MBa®

MORTGAGE BANKERS ASSOCIATION

October 27, 2020

Office of the Comptroller of the Currency
Chief Counsel's Office
Attn: Comments Processing
400 7th Street SW
Washington, DC 20219
Docket ID OCC-2020-0008

Ann E. Misback, Secretary
Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue, NW
Washington, DC 20551
Docket No. OP-1720

Robert E. Feldman, Executive Secretary
Attention: Comments/Legal ESS
Federal Deposit Insurance Corporation
550 17th St NW
Washington, DC 20429
RIN 3064-ZA16

David P. Grahn, Director
Office of Regulatory Policy
Farm Credit Administration
1501 Farm Credit Drive
McLean, VA 22102-5090
Docket No. FCA RIN 3052-AD42

Gerard P. Poliquin, Secretary of the Board
National Credit Union Administration
1775 Duke Street
Alexandria, VA 22314-3428
NCUA RIN 3133-AF14

**Re: Comments on Proposed Interagency Questions and Answers Regarding Flood Insurance**

Dear Ladies and Gentlemen:

The Mortgage Bankers Association (MBA)[1] respectfully submits these comments on the interagency questions and answers regarding flood insurance (Q&As) proposed by the Office of the Comptroller of the Currency (OCC), the Board of Governors of the Federal Reserve System (Board), the Federal Deposit Insurance Corporation (FDIC), the Farm Credit Administration

[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 to 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 2,300 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.mba.org.

(FCA), and the National Credit Union Administration (NCUA) (the Agencies).[2] We appreciate the Agencies' ongoing efforts to provide clarity on flood insurance requirements, an important component of residential, commercial and multi-family real estate finance.

We recognize the Agencies' long-standing efforts to address these types of challenges for the benefit of institutions and examiners alike through the development and dissemination of detailed Q&As. The Agencies' flood insurance regulations (Regulation) apply across a wide variety of complex lending situations, and the Q&As form a necessary bridge between the Regulation and the real-world situations to which it applies. Rules that may seem clear in general terms often are more complicated in practice, particularly in situations outside of the norm, or involving situations that are not contemplated by the Agencies' examples. Also, applications of the Regulation that may seem clear in single-family lending situations are often far less clear in the context of commercial lending or multifamily transactions.

We developed our comments on the proposed Q&As with the contribution of a substantial working group of lenders, servicers, service providers, and insurance providers that operate at the front lines of the transactions and circumstances to which the Regulation applies. We highlight areas of possible confusion or examples where there is a lack of clarity, and provide additional information about the factual scenarios our members experience, to help institutions and regulators share a common understanding of flood insurance requirements and compliance, across the broad range of circumstances in which they apply. We hope that sharing practical operational perspectives can make the Q&As more effective in communicating and clarifying the application of the Regulation.

Our specific comments below address the following Q&As:

- **Coverage 1, 2, and a proposed new Q&A**
- **Force placement 1, 2, 6, 8 and 10, 9, and 16**
- **Applicability 2, 6, and 9**
- **Zone 1**
- **Notice 1 and a proposed new Q&A**
- **Required Use of Standard Flood Hazard Determination Form (SFHDF) 2**
- **Exemptions 3**
- **Servicing 2**

We would be pleased to follow up on any of our comments with additional information or documentation that might result in additional clarity.

## A. COVERAGE

The comments below respond to proposed Coverage 1 and 2, and we also propose adding an additional Coverage Q&A on deductibles.

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[2] 85 Fed. Reg. 40442 (July 6, 2020); available at https://www.federalregister.gov/documents/2020/07/06/2020-14015/loans-in-areas-having-special-flood-hazards-interagency-questions-and-answers-regarding-flood

### 1. Coverage 1

Coverage 1 addresses factors to consider when determining whether a flood insurance policy issued by a private insurer provides sufficient protection, consistent with general safety and soundness principles. While we have no comment directly on Coverage 1, we note that the Agencies intend to separately release future Q&As relating to the private flood insurance rule.

As the Agencies prepare those future Q&As on the private flood insurance rule, we urge the Agencies to consider that, in practice, a lender will rarely have the actual insurance policy to review prior to closing. Therefore, the evaluation of private flood insurance is necessarily a two-step process. Prior to closing, it is likely possible to conduct only a preliminary evaluation of the policy based on information provided in a declarations page, which is followed by an evaluation of the entire policy after closing.

This practical issue has been recognized in the context of Force Placement 11, which addresses documentation "sufficient to demonstrate evidence of flood insurance in connection with a lender's refund of premiums paid by a borrower for force-placed insurance during any period of overlap with borrower-purchased insurance." As noted in the answer to Force Placement 11, and as stated in the Regulation, "a lender must accept from the borrower an insurance policy declarations page that includes the existing flood insurance policy number and the identity of, and contact information for, the insurance company or its agent." In that circumstance, if the borrower presents a declarations page from a private insurance policy, a lender would need to accept that policy for purposes of refunding premiums associated with a lender-placed policy. Upon receipt of a complete copy of the private policy, however, the lender may determine that the policy should not be accepted.

Applying this same analysis to the review of private flood insurance policies would similarly result in the two-step process discussed above. Prior to closing, the lender could evaluate the declarations page of private flood policy. The required evaluation of the entire policy could then occur after closing.

### 2. Coverage 2

Coverage 2 addresses the use of "portfolio-wide" coverage for compliance with flood insurance purchase requirements.

As an initial matter, the reference to "private insurance policy" in both the question and answer could create unnecessary confusion as to the subject matter addressed by this Q&A. In contrast to borrower procured private flood insurance policies addressed in Coverage 1, this Q&A addresses whether a lender could purchase a flood insurance policy to provide blanket coverage for its portfolio in lieu of either requiring borrowers to obtain their own flood insurance coverage or lender placing a property-specific insurance policy to satisfy the lender's force-placed insurance requirements. We recommend modifying the language in this Q&A to recognize these distinctions.

