Open Access to Condominiums — Often the Most Affordable Homeownership Option — and Make Other Needed Housing Reforms

Congressional Action Needed

On February 2, 2016, the U.S. House of Representatives passed H.R. 3700, followed by the U.S. Senate on July 14, 2016. At this time, no further Congressional action is needed on the issue. The bill awaits signature by the President.

Congressional Actions To Date

- H.R. 3700, introduced by Reps. Luetkemeyer (R-MO) and Cleaver (D-MO) passed the House by a vote of 427–0.
- H.R. 3700 passed the Senate by unanimous consent with the leadership of Senators Menendez (D-NJ) and Scott (R-SC).

What To Tell Your Representatives And Senators

- Thank your Representative for supporting H.R. 3700. The bill passed unanimously by a vote of 427–0.
- Thank your Senator for supporting H.R. 3700.

Issue Background

Many first-time homebuyers turn to condominiums as a more affordable option for homeownership. Condominiums make up about 9 percent of the housing stock, but their share of the FHA portfolio is only 4.1 percent. Current FHA condo lending rules restrict the number of condos available to homebuyers, thus limiting the often most affordable, appropriate choice for many families. Changes to the processing of rural housing loans will improve access for deserving families, and reforms to federally assisted housing programs will ease burdens for landlords and improve access for residents.

H.R. 3700:

- Solves a number of concerns regarding FHA's condo rules:
  - Reduces the FHA condo owner occupancy ratio to 35 percent, unless FHA takes alternative action to reduce the ratio below its current level.
  - Directs FHA to streamline the condo recertification process.
  - Provides more flexibility for mixed use buildings.
  - Mirrors the Federal Housing Finance Agency's (FHFA) rules regarding private transfer fees for FHA condo lending.
- Provides permanent authority for direct endorsement for approved lenders to approve Rural Housing Service (RHS) loans.
- Makes reforms to federally assisted housing programs to streamline the programs.

FHA's Restrictions are Limiting Access to One of the More Affordable Homeownership Options

- Condominiums are often the first step on the housing ladder for first-time homebuyers.
- They also can be the most affordable and desirable option for single people, young families, urban dwellers, and older people looking to downsize.
- Currently less than 10 percent of all condos have FHA approval (according to the Community Associations Institute).

FHA's Condo Rules are Too Restrictive

- Current FHA rules require that no less than 50 percent of condo units are owner occupied. Freddie Mac and Fannie Mae have no such restriction when the home is being purchased as a principal residence, which all FHA borrowers are required to be. Since FHA reviews the financial health and reserves of the property to ensure they meet FHA requirements, owner occupancy ratios should be irrelevant.
- FHA limits commercial space to 25 percent of the property. The popularity of "town center" developments and multi-use properties make many newer building ineligible for FHA. Under the current rules, parking garages count as commercial space and can greatly skew the ratio. FHA does allow waivers, but they are rarely granted.
- FHA prohibits any kind of transfer fee—even those that benefit the homeowner. Freddie Mac's and Fannie Mae's regulator, the Federal Housing Finance Agency, conducted a rule making on this very issue several years ago and determined that transfer fees that benefit the homeowner are acceptable.

Rural Housing Loans Should be Streamlined

- Many rural Americans rely on the 502 Rural Housing Guaranteed Loan Program to provide them with access to affordable mortgage credit.
- These loans are self-funded and budget neutral, meaning the fees paid for borrowers fully pay for the program.
- Today, every guaranteed loan must be individually reviewed by a staffer at the Rural Housing Service. FHA and VA's mortgage insurance programs utilize approved private lenders for direct endorsement.

Federally Assisted Housing Needs Reform

- Easing burdens on federally assisted property owners, managers and housing authorities will improve access to affordable rental housing.
- Nearly all the provisions in the bill have been supported in Congress but haven't become law.

Opposing Viewpoints

- H.R. 3700 passed the House 427–0 with NO OBJECTIONS and the Senate by unanimous consent. No individuals, think tanks, or groups have expressed concern with the legislation.

