National Flood
Determination Association

May 7, 2008

Board of Governors of the Federal Reserve System
20th Street and Constitution Avenue, NW
Washington, DC 20551
Via email at regs.comments@federalreserve.gov

Re: Docket No. OP–1311

On March 21, 2008, the Federal Regulators jointly issued a Notice within the Federal Register requesting public comment on the proposed revisions to the 1997 FFIEC "Interagency Questions and Answers Regarding Flood Insurance" ("Q&A"). As specified within the attached document, the National Flood Determination Association ("NFDA") urges your consideration of our concerns with regard to particular guidance provided in the proposed Q&A.

The NFDA is a professional association of companies that works with federally regulated lenders to facilitate compliance with the mandatory purchase requirements under the National Flood Insurance Program ("NFIP"), the result of which is that improvements located in the Special Flood Hazard Area ("SFHA") are covered by flood insurance. Member companies of the NFDA also provide services to insurance companies and agents for rating flood policies under the NFIP, and to other insurance-related entities for risk management purposes. Depending on the marketplace, our industry completes 20 to 30 million flood hazard determinations per year. Annually, the industry responds to as many as 1,250,000 telephone inquiries from lenders, insurance agents and homeowners by answering questions that arise over flood hazard determinations, FEMA's flood maps, as well as the NFIP itself and its requirements. As a result our extensive experience, we have an understanding of the flood regulations governing lenders, the NFIP rating guidelines, and the insurance companies' and lending institutions' processes and procedures related to flood zone determinations.

We appreciate the opportunity to provide our comments and your willingness to consider them as you move forward to a final Q&A.

Sincerely,

Cheryl A Small

Cheryl Small
Vice-President and Policy Adviser
National Flood Determination Association

Enclosures: "NFDA Comments on Section XV (Questions 64 and 65) of the Proposed Interagency Questions and Answers Regarding Flood Insurance" (2-page document)

9249 S. Broadway 200-435
Highlands Ranch, CO 80129

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NFDA Comments on Section XV (Questions 64 and 65)
of the Proposed Interagency Questions and Answers Regarding Flood Insurance

The NFDA has serious concerns about proposed questions and answers 64 and 65 of the "Interagency Questions and Answers Regarding Flood Insurance" ("Q&A") which would require that lending institutions have processes in place to identify and resolve flood zone discrepancies between the lender's Standard Flood Hazard Determination form ("SFHD") and the NFIP flood insurance policy. If accepted as proposed, lenders would be responsible for (1) identifying discrepancies; (2) working to determine if discrepancies are "legitimate" according to the Regulators, and documenting those cases; (3) resolving the discrepancies that are not legitimate; (4) involving borrowers in the Letter of Determination Review process through FEMA when discrepancies are not resolved; and (5) incorporating processes to ensure that there is no more than "occasional" instances of unresolved discrepancies or be subject to violations and fines. Lending institutions and insurance companies utilize in many cases third party providers, such as NFDA member companies, for this flood zone information and these private companies have developed their own processes to identify and resolve discrepancies when they arise.

By executing sanctions against lenders for not successfully identifying and resolving flood zone discrepancies, the proposed Q&A appears to create a duty for lending institutions which presently does not exist under the federal regulations, that is, a duty to ensure that a flood insurance policy is rated properly. Pursuant to these regulations, enacted by each Regulatory Agency from the Riegle Community Development and Regulatory Improvement Act of 1994, P.L. 103-325, lenders must ensure that new loans are covered by flood insurance "in an amount at least equal to the outstanding principal balance of the loan or the maximum limit of coverage made available under the Act" and that during the term of the loan that the amount of flood insurance is not "less than the amount required for the property" 42. U.S.C. 4012a. Thus, in order to be compliant lenders must ensure that (1) flood insurance is in place on designated loans and (2) is in an amount sufficient according to the requirements. There is no reference in the legislative history of the Act, of which we are aware, that equates the zone used by an insurance company to rate a policy to a lender's compliance requirements as described above.

