



December 29, 2014

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Secretary  
Board of Governors of the  
Federal Reserve System  
20<sup>th</sup> Street and Constitution Ave., NW  
Washington DC 20551  
Docket No. R-1498

Legislative & Regulatory Activities  
Division  
Comptroller of the Currency  
400 7<sup>th</sup> Street, SW  
Washington DC 20219  
Docket ID OCC-2014-0016

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***RE: Loans in Areas Having Special Flood Hazards***

Ladies and Gentlemen:

On behalf of the Community Associations Institute (CAI)<sup>1</sup>, I am pleased to submit the following comments on the joint proposed rulemaking concerning escrow of flood insurance premiums and other matters applicable to federally-

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<sup>1</sup> CAI is the only national organization dedicated to fostering competent, well-governed community associations that are home to approximately one in every five American households. For more than 40 years, CAI has been the leader in providing education and resources to the volunteer homeowners who govern community associations and the professionals who support them. CAI's more than 33,000 members include community association volunteer leaders, professional managers, community management firms and other professionals and companies that provide products and services to associations.

related mortgage loans secured by real property located in areas designated as having a special flood hazard risk.

***Support for Implementation of Escrow Exemption for Community Associations***

CAI strongly supported passage of the Homeowner Flood Insurance Affordability Act (HFIAA)<sup>2</sup> to ensure continued availability of flood insurance for residents of community associations.<sup>3</sup> In enacting HFIAA, Congress protected homeowners from the unintended consequences of exorbitant flood insurance premium increases. Absent congressional action, financially stable households faced requirements to purchase unaffordable flood insurance policies or accept unaffordable forced-place flood insurance policies. Either prospect significantly increased risks of foreclosure and families being evicted from their homes.

In addition to protecting homeowners from untenable outcomes arising from well-intended public policy, Congress refined statutory requirements concerning escrow of flood insurance premiums. Section 25 of HFIAA provides three exceptions to mandatory escrow requirements for flood insurance premiums. Of primary concern to community associations is the statutory exemption from premium escrow requirements in those instances in which a community association purchases and maintains flood insurance coverage as a common expense.

The Agencies' proposal appears to hew closely to the statute, which makes explicit that flood insurance premiums paid as a common expense by a "...*condominium association, cooperative, homeowners association, or other applicable group...*" are exempted from escrow requirements.<sup>4</sup> Further, the proposed rule mirrors the flexibility the Agencies sought to provide in the 2013 joint rulemaking concerning escrow requirements for flood insurance premiums.<sup>5</sup>

**CAI members support the Agencies' language exempting community association homeowners from the mandatory escrow requirements as proposed.**

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<sup>2</sup> P.L. 113-89

<sup>3</sup> There are three basic forms of community associations: (1) planned communities; (2) condominium associations; and, (3) housing cooperatives.

<sup>4</sup> 42 U.S.C. § 4012a(d)(1)(B)(II)

<sup>5</sup> See 78 FR 65108. The Agencies proposed an exemption from mandatory escrow requirements where a common interest community purchased and maintained a Residential Condominium Building Association Policy through the National Flood Insurance Program or other flood insurance policy providing comparable coverage.

***Escrow of Flood Insurance Premiums Where Association Policy Is Insufficient***

CAI members believe that all community associations should develop and adopt a risk management and insurance program designed to both identify and insure against a community's risks of loss.<sup>6</sup> By working with a certified Community Insurance and Risk Management Specialist (CIRMS)<sup>7</sup>, community associations can identify risks and create a risk management program that allocates funding to insure against and mitigate risks of loss.

In the ***Supplementary Information*** accompanying the proposed regulatory language, the Agencies state—

*As the Agencies discussed in the October 2013 Proposed Rule, if the amount of the policy purchased by the condominium association, cooperative, homeowners association, or other applicable group is insufficient to meet the mandatory flood insurance purchase requirement, the borrower would be required to obtain a supplemental policy to cover the deficiency. The Agencies would expect that the regulated lending institution escrow the premiums and fees for the supplemental policy unless the small lender exception applies. For example, if a condominium association purchases an RCBAP or a private flood insurance policy for less than the amount of insurance required by the mandatory purchase requirement under the FDPA, the borrower would need to obtain a dwelling policy for supplemental coverage. If the borrower is required to obtain a dwelling policy at the time the loan is made, increased, extended, or renewed, under the proposed rule, the regulated lending institution would be required to escrow the premiums and fees for such policy.<sup>8</sup>*

CAI members have voiced concern the Agencies' proposal could lead to an inequitable and untenable outcome if a lender seeks to require that a single association household purchase flood insurance to insure association common elements against flood loss. The association bears responsibility—generally as a

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<sup>6</sup> To view CAI's Public Policy on Community Association Risk Management and Insurance, visit <http://www.caionline.org/govt/policies/Pages/COMMUNITYASSOCIATIONRISKMANAGEMENTANDINSURANCE.aspx>

<sup>7</sup> CAI's prestigious CIRMS designation is available to insurance professionals with a demonstrated high level of competency within the risk management profession. To earn the CIRMS designation, insurance professionals must have a minimum of five years experience in the field of community association insurance, meet and maintain high legal and ethical standards, completed significant professional educational requirements, and meet continuing education requirements. For more information on CAI's CIRMS designation, visit <http://www.caionline.org/career/designations/Pages/cirms.aspx>

<sup>8</sup> *Joint Proposed Rulemaking—Loan in Areas Having Special Flood Hazards: IV. Section-by-Section Analysis, —\_Escrow Requirements.* (79 FR 64518).

matter of law or contract—for insuring common elements while individual homeowners have the responsibility to insure property where there is an exclusive right of use (i.e. a condominium unit).