Tax Policies Supporting Real Estate are Vital to the Economy

Congressional Action Needed

- Congress is very unlikely to pass tax reform in 2016. However, lawmakers and their staffs are now developing tax reform proposals for next year when we will have a new president and possibly a shift in control of the Senate and/or House.
- Now is the time for Members of Congress and their staffs to be reminded how vital the current real estate tax provisions are to the housing market and the economy. Reform ideas that repeal or weaken tax provisions that encourage homeownership must be rejected. We need tax reform, but it must first do no harm.

Congressional Actions To Date

- Though no viable tax reform legislation has been introduced in the current Congress, House and Senate leaders on both sides of the aisle are developing plans to move their vision of tax reform next year, when political conditions are likely to be more favorable.

What To Tell Your Representatives And Senators

- **Mortgage Interest Deduction (MID):** For more than a century, the MID has helped put homeownership within the reach of millions of Americans, strengthening families and society. *Reject tax reform plans that eliminate or marginalize the mortgage interest deduction for primary and second homes, and be wary of proposals that greatly increase the standard deduction. Such plans can covertly cripple the tax benefits of owning a home for most while adding little simplification.*
- **Property Tax Deduction:** Some reform plans would repeal the deduction for state and local taxes, including those for real estate. This idea would not only raise taxes on millions of middle-income Americans, but would also place homeownership beyond the means of many who want to buy their first home. *Say no to tax reform that repeals the property tax deduction.*
- **Like-Kind Exchanges:** For almost 100 years, the Section 1031 provision has encouraged growth by permitting real estate held for investment to be exchanged for property of a like-kind on a tax-deferred basis. Exchanges are essential to the commercial real estate sector and to the economy. If repealed, fewer redevelopment projects will go forward, and fewer jobs will be created. The like-kind exchange provision provides liquidity to an illiquid asset. *Repealing it would harm economic growth and cost jobs.*

Issue Background

While tax reform has little chance of enactment this year, proposals coming forward now from House and Senate tax leaders will likely be the ones in play when political conditions line up in favor of moving tax reform, which could be as soon as next year. Members of Congress need to be reminded *now* that tax change ideas that harm real estate are non-starters.

Housing Tax Incentives Must Be Preserved

- More than 75 percent of homeowners utilize the mortgage interest deduction at some point over the period they own a home.
- For many homeowners, the property taxes deduction is substantial, and one that continues long after a mortgage is paid off.
- The value of both the mortgage interest and property tax deductions is imbedded into house prices. Eliminating the MID alone would cause on average an 11 percent drop in home values; decreasing the deduction, even for a limited group, would compress the value of *all* homes.
- Limiting or removing the tax incentives of homeownership would not only rattle the economy, but would also weaken families, society, and undermine the American Dream.

Like-Kind Exchanges Must Be Retained

- Repealing the like-kind exchange provision would be counterproductive to economic growth and job creation with little gain in revenue.
- Two separate tax reform plans by former tax committee chairmen (Baucus and Camp) proposed the repeal of Section 1031, and the President's budget again this year advocated a major cutback. Members of Congress and their staffs must be educated on the importance of the like-kind exchange provision to their own states and districts.

Opposing/Supporting Viewpoints

- Critics will argue that a simpler tax code with lower rates is better for housing than the current system, and the MID most benefits high-income homeowners who do not need help buying a home. Supporters will respond that 88 percent of all those claiming MID earn less than $200,000, and limiting or repealing current housing tax incentives would hurt the housing sector and unfairly harm homeowners, who already pay 80–90 percent of all federal income tax.
- Critics will argue that deductions for state and local taxes subsidize high taxes and encourage bloated governments. Supporters will say repealing the property tax deduction would unfairly cause double taxation of the same income.
- Some reformers believe eliminating itemized deductions would greatly simplify the tax system. Advocates for home ownership counter that the small reduction in complexity achieved by raising the standard deduction would come at too high a price—the loss of tax incentives for owning a home, and the resultant harm to the housing market and economy.
- Critics argue the like-kind exchange provision is a loophole that exclusively benefits those fortunate enough to own investment property. However, real property advocates such as NAR counter that repeal or cutback of the provision would harm economic growth and job creation.

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Provide Private Flood Insurance Options

Congressional Action Needed

Senate consideration and passage of H.R. 2901, the "Flood Insurance Market Parity and Modernization Act" sponsored by Reps. Dennis Ross (R-FL) and Patrick Murphy (D-FL).

