

## ***COASTAL FORUM***

### **Myth of the Subsidized Beach Resident**

*By*

James R. Houston

*Coastal and Hydraulics Laboratory*

*US. Army Engineer Waterways Experiment Station*

A common myth is that all beach residents have or are eligible for subsidized flood insurance provided by the National Flood Insurance Program (NFIP) at great cost to taxpayers. In fact, only a tiny percentage of the NFIP's policy base is located in coastal flood-prone areas, and these areas have paid more in premiums than they have received in flood claims. All NFIP insurance currently sold is completely actuarial with rates fully reflecting flood-damage risk and without taxpayer subsidies. Flood-insurance subsidies flow to communities "grandfathered" by the original NFIP legislation, and most of these communities are located along rivers.

A widespread misunderstanding is that all NFIP flood insurance (in particular, that of beach residents) is heavily sub-sidized. For example, John Stossel, ABC News, stated in a recent nationally-televised program, "You should know that the government also spends lots of your tax dollars subsidizing rich people. The subsidized insurance goes to affluent homeowners here in Malibu, where the movie stars live, in Kennebunkport, where George Bush has his home, and here in the elegant Hamptons in New York. Now, private insurance companies would wisely be reluctant to insure houses like these. Only Uncle Sam is a big enough

sucker - so much so that he allows people like me to freeloader off you taxpayers." Opponents of coastal development usually claim the imagined subsidy to coastal residents is quite large. "Taxpayers who pass by expensive, exposed beach houses may not realize that taxpayers' dollars insure many of these luxury homes against storms and erosion that can cause billions of dollars in damages."<sup>2</sup> Coastal dwellers are sometimes portrayed as having subsidized flood insurance that is provided through taxing the proverbial suffering farmer in Kansas or some other Great Plains state. "If you want to live on the coast, live on the coast. Don't involve the pocket of the taxpayer in Topeka, Kansas 3

What are the facts? Edward Pasterick, Chief of the Financial Division and Acting Executive Administrator, Federal Insurance Administration, Federal Emergency Management Agency (FEMA) notes that only 3 percent of NFIP policies are located in coastal flood-prone areas.' Moreover, these coastal areas have paid more in premiums than they have received in flood claims.<sup>4</sup> Since 1982 or completion of a community's first flood-insurance-rate map, all buildings insured under the NFIP including those in coastal communities, "...are charged actuarially-sound insurance rates that fully reflect the building's risk of flooding."<sup>5</sup> Older NFIP policies in effect between NFIP initiation and establishment of actuarially-based rates are subsidized. The percentage of policies that are subsidized is currently 38% versus 70% in 1978, and it will continue to decline since all new policies are actuarial.<sup>5</sup> These older subsidized policies are overwhelmingly in riverine flood areas. Between 1978 and 1995, actuarially-based NFIP policies in special flood-hazard areas such as the coastal high-hazard zone have generated a \$169 million surplus

after claims and expenses were paid for administering the Program.<sup>5</sup> Therefore, actuarially-based NFIP policies are not subsidized by taxpayers. The NFIP has an operating deficit since its establishment in 1968 only due to heavy losses from riverine flooding in 1992, 1993, 1995, and 1996. Because most older subsidized policies are in riverine areas, the Kansas farmer may well have received subsidized flood insurance and is certainly not subsidizing flood insurance of coastal residents who have paid more in premiums than they have collected in claims. For example, the NFIP has paid Missouri policy holders more in claims than California policy holders~.

Why is there a myth that all beach residents have or are eligible for subsidized flood insurance? Media reporting of floods often highlights structures that have been repeatedly flooded and restored through the NFIP. Two percent of NFIP policies receive 40 percent of NFIP payments<sup>7</sup> because these 'grandfathered' policies cover structures that are at elevations much below the 100-year flood level and, therefore, they are repeatedly flooded. Laws governing the NFIP allow restoration of structures that have been repeatedly flooded. This repeated restoration is wasteful and makes an interesting story that the media naturally covers.'<sup>9</sup> However, the story often leaves the impression that all NFIP insurance is subsidized. Although repeated flooding is mostly riverine with repeated-flooding claims in the coastal high-hazard zone representing only 3 percent of claims,<sup>7</sup> coastal-development foes have used the perception that all NFIP insurance is subsidized to help make their case against coastal development.

A recent front-page article in the Wall Street Journal<sup>9</sup> is a good example of a story focusing on NFIP insurance and

repeat-ed flooding that leaves the impression that all NFIP insurance is subsidized and coastal flooding is the primary repeat-flooding culprit. The phrase 'federally subsidized flood insurance' is used several times in the article, but there is no mention that NFIP flood insurance sold since 1982 has been completely actu-arial and a majority of outstanding policies are actuarial. The article discusses only coastal flooding and says, "In recent years, development along coasts has grown, and costs associat-ed with beach communities have spiraled upward. In the past five years, the federal government has spent about \$40 billion on flood relief."<sup>3</sup> The implication is that much of this huge cost is borne by the NFIP and results primarily from coastal flood-mg. NFIP has made \$3.3 billion in flood-insurance loss pay-ments the last 5 years, but only 3 percent of these payments have been for flooding in the coastal high-hazard zone.<sup>7~</sup>" In addition, policy holders in the coastal high-hazard zone have paid insurance premiums that have exceeded loss payments.<sup>4</sup> The article ends with coastal-development opponent, Orrin Pilkey, explaining why coastal development is bad. Dr. Pilkey also appeared with John Stossel in the ABC News television program, and both criticized NFIP to FEMA's Administrator, James Lee Witt. Stossel said of Dr. Pilkey, "Re says both disas-ter relief and federal flood insurance just encourage people to stay in harm"s way." Coastal-development opponents help per-petuate myths about the NFIP.

The NFIP has received bad press, but it has been an over-all success. It was established to reduce flood damages by offer-ing communities incentives to adopt and enforce floodplain- management ordinances that met minimum criteria established by FEMA. These criteria require structures be elevated to or above the 100-year flood

elevation, and, in the case of coastal areas, designed to withstand wave impacts. FEMA estimates that meeting its floodplain-management requirements generally adds less than 5 percent to construction costs of structures.<sup>5</sup> The NFIP has been successful in reducing flooding damages, because buildings constructed to NFIP minimum standards sustain 77 percent less in losses than those not built to these standards.~ FEMA estimates that since 1995, community flood-plain-management ordinances established to comply with NFIP requirements have saved more than \$800-million annually." Further, the Coastal Barrier Resources Act (CBRA) of 1982 relies on the NFIP to discourage building in fragile coastal areas by prohibiting sale of flood insurance in areas covered by the Act.<sup>2</sup>

In summary, only 3 percent of NFIP policies are in coastal communities, and these communities have generated more pre-mium income to NFIP than they have received in loss claims. All NFIP policies sold since 1982 (or earlier if flood-hazard maps from FEMA were available) are based on actuarial rates and are not subsidized. Opponents of coastal development lament the imagined sacrifice of the Kansas farmer in subsidiz-ing flood insurance for rich coastal residents, but riverine flood losses have caused the NFIP to run a deficit. Coastal residents have to date paid more in premiums than they have received in loss claims. The NFIP discourages building in CBRA-protected coastal areas and successfully encourages wise coastal-zone construction that puts structures and people out of harm's way, thereby saving Americans \$800 million a year.

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