For example, the Q&A could clarify that it does not address issues specific to borrower-procured private flood insurance policies under the July 2019 private flood insurance rule by substituting "lender's" for "private" in both the question and the answer. While these lender policies may in fact be private flood insurance policies, what makes those policies relevant to this Q&A is the fact that they are lenders' policies and not borrowers' policies.[3]

To further clarify that this answer does not address issues specific to borrower-procured private flood insurance policies under the July 2019 private flood insurance rule, we recommend adding an additional paragraph to the answer similar to the following:

> Lenders are not prohibited from purchasing a lender's master flood insurance policy that provides coverage for its entire portfolio by allowing the lender to obtain loan-level force-placed policies as necessary to comply with the lender's force-placement obligations, as well as the customary gap coverages available under these policies. For example, in a map-in situation where both the lender and borrower learn about the map in after the fact, these lender policies often provide backdated coverage to the map-in date without necessarily needing to issue a loan-level policy for the gap period.

### 3. Additional Coverage Q&A on Deductibles

We understand from our members that the role a deductible plays, or does not play, in determining the amount of coverage required for flood insurance compliance has been a source of confusion. For example, Coverage 1 and Amount 9 address deductibles against standards of safety-and-soundness/sound business practices. The final sentence of Amount 9, however, shifts the focus of the deductible analysis from safety and soundness to the relationship between the deductible and the insurable value of a property as a measure of determining whether the mandatory purchase requirement has been satisfied. We believe that institutions and supervisory personnel would benefit from a new, foundational Q&A that describes the function of a deductible more generally and explains the role of a deductible in a safety-and-soundness consideration rather than discussing deductible as related to adequacy of coverage in satisfaction of the mandatory purchase requirement. To that end, we suggest that the Agencies add a Q&A such as the following:

> **Coverage [NEW]. For purposes of the mandatory coverage requirements, is the amount of coverage provided by a flood insurance policy reduced by the amount of the deductible under that policy?**
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> No. A deductible in a flood insurance policy does not reduce the amount of coverage provided by the policy. Rather, an insurance policy deductible is "a fixed amount of an

[3] With that revision, proposed Coverage 1 would provide as follows:

> **COVERAGE 2. May a lender rely on a ~~private~~ lender's insurance policy providing portfolio-wide coverage to meet the flood insurance purchase requirement or the force placement requirement under the Regulation?**
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> No. A ~~private~~ lender's insurance policy that provides a lender portfolio-wide coverage may provide protection to the lender in certain circumstances. A lender may not use such a portfolio-wide flood insurance policy to satisfy its obligation to ensure the flood insurance purchase requirement is satisfied at the time a loan is made, increased, renewed or extended. For example, ….

insured loss that is the responsibility of the insured and that is incurred before any amounts are paid for the insured loss under the insurance policy."[4] As a result, when determining whether a policy provides the necessary coverage, the lender should consider the coverage limits provided in the flood insurance policy separately from consideration of the deductible contained within that policy.

For example, a property with an estimated insurable value of $100,000 securing a loan with an unpaid principal balance of $50,000 is required to have flood insurance with a $50,000 coverage limit and is permitted to have a $10,000 deductible. The deductible reduces the insured loss payable amount and does not reduce the coverage amount. Thus, in the event of a claim where the loss amount is $50,000, the policy would pay the amount of the loss up to the coverage limit ($50,000) in excess of the deductible ($10,000) or $40,000 ($50,000 - $10,000). In the event of a claim where the loss amount is $15,000, the policy would pay the amount of the loss up to the coverage limit in excess of the deductible, or $5,000 ($15,000 - $10,000). If the property were to sustain a $60,000 loss (of the estimated insurable value of $100,000), the policy would pay the amount of loss up to the coverage limit in excess of the deductible or $50,000 ($60,000 - $10,000). In all events, if the loss payable amount is less than the deductible, no payment would be made by the insurance carrier. Rather, the insured would be solely responsible for that loss.

While a policy deductible is not relevant to a determination of whether a policy provides the necessary coverage limits, lenders should consider the possible safety and soundness impact of the policy deductible. For example, in Coverage 1, a policy's deductible may be a factor a lender considers in determining whether a private policy "provides sufficient protection of a loan." Similarly, as provided in Amount 9, it may not be a sound business practice to always allow the maximum deductible.

## B. FORCE PLACEMENT

Our comments below address Q&As Force Placement 1, 2, 6, 8 and 10, 9, and 16.

### 1. Force Placement 1

Q&A Force Placement 1 asks: "What is the requirement for the force placement of flood insurance under the Act and the Regulation?" The answer appropriately begins by identifying the time "when a lender makes a determination that the collateral securing the loan is uninsured or underinsured," as the event that triggers a requirement to begin the force-placement process. This starting point is consistent with the underlying Regulation cited in the answer. The use of the term "determination" establishes a reference point that lenders can use to develop procedures to reasonably ensure compliance with the force-placement requirements.

[4] The Federal Emergency Management Agency (FEMA) defines "deductible" as "The fixed amount of an insured loss that is the responsibility of the insured and that is incurred before any amounts are paid for the insured loss under the insurance policy." Available at: https://www.fema.gov/national-flood-insurance-program/definitions.

The final sentence of the answer, however, departs from that language, referring to a situation where a lender "is aware":

> In addition, before the lender or servicer must force place flood insurance, if the lender or servicer is aware that a borrower has obtained insurance that otherwise satisfies the flood insurance requirements but in an insufficient amount, the lender or servicer should inform the borrower an additional amount of insurance is needed in order to comply with the Regulation.

This part of the Q&A would better facilitate compliance procedures if it were recast by reference to "a determination" rather than "an awareness."[5] We recommend that the agencies replace "awareness" with "a determination."

2. **Force Placement 2**

Force placement 2 addresses the timing for sending the force-placement notice to the borrower. The answer indicates that the Agencies expect that such notice will be provided to the borrower at the time of determination of either no coverage or insufficient coverage, allowing only for a "brief delay" supported by a "reasonable explanation" for the delay. The answer gives an example of a reasonable explanation where the lender uses "batch processing" to send the force-placement notice.

