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**Re: Loans in Areas Having Special Flood Hazards – Private Flood Insurance;
Docket ID OCC–2016–0005, RIN 1557–AD67; Docket No. R–1549, RIN 7100–AE60; RIN
3064–AE50; RIN 3052–AD11; RIN 3133–AE64**

Ladies and Gentlemen:

The American Bankers Association¹ appreciates the opportunity to comment on the proposal by the Office of the Comptroller of the Currency (OCC), the Board of Governors of the Federal Reserve System (the Federal Reserve Board), the Federal Deposit Insurance Corporation (FDIC), the Farm Credit Administration (FCA), and the National Credit Union Administration (NCUA) (collectively, the Agencies) to amend their respective regulations regarding loans in areas having

¹ The American Bankers Association is the voice of the nation's \$16 trillion banking industry, which is composed of small, regional and large banks that together employ more than 2 million people, safeguard \$12 trillion in deposits and extend more than \$9 trillion in loans.

special flood hazards, implementing the private insurance provision of the Biggert-Waters Flood Insurance Reform Act of 2012 (BWA or the Act).²

I. SUMMARY OF COMMENT

BWA was enacted on July 6, 2012, with the goal, among others, of expanding the private flood insurance market. However, due to a very narrow definition of private flood insurance, the Act has had the opposite effect on the private flood insurance market.

BWA directed the Agencies to write implementing regulations regarding the acceptance of private flood insurance. The Agencies proposed implementing regulations in October 2013 (2013 Proposed Rule). ABA commented on the proposal (2013 Letter) and we appreciate the Agencies consideration of our comments as well as other comments from the industry. Rather than finalizing a rule that could have exacerbated the challenges faced by the industry, the Agencies have proposed a revised rule to guide lenders' acceptance of private flood insurance policies (Proposed Rule).³

The Proposed Rule provides two paths to facilitate a lender's acceptance of private flood insurance policies – a “Compliance Aid” to assist with the acceptance of the flood insurance policies that meet the explicit statutory definition of “private flood insurance,” and standards for the exercise of lender discretion to accept private flood insurance policies that differ from the explicit statutory definition of private flood insurance. In addition, the Proposed Rule proposes standards for the acceptance of mutual aid society “policies” – guarantees from certain religious or cultural institutions to rebuild a property in the case of a flood or other hazard.

ABA believes that the Proposed Rule is a well-intentioned attempt to support lender acceptance of private flood insurance and to advance an important objective of BWA to stimulate development of a private flood insurance market that will expand and improve the flood insurance options available to borrowers and reduce reliance on the National Flood Insurance Program (NFIP). However, several requirements of the Proposed Rule may, in fact, impede a lender's ability to accept private flood insurance policies, causing confusion and delay for the borrower, and undermining Congressional intent.

ABA supports both the Compliance Aid and the path for a lender to exercise discretion, but we note that the requirement in both – that a lender essentially conduct a detailed analysis of a private flood insurance policy and compare it to a Standard Flood Insurance Policy (SFIP) issued under the NFIP – will impede the acceptance of private flood insurance. This requirement poses challenges for two reasons. The first is that lenders are not insurance experts, and they lack the resources and expertise to conduct a full-scale analysis and comparison of the two typically

² Public Law 112-141, 126 Stat. 916 (2012).

³ Loans in Areas Having Special Flood Hazards-Private Flood Insurance, 81 Fed. Reg. 78063 (Nov. 7, 2016) (Proposed Rule).

different policies. The second is that there can be a delay between when coverage is obtained and when the full policy is provided to the lender. When combined with the extended time frame lenders will require to review and compare the policies, the result may be extensive delays and borrower frustration.

By contrast, we believe the statutory goal of encouraging the acceptance of private insurance options that protect both the borrower and lender in the event of a flood can be achieved through less restrictive means. For the Compliance Aid, as we suggested in our 2013 Letter, an endorsement or verification from the insurer confirming that the flood insurance policy meets the statutory definition of private flood insurance is all that should be required – such an endorsement would provide recourse and protections to both the borrower and lender and obviate the need for a complete policy comparison by the lender.

Further, to encourage lenders to exercise discretion to accept a policy that does not meet BWA’s definition of private flood insurance, we urge the Agencies to identify clearly those elements a private flood insurance policy *must* (or *must not*) contain. This, in turn, would enable a lender to obtain that specific information from the insurance agent and conduct a targeted review to ensure the private policy meets those key elements, without requiring extensive insurance knowledge that lenders do not usually have.