Congressional Actions To Date

- H.R. 2901 passed the House of Representatives by an overwhelming bipartisan vote of 419–0.
- No action to date in the Senate.

What To Tell Your Representatives and Senators

- Thank your Representative for supporting H.R. 2901.
- Urge your Senator to bring up and pass the House bill.

Issue Background

Federal law requires that property owners with federally related mortgages buy and maintain a minimum amount of flood insurance coverage for properties located in Special Flood Hazard Areas. Currently, property owners may not satisfy this "continuous coverage" requirement with some private market alternatives to the National Flood Insurance Program (NFIP). If a policyholder leaves the NFIP for one of these market options, they could jeopardize their grandfathered status and face substantial rate increases should they later return to the NFIP.

H.R. 2901 would:

- Clarify that property owners may satisfy the mandatory purchase requirement with either an NFIP policy or private market coverage that meets state law.
- Ensure that consumers can move freely between the NFIP and private coverage without penalty.
- Preserve the NFIP as a viable choice, keeping homeowners from becoming stranded should private insurance options contract or become more expensive after major floods.
- Maintain important consumer disclosures, as well as Fannie Mae/Freddie Mac's ability to examine the financial solvency of private insurers and protect taxpayers.

Current Law Limits the Flood Insurance Options Available to Property Owners

- Right now, NFIP is the only de facto source of the flood insurance coverage required for properties with federally backed mortgages.
- The private market may be able to offer comparable coverage at lower cost than the NFIP.
- Consumers need options and a competitive market for well-priced flood insurance coverage that meets their individual needs.

Expanding Choice is a Good First Step Toward a Comprehensive Reauthorization of the National Flood Insurance Program

- NFIP is up for reauthorization in 2017.
- This bill is an incremental step in the meantime to offer additional options to property owners.
- A strong NFIP coupled with a consumer-friendly private insurance market will provide property owners with the choices they demand.

Opposing Viewpoints

- Some have expressed concern about the private market "cherry picking" and leaving the NFIP with the most risky policies and less revenue to keep the program solvent over the long term.
- Another concern is the non-admitted or surplus line insurers could offer less coverage than an NFIP policy and expose Fannie Mae/Freddie Mac to risk as the market assumes a greater share of policies.

Supporting Viewpoints

- The bill clarifies that property owners may satisfy the federal mandatory purchase requirement with private flood insurance and will not lose their grandfathered status if they later return to the NFIP.
- Neither the private market nor NFIP debt is likely to balloon due to these bill technical corrections.
- There is already a considerable private market for flood insurance, which according to the data, is not targeting the lowest risk NFIP policies but is offering better coverage at lower cost in high risk zones.
- With or without the bill, that market will continue to grow as long as NFIP continues to set rates that do not reflect the true risk in many parts of the country.
- NAR supports strengthening the long term viability of NFIP but the answer is not to keep properties locked in the program so they can keep cross subsidizing others.
- The best way to strengthen NFIP is to attract voluntary participation through rate reforms and bring down the overall risk through mitigation, and the best place to do it is the 2017 reauthorization bill.
- In the interim, this modest bill could offer immediate rate relief for some policyholders who are being charged too much by the NFIP and assess the private market's ability to offer a competitive product.
- Attached is more detailed point-by-point response to concerns raised.

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Fact Checker
"Flood Insurance Market Parity and Modernization Act"

Some consumer and lender groups are re-raising concerns about the Flood Insurance Market Parity and Modernization Act, HR 2901. These concerns were already the subject of extensive hearings and amendments in the House and focused less on the bill itself and more on hypothetical long-term scenarios involving national flood insurance premiums and debt. NAR addresses specific issues below but in general, we can only speculate about the future. What we know for sure right now is that many in the federal insurance program are paying too much and more than their fair share of the risk. The answer is not to keep these property owners locked in the program so they can keep cross subsidizing others. NAR urges the Senate to immediately take up and pass the House bill HR 2901, as is, in order to offer private market options and short-term rate relief. In the longer term, NAR members believe that the best way to keep risk-based rates affordable is to reduce the overall risk in the system. We also urge the Senate to add a substantial mitigation reform title to next year's reauthorization bill, and NAR stands ready to assist with these efforts in order to reauthorize and strengthen the long-term viability of the program.