Our members have indicated that, through the examination process, they have experienced varying interpretations among the Agencies (and even within the same agency) and their examiners on what constitutes a "brief delay" and what is a "reasonable explanation" for the delay.

From an operational stand point, following the lender's determination of no coverage or insufficient coverage, and during the 45-day notice period, the lender's force-placed insurance policy will provide coverage as of the date of a lapse in coverage or insufficient coverage, regardless of when the notice is actually provided to the borrower.

We also understand from our members the industry practice is to provide the amount of coverage required on the notice to the borrower and determining this amount of coverage may take some time in certain circumstances. For example, while it may not take long to determine the amount of coverage needed in a residential loan scenario where the loan is secured by one property with one building, the same is not true for complicated commercial loans secured by multiple properties and buildings.

Based on how this answer may be interpreted, a lender may feel compelled to rush a notice to the borrower that contains insufficient or inaccurate information solely to ensure technical compliance. Instead, we recommend that the Agencies allow sufficient time for lenders to prepare

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[5] For example, that sentence might be revised to read as follows: "In addition, if a lender's or servicer's determination that the collateral securing the loan is underinsured is based on a determination that a borrower has obtained insurance that otherwise satisfies the flood insurance requirements but in an insufficient amount, the notice of force placement should inform the borrower that an additional amount of insurance is needed in order to comply with the Regulation."

accurate and helpful notices to borrowers, recognizing the potential operational difficulties that could arise. For example, instead of the phrase “brief delay,” we suggest the phrase “reasonable delay.” In addition, we suggest adding the following to the batch processing example: “batch processing or the operational time necessary to determine the amount of coverage required, and to prepare and send the notice, based on the particular facts and circumstances of the loan.”

### 3. Force Placement 6

In Force Placement 6, the Agencies propose a new Q&A describing a situation in which a lender makes two different determinations regarding lapse or insufficiency of flood insurance coverage. Specifically, the Q&A describes a lender who (1) makes a determination a designated loan has no or insufficient flood insurance coverage and sends the borrower a force-placement notice beginning the 45-day notice cycle; and (2) the lender then makes a subsequent determination, within that 45-day notice cycle, that the designated loan has no or insufficient coverage. In the answer, the Agencies advise that once a lender makes a determination that a loan has no or insufficient coverage, if the borrower does not cure that lapse of insufficiency, the lender must force place within 45 days of the initial determination. The answer does not address the effect of the lender’s “subsequent determination.”

A specific example can illustrate the issue. Assume a lender makes a determination that a designated loan has no flood insurance in place and requires $150,000 in coverage limits. The lender notifies the borrower of the lapse and initiates the 45-day letter cycle. On day 20 of that 45-day cycle, the borrower provides the declarations page of a flood insurance policy with limits of only $100,000. The lender then makes a “subsequent determination” that, while the designated loan may now be covered by a flood insurance policy, that coverage amount is insufficient. In proposed Force Placement 6, the Agencies conclude that the “subsequent determination” does not require the initiation of a new 45-day notice cycle.

This conclusion is inconsistent with the Flood Disaster Protection Act (FDPA) and answers to other Force Placement Q&As, which suggest that each “determination” triggers its own 45-day notice cycle. The FDPA is specific that a lender’s determination of lapse or insufficiency may occur “at any time” during the term of the loan.[6] The Act requires that following such “determination” the lender “shall notify the borrower” of the steps the borrower should take to cure the lapse or deficiency.[7] Thus, under the Act, the 45-day notice cycle follows a determination of lapse or insufficient coverage. Similarly, in the responses to Force Placement questions 2 and 4, the Agencies advise that a lender cannot notify a borrower of a lapse or deficiency prior to the lender’s determination of such lapse or deficiency. In Force Placement Q&A 4, the Agencies advise that a lender may not initiate the 45-day notice cycle in anticipation of an insufficiency in coverage. Rather, the lender must first make a determination of lapse or insufficiency and then notify the borrower of that determination.

[6] 42 U.S.C. § 4012a(e)(1).

[7] Id.

In contrast, the response in proposed Force Placement 6 suggests that a "subsequent determination" of lapse or insufficiency, if made during a 45-day notice cycle, should be treated differently than a determination made at any other time during the term of the loan. If in fact the Agencies are advising that a borrower for a designated loan is limited to a single-45 day notice period following an initial determination of lapse or insufficiency of coverage, regardless of any intervening efforts by the borrower to cure that lapse or insufficiency, we would request that the Agencies state so clearly and afford the industry a reasonable time to adapt to this guidance. In addition, as this would be newly communicated guidance, we would request that the Agencies look to apply this interpretation on a prospective basis only, after allowing time for lenders to revise notices, adjust operational practices, and examine additional controls and measures that may be necessary.

**4. Force Placement 8 and 10**

The relationship between premiums and fees arising from force placing flood insurance and the amount of required force placed insurance is addressed both in Force Placement 8 and 10.

> **Force Placement 8. When force placement occurs, what is the amount of insurance required to be placed?**
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> **Force Placement 10. Does adding the flood insurance premium to the outstanding loan balance constitute a triggering event- an ''increase'' that would trigger the applicability of flood insurance regulatory requirements?**

For convenience, we discuss them in reverse order.

The Q&A Force Placement 10 uses the phrases "outstanding loan balance," "existing mortgage loan balance," "additional debt to be secured by the building," "loan amount" and "part of the loan" interchangeably. For example, Force Placement 10 asks about adding flood insurance premiums to the "outstanding loan balance."

The answer to Force Placement 10 describes three methods that a lender might use to charge a borrower for force-placed insurance. The first method describes where the lender adds the premium and fees to the "existing mortgage loan balance." Under this method, if the lender's loan contract with the borrower includes a provision permitting the lender or servicer to advance funds to pay for flood insurance premiums and fees as "additional debt to be secured by the building or mobile home," the answer concludes that such advancement becomes "part of the loan" and thus these premiums and fees would not increase the "loan amount" and would not be a triggering event.

