WNCFirst
Insurance Services

September 16, 2009

By Electronic Delivery Only

Office of the Comptroller of the Currency
250 E Street, SW., Mail Stop 2–3
Washington, DC 20219 regs.comments@occ.treas.gov

Regulation Comments, Chief Counsel's Office
Office of Thrift Supervision
1700 G Street, NW.,
Washington, DC 20552
regs.comments@ots.treas.gov

Jennifer J. Johnson, Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue, NW. Washington, DC 20551 regs.comments@federalreserve.gov

Gary K. Van Meter, Deputy Director
Office of Regulatory Policy
Farm Credit Administration
1501 Farm Credit Drive
McLean, VA 22102–5090
regcomm@fca.gov

Robert E. Feldman, Executive Secretary,
Federal Deposit Insurance Corporation
550 17th Street, NW.
Washington, DC 20429
Comments@FDIC.gov

Mary Rupp, Secretary of the Board
National Credit Union Administration
1775 Duke Street
Alexandria, Virginia 22314–3428
regcomments@ncua.gov

RE: Loans in areas having special flood hazards; Interagency questions and answers regarding flood insurance; OCC Docket OCC-2009-0014; FRB Docket No. R-1311; FDIC RIN No. 3064-ZA00; OTS Docket OTS-2009-0005; FCA RIN No. 3052-AC46; NCUA RIN No. 3133-AD41

Ladies and Gentlemen:

Thank you for the opportunity to present our comments regarding the Supplemental Interagency Questions and Answers referenced above. WNC Insurance Services, Inc. is a leading provider of lender-placed and voluntary flood insurance products and services in the United States. Its client base includes more than seven hundred financial institutions nationwide, providing services through eleven offices (sales and business centers) in three time zones. WNC is one of the Top Five US Coverholders at the world's largest insurance market, Lloyd's of London, and maintains long-term relationships with several "A" rated domestic and international insurance carriers.

Our comments below are limited to Question 60 (sending notice prior to policy expiration) and to Question 62 (charging for insurance that covers the 45 day notice period). We will address Question 62 first followed by Question 60. The terms not defined herein have the same meaning as those in the Interagency Questions and Answers.

COMMENTS AND ANALYSIS

I. COMMENTS – Question 62

62. Does a lender or its servicer have the authority to charge a borrower for the cost of insurance coverage during the 45-day notice period?

Answer: No. There is no authority under the Act and Regulation to charge a borrower for a force-placed flood insurance policy until the 45-day notice period has expired. The ability to impose the costs of force placed flood insurance on a borrower commences 45 days after notification to the borrower of a lack of insurance or of inadequate insurance coverage. Therefore, lenders may not charge borrowers for coverage during the 45-day notice period. This holds true regardless of whether the force placed flood insurance is obtained through the NFIP or a private provider.

While we agree that the Act and Regulation grant a borrower 45 days in which to purchase flood insurance when there is a lapse, we strongly argue that the law expressly *permits* charging a borrower for all insurance actually purchased by the lender in compliance with the Act and Regulation, including a policy providing retroactive coverage during the 45 day notice period. Thus, we assert that proposed Question and Answer No. 62 defeats the express goal of the Act and Regulation, which is to compel borrowers to maintain continuous flood coverage, beginning at loan origination, for the term of the loan and at the borrower's expense.

There are three reasons why this is true: (1) each borrower is notified, at loan origination, of the contractual duty to maintain flood insurance for the term of the loan, at the borrower's expense; (2) force-placed insurance is simply a continuation of the borrower's contractual duty to maintain flood insurance for the term of the loan, at the borrower's expense, which was imposed at loan origination; and (3) there is no express prohibition under the Act or Regulation against charging a borrower for insurance that provides retroactive coverage during the 45 day notice period.

Additionally, proposed Question and Answer No. 62 interferes with the contractual relationship between the lender and the borrower, and with the purpose of the Act and Regulation. Two reasons support this: (1) the purpose of the Act and Regulation is to empower lenders, not limit them, and (2) lenders rely on the loan contract to force-place flood, hazard and wind coverage.

Likewise, proposed Question and Answer No. 62 turns the contractual and legal relationship between the lender and the borrower on its head, for two reasons: (1) the Act was passed for the benefit of Congress and lenders, not borrowers, and (2) lenders would now be required to pay for flood insurance to protect borrowers rather than borrowers paying to protect lenders, as required in the loan contract.

