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**Re: Loans in Areas Having Special Flood Hazards - Private Flood Insurance;  
Docket ID OCC-2016-0005**

This letter is submitted by Wells Fargo & Company and its affiliates ("Wells Fargo") in response to the joint notice of proposed rulemaking issued by the Office of Comptroller of the Currency, the Board of Governors of the Federal Reserve System, the Federal Deposit Insurance Corporation, the Farm Credit Administration, and the National Credit Union Administration (the "Agencies") on October 19, 2016, for "Loans in Areas Having Special Flood Hazards - Private Flood Insurance."

Wells Fargo welcomes the opportunity to comment on the proposal to amend existing regulations clarifying regulatory obligations under the Biggert-Waters Flood Insurance Reform Act of 2012 ("BWA")<sup>1</sup> regarding the acceptance of private flood insurance in satisfaction of the mandatory requirement for flood insurance for properties in special flood hazard areas given as security for loans covered by the Flood Disaster Protection Act ("FDPA"). Since enactment of the BWA on July 6, 2012, the lending and insurance industries, and the public at large, have sought clarification of when private flood insurance may satisfy a borrower's obligation to provide

<sup>1</sup> The Biggert-Waters Act formed part of the Moving Ahead for Progress in the 21st Century Act, Pub. L. No. 112-141, 126 Stat. 405 (2012), appearing in Division F, Title II, Subtitle A of the act at §§ 100201 - 100249, 126 Stat. 916 - 969; the Private Flood Insurance provisions are codified at 42 U.S.C. § 4012a(b)(1)(A).

mandatory flood insurance and the regulatory requirements imposed upon regulated lenders when accepting that form of insurance. Wells Fargo appreciates the efforts of the Agencies to give needed guidance on these important issues.

While we agree with portions of the proposal, we request the Agencies carefully consider certain changes before publication of the final rule. Specifically, both borrowers and lenders need clarity on the circumstances under which a lender may accept private insurance in its discretion when the tendered policy does not contain each necessary provision under the mandatory acceptance section of the proposed rule. This and other provisions needing refinement are outlined in this letter, and Wells Fargo urges the Agencies closely consider these matters to accomplish BWA's strong encouragement of consumer choice in flood insurance products. While long the backbone of flood insurance offerings, consumers should be free to choose between FEMA's National Flood Insurance Program ("NFIP") policies and a range of private insurance solutions providing coverage for property owner's flood losses and at the same time accomplish the FDPA's broad policy objective of safe and sound lending.

## **1. Discretionary Acceptance of Private Flood Insurance**

Wells Fargo commends the Agencies efforts in responding to the many requests raised in comments to the initial proposed rules under BWA to allow lender discretion in applying BWA's criteria for private flood insurance. Allowing lenders to use reasonable discretion in applying the BWA standards for private coverage serves the borrowing public by allowing choice in insurance products, aiding borrowers by keeping required insurance affordable, encouraging insurance industry innovation, and increasing predictability in regulator enforcement of lenders' compliance duties under the FDPA.

Any outline of appropriate discretion in accepting private flood insurance must recognize the interests of borrowers, insurance providers and lenders and not focus narrowly on a comparison of NFIP and private insurance policy language. Private flood insurance policies differ in fundamental ways from those offered under the NFIP (defined as "Standard Flood Insurance Policies" or "SFIP's"). Existing private insurance choices for consumers owning 1-4 family properties have historically been limited, but are increasing as NFIP premiums increase and the insurance industry begins to offer alternative products. A wide variety of private insurance products have evolved to meet the needs of condominium and cooperative associations and commercial businesses, especially for properties valued well in excess of the very low maximum coverage available under the NFIP.

