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The Voice For Real Estate®

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STATEMENT OF VINCE MALTA ON BEHALF OF THE NATIONAL ASSOCIATION OF REALTORS®

Before the

The Subcommittee on Housing and Community Opportunity of the House Committee on Financial Services

"THE FLOOD INSURANCE REFORM AND MODERNIZATION ACT OF 2007, H.R. 1682"

June 12, 2007

Introduction

Thank you, Chairwoman Waters, Ranking Member Biggert, and Members of the Subcommittee for inviting me to testify here today before the Subcommittee on Housing and Community Opportunity and present the views of the National Association of REALTORS® (NAR) on H.R. 1682, the Flood Insurance Reform and Modernization Act of 2007.

My name is Vince Malta. I am the owner and broker of Malta & Co., Inc, a San Francisco California firm handling real property sales and management of over 300 residential rental units. I am a member of the California Association of REALTORS® and National Association of REALTORS® and have held a number of leadership positions in both associations, including serving as the 2006 President of the California Association of REALTORS® and the 2007 Vice-Chair of the Public Policy Coordinating Committee for the National Association of REALTORS®.

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 industries. NAR is the leading advocate for homeownership, affordable housing and private property rights.

Overview

The National Association of REALTORS® supports the efforts of the Committee on Financial Services to reform the National Flood Insurance Program (NFIP). NAR is concerned, however, that certain provisions of H.R. 1682 could negatively impact housing markets, as well as low- and moderate-income renters, would-be homebuyers, and communities.

The Importance of the National Flood Insurance Program

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 markets must be safeguarded.

The National Flood Insurance Program (NFIP) is a unique partnership between our three levels of government. It enables property owners in participating communities to purchase insurance as a protection against flood losses in exchange for state and community floodplain management regulations that reduce future flood damages. Nearly 20,000 communities throughout the United States and its territories participate in the NFIP and have adopted floodplain management ordinances. In each of these communities, the NFIP makes federally-backed flood insurance available to homeowners, renters, and business owners. As a result of these proactive efforts, federal expenditures for disaster assistance and flood control are reduced.

Since its creation, the National Flood Insurance Program has helped to mitigate the escalating costs of repairing damage to buildings and their contents caused by floods. Buildings constructed in compliance with NFIP building standards suffer approximately 80 percent less damage annually than those not built in compliance. According to FEMA, flood damage is reduced by nearly $1 billion a year as the result of communities implementing sound floodplain management requirements and property owners purchasing flood insurance.

As a necessary first step to providing flood insurance and implementing floodplain management regulations, the NFIP identifies and maps the nation's floodplains. This mapping process provides the data needed to design effective floodplain management programs, actuarially rate flood insurance policies, and create public awareness of what areas are subject to flood hazards.

Created nearly forty years ago, the NFIP performed well until the extreme storm season of 2005. As of August 2006, the NFIP has paid more than $17.3 billion in claims for the 2005 floods.[1] This amount is greater than all claims paid out by the NFIP up to that point in time. In prior years, when losses exceeded the NFIP's ability to pay claims, the program was able to borrow money from the U.S. Treasury and pay it back with interest. The very sizeable flood losses resulting from the 2005 storm season have made people take a closer look at the NFIP.

Understandably, many members of Congress, after voting to increase the NFIP's borrowing authority three times, are seeking to reform the NFIP. The National Association of REALTORS® agrees that, given the importance of the NFIP to communities across the country, it is critical that the program be financially stable and actuarially sound. Congress, FEMA, and industry stakeholders, working together, can make a number of changes to ensure that the NFIP rests on a solid footing well into the future.

While the NFIP can be improved, REALTORS® are concerned that some of the provisions of H.R. 1682 might have undesired impacts on certain segments of the population, neighborhoods and communities. NAR encourages Congress to strike a balance between ensuring the long-term fiscal viability of the NFIP and avoiding changes that may result in market inequities and housing affordability problems.

NAR Views on H.R. 1682, the Flood Insurance Reform and Modernization Act of 2007

The National Association of REALTORS® strongly supports the purposes of H.R. 1682, specifically: 1) protecting the integrity of the NFIP by fully funding existing legal obligations owed policyholders, 2) creating additional incentives for homeowners and communities to

[1] Government Accountability Office, "High-Risk Series: An Update," (January 2007), p. 91.

participate in the NFIP, and 3) increasing homeowners' awareness of flood risks. We have concerns, however, with proposed changes to the mapping program, new notification requirements and the elimination of subsidies for non-residential properties and non-primary residences.

Provisions Supported by NAR

- Increase NFIP Borrowing Authority (Section 11): The NFIP must meet its contractual and legal obligations to policyholders by paying claims for flood damages.