Moreover, proposed Question and Answer No. 62 prohibits a lender from compelling a borrower to do what the borrower would do voluntarily – pay for retroactive coverage. This is true because: (1) current practice requires a borrower to pay for retroactive coverage when a borrower voluntarily renews coverage during the first 30 days after expiration; and (2) if the carrier is at fault for the lapsed coverage, a borrower may even be required to purchase a policy with as much as 365 days of retroactive flood coverage.

Finally, under proposed Question and Answer No. 62, reliance upon the Mortgage Clause is misplaced and ill-advised for three reasons: (1) there is no 30 days “free” coverage for normal Expirations, timely Non-Renewals, or end-of-term Cancellations; (2) the only way for a lender to receive coverage after normal policy expiration is for the lender to pay the premium; and (3) claims paid under the Mortgage Clause are paid to the detriment of the borrower.

II. DETAILED ANALYSIS – Question 62

A. Proposed Question and Answer No. 62 defeats the express goal of the Act and Regulation, which is to compel borrowers to maintain continuous flood coverage, beginning at loan origination, for the term of the loan and at the borrower’s expense.

1. Each borrower is notified, at loan origination, of the contractual duty to maintain flood insurance for the term of the loan, at the borrower’s expense.

Any analysis of the mandatory purchase requirements begins with an understanding of its goals. One main goal is to combat coverage lapses created by borrowers.

> A key clarification of the 1994 Reform Act is that flood insurance must be obtained and maintained during the term of the loan. Regulated lending institutions and GSEs are responsible for providing notice of and requiring flood insurance coverage for the term of the loan on buildings located or to be located in any SFHA in participating communities. Flood insurance will be required even if the SFHA designation is first identified after settlement, but during the term of the loan. This requirement is designed to **combat coverage lapses** allowed to occur by individuals who believe they will not be flooded, and therefore discontinue payment of flood insurance premiums during the term of the loan. (FEMA, *Mandatory Purchase of Flood Insurance Guidelines*, August 2008, [“FEMA Guidelines”], p. 5, bold added)

Thus, in order to “combat coverage lapses”, before a designated loan is closed, borrowers are fully informed of their duty to buy flood insurance, and in fact, they must show that they have actually purchased the coverage before the loan may be closed. Both the Act and Regulation require each regulated lender to notify every affected borrower of the duty to maintain flood insurance: (1) for the term of the loan and (2) at the borrower’s expense. (*See*, 42 USCS § 4012a(b)(1), “covered **for the term of the loan** by flood insurance” [bold added]; 12 CFR 339.3, “covered by flood insurance **for the term of the loan**” [bold added]; 42 USCS § 4012a(e)(1), “borrower should obtain, **at the borrower's expense**, an amount of flood insurance . . . **for the term of the loan**”, [bold added]; 12 CFR 339.7, “borrower should obtain flood insurance, **at the borrower's expense** . . . **for the remaining term of the loan**”, [bold added].) Thus, beginning at loan origination, a borrower is fully aware of, and compelled by, the lender to purchase flood insurance, for the term of the loan, at the borrower’s expense. Force-placement does not change this requirement; it merely continues it.

2. **Force-placed insurance is simply a continuation of the borrower's contractual duty imposed at loan origination to maintain flood insurance for the term of the loan, at the borrower's expense.**

Because borrowers are notified at loan origination of the contractual duty to maintain flood insurance for the term of the loan; and at the borrower's expense, when a loan becomes uninsured, the Act and Regulation expressly authorizes a lender to purchase flood insurance, at the borrower's expense. As stated above, this is simply a continuation of the contractual duty that was first imposed by the lender upon the borrower at loan origination. However, to remove any doubt, Congress expressly authorized lenders to charge borrowers for the lapsed coverage.

> The lender ". . . may charge the borrower for the cost of premiums and fees incurred by the lender or servicer for the loan in purchasing the insurance." (42 USCS § 4012a(e)(2))

The above-quoted statute *expressly* permits the lender to charge the borrower for the cost of force-placed insurance. If the goal is continuous flood coverage for the life of the loan, and the expectation is that the borrower would maintain that coverage at the borrower's expense, beginning at loan origination, then it makes perfect sense that Congress would expressly empower lenders to charge borrowers for force-placed coverage. If this were not so, one would expect to see a direct prohibition against the practice, or at least a court decision to the contrary. No such prohibition exists.

