December 1, 2011

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Re: Loans in Areas Having Special Flood Hazards; Interagency Questions and Answers Regarding Flood Insurance; OCC Docket OCC-2011-0024; FRB Docket No. OP-1431; FDIC RIN No. 3064-ZA00; FCA RIN 3052-AC46; NCUA RIN 3133-AD41

Dear Sir or Madam:

The Mortgage Bankers Association[1] appreciates the opportunity to present our comments regarding the three revised questions and answers relating to flood insurance published October 17, 2011. We

[1] The Mortgage Bankers Association (MBA) is the national association representing the real estate finance industry, an industry that employs more than 280,000 people in virtually every community in the country. Headquartered in Washington, D.C., the association works to ensure the continued strength of the nation's residential and commercial real estate markets; to expand homeownership and extend access to affordable housing to all Americans. MBA promotes fair and ethical lending practices and fosters professional excellence among real estate finance employees through a wide range of educational programs and a variety of publications. Its membership of over 2,200 companies includes all elements of real estate finance: mortgage companies, mortgage brokers, commercial banks, thrifts, REITs, Wall Street conduits, life insurance companies and others in the mortgage lending field. For additional information, visit MBA's Web site: www.mortgagebankers.org.

appreciate your attention to this matter, and look forward to your review of our concerns expressed below.

Proposed New Question and Answers

Question 60: When should a lender send the force placement notice to the borrower?

Answer: To ensure that adequate flood insurance coverage is maintained throughout the term of the loan, a lender or its servicer must notify a borrower whenever flood insurance on the collateral has expired or is less than the amount required for the property. The lender must send this notice upon receipt of the notice of cancellation or expiration from the insurance provider or as a result of an internal flood policy monitoring system. Notice is also required when a lender learns that a property requires flood insurance coverage because it is in an (Special Flood Hazard Area) SFHA as a result of a flood map change (which is occurring in many communities as a result of FEMA's map modernization program). To avoid the expiration of insurance, the Agencies recommend that the lender also advise the borrower when flood insurance on the collateral is about to expire.

MBA generally agrees with the revised Answer to Question 60. We note, however, that a borrower may have secured a replacement policy prior to the lender's receipt of notice of cancellation or expiration from the initial insurance provider. We recommend, therefore, that the Answer be modified so that a lender is not required to take action on the receipt of a cancellation or expiration notice, if the lender has evidence that a replacement policy compliant with the law is in place.

Further, we agree that it is preferable to avoid the need to lender place the insurance. However, with regard to the recommendation, we believe that the expiration notice required to be made by the "Director (or its designee)"[2] is the appropriate notification vehicle. We do not believe that an additional notice provided prior to expiration from the lender would add value; moreover, the additional notice may result in confusion due to the timing of such duplicate notices.

For 1-4 family properties, where the loan is not escrowed, it is duplicative for the lender to send a notice in addition to the notice required to be sent by the insurance company. The insurance provider has the most accurate information about upcoming policy renewals and the actual date of expiration. In addition, it may be confusing to the consumer because it is the insured's right to change insurance providers when he or she chooses. The lender would not know if the consumer is in the process of shopping for insurance, and has purposely not made a payment to the original insurance company because he or she is negotiating with a new provider. Finally, on escrowed loans such a notice would be superfluous given that the servicer will pay the policy premium prior to the expiration date.

In summary, while we support the Agencies' concern that the borrower receives notice of policy expiration, we believe that the current mechanism is the most accurate and least burdensome method of notification; we recommend that you strike the final sentence of the Proposed Answer 60.

Question 62: When may a lender or its servicer charge a borrower for the cost of insurance that covers collateral during the 45-day notice period?

[2] 42 U.S.C. § 4104A(c) (2008).

<u>Answer</u>: A lender or its servicer may charge a borrower for insurance coverage for any part of the 45-day notice period in which no adequate borrower-purchased flood insurance coverage is in effect, if the borrower has given the lender or its servicer the express authority to charge the borrower for such coverage as a contractual condition of the loan being made. Any policy that is obtained by a lender or its servicer, the premium of which is charged to the borrower pursuant to a contractual right, should be equivalent in coverage and exclusions to an NFIP policy and cover the interests of both the borrower and the lender.

The Agencies encourage institutions to explain their force-placement policies to borrowers (including their policy on charging for force-placement coverage for the 45-day period and the timing of that charge) and encourage lenders and servicers to escrow flood insurance premiums. Following these recommendations could result in less force placement of flood insurance. Further, Regulation Z requires lenders to establish an escrow account for the payment of property taxes and mortgage-related insurance required by the lender, including flood insurance, for all "higher priced" first-lien mortgage loans.

