May16, 2008

Mira N. Marshall
Senior Policy Analyst (Compliance)
Division of Supervision and Consumer Protection
Federal Deposit Insurance Corporation
550 17th. Street, NW
Washington, DC 20429

Re: RIN Number 3064-ZA00
Loans in Areas Having Special Flood Hazards; Interagency Questions and Answers Regarding Flood Insurance

Dear Ms. Marshall:

We appreciate the opportunity to comment on the proposed Interagency Questions and Answers Regarding Flood Insurance. Banker's Compliance Consulting is a regulatory compliance consulting firm that provides compliance consulting and auditing services to hundreds of financial institutions regulated by all of the Federal financial institution regulatory agencies.

Following are our comments on the proposed Frequently Asked Questions (FAQs) in which further clarification by the regulatory agencies would be appreciated.

Question/Answer #3 & #40

The answer to question #3 states a purchased loan (100% purchased) is not an event that triggers the flood insurance requirements. The answer to question #40 states, "*each participating lender remains individually responsible for ensuring compliance with the Act and Regulation*." It also indicates the Regulatory Agencies expect that all lenders of a participation loan (less than 100% purchased) have controls in place to ensure compliance with the flood insurance requirements.

Why does a partial loan purchase place more burden on a financial institution than 100% loan purchase? If a purchasing lender can rely on the original lender for compliance with the flood insurance requirements of a 100% loan purchase why can't a participating lender rely on the lead lender for a partial loan purchase? Having the participating banks duplicate these requirements would be a waste of time and resources. Further comment and consideration would be appreciated on this answer (#40).

<u>Question/Answer #7</u>
We have concerns with the concept and clarity of the following guidance stated in the answer to Proposed Question and Answer #7 (emphasis added):

> *"In determining coverage amounts for flood insurance,* ***lenders often follow the same practice used to establish other hazard insurance coverage amounts****. However, unlike the insurable valuation used to underwrite most other hazard insurance policies, the insurable value of improved real property for flood insurance purposes also includes the repair or replacement cost of the foundation and supporting structures.* ***It is very important to calculate the correct insurable value of the property; otherwise, the lender might inadvertently require the borrower to purchase too much or too little flood insurance coverage****. For example, if the lender fails to exclude the value of the land when determining the insurable value of the improved real property,* ***the borrower will be asked to purchase coverage that exceeds the amount the NFIP will pay in the event of a loss****."*

The concern is the use of hazard insurance as a calculation tool to determine an appropriate amount of flood insurance. Flood insurance does not include the same coverage as hazard insurance. For example, the numbered items listed below are not covered by a dwelling flood insurance policy, yet if you insure something using the hazard insurance replacement cost value as your calculation tool you will end up requiring an amount of insurance that is greater than the "insurable value" of the structure. This over-insurance occurs because many of the items listed below are covered by a hazard insurance policy but not by a flood insurance dwelling policy.

1. Personal property not inside the fully enclosed building;
2. A building, and personal property in it, located entirely in, on, or over water or seaward of mean high tide if it was constructed or substantially improved after September 30, 1982;
3. Open structures, including a building used as a boathouse or any structure or building into which boats are floated, and personal property located in, on, or over water;
4. Recreational vehicles other than travel trailers whether affixed to a permanent foundation or on wheels;
5. Self-propelled vehicles or machines, including their parts and equipment. However, we do cover self-propelled vehicles or machines not licensed for use on public roads that are:
    a. Used mainly to service the described location, or
    b. Designed and used to assist handicapped persons, while the vehicles or machines are inside a building at the described location;
6. Land, land values, lawns, trees, shrubs, plants, growing crops, or animals;

7. Accounts, bills, coins, currency, deeds, evidences of debt, medals, money, scrip, stored value cards, postage stamps, securities, bullion, manuscripts, or other valuable papers;
8. Underground structures and equipment, including wells, septic tanks, and septic systems;
9. Those portions of walks, walkways, decks, driveways, patios, and other surfaces, all whether protected by a roof or not, located outside the perimeter, exterior walls of the insured building or the building in which the insured unit is located;
10. Containers, including related equipment, such as, but not limited to, tanks containing gases or liquids;
11. Buildings or units and all their contents if more than 49 percent of the actual cash value of the building or unit is below ground, unless the lowest level is at or above the base flood elevation and is below ground by reason of earth having been used as insulation material in conjunction with energy efficient building techniques;
12. Fences, retaining walls, seawalls, bulkheads, wharves, piers, bridges, and docks;
13. Aircraft or watercraft, or their furnishings and equipment;
14. Hot tubs and spas that are not bathroom fixtures, and swimming pools, and their equipment such as, but not limited to, heaters, filters, pumps, and pipes, wherever located;
15. Property not eligible for flood insurance pursuant to the provisions of the Coastal Barrier Resources Act and the Coastal Barrier Improvement Act and amendments to these acts;
16. Personal property you own in common with other unit owners comprising the membership of a condominium association.