ABA also appreciates the Agencies attempt to provide standards to facilitate the acceptance of a commitment by a mutual aid society to repair or rebuild a borrower’s property as satisfying the mandatory purchase obligation. However, the Proposed Rule must articulate clearly when a mutual aid policy will be deemed acceptable, given that these commitments rarely, if ever, remotely resemble an SFIP.

II. BACKGROUND

The enactment of BWA set in motion sweeping change to the National Flood Insurance Program, which included reform of the flood insurance premium rate structure, flood hazard mapping, and floodplain management and mitigation.⁴ Congress’ overriding objective in passing the Act was to achieve the financial solvency and stability of the federal flood insurance program, and to that end BWA included a provision intended to encourage greater private sector participation by requiring lenders to accept “private flood insurance” – that is flood insurance policies that are not backed by the NFIP. However, BWA defined “private flood insurance” very narrowly. In the four years since the Act was signed into law, this definition of “private flood insurance” has discouraged rather than encouraged the goal of expanding the private flood insurance options available to borrowers.

⁴ Although well intentioned, the law presented a number of interpretive questions and unintended consequences, some of which Congress addressed by enacting the Homeowner Flood Insurance Affordability Act of 2014 (HFIAA) in March 2014. HFIAA, however, did not amend BWA’s private flood insurance provision.

BWA *requires* that lenders accept private policies that meet certain specific standards, yet few lenders have the capacity and expertise to determine whether policies meet the standards. Lenders also report that the private policies they receive rarely meet with precision one or more of these rigid statutory criteria imposed in the statute—particularly in the case of complex commercial flood insurance policies and multi-peril policies. However, many of these policies, from a safety and soundness perspective, provide sufficient protection. Indeed, many commercial borrowers use carefully crafted multi-peril policies to protect their business operations, often with the assistance of professional insurance consultants.

The definition of “private flood insurance” in BWA was incorporated with little debate or opportunity to consider whether the statutory provision would achieve the intended result of encouraging the development of private flood insurance options. It may be that some change must be effectuated through legislation. Absent legislative amendment, however, the Agencies have moved forward with their obligation under BWA to write regulations directing lending institutions “to accept private flood insurance as satisfaction of the [mandatory] flood insurance coverage requirement . . . if the coverage provided by such private flood insurance meets the requirements for coverage” detailed in the statute.⁵

We welcome the opportunity to comment on this revised Proposed Rule, and to propose further modifications that we believe are necessary to encourage lenders to accept private flood insurance policies in satisfaction of the mandatory purchase obligation.

III. COMPLIANCE AID FOR MANDATORY ACCEPTANCE

In the 2013 Proposed Rule the Agencies suggested a safe harbor for private flood insurance policies; they proposed that a private policy would meet the statutory definition of “private flood insurance” if a state insurance regulator made that determination in writing. ABA supported the inclusion of the proposed safe harbor, as it would permit the lender to rely upon the expertise of state insurance authorities to make the determination that the terms of a particular policy were consistent with the statutory definition of private flood insurance.⁶ In our 2013 Letter, ABA also suggested an additional or alternative path to a safe harbor, which was based upon a licensed insurer certifying, in a written endorsement to the policy or on company letterhead accompanying the policy, the policy conforms to the statutory minimum requirements for private flood insurance.

The Agencies noted in the supplemental information to the current Proposed Rule that state insurance regulators raised concerns regarding the safe harbor from the 2013 Proposed Rule – including concerns that “a State insurance regulator lacks the legal authority to certify that a

⁵ 42 U.S.C. § 4012a(b).

⁶ See ABA 2013 Letter:

<http://www.aba.com/Advocacy/commentletters/Documents/clABACOMMENTBWA2013Dec.pdf>

private flood insurance policy complies with Federal law”⁷ As an alternative, the Agencies now propose a Compliance Aid to assist lenders in determining whether a flood insurance policy meets the definition of private flood insurance. The Compliance Aid adopts elements of ABA’s proposal and permits a lender to rely on the insurer, an expert in the insurance field, to advise whether a private policy meets the statutory definition.

The Compliance Aid requires 1) a written summary provided by the insurer that demonstrates how the policy meets the definition of private flood insurance and confirms that the insurer is regulated in accordance with the definition, 2) verification by the regulated lending institution that the policy includes the provisions identified by the insurer in its summary and that these provisions satisfy the criteria included in the definition, and 3) a provision within the policy or an endorsement to the policy stating that “This policy meets the definition of private flood insurance contained in 42 U.S.C. 4012a(b)(7) and the corresponding regulation”⁸

ABA supports the inclusion of a Compliance Aid. Lenders are not insurance experts, and, as the Agencies note, private flood insurance policies are typically lengthy and complicated. The Compliance Aid, which includes a written summary identifying the relevant criteria within the private policy, permits the lender to rely upon the expertise of the insurer to identify and outline the terms of a particular policy that are consistent with the statutory definition of private flood insurance.

