National Association of REALTORS®

FEMA Risk Rating 2.0

NAR MYTH BUSTER

October 6, 2021

On October 1, 2021, FEMA began implementing a new flood insurance pricing methodology called Risk Rating 2.0: Equity in Action. REALTORS® have been calling for these changes since Congress passed the Biggert-Waters Flood Insurance Reform Act in 2012.

Changes won't take effect for existing policies until April 1, 2022, but many misconceptions about the new rating system are already circulating. This document provides the facts.

MYTH:

Risk Rating 2.0 will lead to higher premiums for most National Flood Insurance Program (NFIP) policyholders.

FACT:

With Risk Rating 2.0, FEMA is updating a 50-year-old rating system to price each home individually – rather than by flood zone – and more accurately using modern insurance industry technologies, standards, and science.

Under Risk Rating 2.0, some NFIP rates will increase while others will decrease, depending on each home's flood risk and replacement value. Without these changes, all rates would continue to climb 18 to 25 percent every year until reaching $63,000 for a $250,000 home under many policies.

Most significantly, Risk Rating 2.0 provides more accurate, science-based rates up front so consumers can make better informed decisions. While the old rating system hid the subsidies, Risk Rating 2.0 tells the truth about the risk and cost to insure a property so people will know *before* they make a decision to buy or build.

MYTH:

Risk Rating 2.0 will lead to unfair premium adjustments.

FACT:

Risk Rating 2.0 will create a more equitable and sustainable flood insurance program by addressing rating disparities. Low-value properties will no longer subsidize high-value properties.

Under the previous system, policyholders with lower-value homes have been paying more than they should, and policyholders with higher-value homes have been paying less than they should. These lower-value homes have some of the highest rates in the NFIP today.

With Risk Rating 2.0, policyholders with lower-value homes will generally see a decrease in their cost of insurance – as FEMA's new methodology accounts for more risk variables and rates each home individually.

And, unlike the current methodology, when a property reaches its full risk rate under Risk Rating 2.0, increases stop.

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MYTH:
Risk Rating 2.0 will change everything about flood insurance.

FACT:
Risk Rating 2.0 maintains the 18 percent cap on annual increases for most rates. It also preserves grandfathered rates, including those for newly mapped and pre-Flood Insurance Rate Maps (FIRM) subsidized homes. Additionally, policyholders can still transfer discounts by assigning their flood insurance policy to the new owner.

MYTH:
FEMA has no basis to raise rates on higher-value properties because they are limited to a maximum of $250,000 for building coverage.

FACT:
Higher-value properties tend to make larger claims to NFIP than lower-value properties. This is what is known in the insurance industry as the "insurance to value" effect, which is why the private insurance market also accounts for replacement cost values in their rate quotes for standard home insurance policies.

For example, if a flood causes only 25 percent damage on a $1 million structure, it will reach the maximum coverage limit payable under the NFIP. Meanwhile, a $100,000 structure will never make a $250,000 claim, even if a flood causes a total loss. Yet, both the $1 million and $100,000 structures can pay the same premium under the old rating system.

Replacement cost value has now been added as a rating factor to ensure properties are insured to value, and lower-value properties are no longer subsidizing higher-value properties.

MYTH:
Risk Rating 2.0 will hurt real estate markets.

FACT:
While NFIP's 50-year-old rating system hid the subsidies, Risk Rating 2.0 provides more accurate and transparent information up front about the true cost of flood insurance.

While some homebuyers may choose to focus their searches on properties that better match their personal flood risk tolerance and price range, others with higher flood risk tolerance and means could make informed decisions to purchase these properties for the amenities they offer, including living close to water in desired communities.

Economic research generally shows that real estate markets are extremely resilient when faced with new flood risk information, including updated flood maps, flood factors on real estate listings, and even major hurricanes. While there may be an initial dip for some properties, property values consistently rebound within a few months and continue to climb annually, while older stock is replaced with newer, higher-value construction. For the most authoritative economic study to date, please see Hino and Burke (2020).

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MYTH:

Risk Rating 2.0 will delay or complicate transactions, as real estate professionals will now have to offer flood insurance or risk assessments.

FACT:

Real estate professionals will continue to be information sources, not flood experts. Like mold, termites, or other property risks clients may ask about, you can share the facts on flood risk and be prepared with list of qualified, trained professionals – NFIP and private market insurance agents, licensed surveyors, and others – who can answer property-specific risk questions.

MYTH:

New flood insurance rates do not match my experience as a real estate professional with certain neighborhoods and properties.

FACT:

To develop Risk Rating 2.0, FEMA collaborated with PhD flood experts and scientists in a multitude of disciplines using the latest technologies, data, and standards. Real estate professionals are strongly encouraged to refer any insurance pricing concerns to licensed professionals or directly to FEMA at NFIPUnderwritingMailbox@fema.dhs.gov to initiate a one- to two-week review process.

If you would like NAR to take a quote to FEMA for review, please provide the property address, current NFIP rate (typically found on a renewal notice), declarations page, elevation certificate (if available), and permission from the homeowner to work with FEMA on the issue.

MYTH:

FEMA created Risk Rating 2.0 without input from stakeholders like NAR.

FACT:

NAR collaborated directly with FEMA in the development of this new methodology. Risk Rating 2.0 is the culmination of thousands of NAR member hours and research dollars.

Following the Biggert-Waters Flood Insurance Reform Act of 2012, NAR formed a member insurance committee to investigate the sudden, excessive rate hikes. NAR convinced Congress to delay the rates for a decade while we hired independent actuaries and worked with FEMA to diagnose the problem and propose solutions.

In creating Risk Rating 2.0, FEMA adopted most of NAR's committee recommendations – making this new methodology a big win for REALTORS® and consumers.