This is contrasted with the two other methods, in which premiums and fees are either (a) not "part of the loan" where they are accounted for in a "separate unsecured account" or (b) billed directly to the borrower. The Agencies conclude that neither of these methods is a triggering event. In short, the Answer to Force Placement 10 appears to assume that where the contract permits the advance of premium and fees to be secured that those premiums and fees are necessarily added to the outstanding principal balance of the loan. From an operational standpoint, however, this is not the case.

Both the Act and the Regulation require the lender to consider the "outstanding principal balance" of the loan when determining the amount of flood insurance required. The outstanding principal balance of a loan is distinct from the other amounts that might be due and owing on the loan, such as accrued interest, advances, and fees. Operationally, outstanding principal balance, interest, advances, and fees are distinct and separate concepts for legal and accounting purposes, as well as for flood compliance purposes.

In light of this, and to provide clarity on the issue for all stakeholders, we recommend referencing uniform security instruments in residential lending to demonstrate how these governing documents address additional debt that is secured by the property. For example, Section 5 of the Fannie Mae/Freddie Mac Uniform Security Instrument provides:

> [a]ny amounts disbursed by Lender under this Section 5 shall become additional debt of Borrower secured by this Security Instrument. These amounts shall bear interest at the Note rate from the date of disbursement and shall be payable, with such interest, upon notice from Lender to Borrower requesting payment.

This contractual provision allows the lender to advance premiums for flood insurance and provides that such advancements "become additional debt" of the borrower. Within the industry, this additional debt is not typically added to the outstanding principal balance of the loan but is instead accounted for in a separate advance or escrow account. While it may be accurate to say that these premiums and fees are part of the "part of the loan," it does not necessarily mean they are part of the loan's outstanding principal balance.

To avoid confusion, we would propose revising Force Placement 10 as follows:

> **Force Placement 10. Does ~~adding the~~ advancing a flood insurance premium ~~to the outstanding loan balance~~ constitute ~~a triggering event~~ an ''increase'' that ~~would~~ trigger the applicability of flood insurance regulatory requirements?**
>
> The Act and the Regulation require a lender to notify the borrower that the borrower should obtain adequate flood insurance when the lender determines that a building or a mobile home located or to be located in a Special Flood Hazard Area is not covered by any or adequate flood insurance. If the borrower fails to obtain adequate flood insurance within 45 days, then the lender must purchase insurance on the borrower's behalf. The lender may charge the borrower for the premiums and fees incurred by the lender in purchasing the force-placed flood insurance.
>
> Among the various methods that a lender might use to ~~charge a borrower for~~ recoup the cost of force-placed flood insurance from the borrower are: (1) ~~Adding~~ accounting for the premium and fees by adding them to the ~~existing mortgage loan~~ outstanding principal balance of the loan; (2) ~~adding~~ accounting for the premium and fees as a separate advance; or (3) billing the borrower directly for the premiums and fees of the force-placed flood insurance. The treatment of force-placed flood insurance premiums and fees depends on the method the lender chooses for charging the borrower.

Premium and Fees Added to ~~Mortgage Loan~~ Outstanding Principal Balance

If the lender's loan contract with the borrower includes a provision permitting the lender or servicer to advance funds to pay for flood insurance premiums and fees and add them to the loan's outstanding principal balance, such an advancement ~~would be considered part of the loan. As such, the addition of the flood insurance premiums and fees to the loan balance~~ is not considered an ''increase'' in the loan amount, and thus would not be considered a triggering event. If, however, there is no explicit provision permitting this type of advancement of funds in the loan contract, the addition of flood insurance premiums and fees to the ~~borrower's loan~~ outstanding principal balance of the loan would be considered an ''increase'' in the loan amount, and, therefore is considered a triggering event because ~~no advancement~~ the addition of advanced funds to the outstanding principal balance was not contemplated as part of the loan. (See also Q&A Force Placement 8).

Accounting for Premium and Fees as a Separate Advance

If the lender's loan contract with borrower includes a provision permitting the lender or servicer to advance funds to pay for flood insurance premiums and fees as additional debt to be secured by the building or mobile home but accounted for as a separate advance (i.e., the advanced amounts are not added to the outstanding principal balance of the loan), this approach does not result in an increase in the loan balance and, therefore, is not considered a triggering event.

Premium and Fees Billed Directly to Borrower

If the lender bills the borrower directly for the cost of the force-placed flood insurance, ~~this approach does~~ there is not an increase in the outstanding principal balance of ~~the loan balance~~ and is not considered a triggering event.

To conform Force Placement 8 to a revised Force Placement 10, we would recommend that Force Placement 8 be revised. This includes revising the language in proposed Force Placement 8 that would require a lender to "anticipate" that a premium for lender placed flood insurance will increase the outstanding principal balance of the loan. The proposed answer would require a lender to obtain a lender placed policy with coverage limits of $202,000 where a $2,000 premium would be added to the outstanding balance of the loan, increasing that balance to $202,000.

Requiring a lender to "anticipate" how a lender placed premium may affect the outstanding principal balance of a loan presents operational issues for lenders and servicers. For example, the lender's correspondence to the borrower would have advised that the borrower must procure flood insurance in the amount of $200,000. If the borrower subsequently provides proof of insurance for $200,000, but the outstanding balance of the loan is now $202,000 due to the addition of the flood insurance premium, must the lender reject the borrower's $200,000 policy as insufficient triggering a new lender placed notice cycle?

Similarly, to the extent there is an overlap in borrower procured coverage and lender placed coverage, the refund of any lender placed premium would create a new outstanding balance to which the lender must ensure adequate flood coverage is available. In addition, including the lender placed premium in the coverage amount calculation will create a mathematical and data processing issue in which the premium amount and outstanding loan balance will be ever increasing on an incremental basis.

To avoid the operational issues created by this scenario, recommend that the proposed answer be revised as set forth below to allow the lender to determine coverage limits based on the outstanding principal balance of the loan at the time the lender placed policy is procured rather than to "anticipate" or predict how the premium may affect the outstanding balance of the loan at a later, undetermined, date.

