013, FEMA will require applicants for new policies and renewals to provide property status (residential or business).

- The act states that subsidies will be eliminated for policies that have received cumulative payment amounts for flood-related damage that equaled or exceeded the fair market value of the properties, and for policies that experience damage exceeding 50 percent of the fair market value of properties after enactment. Currently, FEMA is unable to make this determination as it does not maintain data on the fair market value of properties insured by subsidized policies. FEMA officials said that they have been in the process of identifying a data source.
- The act eliminates subsidies for severe repetitive loss policies and provides a definition of severe repetitive loss for single-family homes. However, it requires FEMA to define severe repetitive loss for multifamily properties and FEMA has not yet developed this definition.

The act also requires FEMA to phase in full-risk rates on active policies that no longer are eligible for subsidies, but we found that FEMA generally lacks information needed to establish full-risk rates that reflect flood risk for the properties involved and also lacks a plan for proactively obtaining such information. Federal internal control standards state that agencies should identify and analyze risks associated with achieving program objectives, and use this information as a basis for developing a plan for mitigating the risks. In addition, these standards state that agencies should identify and obtain relevant and needed data to be able to meet program goals. However, in July 2013 we reported that FEMA does not have key information used in determining full-risk rates from all policyholders. According to FEMA officials, not all policyholders have elevation certificates, which document their property's risk of flooding. Information about elevation is a key element in establishing premium rates on certain properties. Elevation certificates are required for some properties, but optional for others. According to FEMA officials, consistent with the act they are phasing in rate increases (of 25 percent per year) for policyholders who no longer are eligible for subsidies. The increase will continue until the rates reach a specific level or until policyholders supply an elevation certificate that indicates the property's risk, allowing FEMA to determine the full-risk rate.

Although subsidized policies have been identified as a risk to the program because of the financial drain they represent, FEMA does not have a plan to expeditiously and proactively obtain the information needed to set full-risk rates for all of them. Instead, FEMA will rely on certain policyholders to voluntarily obtain elevation certificates, which can be expensive for the property owner. Those at lower risk levels have an incentive to do so because they may then be eligible for lower rates. However, policyholders may not know their risk level, and policyholders with higher risk levels have a disincentive to voluntarily obtain an elevation certificate because they then could pay a higher premium. In our July 2013 report, we concluded that without a plan to expeditiously obtain property-level elevation information, FEMA will continue to lack basic information needed to accurately determine flood risk and continue to base full-risk rate increases for previously subsidized policies on limited estimates. As a result, FEMA's phased-in rates for previously subsidized policies still may not reflect a property's full risk of flooding; with some policyholders paying premiums that are below and others paying premiums that exceed full-risk rates. We recommended that FEMA develop and implement a plan, including a timeline, to obtain needed elevation information as soon as practicable.[14] FEMA agreed with this recommendation and plans to evaluate the appropriate approach to obtain or require the submittal of this information.

The Biggert-Waters Act also requires a number of other changes that the agency has been starting to implement. For example FEMA must adjust rates to accurately reflect the current risk of flood to properties when an area's flood map is changed, subject to any other statutory provision in chapter 50 of Title 42 of the Unites States Code.[15] As we reported in July 2013, FEMA has been determining how this provision would affect properties exempted from rate increases when they were remapped.[16] The act also requires FEMA to develop a plan for repaying the current debt owed to Treasury and establish a catastrophic loss reserve fund. FEMA officials told us that Superstorm Sandy delayed development of the repayment plan, but they are scheduled to submit a plan to Congress on September 30, 2013. They also noted that they planned to create a reserve fund by increasing each premium by a certain percentage (as the

[14]GAO-13-607.

[15]42 U.S.C. § 4015(e).

