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HEARING BEFORE

THE UNITED STATES HOUSE OF REPRESENTATIVES
COMMITTEE ON FINANCIAL SERVICES
SUBCOMMITTEE ON HOUSING AND COMMUNITY OPPORTUNITY

ENTITLED

"LEGISLATIVE PROPOSALS TO REFORM THE NATIONAL FLOOD INSURANCE PROGRAM"

WRITTEN TESTIMONY OF

MOE VEISSI, 2010 FIRST VICE PRESIDENT

NATIONAL ASSOCIATION OF REALTORS®

APRIL 21, 2010

Introduction

Chairwoman Waters, Ranking Member Capito, and members of the Subcommittee, on behalf of more than 1.2 million REALTORS® who are engaged in all aspects of the residential and commercial real estate industry, thank you for inviting me to testify today regarding legislation to reform the National Flood Insurance Program (NFIP).

My name is Moe Veissi. A REALTOR® for 40 years, I am broker/owner of Veissi & Associates Inc., in Miami, Florida. I have been active within the National Association of REALTORS® (NAR), holding significant positions at both the state and national levels. Since 2002, I have been the President of the Florida Association, an NAR Regional Vice President, and a member of the NAR Board of Directors. Most recently, I was elected NAR First Vice President for 2010.

On March 28, 2010, statutory authority for the NFIP expired. Unable to reconcile differences between the House and Senate flood insurance reform bills, Congress has adopted seven short-term extensions since September 2008 – all within a few days of the deadline (This includes the current extension to May 31). This month-to-month approach hinders a recovering real estate market and creates uncertainty for the more than five and a half million taxpayers who depend on the NFIP as their main source of protection against flooding, the most common natural disaster in the United States. Without flood insurance, federally-backed mortgages may not be secured for residential or commercial real estate transactions in nearly 20,000 communities across the nation. NAR urges Congress to enact at minimum a five-year extension that strengthens the program's fiscal foundation while also avoiding changes that may result in market inequities and housing affordability problems.

The Importance of the National Flood Insurance Program

Congress established the NFIP in 1968 so that property owners would have access to affordable insurance against losses due to flooding. This program represents a unique partnership among property owners, all levels of government, and the private sector, and participation is voluntary for communities. These communities participate by adopting floodplain management ordinances to reduce future flood damage. In return, the NFIP makes federally-backed flood insurance available to property owners and renters in these communities.

The NFIP has effectively reduced the costs of flood damage not only to property owners but also taxpayers. According to the Federal Emergency Management Agency (FEMA), flood damage is reduced by nearly $1 billion a year as the result of communities implementing floodplain management ordinances and property owners purchasing flood insurance. Buildings constructed to NFIP standards experience 80 percent less damage than those not built to standards. By ensuring access to affordable flood insurance, taxpayers pay less for post-disaster relief to flood victims. As a program evaluation finds, the program "has clearly induced savings on flood costs" and that "flood insurance has shifted the loss from taxpayers to those who pay the insurance premium."[1] While the NFIP has been effective at reducing societal costs, flood damage since 2005 has highlighted the need for reforming the program to better protect more people at risk and put the program on a stronger financial footing.

As of January 2009, the NFIP owes $19.2 billion to the U.S. Treasury. This includes $2.6 billion that FEMA had to borrow to pay claims for Hurricane Ike and the Midwest floods of 2008. Prior to 2005, the NFIP had been largely self-supporting, collecting sufficient premiums and fees to cover expenses and claim payments. In the few years when this was not the case, the program was able to pay back the debt with interest. Today however, the program is no longer in that position according to the Congressional Research Service.[2]

NAR Supports Long-Term Reauthorization and Reform

NAR supports at minimum a five-year NFIP reauthorization to provide certainty to a recovering real estate market as well as to the millions of taxpayers that depend on the program for flood insurance. NAR also supports reforms that strengthen the program's financial footing by increasing participation in (and therefore funding for) the program and setting premiums for repetitive loss properties according to their full risk. Though supportive of NFIP reform, REALTORS® would oppose the phase-in of "full risk" premiums for all pre-FIRM properties.[3] NAR encourages Congress to strike a balance between ensuring the NFIP's long-term fiscal viability while avoiding changes that could result in non-risk based market inequities as well as housing affordability problems, especially for lower-income homeowners and renters.

<u>Repetitive Loss Properties</u>. NAR supports establishing premiums for repetitive loss properties according to the full risk posed by such properties to the NFIP. These are properties that have repeatedly suffered insured flood losses and declined a reasonable offer of mitigation funding from FEMA. Though a small percentage of properties covered by the NFIP, such properties receive a disproportionate share of payouts from the program.