Further, we appreciate the Agencies’ inclusion of the use of a verification or endorsement by the insurer, as this serves to provide both the policy-holder and the regulated lending institution with additional assurance that a policy meets BWA’s requirements. In addition, it will give insurers issuing private policies more confidence that policy forms accompanied by a Compliance Aid would be accepted on behalf of the insured as compliant flood insurance coverage by regulated lenders.

However, we urge clarification of supervisory expectations for the required “verification by the regulated lending institution that the policy includes the provisions identified by the insurer in its summary and that these provisions satisfy the criteria included in the definition.”

Lenders currently perform a due diligence review of all flood insurance policies to confirm the correct 1) definition of “flood” as a covered peril, 2) flood zone, 3) property address, 4) dollar amount of flood insurance coverage, 5) named insured, 6) mortgagee clause, 7) policy type, and 8) policy period. To comply with the requirements of the proposed Compliance Aid, a lender also could review a written summary *provided by the insurer* to verify that a proffered private flood policy meets the statutory standard. In addition, a lender can confirm that the insurer has included the required verification or endorsement. However, for the reasons discussed below, requiring lenders to conduct additional analysis of the insurance policy to determine whether a private policy meets the definition of private flood insurance – essentially an independent review

⁷ Proposed Rule, *supra* note 3, at 78067.

⁸ *Id.* at 78068.

of the policy against the statutory requirements – will cause significant delay and potential monetary harm to borrowers, in addition to being redundant and unduly burdensome.

A. Both the Borrower and the Lender May Rely Upon A Verification or Endorsement by an Insurer.

The Agencies have requested comment on whether “each of the three criteria in this proposed provision is necessary and feasible.” In addition, the Agencies seek comment on “whether the provision as proposed would assist regulated lending institutions in complying with the requirement to accept insurance policies that meet the definition of ‘private flood insurance.’” In response, ABA believes that the third element – the verification or endorsement from the insurer stating that “This policy meets the definition of private flood insurance contained in 42 U.S.C. 4012a(b)(7) and the corresponding regulation” – should suffice as a means to encourage the acceptance of private policies. The lender review in particular is redundant, and an expectation for extensive lender analysis of a private policy to determine whether a private policy meets the definition of private flood insurance will significantly delay the acceptance of private flood policies and, therefore, discourage their use.

Private flood insurance policies, especially non-residential policies, are typically long, complex, and highly technical contracts. Ultimately, lenders are not insurance experts and lack the capacity to determine whether the provisions, conditions, and exclusions in a proffered policy satisfy the statutory definition of private flood insurance. Indeed, most lenders do not have licensed insurance producers – a certification that identifies the individual as having the required level of expertise to assess insurance policy terms and conditions and coverage requirements – nor do they need to in order to perform their duties and responsibilities as a lender.

Moreover, as we explained in our 2013 Letter, the use of a certification or endorsement can transform a policy that does not otherwise comply into one that does meet the definition of private flood insurance. The certification or endorsement would – as a matter of contract law – serve as a “conformity clause” or compliance guarantee – enforceable by a court of law; that is, it is a contractual commitment by the insurer that, independent of the language in the policy, the policy will be deemed to meet the definition of “private flood insurance” in conformity with Federal law. Courts have recognized that “[i]nsurance contracts often include so-called ‘conformity clauses’ which ‘provide[] that clauses which are in conflict with [statutorily mandated coverage] are declared and understood to be amended to conform to such statutes’”⁹ Accordingly, if an insurer certifies that a policy “meets the definition of private flood

⁹ *Ky. League of Cities, Inc. v. General Reinsurance Corp.*, 174 F. Supp. 2d 532, 540 (W.D. Ky. 2001) (citing 2 Couch on Insurance § 19:2 (3d ed.)). See also *Gross v. Public Storage, Inc.*, No. 12 C 00170, 2014 U.S. Dist. LEXIS 60709, at *5 (N.D. Ill. April 30, 2014) (recognizing as binding the following conformity clause in an insurance election addendum to a storage rental agreement: “If the terms of this Certificate [of Insurance] are in conflict with the laws of the state wherein the Certificate is issued, they are hereby amended to conform to such statutes.”); *Lessard v. Milwaukee Ins. Co.*, 514 N.W.2d 556, 559 (Minn. 1994) (holding that when an insurance policy contains a conformity clause, the clause amends all policy terms in conflict with Minnesota law to conform to

insurance” as provided in both BWA and the corresponding regulation, further analysis by the lender of the policy terms against the statutory language would be redundant.