MBA supports the lender/servicer's right to charge a borrower for lender-placed flood insurance coverage for any part of the 45-day notice period in which no adequate borrower-purchased flood insurance coverage is in effect because it has been cancelled, expired or not renewed, or if the borrower has failed to provide evidence that such coverage is in place. We greatly appreciate the Agencies' consideration of the industry's concerns with the 2009 Proposed Question and Answer and your willingness to reconsider this question.

MBA, however, is concerned with the introduction of additional conditions to the statutory obligation to lender-place insurance and the right to charge the borrower for enforcing the statute. These new conditions do not reflect the law as they appear only to apply if the servicer dates the lender-placed insurance policy to the expiration date of the borrower-purchased policy. For example, this would not apply in other situations where the lender-placed policy creates a 45-day gap.

Express Authority

One of the new conditions required by the proposed Question and Answer is the requirement that lenders or servicers have express authority from the borrower to charge the borrower for lender-placed coverage as a contractual condition of the loan being made. As stated above, this is not a condition imposed by the law. On the contrary, the National Flood Insurance Reform Act of 1994 (NFIRA) mandates lender-placed insurance and grants the right to charge for such insurance, regardless of the loan documents, when the borrower fails to maintain or have sufficient flood insurance. FEMA's Mandatory Purchase of Flood Insurance Guidelines (FEMA's Guidelines) reinforce this position by stating, "the 1994 Act requires a lender to carry out the force placement as a matter of law, independent of the contractual provisions of the loan."[3] A study conducted for FEMA by the American Institutes for Research provides further historical context that supports this view. The study states, "[t]he 1994 Reform Act preempts state laws that limit or prohibit forced placement or *that require a borrower's agreement in order to force place flood insurance*."[4] In effect, the federal mandate overrides not only state law, but any silence in a loan document as to the

[3] *Mandatory Purchase of Flood Insurance Guidelines,* Federal Emergency Management Agency (2007), pg. 41.
[4] Richard J. Tobin & Corinne Calfee, *The National Flood Insurance Program's Mandatory Purchase Requirement: Policies, Processes and Stakeholders*, American Institutes for Research (2005) pg. 49.

servicer's ability to lender place and to recoup the cost of such insurance. Finally, the provision mandating lender-placement of flood insurance and granting the right to charge the borrower for such costs applied to contracts outstanding on or after the date of enactment of the legislation.[5] This protection would logically cover mortgages that were executed prior to 1994 that did not include such express authority since lender-placement was not a condition of the loan.

In addition to our concern regarding older loans, we are concerned with the possible interpretation of this provision on more recent originations. Newer single-family and commercial/multifamily loans include language in their loan contracts allowing them to impose the cost of lender-placed insurance. However, the language differs and may not expressly detail the 45-day period given that such contractual authority is not required by law. For example, the current Fannie Mae/Freddie Mac Single-Family Uniform Instrument states in covenant five, "[i]f Borrower fails to maintain any of the coverages described above, Lender may obtain insurance coverage at Lender's option and Borrower's expense." FHA language in some loans provides that the servicer may lender place insurance and the "Lender may, at any time, collect and hold amounts for Escrow Items in an aggregate amount not to exceed the maximum amount that may be required for Borrower's escrow account under the Real Estate Settlement Procedures amended from time to time (RESPA) …"[6] Although we do not believe the Agencies should move forward with a requirement for "express authority," if the "express authority" condition is left intact, it must be clarified that contractual language described above, including the stated language in Department of Housing and Urban Development (HUD) documents or other comparable language, is sufficient "express authority" to pass-through the charge to the borrower. Requiring more specific contractual language would effectively subsume the entire Question and Answer for existing loans and prohibit the pass-through of costs, despite express authority to do so under NFIRA. Moreover, such policy would certainly ensure gaps in flood insurance coverage. We do not believe that was the Agencies' intent.

In light of our concerns that older loans may not have provisions addressing lender-placed insurance (or the right to charge the borrower) and that newer originations may not be specific as to the 45-day period, we respectfully request that the Agencies remove the "express authority" condition and allow servicers to act under the provisions of NFIRA.

Instead of "express authority," MBA recommends that servicers inform borrowers that the cost of lender-placed insurance will be charged from the expiration date of the borrower-purchased insurance (as suggested by this proposed Question and Answer 62 and by proposed Question and Answer 57). Many servicers already provide such information in their notices. The 45-day notice is the preferred vehicle to address the Agencies' desire for more disclosure because it properly informs the borrower of the costs of insurance, avoids unfairly applying a new standard retroactively to the lending community for performing under the law, and supports the plain language of NFIRA.

