

BUSINESS AS USUAL

The basic truth about hurricane insurance: [The public pays](#)

by Michael Berryhill
illustration Kiersten Essenpreis

OF ALL THE LESSONS BROUGHT HOME TO TEXAS BY HURRICANE KATRINA, perhaps the most problematic is how to prepare for such a storm financially. The simple answer would seem to be insurance, but as Katrina proved, nothing is simple about hurricane insurance. Still, there is one basic truth: Whether the damage comes from wind or flood, the taxpayers will end up shouldering the cost.

Wind damage in the 13 coastal counties of Texas is handled by the Texas Windstorm Insurance Association. The TWIA estimates it can cover a billion dollars a year in losses through its premiums and reserve funds, but if a major storm hits Harris County and the Port of Houston, the damages would far exceed a billion dollars. Half of the association's 131,000 residential policies are in Galveston County. Under current law, if damages amounted to several billion dollars, the association would assess a fee on all Texas insurance companies to make up the difference. The insurers, in turn, would be exempted from paying state taxes on their premiums, draining an estimated \$450 million annually from the state budget until the benefits are paid.

The Texas Association of Independent Insurance Agents commissioned a study that concluded that if a major hurricane hit the Port of Houston, the economic damage would ripple across the entire state's economy. Consequently, the TIIA proposes that policyholders across the entire state should be assessed a premium fee to provide a cushion. Whether folks in West Texas can be persuaded to pay to insure those in East Texas remains to be seen.

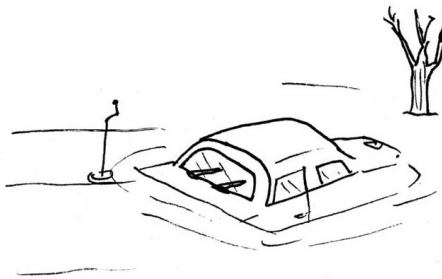
While wind is important, storm surge and rain cause far more damage in most hurricane events. Insurance companies and property owners are still arguing in the courts about whether Katrina did its most virulent damage with wind or water. If their homes were destroyed by water, homeowners without federally subsidized flood insurance are out of luck. And, stunningly, many homeowners in New Orleans didn't buy the relatively cheap flood insurance—so many, in fact, that Gene Taylor, a congressman from Mississippi, introduced a bill to allow the victims of Katrina and Rita to buy flood insurance retroactively.

The congressman can perhaps be forgiven for wanting to turn the basic rules of insurance upside down, because the National Flood Insurance Program defies another basic rule of insurance, which is that the insurer should take in more in premiums than it pays out in benefits. Katrina and Rita combined to hit the federal flood insurance program for roughly \$23 billion. As authorized by law, the program is borrowing from the U.S. Treasury—which is to say the taxpayers—and struggling just to pay the interest on the loans, which amounts to a billion dollars a year. The program takes in an annual premium income of about \$2 billion. Insurance reformers of all political stripes have been calling for reform of the program. House Bill 1682 calls for increasing premiums 10 to 15 percent and would eliminate flood insurance for vacation homes, a provision certain to raise opposition. But no similar bill has been offered in the Senate.

While private insurers have been raising their rates all along the Gulf Coast, it's hard to feel sorry for

them. In Texas last year they scored record profits of 35 percent. Stung by the insurance industry's profits and its insensitive treatment of Katrina victims, some members of Congress are talking about undoing the industry's long-held exemption from antitrust laws.

If flood insurance weren't subsidized by the government, it would probably be too expensive to buy from private insurers, who have all but given up providing it because floods are so hard to predict. The problem with the National Flood Insurance Program, which is administered by the Federal Emergency Management Agency (FEMA), is that makes it seem as though floods are predictable. Created in the 1950s by President Harry S. Truman, whose home state of Missouri was ravaged by river flooding, the program was designed to discourage people from living in floodplain. By mapping floodplains of rivers and streams and making lenders require the purchase of flood insurance by people who were living in floodplains, the legislators hoped to change building patterns. But critics of the program point out that by providing cheap insurance, the federal government has actually encouraged people to develop in areas that are at risk of flooding.



Consider the cost of insuring a modest home valued at \$100,000 on the floodplain near a Texas bay. The cost of homeowner's and windstorm insurance as required by the lender is about \$1,500 a year. The cost of federal flood insurance is \$300 a year. Insurance companies figured out long ago that houses are much more likely to flood than to burn down; that's why they got out of the flood insurance business and have left it to the federal government.

When flood control districts draw up floodplain maps, they create a two-tier system of insurance premiums, creating the illusion for many homeowners that if they don't live in a designated floodplain, they don't need flood insurance. Terms such as "100-year floodplain" create the illusion that a house has one chance in a hundred of being flooded in any given year. The reality, as pointed out in the FEMA Web sites and those of the Harris County Flood Control District, is that during the life of a 30-year mortgage, a home has a 26 percent chance of being flooded. A "500-year flood event" sounds even more unlikely to

happen, but in 1979 Tropical Storm Claudette dumped 43 inches of rain in Alvin, Texas, causing widespread flooding. In 2001 Tropical Storm Allison dropped 38 inches of rain in some parts of Harris County, causing \$5 billion in damage and killing 22 people. About 65 percent of the homes damaged in the two storms were not in the floodplain. Both of these rains would be characterized as "500-year flood events"—but they came 22 years apart. The 500-year event has meaning only if the frequency of such rainfalls could be established over thousands of years.

A hurricane could flood Houston in two ways. A 30-foot storm surge would push water up the Houston Ship Channel as far as the east side of the 610 Loop, and water would likely exceed the floodplain boundaries in all of the recently re-drawn maps. If it were a particularly wet storm, it could also dump 20 inches of rain. The Harris County Flood Control District has modeled stream overflows from rain, and it has modeled storm surges from hurricanes, but significantly, it has not modeled what happens if both events happen at the same time.

After Allison hit, the Harris County Flood Control District redrew the floodplain maps with the latest laser technology. These maps put some new areas in the floodplain and removed others. The total acreage of the floodplain hasn't changed significantly. Homeowners who have been added to the floodplain had until June 18 to "grandfather" their homes into the cheaper insurance rates afforded to those not in the floodplain. That doesn't mean their rates didn't go up, but that they avoided the higher rates paid by those who live in the floodplain.

Mortgage companies require homeowners who live in the floodplain to buy federal flood insurance, but they don't require those outside the floodplain to buy it, even though the odds of being flooded are higher than of being burned out, as previously mentioned. It seems strange that lenders don't routinely require flood insurance. The Harris County Flood Control District and FEMA have conducted elaborate public relations drives to tell people in the Houston area that flooding is capricious, unpredictable, and more possible than they think. The insurance is cheap and is backed by the government. Although Harris County has more than a million residential and commercial structures, only 263,000 policies are in force.

Part of the problem lies in the illusion of safety created by the elaborate mapping and modeling of the floodplain and the use of terms such as "500-hundred-year events" and "100-year floodplain." The communications director of the Harris County Flood Control District, Fred Garcia, puts the problem for Houston much more bluntly: "As far as I'm concerned, we all live in a floodplain." ●