



Date: August 13, 2013

To: LBA Government Relations Council

From: Robert Taylor, CEO
Joe Gendron, Director of Government Relations

Re: Federal Issues Update and Comprehensive Status Report on Flood Insurance

Key Federal Issues

Louisiana bankers deserve better from their government. The LBA and other banking associations around the country have failed to protect the community bank business model from often unnecessary and counterproductive legal and regulatory initiatives. Anti-business policies banks experience themselves and that bankers see with their customers, and frequently misguided “consumer protection” regulations, are strangling many community banks and their customers. Extended low interest rates only add to the challenge of paying for the increased costs of meeting these demands from government and also providing shareholders with value. However, we are working diligently to mitigate these challenges as much as possible, and we believe that we have very strong support to pass legislation from the Louisiana congressional delegation.

The overriding concerns today are regulatory relief for community banking and ending “too-big-to-fail”. There are a large number of regulatory relief measures introduced in the House and Senate all addressing key community bank concerns from QM to privacy notices and many more. Our delegation is ready to support such legislation when they have that opportunity. The key to success is the ability of both parties to work together to achieve legislation they support and not to have an ideological contest between republicans and democrats. There are many in D.C. today who believe it is very possible to have regulatory relief legislation pass this Congress. ***We will continue this focus and ask you to be engaged in our efforts as those opportunities arise.***

Hovering over the financial sector and the economy generally remains the unresolved issue of very large international, systemically connected financial conglomerates that remain a threat to the economy and further, remain a threat for more community bank regulation from the reaction by regulators to their continuing misdeeds and legal entanglements. The next financial crisis, and there will be one, will again result in bailouts of these U.S. based banks if the status quo remains. There is a tremendous amount of literature, commentary and official pronouncements on large bank fragility that addresses this, but this link is one that I pass on: <http://www.nationalaffairs.com/publications/detail/taming-the-megabanks>.

The bottom line is that with “too-big-to-fail” still in existence, the only thing between the taxpayer and/or the FDIC fund to bailout these institutions is loss absorbing tangible capital. The tangible capital position of these institutions is inadequate. Even the federal banking agencies, after promoting Basel III as the answer for years, have finally accepted that higher capital for these large banks is essential as evidenced by their recent proposal. The LBA supports the July 9, 2013 proposal by the OCC, Federal Reserve and FDIC titled “Enhanced Supplementary Leverage Ratio Standards for Certain Bank Holding Companies and their Subsidiary Insured Depository Institutions”. This proposal is extremely significant in that it is an admission by U.S. bank regulators that the Basel III protocol they have promoted is inadequate and dangerous. The proposal itself contains this startling admission: ***“A perception continues to exist in the markets that some companies remain ‘too-big-to-fail’, posing an ongoing threat to the financial system. First, the existence of the ‘too-big-to-fail’ problem reduces the incentives of shareholders, creditors and counterparties of these companies to discipline excessive risk-taking by the companies. Second, it produces competitive distortions because companies perceived as ‘too-big-to-fail’ can often fund themselves at a lower cost than other companies. This distortion is unfair to smaller companies, damaging to fair competition and tends to artificially encourage further consolidation and concentration in the financial system.”*** This is a sea change in regulator attitude. We applaud this development and encourage further steps to mitigate the threat of further taxpayer bailouts.

Our continuing push for credit union taxation goes unabated. [Click here](#) for the LBA press release of July 30, 2013. [Click here](#) to view the July 16, 2013 letter to Louisiana's congressional delegation on taxing credit unions.

Flood Insurance Issue Remains Major Focus for LBA

As we have frequently reported on in recent months, the Biggert-Waters Flood Insurance Reform Act of 2012 passed by Congress will drastically increase flood insurance premiums for many Louisiana home and business owners (as well as for many others around the country). The premium increases, mandated by the Biggert-Waters Act, are intended to bring NFIP premiums up to actuarial rates and make the program financially sustainable. We have been working with our Louisiana congressional delegation and stakeholders in an attempt to minimize the impact of Biggert-Waters, but much work remains. This memorandum describes what is being done in an attempt to mitigate Biggert-Waters, and our current understanding of what is scheduled to take place if Biggert-Waters is unchanged. Keep in mind that this report is based on the many conversations we have had with congressional staffers, other stakeholders, and limited Q&A with FEMA staff. We have been communicating most frequently with Sen. Landrieu's staff, and they are attempting to get much of the information reported below in writing from FEMA. Getting the information in writing from FEMA is important because at times different FEMA staffers have told congressional staffers different things. With that caveat, below is the best information we have at this time.