> **Force Placement 8. When force placement occurs, what is the amount of insurance required to be placed?**
>
> The Regulation states that the minimum amount of flood insurance required "must be at least equal to the lesser of the outstanding principal balance of the designated loan or the maximum limit of coverage available for the particular type of property under the Act."
>
> As discussed in Force Placement 10, there are different methods a lender may choose to charge a borrower for lender placed insurance premiums, depending on its loan contract with the borrower. A lender may add the advanced amounts to the outstanding principal balance of the loan where permitted by the loan contract. Alternatively, a lender may account for the force-placed flood insurance premium and fees in a separate advance account but not add the advanced amounts to the outstanding principal balance of the loan. The amount of flood insurance required to be placed is determined by the outstanding principal balance of the loan.
>
> To illustrate this point, assume that there is a loan with an outstanding principal balance of $200,000, secured by a residential property located in a special flood hazard area that has an insurable value of $350,000. The borrower has a $200,000 flood insurance policy for that property, reflecting the minimum amount required under the Agencies' regulations. If the $200,000 flood insurance policy lapses, the lender, or its servicer must notify the borrower of the need to obtain adequate flood insurance. If the borrower fails to obtain adequate flood insurance within 45 days after notification, then the lender or its servicer must purchase insurance on the borrower's behalf.
>
> If the lender's contract with the borrower permits the lender to add the premium for the force-placed policy to the outstanding principal balance of the loan, the lender must ensure that the policy is issued in an amount sufficient to cover the principal balance as of the date the lender placed policy is in force. Thus, in the scenario described above, the coverage amount of the force-placed policy must be at least $200,000 because that is the outstanding principal balance of the loan at the time the flood insurance is required to be placed.

**5. Force Placement 9**

The last sentence of the answer to Force Placement 9 currently states:

> When a lender or its servicer purchases a policy on the borrower's behalf, the lender or its servicer may not charge for premiums and fees for coverage beginning on the date of lapse or insufficient coverage if that policy purchased on the borrower's behalf did not provide coverage for the borrower prior to purchase.

As we discuss below, the phrase "prior to purchase" in the proposed answer appears to conflict with the final rule on lender placement and is not consistent with industry practice of lender placement.

In addition, by interchanging the concepts of "effective date" and "prior to purchase," the proposed answer to Force Placement 9 appears to conflict with the final rule. In the final rule implementing provisions of Biggert-Waters related to lender placement, the Agencies identified the importance of a policy's "effective date" when they "interpret[ed] Biggert-Waters to permit a regulated lending institution to force place a flood insurance policy purchased on behalf of a borrower that is effective the day after expiration or lapse of a borrower's original insurance policy to ensure continuous coverage." (emphasis added).[8] In that rulemaking, the Agencies acknowledged that such "continuous insurance coverage . . . protect[s] both the borrower and the institution."[9] To ensure such continuous coverage, the Agencies provided that, when an institution discovers a policy with insufficient coverage, "the institution may charge back to the date of insufficient coverage provided the institution has purchased a policy that covers the property for flood loss and that policy was effective as of the date of insufficient coverage."

We note also that the phrase "effective date" used in the final rule implementing Biggert-Waters provisions related to lender placement also aligns with insurance practices within the industry. In general, an insurance policy, by nature of the contractual language, only provides coverage once it is purchased. Therefore, no policy will provide coverage "prior to purchase." Lender-placed policies, however, can provide coverage with an "effective date" that precedes the date the property specific policy is issued. This coverage is obtained through a master agreement between the lender and insurance carrier under which property specific policies are issued in the event of a lapse or insufficiency in coverage. In short, the lender is able to obtain the issuance of a property-specific policy through a lender's master agreement with the carrier that provides an effective date back to the date of lapse or insufficiency of coverage. The borrower is then charged for the coverage that is provided by that property specific policy as of the "effective date" of the policy.

To ensure consistency with the Agencies' final rule on force-placement as well as to comport with industry operational practices, we propose the following language be substituted for the last sentence in the proposed answer to Force Placement 9:

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[8] 80 Fed. Reg. 43216, 43233 (July 21, 2015).

[9] Id.

When a lender or its servicer purchases a policy on the borrower's behalf, the lender or its servicer may charge for premiums and fees for coverage beginning on the effective date of that coverage.

**6. Force Placement 16**

Force Placement 16 addresses a situation in which a lender or servicer receives a notice of remapping that states a property "will be remapped into an SFHA as a future effective date." We are concerned that this question, as phrased, does not reflect the current operational reality for lenders and servicers in which lenders and servicers typically receive such notification only after the map effective date and do not receive advance notice of proposed map changes. As the Agencies note in the proposed answer, a loan secured by a property to be remapped into the SFHA "does not become a designated loan **until the effective date of the map change**" (emphasis added). A lender has no flood compliance obligations until there is a designated loan.

Further, there are instances in which re-mappings do not occur as scheduled. Therefore, to avoid the possibility of confusion, servicers act only upon receipt of a notice of remapping after the map effective date. Requiring a borrower to have adequate flood insurance in place back to the effective date of the remapping could result in a situation in which the lender force-places an insurance policy to a date in the past that will not provide any benefit to the borrower or the lender. Our members have also told us that the Agencies' examiners offer different interpretations or approaches on this issue. While advance notification of a future flood map change might be useful for a lender or servicer for reasons other than compliance, we propose a revised question and answer for Force Placement to provide clarity and consistency regarding compliance obligations, 16 as follows:

**Force Placement 16. When a lender or its servicer receives a notice of remapping that states that a property has been remapped into an SFHA, what do the Act and Regulation require the lender or its servicer to do?**

The Act and Regulation provide that if a lender, or its servicer, determines at any time during the term of a designated loan, that a building or mobile home and any personal property securing a loan is uninsured or underinsured, the lender or its servicer must begin the notice and force-placement process, as detailed in Q&A Force Placement 1. A loan that is secured by property that was not located in an SFHA does not become a designated loan until the effective date of the map change, remapping the property into an SFHA. Frequently, however, a lender is unaware a property has been mapped into a SFHA until after the effective date of the map change. Therefore, when a lender or its servicer receives notice that a property has been remapped into an SFHA, the date the lender notifies the borrower of that map change is the date on which the lender or its servicer must determine whether the property is covered by sufficient flood insurance. If the borrower does not purchase a flood insurance policy within 45 days of the date of the notice of the map change, the lender or its servicer must force-place adequate flood insurance.