- Increase Available Coverage (Sections 7 and 8): The proposed increases in maximum coverage limits for residential properties, non-residential properties and contents coverage would more accurately reflect increases in property and contents values and provide fuller coverage to policyholders. In addition, providing additional coverage for living expenses, basement improvements, business interruption and replacement cost of contents would help protect homeowners and business owners.

- Address Mitigation and Repetitive Losses (Sections 15, 16 and 17): Repetitive loss properties pose a significant financial burden to the NFIP. 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.[2] We agree that amending the flood mitigation assistance program to allow "demolition and rebuilding" should be included as a mitigation measure. We strongly support funding for mitigation activities for individual repetitive loss properties, and extending the pilot program for mitigation of severe repetitive loss properties.

- Build Public Awareness (Section 18): We fully support provisions to increase awareness of the NFIP and provide information on obtaining coverage. NAR believes having the Government Accountability Office (GAO) examine ways to increase low-income family participation in the NFIP is a first step towards ensuring that a greater percentage of at-risk homeowners and renters are able to protect themselves from future flood losses. We would suggest expanding this analysis to include how best to encourage renters to participate in the NFIP because they too are at risk and eligible to purchase content insurance.

[2] 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.

NAR Concerns Regarding Notification Requirements (Section 9)

While NAR supports efforts to increase the visibility of the NFIP, NAR members believe that the brochure and notification requirements for tenants of buildings located in special flood hazard zones proposed by Section 9 will not achieve the intended goal. In order to build the needed awareness of the NFIP, we believe that a broader public education campaign is in order. This effort should be targeted at owners and tenants since flood waters do not discriminate on the basis of property ownership.

Residential property managers have also indicated that the type of a brochure proposed in Section 9 is most likely to be overlooked amongst rental paperwork and the details of moving. A well-designed public awareness campaign would not suffer from this shortcoming. The addition of yet another disclosure requirement would also subject small property owners to potential liability and impose additional compliance costs. NAR has approached the Federal Emergency Management Agency (FEMA) about developing educational materials that can be used to raise awareness among REALTORS® and their clients about the NFIP.

NAR Concerns with Flood Mapping Provisions (Section 21)

NAR is concerned that the requirement in Section 21 to map the 500-year floodplain as part of FEMA's map modernization program may lead to delays in updating the 100-year floodplain maps, now scheduled to be completed in 2010. Accurate and up-to-date flood maps are the keystone to the NFIP insurance program. Without accurate maps, property owners are not able to properly evaluate the risk to their property from flooding.

FEMA has been engaged in a map modernization program to update and digitize the flood maps for the 100-year floodplain for several years. According to a report by the General Accounting Office submitted to the Chair of this Subcommittee in March 2004, when Congress appropriated funds in FY 2003 to allow FEMA to undertake a full-scale update of the nation's flood maps, FEMA expected the effort to take five years to complete.[3] [4]

NAR does not want to see this process delayed further. Consequently, we are concerned that requiring FEMA to map the 500-year floodplain -- a task much larger than updating the existing 100-year floodplain maps -- may delay completion of the 100-year floodplain map update. NAR believes that the ongoing efforts to update the 100-year floodplain maps should be completed before any effort to map the 500-year floodplain is undertaken.

Technical Mapping Advisory Council Should Include a Real Estate Professional (Section 21)

NAR believes that it is important to have a real estate professional serve on the Technical Mapping Advisory Council when it is reestablished. A real estate professional will be able to provide the perspectives of map users, including homeowners and potential homebuyers, and explain how these maps impact real estate transactions.

NAR Opposes the Phase-Out of Subsidies (Section 4)

The National Association of REALTORS® strongly opposes phasing out subsidies for non-primary residences and non-residential properties. Non-primary residences should be given the same consideration as primary residences. Properties built under the same circumstances and facing identical flooding risks should not be charged different premiums. While proponents of eliminating "subsidies" on non-primary residences and non-residential properties argue that such a change would make the NFIP more fiscally sound, there may be significant unintended

[3] U.S. General Accounting Office, "Flood Map Modernization: Program Strategy Shows Promise, but Challenges Remain," March 2004, p. 8.
[4] Ibid.

consequences for renters, business owners, potential homebuyers, neighborhoods and local economies.

The properties receiving “subsidized” or less-than actuarial rates were built prior to December 31, 1974 or the date of completion of the flood map for the community in which the property is located, whichever date is later. Congress authorized the use of these less-than-actuarial rates because these structures were built prior to adoption of the flood maps and without the knowledge of the flooding risks inherent in the sites.