3. **There is no express prohibition against charging a borrower for insurance that provides retroactive coverage during the 45 day notice period.**

As stated above, a lender must compel a borrower to provide continuous flood coverage, for the term of the loan, at the borrower's expense. The Act and Regulation each expressly permit a lender to charge a borrower for the flood insurance the lender is compelled to buy due to a borrower's breach of this duty. In the private flood insurance market, lenders are able to purchase insurance coverage that includes retroactive coverage for the 45 day notice period. In fact, private flood insurance products like this help to bring a lender into strict compliance with the Act and Regulation. Nothing in the Act or Regulation expressly prohibits a lender from purchasing this product and charging the borrower for it. Neither Congress nor the courts have prohibited lenders from charging borrowers for retroactive coverage, although it has been the practice in the industry for many years.

If a lender is prohibited from charging borrowers for 45 days worth of insurance, this defeats the obvious and stated goal of the Act and Regulation – that borrowers be compelled to maintain continuous flood insurance for the term of the loan, at the borrower's expense. Either there will be a break in flood coverage or the insurance will not be maintained at the borrower's expense.

B. Proposed Question and Answer No. 62 interferes with the contractual relationship between the lender and the borrower, and with the purpose of the Act and Regulation.

1. **The purpose of the Act and Regulation is to empower lenders, not limit them.**

Federal law does not regulate borrowers; it regulates lenders. A borrower has no duty under the Act or Regulation to purchase flood insurance and cannot be penalized by the government for failing to do so. The duty to maintain continuous flood insurance and the penalty for its breach fall upon the lender not the borrower. (See, e.g. 42 U.S.C. § 4012a; 12 U.S.C. § 1818(i)(2); and 12 C.F.R. 308 and 339.) However, as FEMA has well noted, one purpose of the Act and Regulation is to *empower* a regulated lender to compel a borrower to maintain continuous flood coverage for the life of the loan.

> The 1994 Reform Act also grants statutory **authority** to a lender or servicer to purchase flood insurance for the building and charge a premium to the borrower if the building is in an SFHA.
>
> By enacting this portion of the law, Congress intended lenders to have clear **authority** to force place; under certain circumstances, they are obligated to force place.
> (FEMA Guidelines, p. 40, bold added)

Although the Act and Regulation grant lenders the authority to force place flood insurance, the law certainly does not limit the contractual rights of the lender.

> The 1994 Reform Act requires a lender to carry out the force placement as a matter of law, independent of the contractual provisions of the loan. Force placement is **not limited** to those situations provided for under the mandatory purchase law.
> (FEMA Guidelines, p. 41, bold added)

The purpose of the Act and Regulation is to empower lenders, not limit them. The key way lenders manage their risks is through their loan contracts with the borrower. This is true, not only for flood risks, but hazard and wind damage risks as well.

2. **Lenders rely on the loan contract to force-place flood, hazard and wind coverage.**

The key way lenders manage their risks is through their loan contracts with their borrowers. This is true, not only for flood risks, but hazard and wind damage risks as well. Thus, it makes sense that the purpose of the Act and Regulation is to empower lenders, independent of the contractual provisions of the loan. This is why FEMA Guidelines repeatedly encourages lenders to the minimum requirements of the Act and Regulation through the loan documents.

For example, FEMA recognizes that lenders have the power to force place flood coverage on buildings located outside of a special flood hazard area, if allowed by their loan documents.

> Lenders, on their own initiative, may require the purchase of flood insurance even if a building is located outside an SFHA. A decision to require coverage under such circumstances is not compelled by the statute, but is founded on the contractual relationship between the parties. Lenders have the prerogative to require flood insurance to protect their investments, provided that they have reserved that option in their mortgage loan document.
> (FEMA Guidelines, p. 11)

Likewise, FEMA recognizes that a lender can rely on the hazard clause of a mortgage loan document to force place additional coverage in an underinsured situation.

