December 21, 2018

The Honorable Jelena McWilliams
Chairman
Federal Deposit Insurance Corporation
550 17th Street, NW
Washington, DC 20429

The Honorable J. Mark McWatters
Chairman
National Credit Union Administration
1775 Duke Street
Alexandria, VA 22314

The Honorable Joseph Otting
Comptroller of the Currency
Office of the Comptroller of the Currency
400 7th Street, SW
Washington, DC 20219

The Honorable Dallas Tonsager
Chairman and CEO
Farm Credit Administration
1501 Farm Credit Drive
McLean, VA 22102

The Honorable Randal Quarles
Vice Chairman for Supervision
Board of Governors of the Federal Reserve System
Eccles Board Building
20th and C Street, NW
Washington, DC 20219

Dear Chairman McWilliams, Comptroller Otting, Vice Chairman Quarles, Chairman McWatters, and Chairman Tonsager:

We write you today regarding your agencies' long-running efforts to finalize the corresponding regulations implementing section 100239 of the Biggert-Waters Flood Insurance Reform Act of 2012 (Biggert-Waters). Based on the testimony of Chairman McWilliams and Comptroller Otting during an October 2, 2018 hearing before the Senate Committee on Banking, Housing, and Urban Affairs[1] and the notice published in the Unified Agenda[2], we understand that your respective agencies have set a target completion date for this work of February 2019.

The delay in promulgating a final rule, and the inconsistencies between the two proposed rules[3], have exacerbated some of the very uncertainties and barriers that prevented growth in the private flood insurance market prior to Biggert-Waters. Because of this, your goal of completing this work early next year is welcome news for the cross-industry stakeholders that we represent. However, we wish to reaffirm the concerns that have been raised regarding the most recent joint proposed rule that was

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[1] *Implementation of the Economic Growth, Regulatory Relief, and Consumer Protection Act: Hearing before the Committee on Banking, Housing, and Urban Affairs, Senate, 115th Congress (2018)*

[2] https://www.reginfo.gov/public/do/eAgendaViewRule?pubId=201810&RIN=1557-AD67

[3] Loans in Areas Having Special Flood Hazards, *78 FR 65107* (2013 Proposed Rule); *and,* Loans in Areas Having Special Flood Hazards – Private Flood Insurance, *81 FR 78063* (2016 Proposed Rule)

published in 2016 in an effort to ensure that any final rule enacted by your agencies is consistent with both the statutory language as well as the intent of Congress. Without significant changes to the 2016 Proposed Rule, we fear what was intended to be an effort to promote the private flood insurance market could effectively constrict the already limited market.

Each of our organizations submitted comments on the 2016 Proposed Rule that outlined the concerns of our respective industries (i.e. lenders, insurers, agents, reinsurers) and the members that we represent. While many of our concerns with the proposed rule were similar, they were expressed from the perspective of our specific industry sectors and the remedies we proposed at that time might have appeared to diverge or conflict for that reason.

Since submitting those comments to the 2016 Proposed Rule, we all have spent substantial time discussing this issue and working together to craft a consensus perspective which addresses the concerns of each of the involved industries in a unified way while ensuring the objectives of the regulators are achieved. The efforts undertaken by this stakeholder group were extensive and required significant give and take by all of the participants. While we all stand by this approach as the best possible way to achieve a final rule that is both workable and consistent with both the letter and spirit of the current statute, we do recognize that additional legislative amendments are likely needed.

Background

As you all are aware, the Flood Disaster Protection Act of 1973 (1973 Act) prohibits federally regulated lenders from issuing loans secured by properties located in a special flood hazard area (SFHA) unless the property is covered by flood insurance. Today, the National Flood Insurance Program (NFIP) has largely been responsible for fulfilling this “mandatory purchase” requirement.

In addition to requiring the federal government to offer NFIP policies at actuarially unsound rates, the 1973 Act significantly limits the ability of the NFIP to offer individual or tailored coverage to its customers. While this one-policy-fits-all approach has worked for some customers, it does limit the ability and options of some to protect their homes and businesses against the unique flooding risks associated with their properties. It is for these properties, as well as for consumers who would like more choices in their coverage options and terms, that the private flood insurance market can play a significant role.

