



NATIONAL ASSOCIATION OF REALTORS®

The Voice For Real Estate®

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STATEMENT OF THE NATIONAL ASSOCIATION OF REALTORS®

For the

**U.S. Senate Committee on Banking, Housing and
Urban Affairs Hearing**

**“An Examination of the Availability and Affordability
of Property and Casualty Insurance in the Gulf Coast
and Other Regions”**

April 11, 2007

Introduction

The National Association of REALTORS® (NAR) appreciates the opportunity to present its views on the availability and affordability of property and casualty insurance in the Gulf Coast and other coastal regions to the Committee on Banking, Housing and Urban Affairs. We thank Chairman Dodd and Ranking Member Shelby for holding this hearing and beginning the discussion to address an issue of concern to homeowners and commercial property owners in the Gulf Coast and other regions of the country.

The National Association of REALTORS® is America's largest trade association, representing more than 1.3 million members involved in all aspects of the residential and commercial real estate business. Ensuring the availability and affordability of property and casualty insurance, therefore, is a top priority for members of NAR.

The storms that hit the Gulf Coast region in 2004 and 2005 have had a significant impact on the availability and affordability of property casualty insurance for homeowners and commercial property owners in the region. These effects have been felt up the Atlantic seaboard as far north as New England. In addition, as other witnesses will testify, the costs associated with the federal recovery efforts from these storms are being borne by taxpayers across the country.

It is for these reasons that NAR strongly encourages the members of this committee and Congress to develop a comprehensive policy that will protect property owners, address insurance availability and affordability, acknowledge the importance and limitations of markets, and recognize the respective responsibilities of property owners and all levels of government.

Overview

The catastrophic events of 2004 and 2005 have shown the need for a comprehensive, forward-looking natural disaster policy. Such a policy would recognize that property owners,

private insurance markets, and all levels of government must work together in order to successfully address the problems (e.g., lack of available and affordable property insurance) currently plaguing disaster-prone areas.

The availability and affordability of property insurance is, at its core, a consumer issue. The importance of available and affordable insurance to homeowners, commercial property owners and those who would like to own their own home or place of business cannot be overstated. Unfortunately, it is also something that consumers nationwide – even those who are not in what have traditionally been considered “disaster-prone” areas – now know all too well.

The National Association of REALTORS[®] believes that any real solution to the insurance problems now facing this country must go beyond a discussion of natural disaster insurance and include a comprehensive natural disaster policy that addresses, but is not limited to, insurance availability and affordability. A comprehensive natural disaster policy also should take into account the responsibilities of multiple actors including property owners, insurance companies and each of the different levels of government in preparing and paying for future catastrophic events. Consequently, although this hearing is titled “An Examination of the Availability and Affordability of Property and Casualty Insurance in the Gulf Coast and Other Regions,” our statement offers suggestions for what REALTORS[®] believe should be included in a comprehensive approach to addressing future catastrophic natural disasters.

Residential and Commercial Properties at Risk

A strong real estate market is the linchpin of a healthy economy, generating jobs, wages, tax revenues and a demand for goods and services. In order to maintain a strong economy, the vitality of residential and commercial real estate must be safeguarded.

Today, insurance availability and affordability concerns are not limited to the Gulf Coast region. We have heard from REALTORS[®] in numerous states, including New York, New

Jersey, South Carolina and North Carolina, expressing concerns about the availability and affordability of property insurance. Their insurance concerns extend beyond homeowners' insurance and include multifamily rental housing and commercial property casualty insurance.

Insurance is a key component to financing the purchase of real estate. Without property casualty insurance, lenders will not lend; without insurance, borrowers are typically in default of their mortgage terms. The limited availability and high cost of insurance, therefore, not only threatens the ability of current property owners to hold onto their properties, but also to slow the rate of housing and commercial investment in these communities. Either of these threats could, in turn, further delay the rebuilding of communities on our storm-ravaged coasts.

The inability to obtain affordable insurance is a serious threat to the residential real estate market, impacting not only single family detached homes, but condominiums, co-operatives and rental units as well. New home purchases, resale transactions and housing affordability are affected in the following ways:

- **Homeowners' insurance is a necessary component in securing a mortgage and buying and selling a home.** If a potential homebuyer is unable to obtain or afford the required insurance, the sale will not be completed. As a result, potential homebuyers are excluded from the market.
- **The cost of owning a home is directly tied to insurance costs.** Homeowners are required by their mortgage lenders to maintain homeowners insurance, regardless of its cost. If the homeowner is unable to afford the cost of that insurance, the mortgage is in default and the lender may foreclose. If disaster insurance coverage is required, potential buyers may choose not to purchase a home because the insurance they need is too expensive. If disaster coverage is optional but expensive, owners may choose to go unprotected.
- **Insurance costs impact rent levels.** Insurance costs incurred by multi-family property owners are ultimately passed on to tenants through higher rents. This impacts housing affordability, particularly for low-income renters.