Lenders must not seek to compel an association homeowner to individually purchase or otherwise accept responsibility for a flood insurance policy for property over which the homeowner does not maintain an exclusive right of use. If lenders mistakenly or misguidedly attempt to require that a homeowner insure common property or force place coverage in such instances, the homeowner faces the very peril of financial ruin Congress intended to avoid by enactment of HFIAA. This general principle must also control when a lender determines the need to insure detached, non-residential use structures that are association-maintained common property.

In those instances where an association household is compelled to purchase flood insurance or insurance is force placed, the identity of the insured must be plainly disclosed to the homeowner (i.e. is the insurance policy for the benefit of the owner or the association). Again, CAI strongly opposes any instance in which an individual homeowner is required to insure association common property and disclosure of the insured parties and properties will prevent such an outcome.

Additionally, policies must disclose any applicable policy limits and exclusions, making plain the order and instances in which respective policies will pay out in the event of an insurable loss. Further, the policyholder must be informed of any potential disqualification from, or loss of, claims or compensation under the National Flood Insurance Program or other federal disaster relief programs subject to statutory restrictions on duplication of benefits.<sup>9</sup>

**CAI members generally support the Agencies’ guidance that lenders escrow flood insurance premiums where a homeowner is required to purchase a supplemental flood insurance dwelling policy, but urge the Agencies to require disclosure of the beneficial owner of supplemental or forced place policies and required disclosure of terms, conditions and restrictions of such policies to policyholders.**

***Proposed Supplemental Policy Likely Insufficient to Meet Secondary Market & Federal Government Housing Agency Insurance Guidelines***

CAI members note that while the Agencies are constructively seeking to implement Section 25 of HFIAA, the statute (and by extension the proposed rule) could lead to instances in which a homeowner purchases a supplemental flood insurance dwelling

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<sup>9</sup> In general, the Stafford Act prohibits duplication of disaster benefits where a victim of a federally-declared disaster is eligible for benefits from a private source, such as an insurance policy.

policy, yet remains in violation of key secondary market and federal government housing agency underwriting requirements.<sup>10</sup>

In general, CAI members believe that associations should prudently insure against perils and that associations must also act in a manner that benefits all residents. Maintaining flood insurance coverage that meets federal government housing agency insurance standards is an important role of the association.

In some rare instances, a community association in a special flood hazard area may choose to purchase a flood insurance policy that does not meet minimum secondary market or federal government housing agency requirements. This may be due to, among other reasons, the release of updated flood insurance maps that have newly designated the association as being located in a special flood hazard area, the association or municipality may be contesting a new special flood hazard area designation, or a majority of homes in the association are not mortgaged.

In these instances, a homeowner who purchases a supplemental flood insurance dwelling policy pursuant to the joint proposed rule likely remains in violation of key federal mortgage guidelines while also being at risk of loss due to the fact that neighboring units are either uninsured or underinsured against flood loss. In projects with shared roofs, walls, and points of entry and egress, the habitability of units following an insurable event is dependent on all damaged units and common areas being repaired and restored to safe and sanitary condition. Repairing a unit while surrounding attached units remain infested with mold, for example, does not protect the value of a lender's collateral nor does this protect the interests of the insured homeowner or the association.

While CAI will continue to educate community associations on the need to prudently insure against and mitigate risk of losses, CAI members do not want the Agencies' policy on supplemental coverage to be misinterpreted as intimating that associations may remain uninsured or underinsured against known perils, such as the risk of flooding. CAI understands such an outcome is not the intent of the Agencies and respectfully suggests that clarification of this point in the final regulation will serve a constructive end.

### ***Conclusion***

CAI members believe that homeowner, association and lender interests will be well-served and protected by rigorous enforcement of the recently finalized "Qualified

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<sup>10</sup> Federal housing agencies include: Fannie Mae, Freddie Mac, the Federal Housing Administration, the U.S. Department of Veterans' Affairs, and the U.S. Department of Agriculture. Examples of federal housing agency flood insurance requirements include—FHA Condominium Processing and Approval Guidelines: Section 2.1.9—Insurance Requirements; Fannie Mae Selling Guide: B7-3-07—Flood Insurance Requirements (12/16/2014).

Mortgage” and “Qualified Residential Mortgage” rules. These standards require lenders determine a borrower has the ability to pay all monthly mortgage-related obligations to qualify for safe harbor from certain Truth in Lending Act sanctions or an exemption from risk retention requirements pursuant to the Dodd-Frank Act.

Lender compliance with prudential mortgage underwriting and servicing standards will identify any insurance deficiencies that will cause material harm to a homeowner if credit is extended and the insurance deficiency identified post-closing. The Agencies must conduct rigorous examinations of regulated entities to ensure compliance with all applicable mortgage underwriting and servicing standards to protect homeowners from lender and servicer negligence and to prevent extension of unaffordable mortgage credit.

Thank you for the opportunity to comment on the Agencies’ proposed rule concerning flood insurance policies protecting real property in special flood hazard areas. If CAI or I may be of any additional assistance to the Agencies regarding this proposed rule or any other matter, do not hesitate to contact me at (703) 970-9220.

Sincerely,

Dawn M. Bauman, CAE  
Senior Vice President, Government Affairs  
Community Associations Institute