While there has been a small continual private flood insurance marketplace, Biggert-Waters contained much-needed reforms to the NFIP that allowed the private residential flood insurance market to grow and offer consumers more coverage options to choose from. Included in the reforms in Biggert-Waters, Congress made a direct effort in Section 100239 to incentivize growth in the private flood insurance market by requiring lenders to accept private flood insurance policies that meet certain conditions to satisfy the mandatory purchase requirement.

It is important to note, however, that while Biggert-Waters requires lenders to accept certain private flood insurance policies, it purposely did not alter lenders' discretionary ability to accept non-NFIP policies that do not align precisely to the statutory requirements for mandatory acceptance. Prior to the enactment of Biggert-Waters, and continued through today, lenders have had the ability to review non-NFIP policies on an individual basis to determine if the policy provides the protection required both under the 1973 Act and general safety and soundness principles. It has historically been through lenders' discretionary acceptance that the current private flood insurance market has been able to exist and provide financial protection in areas that the NFIP cannot.

The existence of this discretion by lenders was known to Congress prior to enactment of Biggert-Waters. Therefore, it must be assumed that Congress not only did not intend to limit current authority but rather support such authority.

Definition of "Private Flood Insurance"

Section 100239 of Biggert-Waters provides a statutory definition of "private flood insurance" as it relates to private policies that lenders are required to accept as satisfaction of the mandatory purchase requirement. This statutory definition for "private flood insurance" is divided into three sections: (1) qualifying issuers who may offer a policy that is required to be accepted by the lender; (2) mandatory coverage terms that must be included to ensure that the policy offers coverage that is "at least as broad as" the coverage offered by an NFIP policy; and (3) required contractual provisions that align with those of an NFIP policy.[4]

Qualifying Issuers

In order for a policy to be required to be accepted by a lender, the statute states that it must be issued by an insurance company that is: "(1) licensed, admitted, or otherwise approved to engage in the business of insurance in the state or jurisdiction in which the insured building is located, by the insurance regulator of that state or jurisdiction; or (2) in the case of a policy of difference in conditions, multiple peril, all risk, or other blanket coverage insuring nonresidential commercial property, recognized or not disapproved as a surplus lines insurer."[5]

While not explicitly mentioned in the statute, Congress intended to include surplus lines insurers as writers of residential as well as commercial private flood insurance policies that could qualify for mandatory acceptance under Section 100239. The legislative history, which includes a colloquy between the Chairman of the relevant Senate Committee and the lead Senate sponsor of the provision, makes clear the Congressional intent.[6] Unfortunately, the 2016 Proposed Rule did not take this Congressional

[4] 42 U.S.C. 4012a(b)(7)

[5] Id.

[6] 158 Cong. Rec. S6051 (daily ed. Sept. 10, 2012)

intent into account. In addition to not clearly identifying surplus lines insurers as eligible issuers, the 2016 Proposed Rule failed to recognize that Congress, under Title V of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Dodd-Frank)[7], expressly limited the regulation of the placement of nonadmitted insurance to the state in which the insured resided.

Therefore, Congressional intent was to both authorize surplus lines insurers for both residential and commercial policies as well as align the definition of "surplus lines insurers" with the provisions of Dodd-Frank, which was enacted by Congress prior to Biggert-Waters. As such, we believe your agencies should use their authority to promulgate the rule in a way that the drafters intended; by identifying surplus lines insurers in the regulations and defining these insurers in a way that complies with Dodd-Frank. Such a clarification would not be a substantive change to the statutory definition, but rather a confirmation that the rule is consistent with both Biggert-Waters and Dodd-Frank.