Many of NAR's commercial members in the Gulf Coast and coastal regions have also reported problems with commercial insurance availability and affordability. Members have experienced large increases in premiums-- in some cases more than four-fold with concurrent increases in deductibles and decreases in coverage -- and in some cases, a complete lack of availability. These changes put the property owner at greater financial risk to recover from losses, while also affecting property values since dramatic insurance increases often cannot be passed on to tenants. For example, in the multifamily housing sector, the ability to pass on increased insurance costs in the form of higher rent is often limited by market conditions, rent stabilization laws and strict limits imposed on federally subsidized landlords. The commercial property owner faces similar problems because leases may cover more than one year and may include limitations on the amount of expenses that may be passed on to the tenant. Thus, when insurance costs rise from \$0.10 to \$0.50 cents per square foot, the landlord must absorb most of the increased costs.

Often it is the smaller property owner that suffers the greatest. Small owners cannot offset the increases in insurance costs for one property with lower insurance costs in other parts of the country; nor are they able to negotiate a lower multiple property rate. In commercial real estate, there is a point at which insurance becomes unaffordable -- when insurance expenses are so high that the property no longer generates sufficient income to cover expenses. This problem forces many owners to sell their property.

Catastrophic Natural Disasters are a National Issue

The catastrophic events of 2004 and 2005 should serve as a wake up call that highlights not only the importance of having insurance, but also that individual property owners, insurance companies, all levels of government, and taxpayers have a role in preparing for and recovering

from future catastrophic events. The ongoing recovery from these storms shows that all taxpayers in the country have a stake in a federal natural disaster policy because their tax dollars are funding recovery efforts.

As a result of the 2004 and 2005 hurricanes, attention has focused on Florida and the Gulf Coast states, but other areas of the country are also susceptible to large-scale natural disasters. Damage caused by any of the following events could be as great as, if not greater than, that caused by Hurricane Katrina: a repeat of the 1906 San Francisco earthquake, another 1938 “Long Island Express” hurricane, or a significant seismic event along the New Madrid fault, which extends from northeast Arkansas, through southeast Missouri, western Tennessee, western Kentucky to southern Illinois. While it is true that not all areas of the country are susceptible to the large-scale disaster scenarios above, the effects of these disasters certainly would be felt by all taxpayers.

Elements of a Comprehensive Natural Disaster Policy

The National Association of REALTORS® encourages Congress to develop a comprehensive natural disaster policy that encourages personal responsibility, promotes mitigation measures, ensures insurance availability, and strengthens critical infrastructure (e.g., levees, dams, bridges, etc.). NAR supports the creation of a federal natural disaster policy that will promote available and affordable homeowners' insurance in disaster-prone areas.

NAR supports the creation of a federal policy to address catastrophic natural disasters that:

- 1) Protects property owners by ensuring that transparent and comprehensive insurance coverage is available and affordable, with premiums being reflective of the risk involved;
- 2) Acknowledges the importance of personal responsibility of those living in high-risk areas to undertake mitigation measures, including the purchase of adequate insurance;

- 3) Provides property owners adequate incentives to undertake mitigation measures where and when appropriate;
- 4) Acknowledges the importance of building codes and smart land use decisions while also emphasizing that proper enforcement of both is best left in the hands of state and local governments;
- 5) Recognizes the role of States as the appropriate regulators of property insurance markets while identifying the proper role of federal government intervention in cases of mega-catastrophes; and
- 6) Reinforces the proper role of all levels of government for investing in and maintaining critical infrastructure including levees, dams, and bridges.

NAR believes that now is the time for Congress to address a comprehensive natural disaster policy that includes natural disaster insurance. The lack of a national natural disaster policy has had a measurable direct impact on the availability and affordability of property casualty insurance in many parts of the country. The inability to obtain affordable homeowners' insurance is a serious threat to the residential real estate market – and thus, our economy.

Homeowners and commercial property owners need insurance to protect themselves, their families and their property in case of catastrophe. However, if insurance is not available or affordable, many make the unfortunate, but understandable, decision to purchase only the minimal amount or type of insurance required. This is precisely the decision many Californians have made - buying the required property casualty coverage but foregoing earthquake insurance due to its high cost. The problem with this rational economic decision is that if “the big one” hits, and people are not insured for that type of catastrophe, then the American Taxpayer, that is to say everyone in the country, will pay. NAR believes that people who bear risk should pay a fair share – by obtaining and maintaining adequate insurance coverage.