Equivalent in Coverage and Exclusions to an NFIP policy

The second condition of Proposed Answer 62 requires that in order to charge the cost of the lender-placed policy to the borrower during the 45-day period, the lender-placed policy must be "equivalent in coverage and exclusions to an NFIP policy." Again, MBA is concerned with imposing a condition on the ability to pass-through the cost of insurance, since NFIRA itself grants the authority to do so without the stated conditions.

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[5] 42 U.S.C. § 4012(e)(4) (1996).
[6] Sample Mortgage, Federal Housing Administration, (2001).

In addition, it is unclear what this terminology means as it varies from terminology in Question and Answer 63 and 64.[7] The Answer to Question 63 provides that "[a] private insurance policy may be an adequate substitute for NFIP insurance if it meets the criteria set forth by FEMA."[8] The FEMA Guidelines state that the private flood insurance policy must be "at least as broad" as the coverage under the NFIP standard flood insurance policy. The FEMA Guidelines then reference the National Flood Insurance Program Standard Flood Insurance Policy for such coverages and exclusions.[9]

Further, final Question and Answer 64 addresses when a lender may rely on a private insurance policy that *does not meet* the criteria set forth by FEMA, implying flexibility to this "as broad as" language.

As a result, MBA recommends that the Agencies use the same "as broad as" language found in Question and Answer 63, and refer as well to Question 64 for additional guidance dictating when servicers can deviate from this standard.

Cover Interests of Both the Borrower and Lender

The third condition requires that a lender-placed policy cover the interests of both the borrower and lender. Again, we are unclear as to the intent of this phrase. We are concerned that this new condition mandates a dollar amount of coverage in excess of what is required by law (and thus what is in typical loan documents), such as coverage for the residential and commercial borrower's equity position or for personal property not serving as collateral if the borrower had such borrower-purchased coverage prior to expiration or cancellation. MBA respectfully objects to this condition.

NFIRA specifies the amount of minimum flood insurance that is required, which is the lowest of the following:[10]

- The outstanding principal balance of the loan, or
- The maximum limit of coverage made available under the Act with respect to the particular type of property.

It is clear by the statute that the lender is only required to protect its interest (e.g., the loan amount). If the law had intended to protect the borrower's interest it would have specifically covered the borrower's equity position or other assets. The wording in the Fannie Mae/Freddie Mac Single-Family Uniform Instrument appears consistent with the law by stating, "such coverage shall cover Lender, but might or might not protect Borrower, Borrower's equity in the Property, or the contents of the Property, against any risk, hazard or liability and might provide greater or lesser coverage than was previously in effect."[11] Furthermore, in the context of commercial and multifamily properties, it is not common for lender-placed insurance policies to include the borrower as an insured party.

[7] 74 Fed. Reg. 35944.
[8] *Id.*
[9] *Mandatory Purchase of Flood Insurance Guidelines,* Federal Emergency Management Agency (2007), pg. 20. *"A complete list of coverages and exclusions may be found in the Standard Flood Insurance Policy available on line at (http://www.fema.gov/business/nfip/sfip.shtm."*
[10] *Id. pg. 27.*
[11] Fannie Mae/Freddie Mac Single-Family Uniform Instrument, Form 3047.

Therefore, while a borrower may purchase additional insurance, NFIRA only mandates that insurance cover the outstanding principal balance (UPB) or the maximum insurance coverage available, whichever is lower. Final Question and Answer 13 reinforces the fact that servicers are not required to insure for more than UPB and not for the amount of the borrower's equity position.

Additionally, NFIRA specifies that lender-placed insurance need not cover personal property unless it serves as collateral for the debt.[12] FEMA's Guidelines restate this plain reading of the law: "Flood insurance coverage for contents is not required by the law unless personal property, in addition to a building, secures the loan."[13]

As a result of our aforementioned concerns, MBA respectfully recommends removing the following language: "… cover the interests of both the borrower and the lender." Instead, we recommend that the Answer indicate that the amount of lender-placed coverage is limited to the coverage required under the law and that coverage of the borrower's interests above that required by NFIRA may be obtained, but is not required.

<u>Question 57</u>: What is the requirement for the force placement of flood insurance under the Act and Regulation?