Insurance agents collect the premium from the policyholders based upon the rates provided by the Write-Your-Own Companies (WYOs) which are established by the NFIP. Lending institutions do not have influence over the WYO or the agency, thus a duty would be created without providing lenders with the authority to effectively exercise that duty. Although FEMA Bulletin W-08021, dated April 16, 2008, directs WYO companies to "use the most hazardous flood zone for rating when presented with two different flood zones, unless the building qualifies for the 'grandfathering rule'", some lenders have expressed apprehension about conflicts in these situations, especially when there is an existing policy in place. Some WYOs or agents may be reluctant to dismiss zone information obtained for the purpose of rating in favor of a flood zone which they did not pay for and upon which they may not necessarily expressly rely. This reticence may result in part from concern over exposure to liability which may arise in the event that a policy is mis-rated. We also have concern over exposure to additional liability for the lending institutions which result from the creation of this new duty for overseeing the rating process. Aggrieved borrowers, or other third parties, may bring claims against the lending institution for perceived damages allegedly arising out of an institution's violations of the federal regulations. As a result, some lenders are expending considerable resources on researching, developing, and obtaining direction on proper procedures to follow in order to be compliant.

When discrepancies occur, lenders would need to determine if the discrepancy is "legitimate" based upon the NFIP's "Grandfather Rules". Presently, there is no mechanism whereby lending institutions would be made aware of whether a given rate is grandfathered, thus lending institutions may not be able to confirm whether or not a legitimate reason for the discrepancy exists. We are finding that some lenders are considering ordering two

determinations on a given property—one based upon the current flood map for regulatory purposes and one based upon historic flood maps for grandfathering purposes. Even with a historic determination, lenders would not have the information necessary to confirm whether a policy was grandfathered. Furthermore, the proposed process does not take into consideration another scenario for grandfathering which also could result in insufficient premium for a given policy. The Grandfather Rules enable the insurance company to rate the policy based on a prior Base Flood Elevation (BFE) if appropriate in addition to a historic flood zone. Thus, an agent could rate a policy based upon an incorrect historic BFE, collect insufficient premium, and the property could suffer a flood loss. Given that the SFHD does not require BFE information, the lender may never have knowledge of a BFE discrepancy. Therefore, it is inconsistent to task the lenders with effectuating a partial discrepancy review process for other policy rating factors (such as flood zone) without being able to determine conclusively whether a policy was properly rated. We do not believe that the Regulators intend the review and resolution of flood insurance policy rating factor discrepancies (flood zone, BFE, construction date, etc.) to fall under the purview of lending institutions.

If the lender is unable to reconcile a flood zone discrepancy, the proposed Q&A suggest that the lender and borrower jointly request that FEMA review the determination. The Letter of Determination Review (LODR) process (*44 CFR 65.17*) was established as a means whereby a borrower could dispute or contest a lender's flood determination. However, in a situation involving a dispute over a lender's SFHD versus an insurance rating determination, there may be no dispute from the perspective of the borrower and no incentive for him or her to cooperate (as required by the regulation), especially considering that cooperation may result in an $80 fee and a 45-day delay. Since the LODR process requires that the joint submission occur within 45 days of the lender's notification to the borrower that flood insurance is required, some lenders have pointed out that the LODR process would be impractical or inappropriate in portfolio review situations or in relation to closings that may occur more than 45 days after such notification.

Importantly, lenders, and insurance companies for that matter, already have processes in place with their flood determination providers to review and resolve flood zone determination discrepancies that occur from time to time, usually due to map issues. Lenders have taken the initiative to institute these processes without the threat of sanction, and a majority of discrepancies are resolved prior to the issuance of a flood policy. As a partner in flood compliance with lenders and insurance companies, we can attest to the success of these review processes to ensure that (1) mandatory purchase of flood insurance guidelines are understood when appropriate, and (2) policy rating information is accurate. If a policy happens to be mis-rated, the NFIP Standard Flood Insurance Policy currently has a remedy for this situation *("Reduction and Reformation of Coverage", Section VII.G.*). Through this process, in the event of a flood loss to an insured structure for which the policy was mis-rated based upon a mis-determination of the flood zone, the NFIP would temporarily reduce the amount of coverage available to a policyholder and then notify the policyholder and mortgagee of this reduction and the need for additional premium to be paid in order to reform the policy coverages back to the original amount. While this may certainly be an inconvenience at the time of the loss, it is an effective way to remedy a mis-rating situation and to ensure that the NFIP receives appropriate premium for its policies. Finally, the NFDA has not seen statistical evidence that these mis-rating situations have been so commonplace as to significantly impact the NFIP from a financial perspective.

For the reasons described above, the NFDA does not support the change in the regulations which would subject lending institutions to a finding of non-compliance and the implications arising therefrom for not identifying and resolving flood zone discrepancies. We commit to continue to work with our client companies to ensure that proper flood information is utilized in both industries and to encourage cooperation between all parties involved.