

[GAO Issues Dire Report on National Flood Insurance Program](#)

Property Casualty 360

May 14, 2014 By: Arthur Postal WASHINGTON—The National Flood Insurance Program (NFIP) is a long, dark tunnel with no light in sight, a new Government Accountability Office report indicates, meaning that it is likely to be a political headache for the property casualty insurance industry for some time to come. That's because the report makes clear that the NFIP will remain a football tossed between members of Congress who see subsidizing the program a necessity, and conservatives who say it should be self-supporting. Moreover, the report supports the arguments of conservatives that the 2014 law rolling back the mandate in the 2012 law that requires the phase-in of actuarial rates over five years, will exacerbate the NFIP's solvency issues. Besides the usual concerns, including the fact that the NFIP is unlikely to attain the congressional mandate of paying off its current long-term outlook within the required 10 years, the new GAO study raises another critical issue that has escaped public attention: the fact that there is no means of ensuring that people who by law should have flood insurance—that is, homeowners with mortgages in vulnerable areas—buy the product. It implies that if everyone who should have flood insurance purchases the product, it would ease at least somewhat the revenue shortages that are a key component of its main problem, affordability. As one industry official familiar with the problem acknowledges, “the banks and other lenders are the ‘elephants in the room’, [because] there is no real penalty for not requiring mortgage-holders in flood zones to secure and maintain the coverage.” The report also takes issue with complaints by members of Congress and consumer advocacy groups who argue that the flood mapping activities of the Federal Emergency Management Agency, the federal agency which oversees the NFIP, overstates the risk of flooding. By contrast, the GAO report argues that, “FEMA's methodology for determining full-risk premium rates may not fully reflect the actual risk of flood damage as intended [by Congress].” The report said that as of Dec. 31, 2013, the NFIP owed the government \$24 billion, and had not made a principal payment since 2010. The report also said that the 2012 law which reauthorized the program for five years requires FEMA to issue a report to Congress by January 2013 on a repayment plan setting forth options to repay FEMA's total debt to Treasury within 10

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years. However, as of January 2014, FEMA had not issued such a report. The report said that, according to FEMA officials, preliminary analysis suggests that under FEMA's planned implementation of the act, the agency will not be able to repay its debt within the 10-year time frame. The GAO report said the report will contain options for retiring the debt within 10 years, but that most of the options would require congressional action. As required by the act, FEMA is establishing a reserve fund that could help reduce the need for future borrowing from Treasury, the GAO report said. "However, FEMA is unlikely to initially meet the act's annual targets for building up the reserve, due partly to statutory limitations on annual premium increases," the report said. The report said the 2014 law, which conservatives in Congress abhor, "reinstates" some of the subsidies ordered phased out by the 2012 law. "Phasing out and eventually eliminating subsidies remaining after the 2014 Act poses challenges for FEMA," the report said. For example, the report said, to appropriately revise rates for policies that were previously subsidized (that is, had discounted insurance premiums), FEMA will need information on the relative risk of flooding and property elevations, which generally had not been required for subsidized policies prior to the 2012 law. The report also rightly points out that "premium rate increases arising from the [2012 law] act may also pose affordability challenges for some homeowners." The report acknowledges that the 2014 Act's repeal of certain rate increases in the Biggert-Waters Act will address affordability concerns, "but may also reduce program revenues and weaken the financial soundness of the NFIP program." As to revenues, the report said that overall NFIP penetration rates—the proportion of all properties with flood insurance—are "low," according to estimates based on available limited data. In addition, the report said, while some homeowners are required to purchase flood insurance for the life of their mortgage loans, "information on the extent of compliance with this requirement is limited." The GAO cites several factors as limiting participation in the program, including inaccurate perceptions about the risk of flooding and the cost of purchasing policies, "as well as the inaccurate assumption that flood perils are included in homeowner's insurance policies." The report acknowledges that FEMA has taken a number of steps to broaden participation in NFIP, including development of a national outreach strategy. In addition, the report said, the 2012 law includes several provisions to strengthen enforcement of the mandatory purchase requirement and to address some of the factors that limit participation.