<u>Answer</u>: The Act and Regulation require a lender to force place flood insurance, if *all* of the following circumstances occur:

- **The lender determines at any time during the life of the loan that the property securing the loan is located in an SFHA;**
- **Flood insurance under the Act is available for improved property securing the loan;**
- **The lender determines that flood insurance coverage is inadequate or does not exist; and**
- **After required notice, the borrower fails to purchase the appropriate amount of coverage within 45 days.**

The Act and Regulation require the lender, or its servicer to send notice to the borrower upon making a determination that the improved real estate collateral's insurance coverage has expired or is less than the amount required for that particular property, such as upon receipt of the notice of cancellation or expiration from the insurance provider. The Act and Regulation also require the lender, or its servicer, to give notice and force-place such insurance, if necessary, when a lender learns that a property requires flood insurance coverage because it is in an SFHA as a result of a flood map change.

The notice to the borrower must clearly state that the borrower should obtain, at the borrower's expense, flood insurance in an amount at least equal to the amount required under the NFIP, for the remainder of the loan's term. The notice should also state that if the borrower does not obtain the insurance within 45 days, the lender will purchase insurance on behalf of the borrower and may charge the borrower for the cost of premiums and fees to obtain the coverage, which are likely to be more expensive than if the borrower purchases it. The Agencies encourage institutions to explain their force-placement policies to borrowers

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[12] 42 U.S.C. § 4012a (e)(1) (1996).

[13] *Mandatory Purchase of Flood Insurance Guidelines,* Federal Emergency Management Agency (2007), pg. 31.

(including, where applicable, that they charge for force-placement coverage for the 45-day period and the timing of that charge). In situations where a borrower has not previously been required to have flood insurance (such as a map change), it is a best practice to also provide the Notice of Special Flood Hazards and Availability of Federal Disaster Assistance, which give borrowers important information about the implications of being in an SFHA.
If adequate insurance is not obtained by the borrower within the 45-day notice period, then the lender must purchase insurance on the borrower's behalf. Standard Fannie Mae/Freddie Mac documents permit the servicer or lender to add those charges to the principal amount of the loan.

FEMA developed the Mortgage Portfolio Protection Program (MPPP) to assist lenders in connection with force-placement procedures. FEMA published these procedures in the *Federal Register* on August 29, 1995 (60 FR 44881). Appendix A of FEMA's September 2007 *Mandatory Purchase of Flood Insurance Guidelines* sets out the MPPP Guidelines and Requirements, including force-placement procedures and examples of notification letters to be used in connection with MPPP.

While MBA agrees that the required notice should provide clear information to the borrower, we would recommend the following changes/clarifications to proposed Answer 57.

The Agencies recommend a best practice that lender/servicers provide the Notice of Special Flood Hazards (NSFH) to a borrower during the servicing of a loan when required to purchase insurance for the first time. FEMA Guidelines specify that there is no prescribed language in the law for the 45-day notice but that "lenders and servicers should give a close reading to the statute and regulations for guidance."[14] As proposed, the Answer could be interpreted to be establishing prescribed language or required action not in the law or regulation itself. If a lender or servicer did provide a copy of the NSFH to the borrower along with its 45-day notice it would certainly create confusion given that the NSFH states that the notice is being sent as a result of a loan being made, increased, extended, or renewed.[15] In the proposed Answer 57, a consumer is not participating in any of these activities; in this case, their existing loan now requires flood insurance. It would be confusing for a consumer to receive the NSFH notice when they are not participating in a triggering event for the NSFH. Therefore, we recommend removing the line from the Answer "In situations where a borrower has not previously been required to have flood insurance (such as a map change), it is a best practice to also provide the Notice of Special Flood Hazards and Availability of Federal Disaster Assistance, which give borrowers important information about the implications of being in an SFHA."

Conclusion

The industry applauds your review and further analysis of the Interagency Question and Answers Regarding Flood Insurance. We appreciate the Agencies' recognition that a lender or its servicer may charge a borrower for the cost of insurance that covers collateral during the 45-day notice period. We would appreciate further clarification of the points we raise in our comment letter. Namely, we believe a lender or servicer should be able to rely on the law and charge a borrower for lender-placed coverage during the 45-day notice period. We do not believe new conditions should be attached to the lenders' obligation to ensure that flood insurance is maintained for the life of the loan.

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[14] *Mandatory Purchase of Flood Insurance Guidelines,* Federal Emergency Management Agency (2007) pg. 41.
[15] 12 C.F.R. 22.0 (1997).

We appreciate the opportunity to comment, and we welcome discussion on this matter. If you have any questions or comments please contact Vicki Vidal, Associate Vice President, Loan Administration at (202) 557-2861, or vvidal@mortgagebankers.org; Kathy Marquardt, Associate Vice President of Commercial Servicing and Council Coordination, Commercial/Multifamily Group at (202) 557-2742, or kmarquardt@mortgagebankers.org; or Sandra Troutman, Director, Public Policy at (202) 557-2858 or stroutman@mortgagebankers.org.

Sincerely,

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