In Wells Fargo's experience, many commercial private flood policies provide flexible, affordable protection from loss through coverage for multiple perils (e.g., fire and property casualty, earthquake or business interruption insurance) of which flood risks are but one part of the coverage. These commercial, and in some cases, residential condominium association policies may insure multiple buildings, multiple building types and/or buildings in diverse geographic locations, using combined insurance limits with flexible deductibles fashioned according to the financial circumstances of the insured or third-party occupants of the property. Consequently, most private policies do not neatly fit the narrow confines of the BWA private flood insurance criteria or the proposed definition of private insurance. All of these factors become even more complex in large commercial loans, including syndicated or participated transactions involving multiple lenders, when the borrower has "layered" or "pooled" policies where several different insurance companies are providing some part of the coverage for the property. Those private policies, however, can and do

provide effective and affordable coverage for all parties having an insurable interest in the properties, including lenders, and the applicable mandatory flood insurance regulations should take into proper account all of those important interests. Any regulation in this arena should be slow to limit or restrain lender acceptance of insurance products that sophisticated property owners deem adequate to meet their needs, especially when those same private policies provide adequate coverage for casualty or other losses.

For borrowers and lenders where the collateral is residential condominium buildings, proposed Section 22.3(c)(3)(ii) imposes an impossible standard, because the lender is not an express loss payee under those types of private policies, nor is the lender in a place to dictate policy terms. This standard for acceptance should be expanded to recognize those circumstances as an exception, perhaps simply by adding to that section "except where policy owner is a condominium association and the property securing the loan is a residential condominium."

Section 22.3(c)(3)(iv), while recognizing needed discretion in the areas of deductibles and policy terms and conditions, is potentially ambiguous and is likely too narrow in requiring an unduly detailed comparison between a private policy and the appropriate SFIP policy. Requiring that the private policy deductible be "similar" leaves open a variety of possibilities (e.g., similar in amount, similar in proportionality to the coverage provided under the policy, similar in overall affordability for a borrower, etc.). A crucial addition to that section should clearly allow the lender to accept deductibles which are *proportionally* similar, and doing so would not seem to violate the intent of BWA. For example, the existing maximum SFIP deductible for a nonresidential property (i.e., a commercial building) is \$50,000, and the maximum available coverage is \$500,000. For a large commercial loan where, for example a \$1,000,000 maximum coverage flood private policy is obtained, the lender should be allowed to apply its reasonable discretion to accept an approximate \$100,000 deductible where the lender considers the borrower financially able to pay that level of deductible in the event of a loss. Likewise, a lender should be free to consider the presence of higher deductibles in the borrower's hazard or other property insurance as additional grounds to accept a higher, but appropriate deductible under the circumstances. The Agencies should recognize the impact mandating smaller deductibles can have on the affordability of insurance and allow lenders to use their credit and risk expertise to reasonably allow higher deductibles than those available under NFIP policies.

We believe the proposed discretionary standard imposes an unnecessarily detailed comparison of a private policy to the NFIP counterpart. As commonly interpreted in statutes and regulations, the word "including" appearing in Section 22.3(c)(3)(iv)(B) seems to require an exhaustive comparison of an SFIP by not restricting the required areas of comparison. If the private policy otherwise meets the standards in subsections (i) through (iii) of 22.3(c)(3), and in the sound discretion of the lender has "reasonably determined that the private policy provided sufficient protection of the loan secured by the property..." under subsection (iv)(2), then the private policy should be deemed adequate without the need to compare the policy with the SFIP beyond proportionally similar deductibles, exclusions and conditions. The Agencies should use care to not impose on lenders a standard befitting an expert in the insurance industry merely to assess basic regulatory adequacy of a private flood policy.

Respecting the obligation of the lender to properly document its findings under subsection (iv)(B)(3), Wells Fargo encourages the Agencies to accept existing practices used by many lenders today through a basic checklist as it reviews the private flood policy and avoid imposing extensive and time-consuming or burdensome documentation efforts which may impact borrowers by

delaying loan closings. The emphasis should be on a lender's use of consistent but efficient simple practices to assure overall compliance with the regulations.