Property owners should have confidence that their homes and businesses will survive future catastrophic events. Appropriate mitigation measures can help to create that confidence. Federal and state governments can provide incentives (e.g., tax credits, insurance rate reductions)

to property owners to undertake appropriate mitigation measures for their homes and businesses. Research conducted by the Multihazard Mitigation Council of the National Institute of Building Sciences found that a dollar spent on mitigation saves society an average of four dollars.¹

States are the appropriate regulators of property insurance markets, but there is a proper role for the federal government in addressing mega-catastrophes. Some disasters are just too large or unpredictable for the private market to deal effectively with the resulting damage. At some level, there may be an appropriate role for the federal government to intervene in insurance markets to prevent market disruption and insolvencies among insurance companies. The level of intervention, however, must be set at a level that will not interfere with normal market forces. The difficulty lies in determining the level at which such intervention would be appropriate

Finally, an essential part of a comprehensive natural disaster policy is the recognition of the basic responsibility of government at all levels to build and maintain infrastructure.

Hurricane Katrina was not the largest hurricane to ever hit the Gulf Coast, but the failure of the levees protecting New Orleans contributed significantly to the loss of life and property from that storm. USA Today reported on January 29, 2007, “The Army Corps of Engineers has identified 146 levees nationwide [including five in Connecticut] that it says pose an unacceptable risk of failing in a major flood.”² Last year, the city of Hartford, Connecticut spent \$5 million to repair levees to protect thousands of properties worth approximately \$2 billion – properties that otherwise would have been required to purchase flood insurance.³ The cost of maintaining levees can prove very costly, but is a relative bargain when compared to the potential loss of life and property as shown by the failure of the levees in New Orleans. Moving forward, NAR

¹ Multihazard Mitigation Council, “Natural Hazard Mitigation Saves: An Independent Study to Assess the Future Savings from Mitigation Activities, Volume 1 – Findings, Conclusions and Recommendations,” National Institute of Building Sciences, Washington, D.C. (2005), p.5.

² Peter Eisler, “146 U.S. Levees May Fail in Flood,” USA Today, January 29, 2007.

³ http://www.usatoday.com/news/nation/2007-01-28-levees_x.htm?POE=NEWISVA

³ Ibid.

believes that all levels of government must do a better job of shouldering their respective responsibilities.

To summarize, NAR believes that it is in the best interests of all Americans to have a comprehensive federal natural disaster policy that includes aggressive mitigation and appropriate assumption of risk so that affordable insurance for homeowners and commercial properties is available. Having a comprehensive natural disaster policy is essential in the coming years. There is no guarantee that 2007 or any future years will be as benign for natural catastrophes as 2006. The question is not whether there will be another Katrina-like event in size and scope of destruction, but when. As we have learned, it is far less costly to prepare ahead of time than to fund recovery efforts.

Proposed Legislative Approaches

Congress has, with varying levels of success, debated and voted on natural disaster legislation since the 1990s. The National Association of REALTORS[®] encourages a healthy and vigorous debate during the 110th Congress that leads to sound and productive legislation. NAR supports the efforts of members of Congress, especially Senators Bill Nelson (D-FL) and Mel Martinez (R-FL), who have introduced and co-sponsored seven bills to address this critical issue.

Legislation introduced in the Senate during the 110th Congress takes different approaches to addressing the natural disaster insurance issue including: allowing insurance companies to accumulate tax-deferred catastrophic reserves (S. 926), allowing homeowners to create catastrophic savings accounts similar to health savings accounts (S. 927), offering mitigation tax credits (S. 930), streamlining regulations for “surplus lines” of insurance (S. 929), creating a federal fund to sell reinsurance to states with catastrophe funds (S. 928), funding hurricane research (S. 931), and creating a bi-partisan commission to study various insurance-related ideas and report back to Congress (S. 292).

NAR encourages the Committee to evaluate carefully each of these approaches and also consider the benefits that would be derived from providing additional funding for infrastructure needs. Mitigation has been proven to save money in the long-run. Ensuring that infrastructure is sound, as shown by the comparison of Hartford and New Orleans above, can also be life-saving. NAR believes that all reasonable proposals should be considered as part of a comprehensive solution to address future catastrophic events. The ultimate result of any legislation should be to ensure that property casualty insurance is available and affordable to homeowners and commercial property owners.

As a first step toward creating a comprehensive natural disaster policy, NAR strongly encourages the Committee to enact legislation to reform the National Flood Insurance Program in order to ensure its long-term viability.

Conclusion

Thank you again for offering the opportunity to present to the Committee the views of the National Association of REALTORS[®] on the need for a comprehensive natural disaster policy. NAR encourages Congress to develop a comprehensive approach to natural disaster preparedness that encourages personal responsibility, promotes mitigation measures, ensures insurance availability, and strengthens critical infrastructure (e.g., levees, dams, bridges, etc.).

Passage of an appropriate comprehensive national disaster policy is a top legislative priority for REALTORS[®] nationwide. We stand ready to work with the members of the Committee on Banking, Housing and Urban Affairs and others in Congress to develop a responsible natural disaster policy that addresses the needs of consumers, the economy and the nation.