A certification or endorsement by an insurer is a legally binding agreement on the part of the insurer. As the Agencies have recognized, if there is a dispute as to coverage at a later point, both the borrower and the lender would be able to rely on that certification for recourse.¹⁰ Further, a certification or endorsement by an insurer providing that a policy meets the definition of private flood insurance may conform a policy that does not otherwise precisely meet the terms of the definition – as most private policies do not – and resolve any discrepancies accordingly. As such, the assurance clause should turn a policy that may not meet precisely the definition of private flood insurance into one that does, regardless of the policy specifications contained within the remainder of the policy.

Moreover, as we pointed out in our 2013 Letter, state insurance authorities have the power to investigate and have enforcement authority to punish insurers that fail to adhere to policy terms and conditions. Accordingly, both the borrower’s and the lender’s interests should be adequately protected by an appropriate endorsement, making additional lender analysis redundant.

B. A Full Scale Analysis of a Private Flood Insurance Policy by a Lender Will Cause a Borrower Unnecessary and Undue Delay Closing the Loan.

Conducting the proposed independent verification by the lender that the policy includes the provisions identified by the insurer in its summary, and that these provisions satisfy the criteria included in the statutory definition of private flood insurance, will result in unnecessary delay of loan closures and add expense to the borrower.

As proposed, the Compliance Aid appears to require independent analysis by the lender of a private flood insurance policy to determine whether it will satisfy the mandatory purchase obligation. Obviously, this review must occur prior to closing; however, there may be a delay between the initiation of coverage, and delivery of the complete policy to the lender. To satisfy the mandatory purchase obligation at closing, an insurance agent typically provides the lender with an application and paid receipt, a certificate of insurance, or the declarations page. As FEMA and the Agencies recognize, a “copy of the Flood Insurance Application and premium payment, or a copy of the declarations page” is sufficient evidence of proof of purchase for new policies, and “certificates or evidences of flood insurance, and similar forms” may be sufficient evidence for policy renewals.¹¹

the law). In some cases, even if a policy does not contain a conformity clause, it will be treated as if it contains one. *See Ky. League of Cities*, 174 F. Supp. 2d at 540-41.

¹⁰ Proposed Rule, *supra* note 3, at 78068.

¹¹ FEMA Letter W-13013, available at: <http://bsa.nfipstat.fema.gov/wyobull/2013/w-13013.pdf>. *See also, for example*, Comptroller’s Handbook, Office of the Comptroller of the Currency, “Flood Disaster Protection,” App F. Available at: <https://www.occ.gov/publications/publications-by-type/comptrollers-handbook/flood.pdf>.

Without a complete policy, however, the lender cannot conduct the necessary verification. Accordingly, a lender may be forced to delay the closing until the complete policy has been obtained and the review can be completed. And as discussed above, because most lenders lack the expertise to verify independently that the policy includes the provisions identified by the insurer in its summary and that these provisions satisfy the criteria of the statute, lenders with the resources to do so may consult outside counsel or insurance experts for assistance with the review, resulting in additional delay and expense that may be passed on to the borrower.

This problem may be exacerbated on loans with lender-placed flood insurance. To demonstrate that a borrower has obtained flood insurance coverage, the borrower must only provide the declarations page and insurance agent contact information to the lender, and the lender is required to refund to the borrower all premiums paid for the lender-placed insurance within 30 days, whether or not the lender is able to obtain the complete private flood insurance policy and analyze it for sufficiency within that time.¹² If the lender subsequently discovers that the policy does not meet the definition of private flood insurance, the lender may be forced once again to lender-place flood insurance. As such, a lender and borrower may be locked into an ongoing cycle of lender-placement and refunds as lenders attempt to obtain and review the complete private flood insurance policy.

Borrowers faced with external pressures may feel obliged to purchase an NFIP policy, which may provide less robust coverage than a private flood policy, simply to close the loan in a timely manner and avoid confusion and complication at renewal. Moreover, some borrowers that hold an existing multi-peril policy purchase an *additional* NFIP policy to avoid the delay, incurring unnecessary expense for duplicative insurance. As discussed above, however, adding this verification obligation serves no meaningful purpose. Instead, the lender should be able to rely upon the summary and endorsement provided by the insurance agent, along with the certificate of insurance, the declaration page, or other permissible evidence. This places responsibility for the evaluation with the insurer, who has the requisite expertise, as well as access to the policy, to complete the analysis and issue a written summary in a timely manner.