## C. APPLICABILITY

The comments below respond to proposed Applicability 2, 6, and 9.

### 1. Applicability 2

The Agencies and financial institutions have struggled to determine the appropriate treatment under the Regulation of low-value buildings that are part of a multi-building parcel of land that secures a loan, but that are not material to the lending transaction. On the one hand, the Regulation provides that the institution shall not make, increase, extend, or renew any designated loan unless the building or mobile home and any personal property securing the loan is covered by flood insurance for the term of the loan. On the other hand, it is an economic waste for a lender to require a borrower to protect that lender by purchasing flood insurance on buildings whose value is not material to the financial institution's risk of loss from flood or mudslide damage.

Currently, Applicability 2 addresses these conflicting principles as follows:

> **Applicability 2. Some borrowers have buildings with limited utility or value and, in many cases, the borrower would not replace them if lost in a flood. Must a lender require flood insurance for such buildings?**
>
> Lenders must require flood insurance on a building or mobile home when those structures are part of the property securing the loan and are located in an SFHA in a participating community. However, flood insurance is not required on a structure that is part of a residential property but is detached from the primary residential structure of such property and does not serve as a residence.
>
> If the limited utility or value structure does not qualify for the detached structure exemption, a lender may consider ''carving out'' the building from the security it takes on the loan to avoid having to require flood insurance on the structure. However, the lender should fully analyze the risks of this option. In particular, a lender should consider whether and how it would be able to market and sell the property securing its loan in the event of foreclosure.[10]

This long-standing Q&A, even as revised, acknowledges the safety-and-soundness impacts on any institution that uses this approved "carve-out" approach, warning institutions that removing individual buildings from a security instrument could impair the ability "to market and sell the property securing its loan in the event of foreclosure." In effect, the financial institution has the choice of (1) requiring borrowers to purchase insurance that is of no material benefit to the transaction; or (2) avoiding that requirement through an approach that may increase the potential loss severity upon default for the loan. In either case, the lender can achieve technical compliance with the flood insurance purchase requirement in ways that serve no other purpose.

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[10] 85 Fed. Reg. at 40455 (footnotes omitted; spacing between second and third sentences of answer added for clarity of discussion).

We suggest an alternative "carve-out" approach, which we believe can enable lenders to achieve technical compliance with the purchase requirement in a way that also serves the underlying purpose of the requirement, as follows.

> **Applicability 2. In some cases where a property securing a loan contains multiple buildings, a lender may prudently exclude value of some of those buildings when underwriting the credit risk of the loan and determining the adequacy of collateral where the value of those buildings in not material to the lender's credit risk. Must a lender require flood insurance for such buildings?**
>
> As a general matter, lenders must require flood insurance on a building or mobile home when those structures are part of the property securing the loan and are located in an SFHA in a participating community. However, flood insurance is not required on a structure that is part of a residential property but is detached from the primary residential structure of such property and does not serve as a residence.
>
> In some cases, a parcel of property securing the loan may include multiple buildings that do not qualify for the detached structure exemption. Where the lender prudently determines that the value of only a subset of buildings located on that parcel is sufficient to establish the adequacy of the collateral for the loan, the lender may consider "carving out" the value of any other structures from the underwriting. The lender may nevertheless determine to include all buildings in the security instrument as a matter of convenience in closing the loan and in marketing the parcel of land if necessary.
>
> While the Regulations require that any building securing a loan be covered by flood insurance for the term of the loan,[11] the underlying purpose of the flood insurance requirement on depository institutions is to reduce economic distress to depository institutions caused by their exposure to potential flood and mudslide damage.[12] Therefore, buildings that are included as security for a loan as a matter of convenience, and not to protect the lender by providing material credit support for the loan, are not considered to be buildings "securing the loan" that need to be covered by flood insurance. Specifically, where lender documentation demonstrates that the lender did not rely upon the value of particular buildings when underwriting the loan, the excluded buildings need not be

[11] See, e.g., 12 C.F.R. § 22.3 ("Requirement to purchase flood insurance where available. (a) In general. A national bank or Federal savings association shall not make, increase, extend, or renew any designated loan unless the building or mobile home and any personal property securing the loan is covered by flood insurance for the term of the loan.").

[12] See 42 U.S.C. § 4001(a) ("The Congress finds that … from time to time flood disasters have created personal hardships and economic distress which have required unforeseen disaster relief measures and have placed an increasing burden on the Nation's resources …."); see also 42 U.S.C. § 4002(a)(4) ("The Congress finds that … Federal instrumentalities insure or otherwise provide financial protection to banking and credit institutions whose assets include a substantial number of mortgage loans and other indebtedness secured by property exposed to loss and damage from floods and mudslides ….).

> covered by flood insurance, even where they are nominally covered by an instrument securing the loan.
>
> Alternatively, where the lender did not rely upon the value of a building when underwriting the loan, a lender may consider ''carving out'' the building from the security it takes on the loan to avoid having to require flood insurance on the structure. However, the lender should fully analyze the risks of this option. In particular, a lender should consider whether and how it would be able to market and sell the property securing its loan in the event of foreclosure.

We recognize that this recommendation may be a departure from how the Agencies have historically viewed the issue of how to treat structures whose value is of no material importance to the lending transactions, and we urge the Agencies to use the process of considering comments on the proposed Q&As to consider this or other alternative approaches.