The Proposed Question and Answer makes the use of hazard insurance as a measuring stick sound like an “apples” to “apples” comparison when it’s really “apples” to “oranges”. Therefore, we ask for further clarification on the use of a hazard insurance replacement cost value as an appropriate flood insurance calculation tool. Requiring lenders to identify the hazard insurance replacement cost, determine what portion of the replacement cost is attributed to the 16 items listed above, subtract that from the overall hazard insurance replacement cost value and then add back a value for the foundation, supporting structure, etc. referenced in the FAQ is not realistic, efficient or feasible. This is better left to an insurance agent not a lender.

<u>Question/Answer #7, #10, #12, etc.</u>
The term "insurable value" is a key term referenced throughout the proposed questions and answers. Question seven attempts to define "insurable value." However, the definition provided, ("*the overall value of the property securing the designated loan minus the value of the land on which the property is located*,") only leads to more questions because the term "overall value" is used in the definition but it is not defined. Please define the terms "overall value" and "insurable value".

We would also like to see clarification of another area of confusion pertaining to the amount of flood insurance. The Mandatory Purchase of Flood Insurance Guidelines (MPFIG) indicate the term "insurable value" means "100% replacement cost value". While we understand the FAQs do not indicate RCV must be used, our discussions with numerous Federal regulatory field examiners indicate they expect financial institutions to use RCV when calculating the correct amount of insurance.

The problem with using RCV in every instance is that there are only two types of structures that will ever receive a settlement using RCV at the time of a loss: principal residences that are fully insured and residential condominiums. All other structures will be settled using actual cash value at the time of a loss. To force lenders to require borrowers to purchase flood insurance up to the RCV will result in many instances in which the insurance pay out will never be realized at the time of a loss. This practice does not seem prudent, will be difficult for lenders to require, will cause lenders to suffer reputation risk and may be seen as an unfair and/or deceptive act or practice. The MPFIG even states that using replacement cost value (RCV) "*meets or exceeds the minimal compliance standards*" (page 27 of the FEMA Guidelines).

Without clear guidance, regulators and bankers are forced to look to the FEMA Guidelines for assistance. Due to these facts, we ask there be a clarification made that lenders are <u>NOT</u> required to use RCV when calculating insurance coverage. Field examiners are very misinformed on this issue.

<u>Question/Answer #21 & #22</u>

These questions specifically address agricultural lending yet question #21 states the "*Act does not differentiate agricultural lending from other types of lending*." Why be so specific? Other types of lending (commercial or residential) also have to deal with low value buildings like the ones discussed in question #21 and multiple buildings spread out over a large area such as those discussed in #22. We recommend changing these questions so they do not specifically address agricultural loans but rather all loan types where the collateral may include multiple structures or low value buildings.

<u>Question/Answer #26</u>

The answer to this question states "lenders are encouraged to apprise the borrower of this risk" as it pertains to coverage shortfalls for condominium dwelling policies. Bankers are not insurance agents and are often not familiar with insurance industry practices. We feel insurance agents are the best source to "apprise the borrower of the risk". Please remove reference to lenders being burdened (even "encouraged") this way.

<u>Question/Answer #31</u>

The answer to this question states "requires a flood determination when <u>application</u> is made for the loan". The submission of an application does not trigger these requirements. Rather, these requirements are triggered upon making, increasing, renewing or extending a loan. We would not want the reader to misinterpret this question and feel they are required them to pull a flood determination when they receive an application.

<u>Question/Answer #33</u>

The subordinate lien mentioned in this answer appears to be limited to a home equity loans. This requirement applies to any subordinate lien secured by the improved real estate not just home equity loans. Please clarify that this answer applies to all subordinate lien loans.

Question/Answer #35

This question and answer merely states that content insurance is required in certain instances. We often see bankers struggle with determining how much content insurance is required. For instance, consider the following scenario on a commercial building that many banks might face:

Loan Amount	$200,000
Building Value	$150,000
Content Value	$100,000
Maximum Insurance	$500,000 each (contents & building)

Must the lender obtain flood insurance for $150,000 on the building and $100,000 on the contents? If so, the total insurance in place on the loan will be $250,000. Is this required when the loan is only for $200,000? Can we apply the "multiple building" logic (see FAQ #11) and only insure the building and contents for a total of $200,000 as long as some insurance is allocated to each (for example, $150,000 to the building and $50,000 to the contents)? We encourage you to clarify exactly how much content insurance will be required to meet regulatory guidelines. Examples of calculating the proper content insurance would also be very beneficial.

Section XI Force Placement

This is not in response to any question or answer in the proposed FAQs; however, this is an area that needs further clarification. Can the force placement notice be sent out 45 days prior to policy expiration? In other words, can a lender start the force placement "clock" before a policy expires or must the lender wait until the insurance has expired and then begin the force placement procedures (and the 45 day "clock")?

The FEMA Guidelines indicate the lender can begin the "45 day clock" prior to the expiration of a MPPP policy. Is this possible for other types of flood insurance policies?

Thank you again for the opportunity to submit comments on this invaluable guidance.

Sincerely,

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