> In an underinsured situation, when the borrower and/or agent of record refuse to cooperate with the new lender, the loan should not be made. If the loan has already been extended, the lender should exercise recourse as provided under the terms of the loan document.
> (FEMA Guidelines, p. 41)
>
> If a secondary lienholder determines that a first mortgagee has neglected to obtain flood insurance coverage, the secondary lienholder must be assured that coverage is purchased on the entire outstanding loan amount in order to comply with the statutory requirements as well as to protect its priority as to insurance proceeds. Similarly, if the first mortgage has insufficient coverage, the borrower must cure this deficiency by purchasing additional coverage sufficient to protect all outstanding loans. If not, the loan should not be made. Apart from the provisions of the 1973 Act, the lender can rely on the hazard clause of the home equity or second mortgage loan document in requiring coverage in any underinsured situation.
> (FEMA Guidelines, p. 33)

In fact, FEMA encourages a lender to follow the same business practices for flood insurance that the lender uses for hazard insurance, as outlined in the mortgage loan document.

> Lenders should follow the same general business practice in calculating the flood insurance coverage amount on a building as they do in placing other hazard coverage, e.g., homeowners insurance. The terms and conditions of the hazard clause contained in the loan document fully describe the rights and conditions of the parties.
> (FEMA Guidelines, p. 27)

The purpose of the Act and Regulation is to empower lenders, not limit them. One key way a lender manages its risks is through it loan documents. Lenders rely on the hazard clause of their loan documents to force place flood, hazard and wind coverage, without a lapse in coverage, by purchasing retroactive coverage for the "gap" created during the notice letter cycle. Proposed Question and Answer No. 62 interferes with the contractual relationship between the lender and the borrower, and with the purpose of the Act and Regulation by prohibiting lenders from relying on their loan documents to force place flood coverage like they force place hazard and wind coverage. This seems unreasonable and inconsistent with the stated purpose of the law.

C. Proposed Question and Answer No. 62 turns the contractual and legal relationship between the lender and the borrower on its head.

1. The Act was passed for the benefit of Congress and lenders, not borrowers.

As stated above, borrowers are not regulated by federal law; neither the Act nor the Regulation applies to borrowers. Likewise, the Act was not passed for the benefit of the borrowers. (*See, e.g.*, Custer v. Homeside Lending, Inc., 858 So. 2d 233, 245 (Ala. 2003) ["The specific statutes in question were not enacted for the special benefit of the borrowers. . . . This statute seems primarily concerned with protecting lenders, not borrowers."] *quoting*, Hofbauer v. Northwestern National Bank of Rochester, 700 F.2d 1197, 1200 (8th Cir. 1983); *see also*, Norris v. Union Planters Bank, 739 So. 2d 869, 874 (La. Ct. App. 1999); Mid-America National Bank of Chicago v. First Savings & Loan Ass'n of South Holland, 737 F.2d 638, 642-43 (7th Cir. 1984).)

Moreover, because borrowers are neither regulated nor protected by the Act, courts have unanimously held that borrowers have no private right of action against lenders or insurers under the Act. (*See, e.g.,* Wentwood Woodside I LP v GMAC Commer. Mortg. Corp., 419 F3d 310, 323 (5th Cir. 2005) ["Every single federal court to consider whether a federal private right of action arises under section 4012a has concluded that the federal treasury, not individual mortgagors like Wentwood, is the class the statute intends to protect."].) The Act was passed for the benefit of Congress and lenders, not borrowers. Similarly, the flood insurance requirement in the loan contract between the lender and the borrower was included for the benefit of the lender, not the borrower.

2. **Lenders would now be required to pay for flood insurance to protect borrowers rather than borrowers paying to protect lenders, as required in the loan contract.**

By prohibiting lenders from charging borrowers for retroactive flood insurance coverage for the 45 day notice period, proposed Question and Answer 62 turns the contractual and legal relationship between the lender and the borrower on its head. Although purchased and paid for by the lender, retroactive insurance coverage for the 45 day notice period provides an indirect benefit to the borrower, as does any force-placed flood insurance policy. It will pay down the borrower's mortgage or provide funds to repair the property. Unless the lender is allowed to charge the borrower, this is free insurance paid for by the lender, which is exactly opposite of the intent of both the Act and the loan agreement. Under the Act and the loan agreement, the borrower is required to buy flood insurance to protect the lender. Proposed Question and Answer No. 62, forces the lender to buy insurance to protect the borrower, or remain uninsured.

D. Proposed Question and Answer No. 62 prohibits a lender from compelling a borrower to do what the borrower would do voluntarily – pay for retroactive coverage.

1. **Current practice requires a borrower to pay for retroactive coverage when a borrower voluntarily renews coverage during the first 30 days after expiration.**

At loan origination, a borrower is compelled to purchase flood insurance for the term of the loan, at the borrower's expense. When the borrower's policy reaches expiration, all NFIP compliant flood insurance policies contain the following provisions for handling policy renewal.