IV. DISCRETIONARY ACCEPTANCE

As previously explained, BWA amended the mandatory purchase requirement to require lenders to accept a private flood insurance policy, if the coverage provided by the private policy meets the definition of “private flood insurance.”¹³ Very few policies, however, satisfy precisely the definition of private flood insurance. Lenders are reluctant to accept a policy that appears to be close to the requirements of BWA – and provides adequate insurance coverage from the perspective of both the lender and the borrower – but does not match the definition exactly,

¹² 42 U.S.C. § 4012a(e)(3); 12 CFR § 22.7(b); 12 CFR § 208.25(g)(2); 12 CFR § 339.7(b); 12 CFR § 614.4945(b); 12 CFR § 760.7(b).

¹³ 42 U.S.C. §4012a(b)(7).

because the bank may be assigned civil money penalties in the amount of \$2000 per violation, if an examiner later disagrees with the bank's decision.

ABA appreciates the Agencies' recognition of the challenge this poses for lenders and borrowers alike and its potential for limiting significantly the development of a vibrant and competitive private flood insurance market. Notably, the Agencies propose a standard by which to permit lenders to use discretion to accept policies that do not fully meet the definition of private flood insurance. We support this proposal; as we noted in our 2013 Letter, permitting lenders to use discretion to accept policies that are outside the four corners of the definition of private flood insurance will provide borrowers with many more choices, and potential cost savings, for flood insurance.

The Agencies propose the following criteria in order to determine whether a private flood insurance policy meets the discretionary standard:

1. The flood insurance policy would be required to be issued by an insurer that is licensed, admitted, or otherwise approved to engage in the business of insurance by the insurance regulator of the State in which the property to be insured is located. In the case of a policy of difference in conditions, multiple peril, all risk, or other blanket coverage insuring nonresidential commercial property, the policy is issued by a surplus lines insurer recognized, or not disapproved, by the insurance regulator of the State where the property to be insured is located.¹⁴
2. The flood insurance policy would be required to cover both the mortgagor(s) and the mortgagee(s) as loss payees.¹⁵
3. The flood insurance policy must provide for cancellation following reasonable notice to the borrower only for reasons permitted by FEMA for an SFIP on the Flood Insurance Cancellation Request/Nullification Form, in any case of nonpayment, or when cancellation is mandated pursuant to State law.¹⁶
4. The flood insurance policy must either be "at least as broad" as the coverage provided under an SFIP, or provide coverage that is "similar" to coverage provided under an SFIP, including when considering deductibles, exclusions, and conditions offered by the insurer.¹⁷
5. To determine whether the coverage is similar to coverage provided under an SFIP, the regulated lending institution would be required to (1) compare the private policy with an SFIP to determine the differences between the private policy and an SFIP, (2)

¹⁴ Proposed Rule, *supra* note 3, at 78068.

¹⁵ *Id.* at 78069.

¹⁶ *Id.*

¹⁷ *Id.*

reasonably determine that the private policy provides sufficient protection of the loan secured by the property located in an SFHA, and (3) document its findings.¹⁸

The Agencies request comment on whether “these proposed criteria are appropriate for regulated lending institutions accepting flood insurance policies issued by a private insurer that do not meet the statutory definition of ‘private flood insurance.’”¹⁹ More specifically, the Agencies seek comment on whether the proposed criteria are compatible with industry practice, or whether they would exclude currently accepted policies or significantly limit growth of the market for flood insurance policies issued by private insurers.

ABA appreciates the Agencies’ interest in providing lenders with greater flexibility to accept private policies. With some clarifications and modifications, offered below, we hope lenders will be able to exercise discretion and stimulate development of private flood insurance options which provide ample protection to the borrower and the lender, even where they are outside of the rigid statutory definition.

The first three criteria require some modifications. The second element should be accompanied by a caveat or exception noting that certain borrowers may not be a party to the policy insuring the building itself. For example, insuring condominiums from flood loss is complicated by their unique ownership structure; each building has common elements owned by all and individually owned units. The borrower/mortgagor, as the owner of an individual unit, would be an indirect beneficiary of the condominium association’s policy as an interest holder in the property, but would not be listed as an insured on the policy. ABA recommends a clarification that in such instances, such private policies may be acceptable – at the lender’s discretion – as the borrower and the lender would each still be protected.

Regarding the third element, ABA also appreciates the Agencies’ proposed requirement for a cancellation notice to be “reasonable.” We emphasize, however, that timeframes are unlikely to conform specifically to the time frames provided by the NFIP, as industry standard and state mandated time frames differ from those in an SFIP.

It is the fourth (which also encapsulates the fifth) element – the requirement that a private flood insurance policy be either “at least as broad” as the coverage provided under an SFIP or provide coverage that is “similar” to coverage provided under an SFIP – that requires the most modification and clarification in order to enable lenders to exercise discretion to accept a private flood insurance policy.

