



# Risk Management BULLETIN

Texas Water Conservation Association Risk Management Fund



## Flood Coverage

Two of the most powerful and destructive forces on earth are water and wind. Homeowners and business owners along the coasts and the water courses of the United States know this terrible fact only too well. The destructive power of hurricanes and floods do billions of dollars of damage every year, much of it uninsured. According to a recap of disaster losses by Weather Underground in 2011 there were losses from tropical storm winds and floods in the United States totaling \$15.2 billion. And 2011 had only one landfall in the United States by a named hurricane, Irene a category 1 storm. Over the years, insurance companies have suffered devastating financial losses from tropical storms and floods, forcing some into liquidation. As a protective measure, many insurers withdraw from areas that are exposed to these events. Sometimes they even withdraw from whole states like Florida after 2005 when five hurricanes ravaged the state. This trend continues in Texas when in 2012 State Farm Insurance announced that they were canceling over 11,000 homeowner's policies in the Texas coastal counties of Brazoria, Chambers, Galveston, Jefferson and Orange.



Over the last several years, as the insurance market shrank for wind and flood damage, two insurance facilities arose to take the place of traditional insurance companies. For flood coverage, the national government stepped in and formed the National Flood Insurance Program of the Federal Emergency Management Agency after Hurricane Betsy in 1965. For winds associated with tropical storms, state governments established wind storm pools, much like assigned risk automobile liability pools to provide coverage through a market of last resort. Now, because there are alternative ways to provide coverage, most insurance companies no longer provide coverage for these two hazards

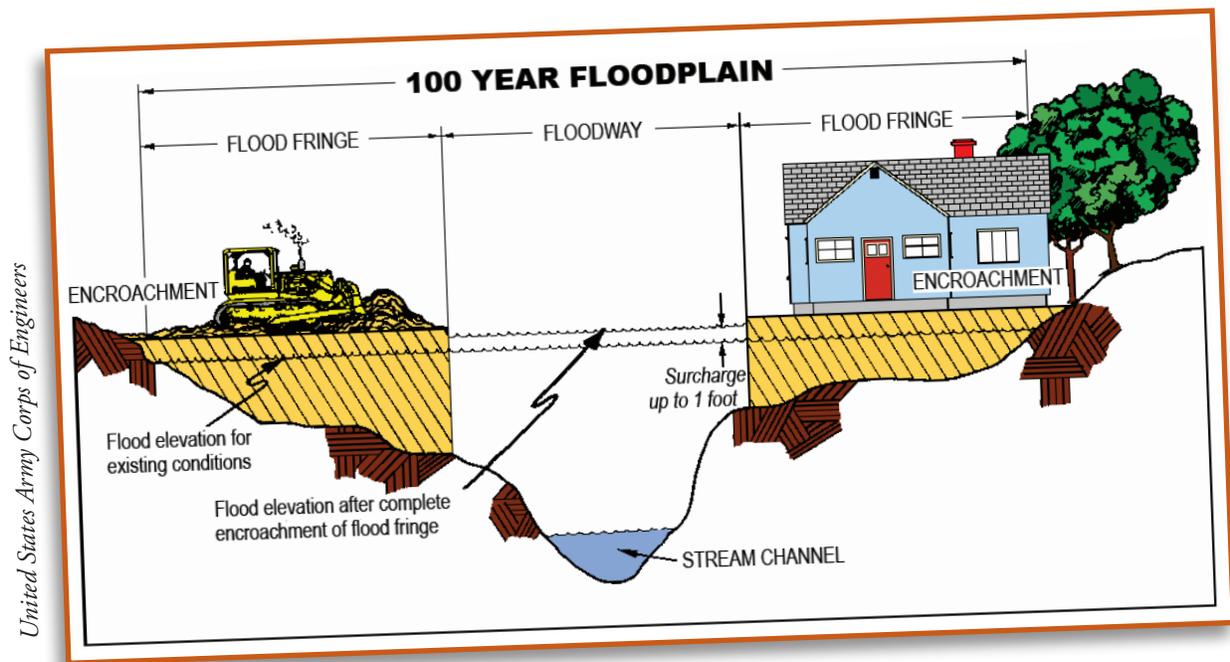
in coastal areas or in flood plains. The Texas Water

