The Daily Dish

The NFIP Blues

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Eakinomics: The NFIP Blues

Eakinomics honestly cannot explain its obsession with the National Flood Insurance Program (NFIP), nor its stubborn hope that Taylor Swift will cash in her celebrity to demand decent incentives and protection of the American taxpayer. Policymakers' continued insistence on providing underpriced insurance with the taxpayers' backing, the repeated payouts to rebuild in places where no home should ever be built, and Congress's insistence that we need instead to be concerned about the impact on those being subsidized and bailed out just makes me crazy. And if anyone is well-positioned to whine about perpetual disappointment, it is Ms. Swift. Still, it is a mystery.

And the mystery is only deepening because – drum roll – the Democrats in the House of Representatives are poised to make things worse! Thomas Wade has the full story; here's the thumbnail version.

Let's begin with his pithy summary of the NFIP: "The National Flood Insurance Program is the principal provider of flood insurance in the United States and plays a crucial role in reducing the financial loss impacts of flooding for over 5 million Americans. Administered by the Federal Emergency Management Agency (FEMA), the NFIP was originally intended to be the facilitator of a private market of flood insurance and an insurer of last resort, but it has since morphed into the market itself via a burdensome federal program that has cost taxpayers at least $40 billion, is losing $600 million annually, and remains $20.5 billion in debt to the Treasury."

Insurance, the pricing of insurance, and government backstops for private insurance are not exactly the exclusive domain of Mensa-member rocket scientists aided by artificial intelligence. No, the way these work is something that is known. Yet Congress refuses to put the program on a sound footing. "Since fiscal year 2017, for example, the program has undergone 16 short-term extensions and brief lapses."

One of the real problems with the program is its adherence to outdated flood zone maps as the key way to measure risk. So FEMA's announcement on April 8, 2021, of a new approach to its flood risk pricing methodology, dubbed Risk Rating 2.0, represented real progress. "The key element of the project is to tailor FEMA's Risk MAP process and in particular to assess individual homes on the basis of individual risk, replacing the blunt metric of elevation of homes within a certain flood zone. FEMA will instead consider a wider range of variables, from flood frequency, to type of flood, to distance from water source, and consider homes on a case-by-case basis."

Risk Rating 2.0 would be fantastic, and I wanted a t-shirt. It would also mean higher (perhaps much higher) premiums for some expensive properties in risky locations, and Congress is allergic to higher premiums even for affluent constituents. So it is not surprising that when House Financial Services Democrats circulated a draft plan to reauthorize the NFIP, it capped at 9 percent the amount a premium can rise in any year. Bye bye Risk Rating 2.0.

Worse, much worse, it contains forgiveness for $20 billion of NFIP debt, essentially eliminating what it owes to the Treasury. It also eliminates the only incentive to get the NFIP to raise premiums, firmly entrenches in the NFIP the notion that future debt will be forgiven, and adds a healthy dose of moral hazard to the existing toxic mix of programmatic problems.

Alas poor Eakinomics. As the American philosopher Eric Hoffer put it, "Disappointment is a sort of bankruptcy – the bankruptcy of a soul that expends too much in hope and expectation." Write a song about that.