¹⁸ *Id.*

¹⁹ *Id.*

A. Lenders Lack the Expertise to Determine Whether Coverage Is “At Least as Broad” as an SFIP.

As we noted in our 2013 Letter, the “at least as broad as” standard creates an inflexible test that will result in a high private policy denial rate and frustrate BWA’s goal of encouraging greater private sector participation in the flood insurance market. Although ABA appreciates the Agencies’ attempt to clarify those elements of a private flood insurance policy that must be compared to an SFIP, the exercise nevertheless demands an understanding of insurance terms, coverages, and exclusions which lenders typically lack. Ultimately, the “at least as broad as” standard requires lenders to conduct a comparison of the private flood insurance policy to an SFIP. Flood insurance policies – and particularly the multi-peril commercial policies that comprise the majority of the private market – are lengthy, complex, and technical contracts. It defies practicality to expect a lender without insurance expertise to conduct such a comparison.

In addition, very few private policies will meet this standard, particularly with respect to the deductibles in private policies, which may be higher than those of an SFIP, because NFIP coverage limits may be lower than those contained in a private policy. Standard industry cancellation notice periods often differ as well.

Further, the resulting delays as lenders attempt to conduct such reviews will negatively impact borrowers, who may feel obliged simply to purchase an NFIP policy in order to close the loan in a timely manner, even when a private or multi-peril policy may offer more appropriate protection.

B. Lenders Require Clarity as to How to Determine that “Coverage Is Similar” to an SFIP.

An alternative standard proposed by the Agencies would permit a lender to accept a private policy with coverage “similar to” an SFIP, including when considering deductibles, exclusions, and conditions offered by the insurer. Both lenders and examiners, however, need clarity as to how best to determine, with consistency, that a policy’s coverage is “similar.” In the absence of clarity, lenders may be apprehensive to exercise their discretion, frustrating borrowers who seek to purchase private flood insurance policies that may offer better, more affordable, coverage but have conditions, exclusions and deductibles that cannot be matched confidently to the criteria. Moreover, for lenders to be able to exercise discretion confidently, they need assurance that *examiners* also clearly understand the expectations surrounding the exercise of discretion.

ABA urges the Agencies to make the clarifications described below in order to permit lenders to exercise their discretion while providing safeguards against policies that do not sufficiently protect the collateral securing the loan.

1. Lenders Require Clear Guidance as to How to Evaluate Deductibles.

Lenders require clarification about expectations for “similarity” in the case of deductibles. Private flood insurance policy deductibles are rarely comparable to SFIP deductibles, in part because private flood insurance policies may have higher coverage amounts than NFIP policy maximums. NFIP policies have a maximum of \$250,000 for residential structures and \$500,000 for commercial structures. Private multi-peril policies, by contrast, may be written to cover the risk of significantly higher losses. Accordingly, to promote affordability, their deductibles tend to be higher than the maximum deductibles for NFIP policies.

Lenders are unlikely to use the proposed discretionary standard if there is an expectation for a private policy’s deductible to have a maximum dollar value that matches the corresponding SFIP deductible. To avoid this result, which would frustrate Congressional intent, we urge the Agencies to clarify that their expectations for evaluating how and when deductibles will be considered “similar.” For example, lenders may determine whether the deductible to insurable value ratio of a private policy is proportional to the deductible to insurable value ratio of an SFIP. The NFIP permits a maximum deductible of \$50,000 on commercial properties, which is 10% of the statutory policy maximum of \$500,000. Using a similar proportionality standard, a lender could use a \$2 million deductible for a private policy that would insure \$20 million in loss assuming it would be acceptable under the lender’s credit-risk underwriting policy. Ultimately, deductibles must be determined by an individualized assessment of the borrower and policy.

2. The Agencies Must Enumerate Required Exclusions and Conditions in the Regulations to Enable Lenders to Identify Them.

To encourage use of the discretionary exemption, the Final Rule also must describe the specific exclusions and conditions lenders are obligated to identify and compare. Private flood insurance policies, particularly multi-peril policies, contain numerous exclusions and conditions, many of which are complex and do not readily compare to any counterpart within an SFIP. Lenders should not be expected to conduct a broad and open-ended review and comparison of a policy’s exclusions and conditions.

In addition, as discussed above, lenders may experience delays in obtaining the final and complete insurance policy. Identifying in the rule the specific exclusions and conditions that a private flood insurance policy must – or must not – contain would enable a lender to request from the insurance agent the relevant information to make a timely determination about the policy, protecting the borrower from lengthy, unnecessary delays.