Conservation Association Risk Management Fund is no exception. If not properly structured, the huge exposures in the TWCARMF to losses caused by flood or named storm winds could destroy the solvency of the Fund and endanger the financial health of its members. Despite the Fund's limitations on coverage in coastal counties, Hurricane Ike still caused almost \$700,000 in claims outside the coastal zones. The Fund has also paid claims caused by other recent hurricanes such as Dolly and Rita.

Members who have substantial exposures to loss from wind or flood have a critical need for flood and wind insurance. So, how does a member cover its buildings and other property in flood zones or along the coast of Texas? This bulletin will examine flood insurance and how the TWCARMF coordinates and supplements coverage for its members. A separate bulletin will examine the same issues for wind and hail coverage in Texas for members of the TWCARMF. The insurance facility that provides flood coverage is the National Flood Insurance Program.

### THE NATIONAL FLOOD INSURANCE PROGRAM

Flood insurance is provided by the National Flood Insurance Program for property that is in a 100 year flood plain or coastal storm surge zone. The 100 year flood plain is known as Zone A. This geographical zone represents the land area that would be covered by flood waters from a flood that would occur on average once every 100 years. Another way of expressing this frequency is a 1% chance of a flood of this magnitude in a given year. This does not mean that a flood of this magnitude will only occur once in a 100 year period. In reality a 100 year flood can occur twice in a year, two years in a row or only once in 300 years. It all depends on local geography and meteorological conditions. To make matters even more unpredictable, changes in local conditions can increase or decrease the likelihood of floods. For instance, as rural areas see housing developments, new schools and shopping centers, the amount of impervious surface increases due to new roads, parking lots and buildings. This increases runoff into existing waterways. Subsidence in areas where large amounts of groundwater are being pumped out of underground aquifers can also make areas more susceptible to flooding. Likewise, construction of new dams, diversion structures, levees and runoff retention ponds can reduce the potential for flooding.



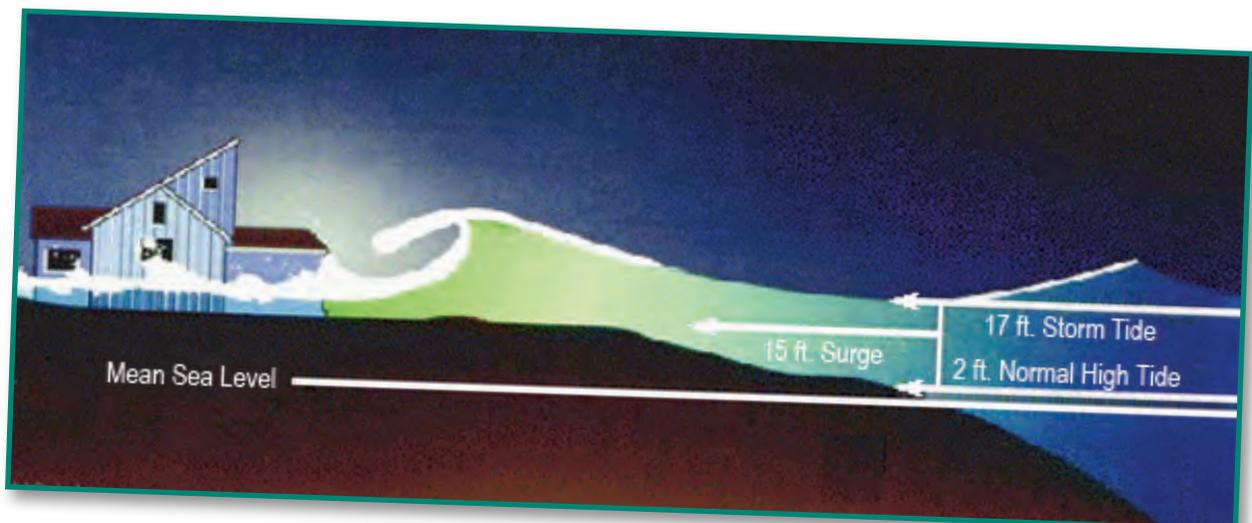
If a member's property is within the flood hazard area of a 100 year floodplain as illustrated above, it is not protected against flood damage by coverage issued by the TWCARMF.