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.[4] NAR supports amending the flood mitigation assistance program to allow "demolition and rebuilding" as a mitigation measure. In addition, NAR supports funding for mitigation activities for individual repetitive loss properties, and extending the pilot program for mitigation of severe repetitive loss properties.

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[1] Pacific Institute for Research, "Costs and Consequences of Flooding and the Impact of the National Flood Insurance Program" (October 2006), p. 28 (hereafter, "PIR Study").

[2] Congressional Research Service, "National Flood Insurance Program: Background, Challenges, and Financial Status," (July 2009).

[3] By "Pre-FIRM," we are referring to properties built prior to December 31, 1974 or the date of completion of the flood map for the community in which the property is located.

[4] 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.

Increased Participation**.** Another way to help support the future stability of the NFIP is to encourage participation in the NFIP. Increasing participation would lead to increased funds for the NFIP, help property owners recover from flood losses, and decrease future federal assistance when uninsured properties flood and suffer loss.

Educating consumers would increase participation. Many consumers may not be aware that flood insurance is available to them. Only 50% of homeowners in federally designated flood areas purchase flood insurance.[5] NAR would strongly support provisions for outreach, education and information to consumers about the availability and importance of flood insurance.

Offering additional coverage also would attract new NFIP participants. Increasing the 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. Coverage limits have not been adjusted despite inflation since 1994. In addition, adding coverage for living expenses, basement improvements, business interruption and replacement cost of contents would help increase protection for home- and small-business owners.

NAR Opposes Phasing-in "Full Risk" Premiums for all pre-FIRM Properties

NAR opposes phasing-in "full risk" premiums for non-residential and non-primary residential properties. Similarly we oppose such a phase-in for residential properties based on the sale price. NAR encourages Congress to strike a balance between ensuring the long-term fiscal viability of the NFIP while avoiding changes that could result in market inequities as well as housing affordability problems, especially for lower-income homeowners and renters.

Commercial Properties. Similar properties facing the same risk of loss should not be charged different rates. Both lack access to affordable property insurance in the private market at a time when commercial real estate is struggling with the greatest liquidity crisis since the Great Depression. Often it is the small commercial property owner that suffers the greatest. These are the owners of America's small businesses that are the engine of job creation and innovation and backbone of their local communities. But due to their single location, these owners are not as able to 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 as larger owners might be able to do. For small businesses that own their properties, there is a point at which insurance becomes unaffordable, i.e. when insurance expenses are so high that property no longer generates sufficient income to cover expenses. This problem can force owners to sell their properties. It can also lead to mortgage default and even foreclosure, especially during an uncertain economy when there are little-to-no buyers.

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[5] PIR Study, p. 36.

Residential Properties. NAR also opposes phasing-in "full risk" premiums for pre-FIRM primary or non-primary residences, including those proposals that would focus on properties based on the home's occupancy and/or sales price. Once again, Realtors® believe that properties facing the same risk of loss should not be charged different rates. While we would support increasing rates on properties with repetitive losses and thus a disproportionate share of NFIP payouts, increasing the rate on only some property owners directly or indirectly due to their income or assets would be unprecedented for the NFIP.

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. It should be noted that the use of this term "subsidized" is misleading; Congress authorized a discount for such "pre-FIRM" structures because they were built prior to adoption of the flood maps and without the knowledge of the flooding risks inherent in the sites. Changing the rules in the middle of the game could have been perceived as unfair or even punitive. It was assumed at that time that eventually these older buildings would be replaced by newer flood resistant construction; in practice, this process has taken longer than assumed.

As noted above, NAR would support removing the discount on properties with repeated flood losses, which receive disproportionate payouts from the program. In these cases, the property owner has been notified but declined a reasonable offer of mitigation funding from FEMA. This would not be changing the rules in the middle of the game. However, when the discount is removed either directly or indirectly based on measures such as type of occupancy or the income or assets of its owner, discounts would no longer be based on risk of payout, and NAR would be forced to oppose such a provision.

Eliminating risk-based discounts would increase the cost of home ownership and rents in older communities as well as those that rely on tourism. This could help to contribute to additional rounds of delinquencies, foreclosures and reduced property tax bases in these communities. FEMA estimates that if the average discounted policy were to pay its full premium, that premium would be increased to about two and a half times the current level; some properties could see premiums increase four-fold or more. Again, there is a limit to the amount that insurance, or any other expense, can increase before owners are either forced to sell their properties, or go without insurance.

NAR is also concerned that this type of approach would also apply to multi-family and single-family residential rental properties, and more importantly, the families that rent these properties. For a renter, the apartment or house in which he or she is living is a primary residence, but could be considered either a commercial property or a non-primary residence because it is non-owner-occupied. Thus, if the discount were eliminated and owners were unable to cover the additional 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.