3. Requiring Lenders to Compare a Private Flood Insurance Policy to an SFIP Policy Is Unnecessarily Redundant.

The Proposed Rule has a separate, additional requirement that lenders “compare the private policy with an SFIP to determine the difference between the private policy and an SFIP.” This requirement is redundant to the requirement that lenders determine how coverage is similar to coverage provided under an SFIP in terms of deductibles, exclusions, and conditions. This comparison should be absorbed into the evaluation of exclusions and conditions, and any obligation for a further comparison, for the reasons discussed in more detail above, should be eliminated as redundant.

4. Lenders Require Guidance as to How to Reasonably Determine that Insurance Policies Provide “Sufficient Protection of the Loan.”

The Agencies have also requested comment on “whether the phrase ‘sufficient protection of the loan’ is adequately clear” and “whether the proposed criteria raise any safety and soundness risks for regulated lending institutions.”²⁰

Lenders and examiners require clear direction about how a lender is to determine that an insurance policy provides sufficient protection of the loan. Currently, lenders perform a due diligence review of all flood insurance policies and confirm the correct 1) definition of “flood” as a covered peril, 2) flood zone, 3) property address, 4) dollar amount of flood insurance coverage, 5) named insured, 6) mortgagee clause, 7) policy type, and 8) policy period. In addition, lenders have extensive experience determining from a safety and soundness perspective whether collateral is adequately insured—judgments that are reviewed regularly by safety and soundness examiners. ABA urges the Agencies to confirm in the rule that a lender’s evaluation of a private flood insurance policy using existing due diligence and safety and soundness reviews satisfies the requirement for determining that a policy “sufficiently protects the loan.”

5. Lenders Require Guidance on Examiners’ Expectations of Documentation.

The Agencies should clearly describe the documentation examiners will expect to review, and beyond the required documentation we would ask that the Agencies direct examiners to grant lenders adequate discretion. Requiring detailed explanations about why a bank chose to accept or reject a particular policy, or to build lengthy justifications of why it used its discretion in a particular way, will significantly increase expenses for the borrower and cause delays.

²⁰ 81 Fed. Reg. at 78069.

C. Flood Insurance Policies for Nonresidential Properties Should Be Afforded Broader Discretion.

Although the Proposed Rule does not contemplate a different discretionary standard for nonresidential properties, in the supplemental materials the Agencies have solicited comment on whether the final rule “should include criteria for the discretionary acceptance of flood insurance policies issued by private insurers for nonresidential properties that are different from the criteria applicable to flood insurance policies issued by private insurers for residential properties.” More specifically, the Agencies inquire whether they should promulgate a rule which would impose significantly fewer requirements for the discretionary acceptance of a private commercial flood policy, i.e., that the policy simply—

(1) [M]eet the amount of coverage for losses and term requirements specified in the mandatory purchase requirement, (2) cover both the mortgagor(s) and the mortgagee(s) as loss payees, and (3) require the regulated institution to determine that the policy provides sufficient protection of the loan secured by the property, consistent with general safety and soundness principles, as is required for the acceptance of coverage provided by mutual aid societies.²¹

ABA appreciates the Agencies’ recognition that the proposed definition of “private flood insurance,” and even the proposed discretionary acceptance provision as it appears in the Proposed Rule, impose very specific requirements with respect to deductibles, exclusions, conditions, and cancellation. These requirements will make it even more challenging for regulated lending institutions to accept complex commercial flood insurance policies and multi-peril policies issued by private insurers, even when such policies would satisfy safety and soundness requirements. As noted above, lenders’ key experience and expertise are in evaluating insurance policies from a *credit risk* perspective to ensure that collateral is adequately protected. For this reason, ABA strongly supports adoption of a broader discretionary standard for nonresidential properties.

V. MUTUAL AID SOCIETIES

The Agencies propose a provision to permit lenders, at their discretion, to accept certain non-traditional flood insurance coverage from organizations that meet the following criteria:

1. The members must share a common religious, charitable, educational, or fraternal bond;
2. The organization must cover losses caused by damage to members’ property including damage caused by flooding, pursuant to an agreement, in accordance with this common bond; and

²¹ *Id.* at 78070.

3. The organization must have a demonstrated history of fulfilling the terms of agreements to cover losses to members' property caused by flooding.²²

Typically, borrowers that rely on assurances from mutual aid societies seek to comply with religious or other strictures on the purchase of traditional flood insurance, which creates significant challenges for a lender trying to serve the customer and comply with the mandatory purchase obligation. Moreover, as FEMA publishes new flood maps, financial institutions may be required to lender-place insurance on properties newly mapped into a special flood hazard area. Having the ability to accept assurances offered by the Mutual Aid Societies would better meet the needs of certain communities and the financial institutions that serve them by keeping down costs and respecting the borrower's religious or other beliefs.