### THE STANDARD FLOOD INSURANCE POLICY

For properties located in a flood zone, the only option for coverage is the National Flood Insurance Program(NFIP). Coverage available from the NFIP includes buildings and contents for both homeowners and businesses. Amounts of coverage available are:

Coverage Type	Coverage Limit
One to four-family structure	\$250,000
One to four-family home contents	\$100,000
Other residential structures	\$250,000
Other residential contents	\$100,000
<b>Business structure</b>	<b>\$500,000</b>
<b>Business contents</b>	<b>\$500,000</b>
Renter contents	\$100,000

Most properties owned by members of the TWCARMF would fall under the “Business Structure” or “Business Contents” categories. The limits are probably adequate for most structures in flood or storm surge zones. If they are not, there are a few options available for the purchase of excess flood insurance. An excess policy would provide limits of liability above the maximum amount of coverage provided in the NFIP policy.



*National Oceanic and Atmospheric Administration*

Now that we know the limits of liability available in the flood policy, the next question is what does the policy cover? The language in the policy that grants coverage reads:

### *I. AGREEMENT*

*The Federal Emergency Management Agency (FEMA) provides flood insurance under the terms of the National Flood Insurance Act of 1968 and its amendments, and Title 44 of the Code of Federal Regulations (CFR).*

*We will pay you for direct physical loss by or from flood to your insured property if you:*

- 1. Have paid the correct premium;*
  - 2. Comply with all terms and conditions of this policy;*
- and*
- 3. Have furnished accurate information and statements.*

*We have the right to review the information you give us at any time and to revise your policy based on our review.*

The first paragraph ties the coverage to the federal law and regulations that created and govern the NFIP. The three conditions after the insuring agreement put the policyholder on notice that they have an obligation to pay the premium and comply with the terms and conditions of the policy and the government has the right to change the policy and premiums based on their review of the information provided when the application for coverage was submitted. The review process can also include changes in flood maps, surveys that establish the elevation of the insured structure or information about the structural integrity of the building.



The *definitions* section of the policy contains important definitions that shape the coverage and conditions of the policy. **Flood** is defined as:

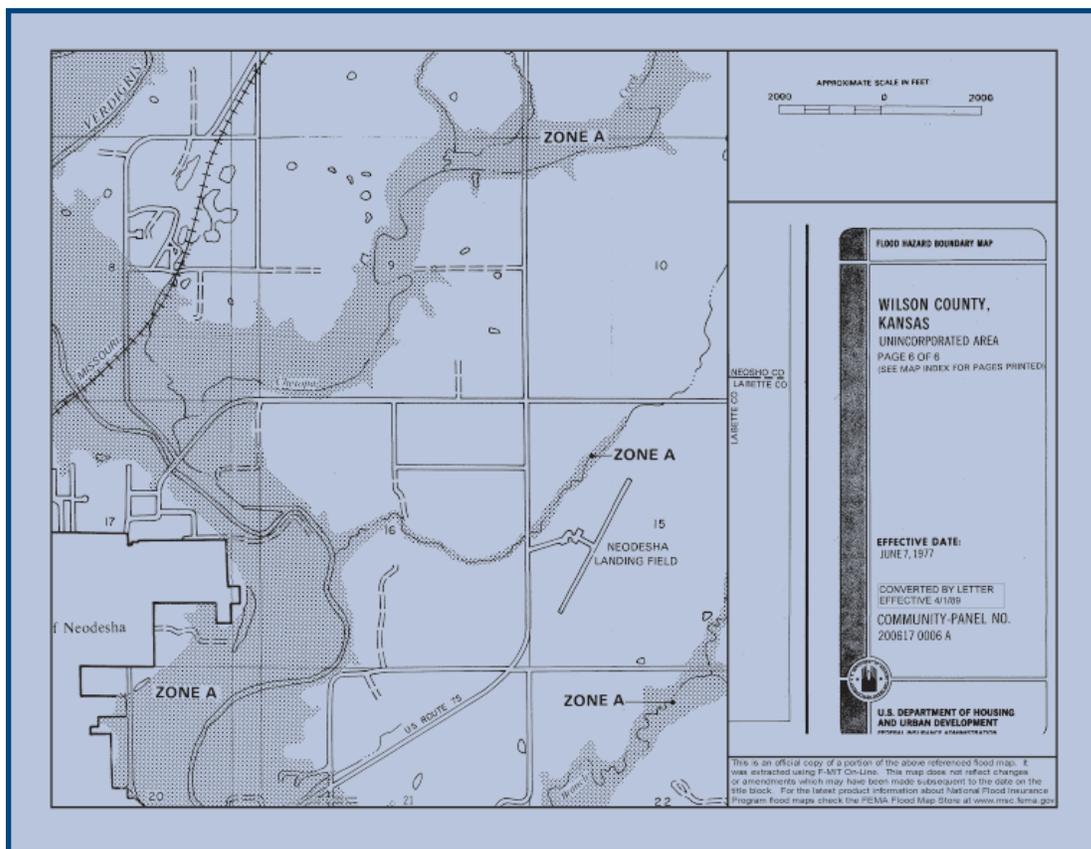
1. *A general and temporary condition of partial or complete inundation of two or more acres of normally dry land area or of two or more properties (at least one of which is your property) from:*
  - a. *Overflow of inland or tidal waters;*
  - b. *Unusual and rapid accumulation or runoff of surface waters from any source;*
  - c. *Mudflow.*
2. *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 in A.1.a. above.*

This is a broad definition that includes “**mudflow**” and the collapse or subsidence of land eroded by water currents or wave action. Mudflow is further defined as:

18. *Mudflow. A river of liquid and flowing mud on the surfaces of normally dry land areas, as when earth is carried by a current of water. Other earth movements, such as landslide, slope failure, or a saturated soil mass moving by liquidity down a slope, are not mudflows.*

Another important definition is that for a building. The key requirements are that it is

*A structure with two or more outside rigid walls and a fully secured roof, that is affixed to a permanent site.*