> **H. Policy Renewal**
>
> **1.** This **policy** will expire at 12:01 a.m. on the last day of the **policy** term.
>
> **2.** We must receive the payment of the appropriate renewal premium within 30 days of the expiration date.
>
> (NFIP, Dwelling Form, p. 12, bold in original)

This is *not* a 30 day "grace" period providing "free" coverage; it is a 30 day compliance period in which renewal will be allowed without a penalty, *if the premium is paid*. If a borrower fails to renew a mandated flood insurance policy in a timely manner before expiration, the borrower may still timely renew the coverage up to 30 days after expiration. However, the renewal policy would provide 30 days retroactive coverage, if the borrower *pays the entire annual premium*.

Thus, for example, if a borrower receives a force-placement notice from a lender, the borrower could either voluntarily purchase a renewal policy for up to 30 days after expiration or allow the lender to force-place the coverage after 45 days. Either way, under current practice, the borrower would pay for retroactive coverage when the insurance was purchased.

By voluntarily paying the premium for the renewal coverage, the policy would issue immediately, but it would be effective as of the expiration date, 30 days earlier. If force-placed, the same would also be true; the coverage would issue immediately, but it would be effective as of the expiration date, 45 days earlier. In either case, the borrower would pay for retroactive coverage.

2. **If the carrier is at fault for the lapsed coverage, a borrower may even be required to purchase a policy with as much as 365 days of retroactive flood coverage.**

The same is also true for flood insurance that was inadvertently allowed to lapse due to the insurer's error in sending out a renewal notice. In that case, the flood coverage could be retroactive for as much as one year.

> **3.** If we find, however, that we did not place your renewal notice into the U.S. Postal Service, or if we did mail it, we made a mistake, e.g., we used an incorrect, incomplete, or illegible address, which delayed its delivery to you before the due date for the renewal premium, then we will follow these procedures:
>
> **a.** If you or your agent notified us, not later than 1 year after the date on which the payment of the renewal premium was due, of nonreceipt of a renewal notice before the due date for the renewal premium, and we determine that the circumstances in the preceding paragraph apply, we will mail a second bill providing a revised due date, which will be 30 days after the date on which the bill is mailed.
>
> **b.** If we do not receive the premium requested in the second bill by the revised due date, then we will not renew the **policy**. In that case, the **policy** will remain an expired **policy** as of the expiration date shown on the **Declarations Page**.
>
> (NFIP, Dwelling Form, p. 12, bold in original)

Thus, for example, if a borrower receives a force-placement notice from a lender, because of a lapse due to the insurer's error, the borrower could either voluntarily purchase a renewal policy for up to 365 days after expiration or allow the lender to force-place the coverage after 45 days. Either way, under current practice, the borrower would pay for retroactive coverage when the insurance was purchased.

By voluntarily paying the premium for the renewal coverage, the policy would issue immediately, but it would be effective as of the expiration date, which could be as much as 365 days earlier because of the insurer's error. If force-placed, the same would also be true; the coverage would issue immediately, but it would be effective as of the expiration date, 45 days earlier. In either case, the borrower would pay for retroactive coverage.

E. Under proposed Question and Answer No. 62, reliance upon the Mortgage Clause is misplaced and ill-advised.

1. There is no 30 days "free" coverage for normal Expirations, timely Non-Renewals, or end-of-term Cancellations.

Under the NFIP Dwelling Form, the Mortgage Clause addresses three scenarios resulting in termination of coverage. (1) Carrier Cancellation – the carrier's termination of coverage before the expiration date (NFIP, Dwelling Form, p. 2), (2) Carrier Non-Renewal – the carrier's refusal to renew coverage for a new policy term, regardless of the insured's willingness to pay the premium or otherwise continue coverage (NFIP, Dwelling Form, p. 11), and (3) Policy Expiration – the natural end of coverage under the terms of the policy. (NFIP, Dwelling Form, p. 12). Each of these events has a separate and distinct meaning within the policy. Each is handled differently under the Mortgage Clause.