Last month Sen. Mary Landrieu successfully added a provision to the 2014 Homeland Security Appropriations bill that would delay certain National Flood Insurance Program (NFIP) premium hikes on “grandfathered” properties for a year. Sen. Landrieu's delay language is a positive step, but it still must pass the full Senate. In June, Congressman Bill Cassidy, working with other Louisiana House Members,

passed a companion provision in the full House. It must be emphasized that the Landrieu-Cassidy delay language would only apply to “grandfathered” properties. In simple terms, “grandfathered” properties are those that were originally outside a flood zone and were later included in a flood zone, or those that were originally in a lower-risk flood zone and subsequently moved to a higher-risk flood zone.

Specifically, the Landrieu-Cassidy amendment language ensures that no funds within Fiscal Year 2014 Homeland Security Appropriations will be used to implement what is commonly known as Section 207 of the Biggert-Waters Act. Section 207 ends current “grandfathered” NFIP rates for policyholders who, through no fault of their own, find themselves below “Base Flood Elevation” requirements of Flood Insurance Rate Maps (FIRMs) issued after their compliance with previous FEMA issued FIRMs. Even without the delay of Section 207, we are told that FEMA is not expected to be ready to implement Section 207 until late 2014. If the one-year delay is achieved by the Landrieu-Cassidy amendment, we are told the implementation of Section 207 would be pushed back until late 2015. Whenever Section 207 is implemented, it will result in dramatic flood insurance premium increases for those with “grandfathered” properties. Section 207 uses a five-year mechanism to phase-in rates, and we are told the increases will be 20% per year based upon the difference between the policyholder’s current premium and the full-risk or actuarially sound premium. Therefore, if the current premium for the grandfathered policyholder is \$500 and the full-risk premium is \$5,000, the premium increase for each year will be \$900 (20% of \$4500). Again, this formula results in the full-risk premium amount being reached in five years. We are told by congressional staffers that FEMA has been unable to provide a figure on how many “grandfathered” policies exist in Louisiana. The estimates we have received vary tremendously in range from around 32,570 policies on the low-end to 229,796 policies on the high-end. We are told “grandfathered” policies apply to both residential and business properties, but the great majority of those policies are applicable to residences.

Although the prospect of implementation of Section 207 is extremely concerning, the more immediate concern has to do with Section 205 of the Biggert-Waters Act. Section 205 deals with “subsidized” policies, which include primary residences, non-primary residences, and businesses. There are approximately 82,000 “subsidized” policies out of approximately 486,500 total flood insurance policies in Louisiana according to FEMA statistics as of December 31, 2012. The term “subsidized” in FEMA speak means properties that were built before a community adopted its first FIRM. We are told in general that FIRMs were first adopted in the late 1970s in Louisiana. We are working to get more accurate data as to when each parish adopted its first FIRM.

Beginning in October of this year, “subsidized” business properties in Special Flood Hazard Areas and Severe Repetitive Loss properties will see 25 percent yearly increases in flood insurance premiums until the full-risk premium is reached. We are told that “subsidized” non-primary residences in Special Flood Hazard Areas such as vacation homes and camps have already been subject to these increases since the beginning of this year. Altogether, about 18,000 policies in Louisiana will be impacted by these immediate 25 percent per year increases according to FEMA statistics. In contrast to the rate increases for Section 207, we are told the 25 percent per year increases under Section 205 will be based on the current premium being paid by the policyholder. Therefore, if the policyholder’s current premium is

\$500, their premium for the first year after Section 205 takes effect will be \$625. This 25% increase over the current year's premium will occur every year until the full-risk premium amount is reached.

Our understanding at this time is that "subsidized" primary residences in Special Flood Hazard Areas that were insured with a flood insurance policy as of the date of enactment of Biggert-Waters (**July 6, 2012**) will retain their subsidized flood insurance rates and not be subject to the immediate 25 percent per year increases beginning in October. However, when those properties are sold, or when the current flood insurance policy lapses (owner decides not to renew), the current subsidized rate will be immediately lost for any new policies. This means that buyers (and potentially lenders) of these properties will be required to pay the full-risk premium or actuarially sound amount upon purchase of the new flood insurance policy.

FEMA staff has also verbally confirmed to us that "subsidized" policies covering primary residences in Special Flood Hazard Areas that were purchased after July 6, 2012 will be subject to the full-risk premium or actuarially sound amount when their flood insurance policy is renewed after October of this year.

FEMA staff has verbally confirmed that all rate increases under Sections 205 and 207 will take place upon renewal of the policy. Therefore, although Section 205 takes effect in October, the actual premium increase on a policy will not occur until that policy is renewed.