> ***RECOMMENDATION #1:*** *Surplus Lines Clarification. The final rule should specify that private flood insurance issued by surplus lines insurers can qualify for mandatory acceptance as within the definition of "private flood insurance," and that surplus lines insurers should be defined as an insurer that has been recognized, or not disapproved, as a surplus lines insurer by the insurance regulator of the state or jurisdiction in which the insured is located, including surplus lines eligibility established in accordance with sections 521 through 527 of the Dodd-Frank Wall Street Reform and Consumer Protection Act 10 (15 U.S.C. 8201 through 8206).*

Mandatory Coverage Terms

The statutory definition requires that "private flood insurance" provide flood insurance coverage which is "at least as broad as" the coverage provided under an NFIP policy.[8] However, the statute defers to the regulators to determine what constitutes "at least as broad," including when considering "deductibles, exclusions, and conditions offered by the insurer."[9]

In the 2016 Proposed Rule, your agencies identified six minimum coverage terms that a private policy must include to be considered "at least as broad" as an NFIP policy. While four of these requirements directly relate to the protection of the safety and soundness of the lending institution, two of the requirements go beyond the role of the regulations of lenders and wade into the regulation of the business of insurance itself.

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[7] Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, 124 stat. 1376, 1590 (2010)

[8] 42 U.S.C. 4012a(b)(7)

[9] Biggert-Waters Flood Insurance Reform Act of 2012, Pub. L. No. 112-141, 126 Stat. 960 (2012)

Congress has expressly and repeatedly deferred to the states for the regulation of the business of insurance, and for that reason, we believe that the final rule should limit the requirements for "as broad as" coverage to those that are within the purview of the prudential regulators.

> ***RECOMMENDATION #2:*** *"At least as broad as." The final rule should provide that a policy is at least as broad as the coverage under a standard flood insurance policy if, at a minimum, the policy defines the term "flood" to include the events defined as a "flood" in a standard flood insurance policy; covers both the mortgagor(s) and the mortgagee(s) as loss payees; contains deductibles no higher than the maximum deductible allowed under a similar standard flood insurance policy or the maximum deductible allowed under Federal National Mortgage Association and Federal Home Loan Mortgage Corporation regulations related to windstorm coverage, whichever is higher; and does not contain conditions that narrow the coverage provided in a standard flood insurance policy.*

Required Contractual Provisions

Finally, the statute requires that "private flood insurance" subject to mandatory acceptance include several contractual provisions that are in line with those included in an NFIP policy. Included in these required provisions are: (1) a requirement for the insurer to give 45 days' written notice of cancellation or non-renewal of flood insurance coverage; and (2) a provision requiring an insured to file suit not later than one year after the date of a written denial of all or part of a claim under the policy.

Each state, through their general regulation of the business of insurance, has requirements related to the time limitations for both cancellation notices and statutes of limitation. These laws are put in place to protect consumers and vary state-to-state. Unfortunately, as Biggert-Waters does not preempt state insurance laws, the statute effectively prohibits "private flood insurance" as it relates to mandatory acceptance in states whose requirements contradict the statutory definition. However, it is important to note that many states have enacted cancellation notice and statute of limitation requirements that provide protection to consumers beyond those outlined in Biggert-Waters. For example, a state may require 60 days' notice to consumers of cancellation or non-renewal; as opposed to the only 45 days' notice required under Biggert-Waters.

Because of this, we believe any final rule should make clear that these statutory limitations are the minimum periods for both requirements, and that policies written in states where the consumer has more time to act remain eligible for mandatory acceptance.

> ***RECOMMENDATION #3:*** *State Law Clarification. The final rule should specify that policies meeting the private flood insurance definition must include cancellation notice provisions requiring the insurer to give written notice of 45 days, or longer when consistent with State law. Similarly, the final rule should specify that policies meeting the private flood insurance definition must include a provision requiring the insured to file suit not later than 1 year, or longer when consistent with State law, after a written denial of a claim.*

Mandatory Acceptance

Section 100239 requires lenders to accept "private flood insurance" policies that meet the definition outlined in the statute. It does not, however, include any process, standard, or mechanism for lenders, who are often not insurance experts, to determine whether a policy meets the definition. This unfortunately places many lenders in a difficult position of having to evaluate whether a policy meets the definition while being subject to civil money penalties if their insurance interpretation is deemed incorrect.