Under the Mortgage Clause, a lender is given an additional 30 days of coverage after a cancellation or non-renewal *notice*. Note, the Mortgage Clause is *not* addressing Expiration:

> If we decide to cancel or not renew this policy, it will continue in effect for the benefit of the mortgagee only for 30 days after we notify the mortgagee of the **cancellation or nonrenewal**.
> (NFIP, Dwelling Form, p. 14, bold added)

The key issue is when the notice is sent. The additional 30 days coverage follows the date the notice is given. Thus, when a cancellation notice is given, the lender has thirty days coverage. However, when a non-renewal notice is given, there may not be any additional coverage at all.

Under the NFIP Flood Manual (May 2009), a renewal/expiration notice is not required to be sent 45 days before expiration of the policy. Rather, a non-renewal notice must be sent *at least* five days prior to policy expiration. (NFIP Flood Manual, REN 1, para. C) However, under state insurance law, and typical industry practice, non-renewal notices are sent at least thirty (30) days prior to expiration. The net effect is that there is **no 30 days additional coverage** following expiration when a policy is non-renewed **with a timely non-renewal notice**.

Likewise, when a cancellation notice coincides with the policy expiration date (sent 30 days before policy expiration), the "free" coverage or extension of coverage for 30 days ends at the policy expiration date rather than mid-term. Finally, there is *no* 30 days additional coverage for a simple policy *expiration*, where the borrower fails to renew or fails to pay the renewal premium.

There is *no* 30 "free" coverage for normal Expirations, timely Non-Renewals, or end-of-term Cancellations. Yet, these are the typical cases when force-placement becomes necessary. In fact, the most common case is a borrower's failure to renew or pay the renewal premium.

2. The only way for a lender to receive coverage after normal policy expiration is for the lender to pay the premium.

As state above, the "free" extended coverage for a lender is only available following two limited circumstances – a mid-term cancellation or an untimely non-renewal notice. However, for all other cases, the only way for a lender to receive coverage after a borrower fails to renew or pay the renewal premium is for the lender to pay the premium. This is not a "grace" period providing free coverage; it is a narrow "safety net" to avoid prejudice to the lender. Moreover, it only applies when a timely claim is made during the 30 days following expiration, which is then denied because the borrower failed to pay the premium. Here's how this works.

As stated above, the policy gives a borrower thirty (30) days following the natural expiration of the policy in which to pay the renewal premium without a lapse in coverage. (NFIP, Dwelling Form, p. 12) However, the borrower must pay that premium *before* a loss occurs, otherwise there is no coverage and the borrower's claim will be denied. (See, Brazil v. Giuffrida, 763 F.2d 1072, 1076 (9th Cir. 1985) ["Payment of a premium after an insurance policy has expired due to nonpayment does not serve to effect coverage for a loss sustained during default and prior to payment."]) Nevertheless, under the Mortgage Clause, if the borrower's claim is denied due to non-payment of premium, the lender is still protected, *if the lender pays the premium*.

> **Q. Mortgage Clause**
>
> If we deny your claim, that denial will not apply to a valid claim of the mortgagee, if the mortgagee:
>
> 1. Notifies us of any change in the ownership or occupancy, or substantial change in risk of which the mortgagee is aware;
>
> 2. **Pays any premium due** under this policy on demand if you have neglected to pay the premium; and
>
> 3. Submits a signed, sworn proof of loss within 60 days after receiving notice from us of your failure to do so.
>
> All of the terms of this policy apply to the mortgagee.
> (NFIP, Dwelling Form, p. 14, bold in original)

While this seems like a reasonable "safety net" for the lender, it still requires payment of the annual premium by the lender. This is *not* free coverage. The only way for a lender to receive coverage after normal policy expiration is for the lender to *pay the premium*. Moreover, the lender will be required to pay the full annual premium, not just coverage for thirty days. Additionally, as seen below, the resulting coverage is disastrous for the borrower.

3. Claims paid under the Mortgage Clause are paid to the detriment of the borrower.

Under the Mortgage Clause, any claim denied to the borrower but paid to the lender results in the carrier being subrogated to rights of the lender to charge the borrower for repayment of the claim under the mortgage.

> If we pay the mortgagee for any loss and deny payment to you, we are subrogated to all the rights of the mortgagee granted under the mortgage on the property. Subrogation will not impair the right of the mortgagee to recover the full amount of the mortgagee's claim.
> (NFIP, Dwelling Form, p. 14)

In the case of a partial loss, the lender would be paid, and the lender would likely then pay to repair the property. While the property would be repaired, thus making the lender whole, the carrier would then be subrogated to the rights of the lender to collect from the borrower for the damages. The reason for this result is because the borrower breached the mortgage by failing to insure the property against flood damage, thereby causing the lender to pay for the damages. Of course, because the lender was able to purchase insurance to cover the loss is no credit to the borrower and does not abrogate the borrower's breach of the loan agreement. The net affect is that the borrower is still indebted under the loan, but must pay the carrier back for the claim. (This is precisely the result that would have occurred if the lender had suffered an uninsured loss. The lender would have repaired the property at its own expense and then charged to borrower for the repairs. The presence of insurance does not change this result.)

