The Star-Ledger

A deluge of misinformation on flood insurance

By: Paul Mulshine - December 02, 2012

When both the tree-hugging Sierra Club and the free-market Cato Institute agree something is a bad idea, you can be pretty sure it's a bad idea. Such an idea is federal flood insurance.

"This is one area we agree with Cato on," said Jeff Tittel of the New Jersey chapter of the Sierra Club. "If market forces actually worked, you wouldn't get people knocking down sand dunes to get better ocean views. They couldn't get insurance."

Mark Calabria of Cato agrees.

"You'd have a lot less incentive to do something dumb if you faced the entire cost of doing something dumb," Calabria said.

Calabria would like the feds to get out of the flood-insurance market, or at the very least reform the program to permit more competition. The first step is to take a realistic look at it.

Ever since Hurricane Sandy tore up the Jersey Shore, we've had to listen to various know-it-alls from places as far afield as California and Canada prove they don't know it all — at least not when it comes to the Jersey Shore. Virtually all of their criticisms center on what they argue is a big federal subsidy that encourages people to build in areas where they could not have gotten private insurance.

Sounds good on the surface. But let us consider that argument in light of the experience of Don Cresitello, a man familiar to many Star-Ledger readers from his many years as the mayor of Morristown.

Several years ago, Cresitello retired to a cottage in Manasquan he bought in 1986. That house was, indeed, built near the ocean, but not because of the federal flood insurance program. It was built around 1910 and the insurance program didn't begin until 1968. Most of the Manasquan beachfront was already built up by then.

As for subsidies, Cresitello doesn't feel like he's getting any bargain. His premium is $3,800 a year, but payouts in the federal program are capped at $250,000. He's having a hard time finding out whether he'll collect even that amount to rebuild his house, which was hit hard in the storm.

"I think I paid premiums close to $75,000 for $250,00 worth of insurance that I might not even get," said Cresitello. "I don’t know if I’m sponging off anyone."

Calabria agreed with Cresitello. He turns the argument of the know-it-alls on its head:

"I think a lot of people are paying an actuarially fair rate," he said. "I think that if the federal government was not offering a flood policy, then the insurance companies would offer a policy."

And that policy could cover all claims, not just flooding. That would mean the adjusters would not have to split hairs, as they now do, on the issue of whether damage was caused by wind or water.

When the federal program began in 1968, he said, there were no accurate flood maps. It was difficult to set premiums. But with current flood-plain maps, the risks can be estimated quite precisely, he said.

That’s proved by the fact that many insurers already write flood policies to cover damage above the current $250,000 level, he said. Why don’t they write policies under that level? Because the feds let them keep a third of the premiums for enrolling people in the government program.

"Why should they offer their own insurance when they can already make a lot of money without taking any risk?" he asked.

As for the risks of living at the Shore, they are vastly overrated. Cresitello’s house, for example, stood for about 100 years before it was destroyed in a 100-year storm. Those aren’t bad odds. He’ll have to replace it with a house high up on pilings, further improving his odds.

Meanwhile, homeowners like him have been paying premiums for decades to subsidize people in places such as the Gulf Coast. In the period between 2004 and 2011, for example, Texas got $6.4 billion in premiums. Louisiana got a staggering $32.4 billion. New Jersey got a mere $535 million, mostly for inland areas.

Federal officials haven’t released post-Sandy flood-insurance payout figures, but the New York Times recently estimated New York and New Jersey will collect about $7 billion. If that’s the case, our homeowners will be getting pretty much what they paid for.

So by all means, let’s end that federal program. It was a bad bet, but it finally paid off. Time to walk away from the table.