The Agencies request that comments address whether "these proposed criteria are appropriate for regulated lending institutions accepting flood insurance policies issued by a private insurer that do not meet the statutory definition of "private flood insurance," In a related request, the Agencies ask for commenters views whether the proposed criteria are compatible with industry practice, or whether the proposed criteria would exclude currently accepted policies or significantly limit the growth of the market for flood insurance policies issued by private insurers.

Except where noted in the preceding paragraphs above, the criteria will allow the needed discretion to accept flood insurance. We hope the Agencies will carefully consider our suggested clarifications and revisions to allow lenders to quickly and predictably assess the adequacy of a borrower's tender of private flood insurance, which should lead to broader availability of private insurance products and enhance consumer choice.

## **2. Mandatory Acceptance of Private Flood Insurance**

Section 22.3(c)<sup>2</sup> of the proposal incorporates the new definition of "private flood insurance" in 22.2(k) and purports to describe the circumstances under which a regulated lender *must* accept a borrower's tender of private insurance. These requirements, however, do not seem to aid or encourage greater use of private flood insurance as an alternative to NFIP policies, and often impose artificially strict requirements on lender acceptance not necessarily tied to the safety and soundness of the loan. In Wells Fargo's extensive experience lending to consumers, small businesses and large commercial enterprises throughout the United States, few if any private flood insurance policies in today's insurance marketplace appear to meet all of the requirements for mandatory acceptance by a lender.

The lack of private flood insurance products meeting these standards for mandatory acceptance is most apparent in commercial lending, but may also arise in residential consumer loans where the property's insurable value substantially exceeds the \$250,000 NFIP coverage limit. Typical flood policies purchased by sophisticated business borrowers and investors of real estate, often after consultation with insurance experts, lack one or more of the required elements under Section 22.3(c) while being fully adequate to protect borrowers' interests and which are sufficient to support lenders' safety and soundness concerns. The most common provisions failing to meet the technical requirements under that Section are: (a) cancelation notice periods shorter than those prescribed under Section 22.3(c)(iii) but which fully comply with state insurance requirements, and (b) higher deductibles than those allowed by 22.2(k)(2)(ii) even though well within a borrower's ability to pay. In fact, mandating an artificially low deductible may pose harm to some borrowers by increasing the cost of flood coverage since more risk than necessary is passed to the insurance company.

Wells Fargo recognizes that much of the difficulty in crafting the scope private insurance within this "mandatory acceptance" universe is due to the narrow confines described in BWA itself, and we respectfully request that that the Agencies join with the lending and insurance industries in encouraging much needed revisions to BWA as the legislative branch considers reauthorization of the NFIP program in the coming months.

<sup>2</sup> For simplicity, all citations to the proposed rule in this letter will be to the version proposed by the Office of the Comptroller of the Currency (OCC) as that agency acts as primary regulator of Wells Fargo Bank, NA and its affiliates.

### **3. Compliance Aid for Mandatory Acceptance**

The compliance aid for mandatory acceptance set out in Section 22.3(2)(2) is an innovative approach to addressing one of the greatest difficulties faced by property owners and lenders using private flood coverage. It encourages insurance providers to include a summary of the policy provisions necessary to meet the mandatory acceptance standards, and to include a provision asserting the policy meets the regulation's new definition of private flood insurance. While a laudable effort, we believe this proposal will do little to encourage use of private coverage. As already mentioned, virtually no existing insurance products meet the proposed definition of private flood insurance. We further believe insurance providers will be hesitant to give this "aid" assuring consistency with the new private flood insurance definition, since doing so may require submission for approval by state regulators as a statement or endorsement of coverage under the policy. Even more important, insurers may well view the compliance aid as potentially expanding coverage or creating an ambiguity when read with other policy provisions, and therefore decline to provide the statement.