For a total loss, the detriment to the borrower is worse. In the case of a total loss, the lender's loan would be paid-off and the insurance carrier would be subrogated to the loan. Thus, the borrower's property would not be repaired, but the borrower would still owe the loan debt, but to the carrier, rather than the lender.

Under current practice, this result is avoided. The borrower would be charged for retroactive coverage and the property would be repaired in any case in which the damages were below the NFIP coverage limit. If the total loss exceeded the NFIP limit, the lender would be paid all or part of its loan balance but there would be no subrogation by the carrier.

III. COMMENTS – Question 60

> *60. Can the 45-day notice period be accelerated by sending notice to the borrower prior to the actual date of expiration of flood insurance coverage?*
>
> *Answer:* No. Although a lender or servicer may send a notice warning a borrower that flood insurance on the collateral is about to expire, the Act and Regulation do not allow a lender or its servicer to shorten the 45-day force placement notice period by sending notice to the borrower prior to the actual expiration date of the flood insurance policy. The Act provides that a lender or its servicer must notify a borrower if it determines that the improved real estate collateral's insurance coverage has expired or is less than the amount required for that particular property. 42 U.S.C. 4012a(e). A lender must send the notice upon making a determination that the flood insurance coverage is inadequate or has expired, such as upon receipt of the notice of cancellation or expiration from the insurance provider or as a result of an internal flood policy monitoring system. This notice must allow the borrower 45 days in which to obtain flood insurance.

While we agree that the Act and Regulation grant a borrower 45 days in which to purchase their own flood insurance in response to an impending renewal, we strongly argue that the law expressly *permits* a borrower to be given 45 days notice immediately *prior* to expiration. There are two reasons why this is true: (1) the 45 notice period in the renewal process under the Mortgage Portfolio Protection Program (MPPP) begins prior to expiration; proposed Question and Answer No. 60 declares this practice to be unlawful, and (2) the stated goal of the Act and Regulation is continuous flood insurance coverage, without a lapse; proposed Question and Answer No. 60 defeats this goal.

IV. DETAILED ANALYSIS – Question 60

A. The 45 notice period in the renewal process under the Mortgage Portfolio Protection Program begins *prior* to expiration; proposed Question and Answer No. 60 declares this practice to be unlawful.

The Mortgage Portfolio Protection Program (MPPP) was established by FEMA to assist lenders with bringing mortgage portfolios into compliance with the federal flood insurance requirements. In particular, the MPPP provides force-placed coverage under a process that is designed to be compliant with federal law. When the MPPP policy is about to expire, the program requires the lender to follow a full notification process before the force placed coverage may be renewed.

> The MPPP is an annual policy and, although it cannot be renewed, it can be rewritten each year if the required procedures are followed.
> (FEMA Guidelines, p. 42)
>
> The MPPP policy is a 1-year policy. Any renewal of that policy can occur only following the **full notification process** spelled out in Addendum 2 that must take place between the lender (or its authorized representative) and the insured/mortgagor, when the insured/mortgagor has failed to provide evidence of obtaining a substitute flood insurance policy. (MPPP Guidelines, p. 6, October 1, 2008, bold added)

The MPPP renewal process requires a lender to follow a "full notification process" consisting of a two or three notice-letter cycle which occurs during a 45 day notice period. However, according to FEMA, the 45 day period begins *before* expiration. The MPPP Guidelines describe the renewal process, in pertinent part, as follows:

> When an MPPP policy has been purchased and the expiration date of that policy is approaching the end of its 1-year term, and the insured has not requested or produced a substitute policy of flood insurance, the following notification process will be followed. This process will consist of a total of three (or, at the lender's option, two) renewal MPPP letters. . . .
>
> The first MPPP Renewal/Expiration Notification Letter will be sent to the insured/mortgagor **at least 45 days prior to the renewal/expiration** of the MPPP policy. It will, at a minimum, contain the following messages:
>
> 1. "This letter is to notify you that the flood insurance policy that was required to be purchased on your property about a year ago is about to expire." . . .