[16]Pub. L. No. 112-141, § 100205, 126 Stat. 405, 919 (2012).

agency deems appropriate) over a number of years beginning October 1, 2013.[17]

We continue to monitor the status of FEMA's actions related to recommendations we have made in prior reports. In 2008, we recommended that FEMA develop a rate-setting methodology that uses data that results in full-risk premiums that accurately reflect the risk of losses from flooding.[18] Data used to develop rates should take into account the effects of long-term planned and ongoing development, including climate change. In response to our continued support of this recommendation as well as requirements in the Biggert-Waters Act, FEMA officials stated that they have made progress. For example, FEMA stated they already have revised damage calculations for flooding events that only reach the foundation of the structure, and performed a study to assess the long-term impacts of climate change. FEMA's ongoing efforts include analyzing water-depth probability curves for the various zones and piloting studies to determine structure elevation and flood depths for various return periods.

In 2009, we also recommended that FEMA consider the actual flood-related expenses and profits of WYOs when setting payment rates, while also taking other actions to ensure the accuracy of this financial information.[19] Consistent with our recommendations, the Biggert-Waters Act requires FEMA to develop a methodology for determining the appropriate amounts that property and casualty insurance companies participating in the WYO program should be reimbursed for selling, writing, and servicing flood insurance policies and adjusting flood insurance claims.[20] The act also requires that FEMA publish a rule revising expense reimbursements and that such reimbursements be structured to track actual flood-related expenses "as closely as practically possible." FEMA officials told us that the agency has begun to obtain actual flood-related financial information and has been working with the

[17]Effective on or after October 1, 2013, a reserve fund ratio of 5 percent of the total premium will be applied to each NFIP policy, with certain exceptions.

[18]GAO-09-12.

[19]GAO, *Flood Insurance: Opportunities Exist to Improve Oversight of the WYO Program,* GAO-09-455 (Washington, D.C.: Aug. 21, 2009).

[20]Pub. L. No. 112-141, § 100224, 126 Stat. 405,936 (2012).

National Association of Insurance Commissioners (NAIC) and conducting other analyses to ensure that WYOs accurately report this information. However, FEMA officials stated that the agency cannot take action that completely addresses our recommendations until the WYOs reliably report to NAIC and that it might take several years before all companies consistently report such information. The agency also has been considering how to best introduce the WYOs' actual flood-related expenses into payment formulas over the next several years, when FEMA expects to have more reliable financial information and less variation in reported expense ratios.

In 2011, we recommended that FEMA improve strategic planning, performance management, and program oversight within and related to NFIP.[21] FEMA agreed with our recommendations and has addressed some of them, such as strategic planning, but it still needs to continue to address the management and operational weaknesses we identified, including human capital planning, acquisition management, policy and claims management systems, financial management, collaboration, and records management. Unless these management issues are addressed, FEMA risks ongoing challenges in effectively and efficiently managing NFIP, including its management and use of data and technology.

In conclusion, when we placed NFIP on the high-risk list in 2006, we noted that comprehensive reform likely would be needed to address the financial challenges facing the program. Since passage of the Biggert-Waters Act, FEMA is taking some important first steps toward implementing the reforms the act requires, but the extent to which the changes included in the act and FEMA's implementation will reduce the financial exposure created by the program is not clear and the program's long-term financial condition is not yet assured. In addition, our previous work has identified many of the necessary actions that FEMA should take to address a number of ongoing challenges in managing and administering the program. Getting NFIP on a sound footing, both financially and operationally, is important to achieving its goals and at the same time reducing its burden on the taxpayer.

[21] GAO-11-297.

Chairman Merkley, Ranking Member Heller, and Members of the Subcommittee, this concludes my prepared statement. I would be happy to answer any questions that you may have at this time.

Contact and Staff Acknowledgments

If you or your staff have any questions about this testimony, please contact me at (202) 512-8678 or cackleya@gao.gov. Contact points for our Offices of Congressional Relations and Public Affairs may be found on the last page of this statement. Other staff who made key contributions to this testimony include Jill Naamane and Patrick Ward (Assistant Directors); Isidro Gomez; Karen Jarzynka-Hernandez; Barbara Roesmann; Rhonda Rose; and Jessica Sandler.

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