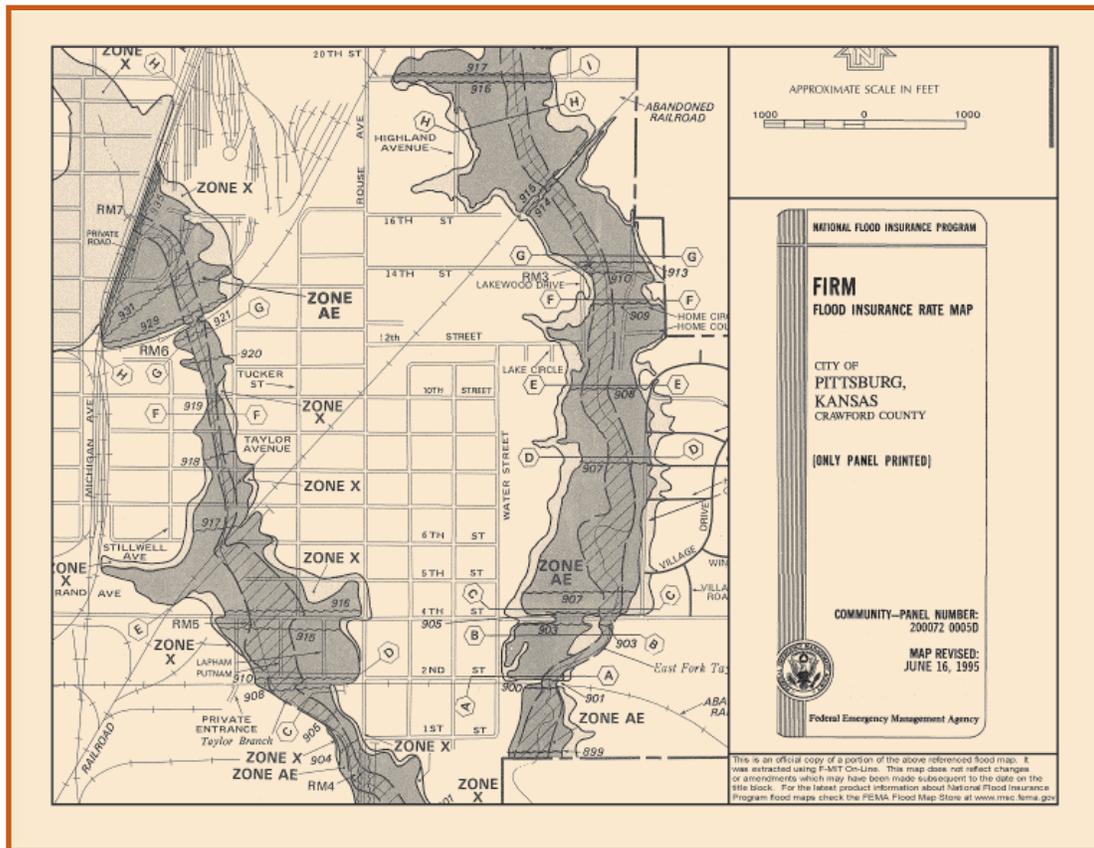


The definition also includes manufactured housing and travel type trailers permanently affixed to a foundation. Another important definition sets out the designations for flood zones that make up the Special Flood Hazard Area:

*An area having special flood, or mudflow, and/or flood-related erosion hazards, and shown on a Flood Hazard Boundary Map or Flood Insurance Rate Map as Zone A, AO, A1-A30, AE, A99, AH, AR, AR/A, AR/AE, AR/AH, AR/AO, AR/A1-A30, V1-V30, VE, or V.*

The “V” designations denote storm surge areas with storm induced wave action. The various “A” designations denote different types of flooding or different ways of determining if an area is subject to flooding. All of them require that flood insurance be purchased and that the area is subject to flood plain management rules and regulations.

Kansas Department of Agriculture, How to Read Flood Maps, power point presentation



Building coverage is described in “**Coverage A – Building Property.**” The policy also extends coverage to personal property inside the insured structure. This “**Coverage B – Personal Property**” is also subject to numerous lists of covered and excluded property. The language of the policy differentiates between “household personal property” or “other than household personal property” (contents related to business operations). The policy covers only one or the other category depending on the use of the structure.

In addition to coverage for a building and its contents, there are two additional coverage parts that provide coverage for actions taken before and after a flood. The first of these is “**C - Other Coverages**” that provides four supplemental coverages. The “Debris Removal” section provides payment for the expense to remove debris from your property after a flood. The second provision, “Loss Avoidance Measures” provides up to \$1,000 for sandbags, fill, pumps and plastic sheeting and your labor to do the work of trying to prevent flood damage. There is also \$1,000 available for “Property Removed to Safety” prior to the flood event and up to \$10,000 available for “damage to covered property caused by pollutants.”

The second major coverage in addition to the building contents and other coverages is “**D – Increased Cost of Compliance.**” This important provision of the policy addresses the rebuilding process after a flood stating:

*This policy pays you to comply with a State or local floodplain management law or ordinance affecting repair or reconstruction of a structure suffering flood damage. Compliance activities eligible for payment are: elevation, floodproofing, relocation, or demolition (or any combination of these activities) of your structure. Eligible flood proofing activities are limited to:*

*a. Nonresidential structures.*

*b. Residential structures with basements that satisfy FEMA’s standards published in the Code of Federal Regulations [44 CFR 60.6 (b) or (c)].*

This coverage provides up to \$30,000 for increased cost of complying with local laws or ordinances in addition to the coverage on the building as long as the total of the two amounts does not exceed the maximum limit of liability stated earlier in this bulletin. As with any other kind of insurance policy there are also exclusions, deductibles, general conditions and guidelines for submitting claims.