Compliance Aid Provision

The 2016 Proposed Rule tried to correct this omission with the inclusion of a "compliance aid provision." While we and other stakeholders support the notion of a compliance aid provision, it was made clear that the specific mechanism proposed in 2016 was unworkable. However, we have identified two potential compliance aid provisions that not only ensure compliance with the statute and regulation but are already common practice in today's insurance market.

Currently, in most states, private insurers offering flood insurance policies outside of the NFIP have been authorized by state insurance regulators to include in their policies what is known as a conforming conditions clause or endorsement. These clauses state that if a provision of the private policy limits the coverage to coverage that is not at least as broad as that available under the Standard Flood Insurance Policy Dwelling Form (SFIP), the private policy would be amended to conform to the SFIP. The inclusion of this language ensures that if there is any disagreement that a private policy is not "at least as broad as the coverage provided under a standard flood insurance policy,"[10] that the policy would be enforced as if compliant with the SFIP.

Additionally, certain states have enacted laws that allow their respective State insurance commissioners to review private flood insurance policies to determine whether the policy complies with federal regulation related to mandatory acceptance. While this requires significant resources by the State insurance commissioners, it allows the primary functional regulators to assist lenders in understanding the terms of coverage in a private flood insurance policy and the applicability of the federal mandatory acceptance requirements. Unfortunately, due to the required resources, not every state will be able to implement these practices.

As both of these compliance aids ensure that a policy, in effect, meets the requirements under the statute; any final rule should provide for automatic acceptance of private flood policies that include a conforming condition clause/endorsement, or that demonstrates that the state insurance commissioner in the state where the property is located has confirmed that the policy is "at least as broad as" the SFIP.

[10] Biggert-Waters Flood Insurance Reform Act of 2012, Pub. L. No. 112-141, 126 Stat. 960 (2012)

Additionally, it is important to recognize that some lending institutions have, or have the means of creating, an internal compliance process beyond the use of a conforming conditions provision or state insurance commissioner certification to review individual and unique private insurance policies in terms of the applicability of mandatory acceptance requirements. At the same time, many lenders do not have the personnel or resources to examine unique private flood policies on an individual basis, and therefore should be permitted to reject policies without a compliance aid, provided the institution considered the policy in a manner consistent with its consideration of other forms of hazard insurance.

> ***RECOMMENDATION #4:*** *Compliance Aid for Mandatory Acceptance. The final rule should provide that a flood insurance policy shall be deemed to meet the definition of private flood insurance under the rule if the insurance policy declarations page(s) attests that the policy includes a conforming conditions clause or endorsement that would amend the private flood insurance policy to provide coverage terms at least as broad as the coverage terms of the Standard Flood Insurance Policy if such terms are not as broad under the private flood insurance policy; or, alternatively, if the State insurance commissioner of the state in which the insured property is located certifies or confirms that the private flood insurance policy is "at least as broad" as the Standard Flood Insurance Policy.*
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> *Furthermore, the final rule should provide that institutions may develop appropriate means of confirming that flood insurance policy meets the definition of private flood insurance in the rule, provided that if a policy includes a compliance aid mechanism in accordance with the rule, the policy shall be deemed to meet this definition without further consideration. For purposes of the rule, if an institution determines that a policy does not meet the definition of private flood insurance, and such policy does not include a compliance aid mechanism in accordance with the rule, such determination will be presumed correct, provided that the institution considered the policy in a manner consistent with its consideration of other forms of hazard insurance for the building or property securing the loan.*

Salability of Associated Loans

In addition to providing lenders a standardized means to determine if a policy meets the definition of private flood insurance as it relates to mandatory acceptance, it is important that a lender's requirement to accept a private flood insurance policy under Section 100239 does not impede the ability to securitize the loan. Specifically, in addition to the requirements that your agencies ultimately include in any final rule, a lender would likely be beholden to the requirements of the Government Sponsored Enterprises (GSEs) related to the financial rating of the insurer.[11]

