



NATIONAL ASSOCIATION OF REALTORS®

*The Voice For Real Estate®*

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## **STATEMENT OF THE NATIONAL ASSOCIATION OF REALTORS®**

### **The Subcommittee on Oversight and Investigations of the House Committee on Financial Services Hearing**

#### **“Insurance Claims Payment Processes in the Gulf Coast after the 2005 Hurricanes”**

**Wednesday, February 28, 2007**

The NATIONAL ASSOCIATION OF REALTORS<sup>®</sup> (NAR) welcomes the opportunity to present our views on insurance issues at this Subcommittee on Oversight and Investigations hearing. There is much to be learned in the aftermath of Hurricane Katrina, especially the importance of having adequate -- and understandable -- property insurance. NAR believes that Congress should adopt a comprehensive approach to natural disaster planning and preparedness. NAR supports a comprehensive natural disaster policy that will ensure the availability and affordability of property insurance. In addition, natural disaster policy should encourage personal responsibility, promote mitigation measures, and strengthen critical infrastructure (e.g., levees, dams, bridges, etc.).

### **The Need for Insurance**

Events of the past few years have left many homeowners and commercial property owners with inadequate or non-existent insurance coverage. There are a variety of reasons: high cost of insurance, high deductibles, and lack of available insurance products in the competitive marketplace. Recent natural disasters have led a number of insurance companies to cancel policies and pull out of markets because they fear that a significant loss could severely impact them.

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.

The issue of available and affordable insurance in disaster-prone areas is a matter of serious concern to REALTORS<sup>®</sup>. We cannot stress enough that the ultimate victims of this insurance crisis – and let us assure you that in many states in the Southeast, it is a crisis – are

consumers frustrated in their attempt to realize the American Dream of homeownership. The insurance availability and affordability crisis in the Gulf Coast region extends beyond homeowners' insurance and touches virtually every aspect of the real estate market. Many of NAR's commercial members have reported problems obtaining commercial property and casualty insurance during the brokerage of commercial real estate. Insurance is a key component to financing the purchase of real estate. The limited availability of insurance threatens to slow the investment in commercial real estate which could, in turn, further delay the rebuilding of our storm-ravaged coasts.

The inability to obtain affordable homeowners' insurance is a serious threat to the residential real estate market. Not only does it imperil the market for single family detached homes, but condominiums, co-operatives and rental units are affected 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 priced out of the market.
- **Homeowners' insurance is tied directly to the cost of owning a home.** If a homeowner is unable to maintain insurance required by a mortgage lender, the mortgage is in default. If disaster insurance coverage is optional, potential buyers may choose not to purchase a home because the insurance they need is too expensive. Others 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 and buyers.

Many of NAR's commercial members in the gulf coast and coastal regions have reported problems with commercial insurance availability and affordability. Members have experienced large increases in premiums, and in some cases, a complete lack of availability. Our commercial members are involved in all aspects of commercial real estate: property management, commercial leasing, sales brokerage, and general real estate advisory services. They have seen first-hand how the insurance climate has affected local economies and the commercial real estate markets.

Members have seen premiums increase dramatically -- in some cases more than four fold with concurrent increases in deductibles and decreases in coverage. These changes put the property owner at greater financial risk to recover from losses, while also affecting property values. 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 limited by rent stabilization laws and strict limits imposed on federally subsidized landlords. The retail sector faces similar problems because lease arrangements are often negotiated with the tenants. These 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. They cannot offset the increases in insurance costs 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 income. This problem forces many owners to sell their property.

## **The National Flood Insurance Program**

The National Flood Insurance Program (NFIP) is an important program that protects homeowners in flood-prone areas. NAR supports changes to the NFIP that will ensure the long-term viability of the program.

Accurate flood maps are the cornerstone of the NFIP. NAR supports adequate funding of FEMA's map modernization program to ensure that flood maps are updated and maintained. NAR also believes that the federal flood insurance program should impose "full risk" premiums for flood insurance on repetitive loss structures that have repeatedly (i.e., more than two occurrences) suffered insured flood losses and have declined a reasonable offer of mitigation funding from FEMA, except in states which have been granted a federal exemption. Flood maps help communities develop flood management strategies, implement more effective land use and building codes, develop disaster preparedness plans, and incorporate disaster planning into regional economic development strategies. We urge Congress to work with FEMA to update these maps as quickly as possible.

We believe that the mandatory purchase requirement under current law must be enforced. Homeowners with mortgages held by federally-regulated lenders whose homes are located in a special flood hazard area are required to purchase and maintain flood insurance. If a property owner fails to obtain and maintain this coverage, their lender is required to purchase this coverage on their behalf and bill the borrower. FEMA should increase enforcement of this requirement, which would increase premium revenue to the National Flood Insurance Program as well as further reduce the costs of a flood event to the federal government.

Having a viable NFIP is a first step, but more needs to be done.

## **A Comprehensive Natural Disaster Policy**

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

- 1) Protects property owners by ensuring that simple, 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, and provide adequate incentives where appropriate;
- 3) Emphasizes the importance of adequate building codes and smart land use decisions and proper enforcement of both by local and state governments;
- 4) Recognizes the role of States in maintaining a viable insurance marketplace while acknowledging the limitations of the marketplace and identifying the proper role of government intervention in cases of mega-catastrophes; and
- 5) Reinforces the proper role of government to invest in and maintain 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 inability to obtain affordable homeowners' insurance is a serious threat to the residential real estate market – and thus, our economy, in several ways. Because homeowners' insurance is a necessary component in securing a federally-related mortgage, an otherwise creditworthy potential homebuyer who cannot obtain the required insurance is priced out of the market. If an existing homeowner is unable to maintain insurance required by a mortgage lender, the mortgage is in default. In lease situations, insurance costs incurred by landlords are ultimately passed along to tenants in the form of higher rents.

NAR supports the creation of a federal natural disaster program that will prevent future disruptions in insurance markets and promote available and affordable homeowners' insurance in disaster-prone areas.

Congress has, with varying levels of interest, debated and voted on natural disaster policies since the 1990s. In the 109<sup>th</sup> Congress, no one approach emerged as a front-runner. NAR supports the efforts of members of Congress who have introduced and co-sponsored legislation to address this critical issue. We encourage a healthy and vigorous debate during the 110<sup>th</sup> Congress that leads to sound and productive legislation.

The issue for NAR is simple: homeowners and commercial property owners need insurance to protect themselves, their families and their property in case of catastrophe. If insurance is not available or affordable, many may choose to go without insurance – precisely the decision many Californians have made due to the high cost of earthquake insurance. If “the big one” hits, and people are not insured, 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.

It is in the best interests of all Americans to have a comprehensive federal natural disaster policy that includes aggressive mitigation, assumption of risk, and affordable and available insurance for homeowners and commercial property owners. Having a comprehensive natural disaster policy that addresses the concerns of property owners, taxpayers and the proper role for government is essential in the coming years. There is no guarantee that 2007 will be as benign 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. Research has shown that, for every \$1 spent on mitigation, results in a post-event savings of \$4.

This issue is an extremely important one to NAR, REALTORS®, homeowners, commercial property owners, and taxpayers. NAR looks forward to working with the Committee on Financial Services and Members of Congress on this important issue.

Thank you.