The Congressional Budget Office (CBO) has found no evidence to suggest that the risk-based discount would cover larger or more luxurious structures, whether inland or in a coastal area.[6] Another study on the NFIP found that those in the middle-income brackets were less likely to live in federally designated flood areas than either of those in the highest or lowest income brackets. That study noted that "low income households [defined as $10,000 - $30,000 per year] live in hazardous areas in order to find affordable housing or because they work in water recreation areas and find the least expensive housing nearby."[7]

NAR would also contend that by maintaining a risk-based discount, Congress would not encourage development of "environmentally sensitive" areas. A report released in October 2006 that found "[t]he common belief that the NFIP has stimulated development that increased flood losses is not supported by our findings."[8]

H.R. 1264, the Multiple Peril Insurance Act

Another focus of this hearing is H.R. 1264, "the Multiple Peril Insurance Act" which has been introduced by Rep. Gene Taylor (D-MS). After Hurricane Katrina, property owners with an insurance policy expected to be reimbursed for the full damage suffered. However, insurers declined to cover wind damage under the homeowner's policy if some of the damage was deemed due to flooding, and the NFIP supplement to the policy would only cover flood-related damage. In effect, property owners who had been paying for years for this insurance were caught in the middle of a legal dispute between insurers and the NFIP.

The Multiple Peril Insurance Act would allow homeowners to buy comprehensive insurance and know that hurricane damage would be covered without lengthy legal disputes over how much damage was caused by wind and how much was caused by flooding. Premiums for the wind coverage would be risk-based and actuarially sound. Coverage would be limited. The CBO has scored the bill as budget neutral.

The bill would also reduce future property damage by requiring participating communities to adopt International Building Codes. Windstorm insurance would be available only where the local governments adopt and enforce the International Building Code or equivalent building standards. Thus the bill would not only prevent insurers from shifting liability back to the federal government, it would also save taxpayers money by increasing the number of properties that are mitigated against future wind damage and paid for by insurance premiums rather than post-disaster federal assistance.

The Need for a Comprehensive Natural Disaster Policy

[6] CBO, "Value of Properties in the National Flood Insurance Program," (June 2007), p. 7.

[7] PIR Study, p. 43.

[8] Ibid, p. 41.

In addition to reforming the NFIP, NAR urges Congress to enact a comprehensive, forward-looking natural disaster policy that encourages personal responsibility, promotes mitigation, ensures insurance availability and affordability, and strengthens critical infrastructure.

Without federal government involvement, the private market will not provide access to affordable insurance for a range of natural catastrophe risks, including wind damage. Home- and business owners demand insurance to protect themselves, their families and their property from catastrophe. However, if insurance is not available or affordable, many make the unfortunate, but rational, economic decision to purchase only minimal insurance. If "the big one" hits, and people cannot afford insurance, everyone will pay through taxpayer-funded disaster assistance.

Today, U.S. policy toward natural catastrophe risk is largely reactive rather than proactive, case-by-case rather than comprehensive, and that has to change. The default approach of the federal government has been to wait and respond: wait for the next disaster and then respond by providing financial assistance to the victims. For example, after Hurricanes Katrina, Rita and Wilma struck the southeastern coastline, the federal government paid for much of the cleanup – all with taxpayer dollars. Of the $88 billion obligated to the Gulf Coast states, $26 billion went directly to under-insured property owners according to the General Accountability Office.[9] That is $26 billion that would not have been necessary or paid by taxpayers, including those not living near the U.S. coast, had a proactive federal policy been in place, to make property insurance more widely available and affordable.

As the PIR study referenced earlier shows, proactively addressing disaster risks benefits all. The decidedly proactive approach taken to flooding risks via the NFIP has reduced the costs of damage not only to property owners but also to taxpayers. The program has reduced the cost because participating communities must adopt floodplain management ordinances and building standards that mitigate against future flood losses. By ensuring access to flood insurance, that reduces the amount of post-disaster federal assistance for which taxpayers have to pay. Proactively addressing the risks that other natural hazards create would save taxpayers additional money.

Having a more comprehensive natural disaster policy is essential in the coming years since there is no guarantee that 2010 or any future years will be as benign for natural catastrophes as 2009. Another Katrina-size disaster or Northridge earthquake are not a question of if, 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 the opportunity to share the Realtor® community's views on needed changes to the NFIP. NAR stands ready to work with members of the Committee to develop meaningful reforms to the

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[9] General Accountability Office, "Natural Disasters: Public Policy Options for Changing the Federal Role in Natural Catastrophe Insurance," (November 2007), Figure 3.

NFIP that will help protect property owners and renters prepare for and recover from future losses resulting from floods.