In July 2012 the National Flood Insurance Program was reauthorized for five more years by Congress. As part of the reauthorization several new provisions were included that could affect coverage and rates. A 10% cap on rate increases was changed to allow up to 20% increases per year. Minimum deductibles of \$1,000 and \$2,000 were imposed depending on the age of the home and the amount of coverage. The law now allows coverage for multi-family structures and imposes mandatory rate increases for structures that have had multiple flood claims, are second homes or commercial structures. In an attempt to bring more clarity to the claims process in coastal zones when both wind and flood or storm surge are involved, there is now a mechanism to use NOAA produced storm data to determine the predominant cause of claims. The dispute between flood and wind insurers after Katrina was a huge problem that seriously delayed thousands of claim settlements. The new law will probably result in increasing costs as the NFIP tries to repay the costs from Katrina and seeks new ways to pay future claims.

For members of the TWCARMF the only coverage available for properties in an A or V flood zone is through the National Flood Insurance Program. If additional limits of liability are needed for business property that exceeds \$500,000 in building value and \$500,000 in contents, excess flood insurance might be available that would cover amounts above the NFIP limits without any additional deductible. For member’s properties affected by flood that are not in the 100 year floodplain or coastal storm surge zones, the limits, coverages and deductibles on your fund property coverage document apply subject only to the maximum coverage amount \$7,500,000.

In the TWCARMF property coverage document there is a grant of coverage for flood. The policy states:

*This agreement covers physical loss or damage caused by or resulting from flood except for property located in High Hazard Zones for Flood.*

In the policy flood is defined as:

*Flood; surface waters; rising waters; storm surge, sea surge, wave wash waves; tsunami; tide or tidal water; the release of water, the rising, overflowing or breaking of boundaries of natural or man-made bodies of water; or the spray therefrom; all whether driven by wind or not; or sewer back-up resulting from any of the foregoing; regardless of any other cause or event, whether natural or man-made, contributing concurrently or in any other sequence of loss. Physical loss or damage from Flood associated with a storm or weather disturbance whether or not identified by name by the U.S. National Hurricane Center or any other meteorological authority, such as the Tokyo Typhoon Center or the Central Pacific Hurricane Center, is considered Flood within the terms of the agreement. However, physical damage by fire, explosion or sprinkler leakage resulting from flood is not considered to be loss by flood within the terms and conditions of this agreement*

A High Hazard Zone for Flood is defined as

*Property located in **flood** zones up to and including 100 year zones as shown in the most recent documentation published by the Federal Emergency Management Agency (FEMA), or other qualified and recognized authority in the absence of FEMA. Also includes property where no **flood** zone designation/classification has been established by FEMA or has been classified as a **high hazard flood zone** by the Fund and indicated as Flood Zone A on the **member's** building and contents schedule*

If property is not in a high hazard zone for flood, the coverage applies just as it would for any other kind of loss subject to a maximum amount. In any single year, the maximum amount available to pay for flood losses would be \$7,500,000 for all locations not situated in a 100 year floodplain or storm surge zone. The member's regular property deductible would also apply. The amount and breadth of coverage provided to members by the Texas Water Conservation Association Risk Management Fund is subject to change based on future loss experience, reinsurance provisions and prudent underwriting as determined by the Fund's Board of Trustees.



### ADDITIONAL RESOURCES

The National Flood Insurance Program is accessible through the following website:

<http://www.fema.gov/business/nfip/>

The National Weather Service provides flood inundation maps in some areas through its Advanced Hydrologic Prediction Service. It uses available input from river and stream gauging systems. It can be reached at

<http://water.weather.gov/ahps/inundation.php>

Storm surge models for the Texas coast predict inundation by storms of varying intensities. They are available at

<http://www.wunderground.com/tropical/>

under the "Hurricane Resources" section on the main page.