The Proposed Rule states that a lender may exercise discretion to accept a "private policy" from a mutual aid society if—

- (i) The supervising Agency has determined that such types of policies qualify as flood insurance for purposes of this Act; (ii) the policy meets the amount of coverage for losses and term requirements specified in the rule; (iii) the policy covers both the mortgagor(s) and the mortgagee(s) as loss payees; and (iv) the regulated lending institution has determined that the policy provides sufficient protection of the loan secured by the property located in a special flood hazard area. In making this determination, the regulated lending institution must: (A) Verify that the policy is consistent with general safety and soundness principles, such as whether deductibles are reasonable based on the borrower's financial condition; (B) Consider the policy provider's ability to satisfy claims, such as whether the policy provider has a demonstrated record of covering losses; and (C) Document its conclusions.²³

ABA appreciates that the Agencies recognize the legitimate and deeply held convictions of groups that seek to use mutual aid assurances in place of commercial flood insurance, and we encourage the adoption of a rule that confirms the acceptability of such an assurance in satisfaction of the mandatory purchase obligation. However, we note that the assurances provided by mutual aid societies, including those provided by the Amish Aid Insurance Plan, which the Agencies note are currently accepted by the OCC,²⁴ do not resemble commercial flood insurance policies and should not be characterized as a "policy" that can or should be compared to an SFIP. They do not state the insurable value of a property or establish deductibles, and they do not name the lender as a loss payee. Instead, they are simply assurances by the community to rebuild the structure and identified out buildings in the event that they are damaged or destroyed by a flood—assurances that lenders who serve these communities know they can depend on.

²² *Id.* at 78065.

²³ *Id.* at 78069.

²⁴ *Id.* at 78070.

We assume that the Agencies are not imposing a requirement for a lender to evaluate mutual aid society assurances by comparing them to commercial flood insurance policies, as such a comparison is impossible. Accordingly, we urge the Agencies to clarify their expectations around these requirements, particularly with respect to the statements quoted above regarding expectations for “the amount of coverage for losses and term requirements,” identification of “loss payees,” and “verif[cation] that the policy is consistent with general safety and soundness principles, such as whether deductibles are reasonable based on the borrower’s financial condition.” As proposed, requiring strict compliance with these expectations would prohibit a lender from offering a mortgage (secured by property located in a flood zone) to a member of a mutual aid society.

We also note that the proposed rule authorizes each of the Agencies to determine whether individual mutual aid society assurances qualify as flood insurance for purposes of the Federal flood insurance statutes. Moreover, the supplemental information indicates that the Federal Reserve Board and the FDIC “expect that cases in which they approve policies issued by mutual aid societies to be rare and limited.”²⁵ By contrast, the supplemental materials state that the OCC currently accepts flood coverage issued by Amish mutual aid societies, such as Amish Aid plans. ABA opposes a rule that would permit the Agencies to adopt different approaches to the acceptability standards for mutual aid society assurances. Ultimately, either mutual aid society assurances should be acceptable to all the Agencies, or, if for some identifiable and adequate reason they do not qualify, they should be treated similarly by each Agency. Inconsistent acceptance will create unnecessary confusion and barriers for borrowers who may already be limited in their banking options due to the rural location of many communities, and who would be further limited if only certain banks are able to accept mutual aid society assurances.

VI. IMPLEMENTATION

Implementation of the proposed rule will require 1) adopting new policies and procedures to ensure that the required analysis is conducted and documented, 2) implementing technology changes to operating systems, and 3) training staff on the new procedures and operating system changes. Accordingly, we request that the Agencies provide at least one year as an implementation period from the date of publication of the final rule.

Further, we urge the Agencies to clarify that the final rule will apply prospectively. To serve those borrowers that would like to insure their property with a private policy, many lenders have used their judgment and discretion to evaluate and accept private policies that they believe safely and soundly insure the collateral, and they must continue to do so, as appropriate, pending publication of a Final Rule. To avoid disruption in the marketplace and frustration of BWA’s objective, the Agencies should assure lenders that any new requirements will only apply prospectively and not disturb existing regulatory determinations.

²⁵ *Id.* at 78070.

VII. CONCLUSION

ABA appreciates the opportunity to comment on the proposed amendments to the regulations regarding private flood insurance for loans in areas having special flood hazards. If you have any questions about these comments or would like to discuss anything further, please contact Anjali Phillips at 202-663-5338 or aphillip@aba.com.

Sincerely,

A handwritten signature in black ink that reads "Anjali Wade Phillips". The signature is written in a cursive style with a large initial 'A' and 'P'.

Anjali Phillips
Senior Counsel, Center for Regulatory Compliance