> 5. "Failure to respond to this notice **within 45 days** (or by [date]) will result in this policy being renewed, and at rates that are most likely to be much higher than are otherwise available." . . .
>
> The requirement for the second MPPP Renewal/Expiration Notification Letter is optional on the part of the participating WYO company. . . .
>
> The third and final notice will be sent out as part of the renewed MPPP policy. . ..
> (MPPP Guidelines, p. 10-11, Addendum 2, October 1, 2008, bold added)

As can be seen in the MPPP Guidelines, the MPPP policy is renewed *at the termination of the current MPPP policy*. There are only two required notices to the borrower. The first notice is sent *45 days prior to expiration* of the current policy and the second notice is sent *with the renewal policy itself*. Proposed Question and Answer No. 60 forbids the 45-day notice period to begin prior to the actual date of expiration of flood insurance coverage. Thus, proposed Question and Answer No. 60 declares the MPPP renewal process to be unlawful.

B. The stated goal of the Act and Regulation is continuous flood insurance coverage, without a lapse; proposed Question and Answer No. 60 defeats this goal.

In the NFIP Flood Insurance Manual, October 1, 2009, ("NFIP Manual"), it states that the NFIP must issue a notice of expiration not less than 45 days before the expiration of the policy and that the goal is to avoid a lapse in coverage:

> The Standard Flood Insurance Policy is not a continuous policy. Each policy contract expires at 12:01 a.m. on the last day of the policy term. Renewal of an expiring policy establishes a new policy term and new contractual agreement between the policyholder and the Federal Emergency Management Agency. The NFIP must issue a notice of expiration not less than **45 days before the expiration** of the flood insurance policy by first class mail to the owner of the property, the servicer of any loan secured by the property, and (if known) the owner of the loan.
> . . .
> Policy renewal documentation and premium should be submitted to the NFIP in advance of the policy expiration date to ensure there is **no lapse in coverage**.
> (NFIP Manual, REN-1, May 1, 2009)

Contained within the notice of expiration, the 45-day notice warns that payment for a new policy must be received within 30 days of expiration of current policy *to avoid a lapse in coverage*. Here is the text of the notice:

> PROVIDED YOUR PAYMENT IS RECEIVED WITHIN 30 DAYS OF THE EXPIRATION OF YOUR POLICY, IT WILL BE RENEWED **WITHOUT A LAPSE IN COVERAGE**. ANY PAYMENT RECEIVED AFTER THE 30-DAY GRACE PERIOD AND PRIOR TO 90 DAYS WILL STILL RENEW YOUR POLICY; HOWEVER, THERE WILL BE A 30-DAY WAITING PERIOD FOR COVERAGE TO BECOME EFFECTIVE. THE 30-DAY WAITING PERIOD BEGINS THE DAY THE PREMIUM IS RECEIVED.
> (NFIP Manual, REN-5, May 1, 2009, all caps in original, bold added)

Clearly, under the NFIP Standard Flood Insurance Policy and in the NFIP 45-day notice, the goal is continuous coverage, *without any lapse*. While a borrower may allow a policy to lapse, under federal law a lender must maintain continuous flood insurance coverage on its interest in the collateral. A lender who allows a lapse in coverage has violated federal law, which requires that the collateral be protected by flood insurance "for the term of the loan". 42 USC § 4012a(b)(1). Proposed Question and Answer No. 60 defeats the stated goal of the Act and Regulation which is continuous flood insurance coverage, without a lapse.

V. CONCLUSION

WNC Insurance Services, Inc. appreciates the opportunity to present comments regarding the Supplemental Interagency Questions and Answers Nos. 60 & 62. This guidance can provide much needed clarity and direction to lenders, servicers and their vendors as they seek to comply with the mandatory purchase of flood insurance regulations. However, for the reasons discussed above, WNC urges the Agencies to guard against defeating the intent of the Act and Regulation by creating Questions and Answers that frustrate compliance rather than facilitate it.

If you have any questions about these comments, please feel free to contact the undersigned as follows: Phone: (626) 463-6472, Fax: (626) 463-2121, E-Mail: JGray@WNCFirst.com.

Sincerely,

Jordan N. Gray, Esq.
Senior Vice President, Compliance and Legal Affairs
WNC Insurance Services, Inc.