### 2. Applicability 6

Applicability 6, which is not a new Q&A, addresses how the flood regulations apply to loans that are being restructured or modified. In light of the anticipated volume of loan modifications that will continue to occur in response to the COVID-19 pandemic, and to provide greater clarity about the types of restructurings and modifications that trigger flood compliance, we request that the answer to this Q&A be expanded to address common types of restructuring or modifications and whether they trigger flood compliance. For example, the following paragraphs could be added to the answer:

> Where a loan modification or restructuring involves recapitalizing delinquent payments and other amounts due under the loan, or amounts that were otherwise originally contemplated to be part of the loan, into the loan's outstanding principal balance and the maturity date of the loan otherwise stays the same, this restructuring would not trigger flood compliance because the lender did not make, increase, renew or extend the terms of the loan.
>
> In contrast, where the loan modification or restructuring changes terms of the loan such as by increasing the principal balance beyond what was contemplated as part of the loan or by extending the maturity date of the loan, this restructuring would trigger flood compliance because the lender increased or extended the terms of the loan beyond what was originally contemplated to be part of the loan.

### 3. Applicability 9

While Applicability 9 is a long-standing Q&A, our members inform us that there is often an inconsistent approach among lenders in these lending arrangements with respect to "upfront due diligence" and "adequate controls to monitor the activities of the lead lender or agent for compliance with flood insurance requirements over the term of the loan."

Applicability 9 indicates that the Agencies will hold participating lenders individually responsible for compliance even in situations where, under the structure of the transactions, the member lacks the authority, or even the ability, to ensure flood compliance. For example, in some transactions, a participating lender may not have the authority in the lending arrangement to lender place flood insurance in the event of a lapse or insufficiency or may even be unaware of a lapse or insufficiency. In such situations, each regulated lender who participates in the transaction could be held individually responsible for ensuring flood compliance when that lender lacks the operational ability to do so.

To clarify what is expected of regulated institutions in these lending arrangements, we suggest the following be added as new paragraphs to the answer to this Q&A:

> With respect to the performance of upfront due diligence and having adequate controls to monitor the activities of the lead lender or agent over the term of the loan, the Agencies expect participating lenders to have written policies, procedures and processes that are commercially reasonable under the circumstances. Where the lead lender or agent is a regulated institution subject to federal flood compliance requirements, the Agencies expect the participating lender to confirm that the lead lender or agent has established written policies and procedures for flood compliance prior to entering into the lending arrangement. While the participating lender is not expected to duplicate the flood compliance of the lead lender or agent, the Agencies expect the participating lender to have controls to confirm that the lead lender or agent is complying and will comply with flood requirements over the term of the loan.
>
> In contrast, where the lead lender or agent is not an institution subject to flood compliance requirements, the commercial reasonableness of the upfront due diligence and controls over the term of the loan may be different. The participating lender may need to perform greater upfront due diligence before entering the lending facility to confirm that the lead lender or agent is capable of compliance with flood requirements. Similarly, the participating lender may need greater controls to ensure that the lead lender or agent is complying and will comply with flood requirements over the term of the loan.
>
> As long as a participating lender has adopted written policies, procedures, and processes for flood compliance when participating in these lending arrangements, a participating, non-lead, lender will not be examined as if they are the lead lender or had made the loan themselves. Rather, the participating lender will be examined for flood compliance only to the extent any flood compliance issues that arise in the lending arrangement are within the reasonable control of that participating lender. For example, where a participating lender does not have the authority in the lending arrangement to lender place insurance in the event of a lapse or insufficiency (or is unaware of a lapse or insufficiency), the participating lender will not be criticized for the failure of the lead lender to place insurance. In such a circumstance, so long as the participating lender has adopted written policies and procedures for managing the risks that are reasonably within that participating lender's control, that lender generally would be viewed as having satisfied its flood compliance obligations.

## F. ZONE

### Zone 1

Zone 1 asks, "What should a lender do when there is a discrepancy between the flood hazard zone designation on the flood determination form and the flood insurance policy?" The answer describes a situation in which a lender or its servicer identifies a flood zone discrepancy at the time of loss, and it identifies two alternative approaches to resolving that discrepancy: (1) the borrower keeps the contracted coverage limits if an additional premium is paid; or (2) the borrower does not pay the additional premium and the lender must proceed with force-placement procedures.

The answer seems to imply—whether intentionally or not—that the resulting underpayment must be resolved at the time of the loss for the policyholder to receive claim payment up to the amount of the contracted coverage limits at the time of the flood loss. The answer also suggests that the policy coverage to settle the active claim will be reduced by an amount commensurate to the underpaid premium unless the servicer initiates force-placement procedures to obtain additional premium amount and thereby maintains the contracted coverage limits.

Those implicit assumptions do not accurately reflect NFIP guidelines and claim handling practices. Under current guidelines, the active claim in this situation would be settled based upon the contracted coverage limits at the time of the flood loss, and the NFIP would initiate procedures to (1) determine the actual premium for the amount of flood insurance coverage based upon the accurate flood zone, and (2) request this additional premium be paid.

We believe the answer can more accurately apply the regulatory requirements to the factual context in which they will apply by revising the answer to acknowledge that there may be other alternatives. For example, a lender could advance the funds necessary to pay the additional premium where permitted by the security instrument. This third alternative would provide the coverage necessary for the lender to satisfy its statutory and regulatory obligations. Specifically, in addition to revising the answer to be consistent with NFIP guidelines and with force placement practices, we recommend replacing the language in the third paragraph of the answer with language similar to the following:

> If the borrower does not pay the additional premium, the result going forward could be inadequate coverage. In that situation, if the security instrument permits the lender to advance the funds necessary to pay the additional premium, the lender may advance the funds necessary to pay the additional premium. Otherwise, lenders must proceed with force-placement procedures when the lender determines there is inadequate coverage.

Further, as we indicated in our comments on Force Placement 6 above, we recommend the Agencies clarify that a lender or servicer must first make a determination that flood insurance is inadequate before initiating the force-placement process. Such a determination can occur only after the lender or servicer receives notice or documentation regarding the reduced amount of coverage.