Again, we are communicating with congressional staffers and FEMA staff and hope to get written responses from FEMA on these particulars. We also are seeking accurate information on the number of "subsidized policies" by parish. We will report more when we know more.

Obviously Section 205 is extremely concerning and will have a dramatic impact on the ability of some home and business owners to sell their properties, along with increased difficulty in continuing to pay their increased flood insurance premiums. Again, we stress that the Landrieu-Cassidy amendment language only provides a delay on premium increases for "grandfathered" flood insurance policies (Section 207), and the delay will not apply to "subsidized" policies (Section 205). Click here to see additional information from FEMA on Sections 205 and 207 of the Biggert-Waters Act. Click here to see a breakdown of the impact of Section 205 on Louisiana flood insurance policies.

In addition to potential legislative fixes, other strong efforts are being made to mitigate the impact of Biggert-Waters. Our congressional delegation has been extremely vocal in calling on FEMA to recognize unaccredited levees (less than 100 year flood protection) and other local flood mitigation elements (such as pumps) when issuing new Flood Insurance Rate Maps (FIRMs). Currently, if a levee only offers 50-year protection, the property protected by this levee is considered as having no protection. However, it recently was announced that five parishes in Louisiana have been approved by FEMA for pilot projects, including Plaquemines, St. Charles, St. Tammany, Lafourche, and Terrebonne Parishes. These pilot projects are designed for FEMA to apply its updated procedures for analyzing and mapping flood hazards in the vicinity of non-accredited levee systems. The new procedures are commonly referred to as Levee Analysis and Mapping Procedures (LAMP), and the hope is that these new

procedures will result in a more realistic depiction of flood risks after accounting for local flood protection features. Ultimately, this should lower flood insurance premiums for affected policyholders.

In other developments, David Miller, head of the National Flood Insurance Program, and FEMA staffers visited South Louisiana on August 8. LBA took part in that visit, along with members of our congressional delegation and other interested stakeholders. We think the trip was helpful in further impressing upon Mr. Miller and other FEMA officials the uniqueness of our coast, as many in attendance stressed that Louisiana is a working coast, unlike many of the beachfront communities that are covered by the flood insurance program. Those in attendance also did a good job of explaining the consequences to Louisiana citizens and communities, and the National Flood Insurance Program itself, if changes are not made.

Also of interest, Sens. Vitter and Landrieu sent a letter to President Obama on July 29 urging him not to nominate FEMA Administrator Craig Fugate to the post of Secretary of Homeland Security until the flood insurance challenges are addressed. Rumors have recently surfaced that Fugate would be nominated to replace Janet Napolitano as Secretary of the Department of Homeland Security. Related to this, during the August 8 meeting with David Miller, Sen. Vitter stated that Mr. Fugate (Mr. Miller's boss) will be called before the Senate Banking Committee next month to discuss these flood insurance issues, and that three questions will be asked of him: (1) Will he delay the implementation of Biggert-Waters because it clearly is not ready for prime-time?; (2) Will he delay the release of new flood maps until locally built levees can be taken into account?; and (3) Will he work with Congress to sort out the issues in the Biggert-Waters legislation?

Finally, various members of our congressional delegation have introduced legislation to make more permanent changes to Biggert-Waters, or to further delay the enactment of its provisions. We appreciate our delegation's hard work on these bills. However, with such a short window between now and October, it is uncertain whether any of these measures will gain traction in Congress to move through the process. The Landrieu-Cassidy amendment language described earlier appears to be the only thing that is seriously on the table in Congress at this point in time.

Based on the above information, Biggert-Waters presents a number of specific concerns to lenders. The most obvious concern is that some borrowers may be priced out of their home or business and will be forced to try to sell their home or business (if they can) or relinquish the property to their lender. Some properties may become unsellable due to cost prohibitive flood insurance premiums. How will this impact certain lender's mortgage loan portfolios? On a broader scale, how will this impact certain local economies and tax bases?

Also of great concern is a lender's obligation to force place flood insurance coverage. Federal law requires lenders to force place insurance (purchase coverage on the borrower's behalf) in situations where a borrower either does not obtain required flood insurance coverage before closing a loan, or allows flood insurance coverage to lapse after the loan is made. Will lenders be on the hook for exorbitant flood insurance premiums that their borrowers cannot afford to repay?

The above examples are illustrative of the many consequences that property owners and lenders may encounter if more is not done to mitigate the impact of Biggert-Waters. LBA will remain fully engaged on this issue and will continue to work for additional relief with our congressional delegation and a broader coalition of industry groups and local officials.