Therefore, it is possible that a lender could be required to accept a private flood insurance policy that would result in the lender having to hold the loan on their books until maturity. As the requirement of a

[11] *See* Part B7-3-01: Property Insurance Requirements for Insurers, of the Fannie Mae Selling Guide; *and* Chapter 8202.1: General property insurance requirements, of the Freddie Mac Single-Family Seller/Servicer Guide

lender to hold these loans on their books for extended periods of time could negatively affect the safety and soundness for the institutions you regulate, your agencies are well within their authority to include a clarifying limitation as it relates to a prudential issue well within your agencies' general regulatory authority.

To ensure that the mandatory purchase requirement under Section 100239 does not have unintended ramifications to a lender, any final rule should include a limitation on the mandatory acceptance requirement to policies offered by insurers the meet the minimum financial rating requirements under the GSEs.

> ***RECOMMENDATION #5****: Mandatory Acceptance. The final rule should provide that lenders must accept private flood insurance, as defined, as satisfaction of the flood insurance coverage requirement, provided that coverage under the flood insurance policy is in the required amount, and that the private insurer meets the applicable minimum financial rating requirements specified by a government sponsored enterprise governing the acceptability of property insurance on loan security.*

Discretionary Acceptance

In certain cases, it may be appropriate for a property owner (both residential and commercial) to obtain coverage with terms that are not the same as the coverage offered under an SFIP. Because of the nature of the individual needs and means of certain property owners, it is important to allow private insurers (in compliance with state insurance laws and regulations) to tailor coverage offered in certain circumstances. That is why under current regulations (and consistent with the policy that your agencies stated in the 2013 rule)[12] lending institutions have the discretion to examine and accept private insurance policies that are compliant to their general requirements to protect the collateralized property used to secure a loan. This is similar to how lenders evaluate other hazard insurance policies, such as homeowners' insurance, when determining if the policy is compliant with safety and soundness principles required by your agencies.

While Section 100239 requires lenders to accept private flood insurance for policies that meet the definition of "private flood insurance," it was never the intent of Congress to alter or eliminate the status quo that authorized lenders, on a discretionary basis, to accept flood insurance outside of a standard flood insurance policy of the NFIP in satisfaction of the mandatory purchase requirement in 12 CFR § 339.3.

Unfortunately, the 2016 Proposed Rule would have altered the current authority of lenders to accept private policies that do not conform to the SFIP on a discretionary basis by imposing burdensome and unnecessary requirements. While it may be justified that lending institutions only accept policies that

[12] 78 Fed. Reg. 210, 65114 (October 30, 2013)

properly secure the collateral used in obtaining a loan, the requirements included in the 2016 Proposed Rule would expand beyond safety and soundness concerns and impede on the role and authorities of State insurance commissioners in the regulation of private insurance and relevant consumer protection. These requirements would directly counter the clear congressional intent of expanding the private flood insurance marketplace by constricting the current marketplace, particularly on commercial lending.

> ***RECOMMENDATION #6:*** *Discretionary Acceptance. The final rule should provide that lenders may accept, or reject, a flood insurance policy issued by a private insurer that is not issued under the NFIP and does not meet the statutory definition of private flood insurance in satisfaction of the flood insurance purchase requirement, if the flood insurance policy is in the proper amount required, and provided the policy covers both the mortgagor(s) and the mortgagee(s) as loss payees (with the exception of a Residential Condominium Building Association Policy), and in the reasonable judgement of the lender, the policy provides sufficient protection of the loan secured by the property located in a special flood hazard area, consistent with the standards and practices used by the lender regarding other property hazard insurance.*

We thank you all for your continued work on this very important issue and would be happy to provide any additional information that you may need as you work to finalize this much anticipated rule.

Sincerely,

American Bankers Association

American Insurance Association

Council of Insurance Agents and Brokers

Independent Community Bankers of America

Independent Insurance Agents and Brokers

National Association of REALTORS®

Property and Casualty Insurers Association of America

Reinsurance Association of America

Wholesale & Specialty Insurance Association