Even if the concerns outlined in the previous paragraph are overcome, lenders, particularly smaller lenders, will see little benefit in the "aid" if held to the language of 22.3(c)(2)(ii) mandating that the lender separately verify that each of the statements in the summary are in fact true of the underlying policy language. If an insurance provider is willing to make the assurance stated in subpart (iii) of that section, the lender should not be required to further examine the policy provisions except to verify the effective dates, coverage amounts and the names of required parties the flood zone and that the subject property appear in the policy. We encourage the Agencies to give lenders the assurance through the final rule that if the "compliance aid" contains the specified language appearing in Sec. 22.3(c)(2)(iii), that alone is sufficient evidence the insurance policy meets the regulatory requirements for acceptance by the lender.

### **4. Required Insurance Documents When Reviewing Private Flood Insurance Policies**

One fundamental difficulty lenders face in accepting private flood insurance involves the differences in the purchase and issuance process between these policies and the NFIP policies. The proposed regulation and its treatment of both mandatory and discretionary acceptance do not provide lenders with needed guidance on the minimum policy documentation which must be received and reviewed before accepting a private policy. Unlike NFIP policies, most private flood insurance policies (and especially those covering residential condominium associations and commercial buildings) are not typically available for review in their entirety for days or weeks after the time when most borrowers must have financing in place to meet their contractual duties for a purchase or refinance of property or other financial needs. In fact, lenders find themselves at times required to delay loan closings to await arrival of all insurance policy documentation after all other loan conditions and documentation requirements are satisfied.

Wells Fargo encourages adding to the proposal an express recognition of this issue, and a provision allowing a lender to accept an abstract or summary of coverage, or an exemplar policy form, together with documentation similar to the "compliance aid" described in 22.3(c)(2) whether the policy is being reviewed under the mandatory or the discretionary standard. In our experience, the time required by the insurance agents and issuers to deliver full private flood insurance policies can have a significant adverse impact on borrowers if lenders are held to a strict duty to have all private policy documentation on hand in order to perform a reasonable determination the policy meets the detailed regulatory definition. Similar issues may arise each time a lender must review a renewed private flood policy, as private policies are often renewed with entirely new policies. To

properly meet BWA's strong encouragement for a robust, effective and affordable private flood insurance market, the Agencies should address this issue in the rule and assure lenders are not left to speculate how the level of documentation might impact how the regulators view a lender's flood insurance compliance measures.

#### **5. Policies Issued by Mutual Aid Societies and Other Alternative Insurance**

Wells Fargo appreciates the flexibility expressed by the Agencies in recognizing policy issues by Mutual Aid Societies as a potentially acceptable type for private flood insurance. While these types of policies are seldom offered for commercial loans, they do occasionally arise in both the residential and small business lending. We believe the requirement for either an Agency or lender determination that each particular mutual aid society has a "demonstrated record of covering losses," creates a major impediment to accepting these policies since there is no established source for that information (other than each lender's individual history with each society). Other than that requirement, the Agencies proposal demonstrates a sincere effort to allow broad discretion to lenders, and we encourage a similar broad view of the required discretion to accept other forms of private flood insurance.

Other variations on traditional private flood insurance are used for large commercial enterprises, including forms of self-insurance where all or part of the risk of flood loss is absorbed by the owner, often with the assistance of professional insurance administrators. We invite the Agencies to evaluate these alternatives as allowable forms of private flood insurance under the standards for discretionary acceptance.

#### **Conclusion**

Wells Fargo sincerely commends the effort evidenced by the Agencies in considering comments given to their initial proposed rule addressing private flood insurance and in issuing this new proposal. We appreciate the opportunity to comment and request consideration of our comments and suggestions to make the final rule an even stronger aid to consumers, lenders and insurers by encouraging responsible use of private flood insurance products.

Sincerely,

A handwritten signature in black ink, appearing to read 'David L. Moskowitz', with a long horizontal flourish extending to the right.

David L. Moskowitz  
Executive Vice President and Deputy General Counsel,  
Wells Fargo & Co.