## G. NOTICE

### 1. Notice 2.

Notice 2 addresses a lender's obligation to provide a Notice of Special Flood Hazards and advises that, "[i]f a lender determines that a mobile home securing a designated loan will be located in an SFHA just prior to closing, the lender may need to delay the closing until the Notice of Special Flood Hazards has been provided in accordance with the Regulation."

The previous version of this Q&A (Q&A 74) afforded the lender flexibility to provide the Notice of Special Flood Hazards to the borrower "as soon as practicable after determination that the mobile home will be located in an SFHA," and it further provided that "lenders should use their best efforts to provide adequate notice of flood hazards to borrowers" as early as possible.

From an operational standpoint, it may not always be possible to determine where on a property a mobile home will be located until after the loan is closed and the mobile home is delivered to the property. The prior response to this question allowed lenders the flexibility to incorporate their flood insurance compliance into the realities experienced in their business operations. We recommend that the Agencies revised Notice to retain the flexibility provided in the prior version of this Q&A.

### 2. Additional Notice Q&A

In the supplementary information to the July 21, 2009 Interagency Questions and Answers Regarding Flood Insurance, the Agencies indicated that they generally consider 10 days before loan closing as a "reasonable" time interval within which to provide the Notice of Special Flood Hazards to the borrower.[13] We understand from our members that their examiners often refer to this time frame during examinations and many of our members manage to this time frame in their operations. While a 10-day notice period is not a precise requirement of the Regulation, because the 10-day period appears to be a well-established and generally accepted time period, we recommend a new Q&A to memorialize this guidance, for example, in the following Q&A:

> **Notice [NEW]. When should a lender provide the Notice of Special Flood Hazards to the borrower?**
>
> As required by the Regulation, lenders must provide a Notice of Special Flood Hazards to the borrower within a reasonable time before completion of any transaction requiring the notice, such as a loan closing. What constitutes "reasonable" notice will necessarily vary according to the circumstances of particular transactions. Borrowers should receive notice timely enough to ensure that (1) the borrower has the opportunity to become aware of the borrower's responsibilities under the NFIP and (2) the borrower can purchase flood insurance before completion of the transaction. As a general matter, the Agencies

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[13] 74 Fed. Reg.35914, 35930 (July 21, 2009).

consider 10 calendar days before loan closing as a “reasonable” time interval within which to provide the Notice of Special Flood Hazards to the borrower.

## H. REQUIRED USE OF STANDARD FLOOD HAZARD DETERMINATION FORM (SFHDF)

### SFHDF 2

CFHDF 2 asks “May a lender provide the SFHDF to the borrower?” The proposed answer responds to that question, but it also introduces the separate topic of the FEMA process for a Letter of Determination Review (LODR), which is outside of the scope of the Question. For clarity and simplicity, we recommend eliminating that second topic by removing the language that follows the first sentence of the answer. If the Agencies determine there is a need to also incorporate the LODR process into the Q&A, we recommend that that topic be incorporated in a separate Q&A devoted solely to that topic.

In addition, for simplicity and clarity, we also recommend that the answer remove the language “so they can better understand their flood risk” to remove any suggestion that a lender must consider a borrower’s intended use of, or possible benefit from, a flood determination before sharing it with a borrower.

> Yes. Although not a statutory requirement, a lender may provide a copy of the flood determination to the borrower~~ so they can better understand their flood risk~~.[14]

## I. EXEMPTIONS

### Exemptions 3

Exemptions 3 provides guidance as to the relationship between the need to obtain a flood hazard determination for a parcel of property and the separate determination of whether any structures on a parcel of property might be exempt from the flood insurance purchase requirement.

> **Exemptions 3. Do detached structures require a flood hazard determination to be performed even if coverage is not required?**
>
> Because a flood hazard determination is often needed to identify the number and types of structures on the property, conducting a flood hazard determination remains necessary for the lender to be able to comply with the flood insurance requirements.

In practice, lenders first obtain a flood hazard determination as to the entire parcel of property to determine if there is a “designated loan” (i.e., “a loan secured by a building or mobile home that

[14] Further, we do not want a borrower to conclude that a property is not in fact subject to flood risk if a SFHDF states the property is not in a SFHA given that flooding in fact also occurs outside of the SFHA. We hope a borrower in this situation would discuss flood risk and the need for flood insurance with his or her insurance agent.

is located or to be located in a special flood hazard area in which flood insurance is available under the Act"[15]). If the property is within a SFHA, the lender then determines whether any detached structure on that property may be exempt under the Regulations, e.g., a detached garage that does not serve as a residence that is part of a single-family residential property. If a property is not located within a SFHA, the property is not subject to the Act and its implementing regulations and the detached structure analysis is inapplicable.

While this practice is reflected in the answer above, the question appears to imply that the presence or absence of exempt structures may affect whether a flood hazard determination is required. To avoid confusion and to better reflect the standard practice, we suggest the question and answer in Exemptions 3 be recast as follows:

> **Exemptions 3. Is a flood hazard determination required even where the secured property may contain detached structures for which coverage is not required under the Regulation?**
>
> Yes. A flood hazard determination is needed to determine whether there is a designated loan. Once there is a designated loan, that designated loan can then be analyzed for any exemptions. Thus, to determine whether the exemption for non-residential detached structures on residential property may apply, a flood hazard determination must be conducted first, without regard to whether there may be any detached structures that could be exempt.

## J. SERVICING

### Servicing 2

Servicing 2 addresses the question of when a lender must provide notice to FEMA or its designee when that lender will be the servicer of the loan. We recommend that the answer to this question be modified to clarify that this notice does not apply where the flood insurance policy involved is a private flood insurance policy. There appears to be no reason to notify FEMA or its designee that the lender is the servicer of the loan when the property securing the loan is not insured by an NFIP policy.

* * *

MBA supports the Agencies' commitment to provide clear and articulate guidance as it relates to implementation of the Flood Act, and we appreciate the opportunity to participate in this process. We hope the Agencies find these comments to be helpful.

[15] See, e.g., 12 C.F.R. § 339.2 (definition of "designated loan").

We would be pleased to provide any additional information the Agencies might find helpful or to respond to questions about any of these comments.

Sincerely,

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