The original intent of the subsidy was to mitigate the increased costs that the new flood insurance mandate would impose on property holders. It was expected that over the long run, these older buildings would reach the end of their useful life and be replaced by newer flood-resistant construction. In practice, this process takes much longer than was assumed. Meanwhile, the expectation has grown that people who own properties in high-risk areas should pay actuarial rates based on their exposure to risk.

It should also be noted that the use of the terms “subsidies” or “subsidized rates” can be misleading. No federal tax dollars are used to pay for the difference between the “subsidized” and actuarial NFIP insurance rates. The difference between the actuarial and “subsidized” rate is simply not collected. It is important to note that the NFIP’s latest Actuarial Rate Review indicates that the average “subsidized” policyholder pays more into the NFIP systems than do non-subsidized properties, roughly $720 in premiums annually as opposed to the average non-subsidized “actuarially rated” policy premium which pays about $350 per year in flood insurance premiums.

The National Association of REALTORS® is concerned that eliminating subsidies would result in yet higher flood premiums, increase the cost of property ownership and rents in these areas, and could lead to increasing delinquencies, foreclosures and reduced property values. FEMA estimates that if the average subsidized policy were to pay its full-risk premium, that premium would be increased to $1,800 per year, or about two and a half times the current level; some properties could see premiums increase four-fold or more. There is a limit to the amount that insurance, or any other operating expense, can increase before owners are either forced to raise rents, sell their properties, or go without insurance. In the case of residential rental properties, it is especially likely that a significant portion of single-family property owners would be hard pressed to absorb such a cost increase without raising rents.

Presently, under the NFIP, flood insurance is purchased for the structure and/or contents. Section 4 of the bill would change this by adding a condition of use (i.e., primary or non-primary residence) requirement to determine the insurance rate for residential properties. Singling out non-residential and non-primary residences would require an annual certification of the use of the property. This would pose an additional burden on FEMA or some other agency to certify use of the property annually.

NAR also has concerns about how this provision would apply to residential rental properties, or more importantly, renters of these homes. For a renter, the house in which he or she is living is a primary residence, but would be considered a non-primary residence under the bill because it is a non-primary residence of the owner. Thus, if the subsidy was eliminated and owners were unable to cover the additional $1,100 - $2,100 in annual flood insurance costs, tenants would face rent increases that would have a dramatic effect on rental housing affordability, especially in the case of low and fixed-income individuals and families.

Given the uncertainty that exists as to how the elimination of subsidies would impact low and fixed-income residents and communities, NAR believes that the GAO study referenced in

Section 18 of the legislation should be expanded to include such an analysis before any actions are taken to eliminate these long-standing subsidies.

Finally, we would point out that the bill's provisions are unclear as to what happens when a non-primary residence is sold and becomes a primary residence. We would argue that the insurance should revert to its previously subsidized rate. It is also unclear how the phase-in of actuarial rates would affect a subsidized primary residence that is sold in 2015 and became a non-primary residence. Multiply this circumstance by several hundred thousand transactions and this could become a certification nightmare.

The Importance of a Comprehensive Federal Natural Disaster Policy

In addition to reforming the National Flood Insurance Program, the National Association of REALTORS® strongly encourages Congress to develop and enact a comprehensive natural disaster policy to mitigate exposure to the risks of natural disasters and foster the availability and affordability of homeowners' insurance coverage.

The National Association of REALTORS® supports the development of a comprehensive natural disaster policy that encourages personal responsibility, promotes mitigation measures, ensures insurance availability, and strengthens essential infrastructure (e.g., levees, dams, bridges, etc.).

NAR believes the creation of a federal natural disaster policy will promote the availability of affordable homeowners' insurance in disaster-prone areas. 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. 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 through taxpayer-funded disaster assistance.

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.

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. The U.S. Army Corps of Engineers on February 1, 2007, released a list of 122 "Levees of Maintenance Concern" that includes 37 levees in California.[5] Moving forward, we believe that all levels of government must do a better job of shouldering their respective responsibilities.

To summarize, we believe 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 since there is no guarantee that 2007 or any future years will be as benign for natural catastrophes as

[5] *See*: U.S. Army Corps of Engineers, "Levees of Maintenance Concern," Feb. 1, 2007.

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.

Conclusion

Thank you again for inviting the National Association of REALTORS® to present its views on H.R. 1682 to the Subcommittee. We stand ready to work with you, Chairwoman Waters, Ranking Member Biggert, Chairman Frank, and all the members of the Committee on Financial Services and others in Congress to enact meaningful reforms to the National Flood Insurance Program and ensure its long-term viability.