Will HR 2901 phase out the National Flood Insurance Program (NFIP)?

- There is no provision in the bill to end the NFIP.
- Under the bill, consumers would be free to purchase private flood coverage without risking their grandfathered status in the NFIP.
- HR 2901 preserves the NFIP as a viable option for those who decide to leave the program for comparable, lower cost coverage in the private market.
- The bill clarifies that private flood insurance satisfies federal purchase requirements if it covers at least the amount of the mortgage loan and complies with state insurance laws.
- It creates a safe harbor for lenders who accept private flood insurance meeting both conditions.
- Lenders would have the confidence to accept one of these private plans without being second guessed by federal bureaucrats for duplicative red tape and paperwork.

Why support legislation that allows homeowners to leave the NFIP?

- The goal of the legislation is to give homeowners more choices to find the coverage that is right for them, not to undermine the NFIP.
- We can work on separate legislation to reauthorize and strengthen the long-term viability of the NFIP by including adequate mitigation assistance to those who remain in the program.
- HR 2901 is modest legislation compared with other proposals that do-away with the program entirely.
- The bill is a good down payment toward a more comprehensive set of NFIP reforms but also offers a reasonable alternative to more substantial privatization efforts.
- Because NFIP charges only national average rates, many properties with below average risk are being overcharged across the country.
- Private flood insurance offers a lower cost option for many of these property owners.
- Nothing in federal law now prevents insurance companies from writing private flood insurance, and nothing in the bill would change this.
- More market competition could also spur NFIP to align rates to risk, keeping more property owners within the NFIP and adding policies in low-risk areas.

Will the bill enable "cherry picking" and leave the NFIP in further debt?

- Not according to data from the insurance companies already writing private flood insurance.
- In fact, these companies are targeting high-risk zones, not low-risk zones and offering better coverage at lower cost than NFIP.
- It is true that:
    - These companies wouldn't be writing unless they can charge less than NFIP but enough to cover their costs, including a normal rate of return; and
    - As the private market's share of flood insurance grows, there could be less revenue for NFIP to pay claims from the less than 2% of properties that repeatedly flood.
- It is also true that with or without this bill, the private market's share of flood policies will continue to grow as NFIP subsidies phase out and NFIP rates increase.
- While we must reduce the NFIP's debt, NFIP's debt is not factored into its insurance pricing.

Will the bill allow under-insurance and expose Government Sponsored Enterprises (GSEs)?

- Current law and HR 2901 require lenders to accept private insurance that covers at least the outstanding balance of the mortgage loan – even though that may not be enough to rebuild.
- The bill specifically states:

  "Nothing in this subsection shall be construed to supersede or limit the authority of [GSEs, federal lenders or regulators] to establish requirements relating to the financial strength of private insurance companies … provided that such requirements shall not affect or conflict with any State law, regulation, or procedure concerning the regulation of the business of insurance."
- The bill does streamline the definition of private flood insurance for mandatory purchase compliance; it would no longer reference deductibles or mortgage interest contract clauses.
- The bill does not however amend banking laws or otherwise prohibit GSEs from requiring lenders to be named co-payees on claim payments under those laws.
- Lenders must still comply with all of these banking laws in addition to flood laws.
- All this bill does is change the first law (flood insurance), not the second (banking).
- The flood law is only amended so that it is silent on banking provisions but the banking laws continue to provide broad federal regulatory authority and discretion over GSEs and lenders.
- HR 2901 would not create a conflict between these laws.
- The American Bankers Association supports the House bill as is.

Will the bill weaken consumer insurance protections?

- HR 2901 would require that private flood insurance meet state insurance laws.
- In addition to state regulatory safety net, the bill was amended to include consumer disclosures and allows policyholders to return to the NFIP if there's any issue with a private insurer.
- NAR members believe that property owners can and should make their own decisions about flood insurance.
- States have been regulating insurance for decades, and are in a better position than banks or federal bureaucrats to protect consumers.
- The National Association of Insurance Commissioners has endorsed the bill and testified that current state laws are adequate to protect private flood insurance consumers.