



November 13, 2003

VIA ELECTRONIC MAIL

Rules Docket Clerk
Office of the General Counsel
FEMA
500 C Street, SW
Room 840
Washington, DC 20472
rules@fema.gov

Re: Federal Emergency Management Agency's Proposed Rule Amending the Federal Insurance Administration, Financial Assistance/Subsidy Arrangement

To the Rules Docket Clerk:

The National Association of Professional Insurance Agents (PIA) hereby submits these comments regarding the Federal Emergency Management Agency's proposed rule amending the Federal Insurance Administration, Financial Assistance/Subsidy Arrangement and related regulations. Founded in 1931, PIA is a national trade association that represents member insurance agents and their employees in all 50 states, the District of Columbia and Puerto Rico. PIA members sell and service all lines of insurance, specializing in coverage of automobiles, homes and businesses. PIA represents its members' interests in state capitals and in Washington, D.C. to ensure that policymakers understand the perspectives and concerns of insurance agents.

PIA supports the goal of the proposed rule. Resolving jurisdictional issues between federal and state courts will lessen the confusion that currently exists in determining jurisdiction over lawsuits related to the National Flood Insurance Program (NFIP) and will help mitigate the costs of litigating such suits.

Despite its worthy goal, PIA opposes the inclusion of the new paragraph 61.5(f) of the proposed rules, which would effectively designate the independent property and casualty agent the "agent" of the insured and not the agent of the Write-Your-Own ("WYO") insurer for purposes of selling and servicing NFIP policies. The new provision is an overly-broad approach

to fixing the jurisdictional issue that would constitute a sea change not only in the flood insurance program, but in insurer-agent relationships, as well. As discussed in more detail below, FEMA should reject the proposed rule change in section 61.5(f) because the proposed change (i) interferes with the contractual relationship between agents and insurers; (ii) violates the National Flood Insurance Act; (iii) overrides long-established legal and practical distinctions between agents and brokers (iv) imposes significant new burdens on agents; (v) is procedurally deficient; and (vi) would harm the National Flood Insurance Program long-term.

Introduction

To put this issue in its proper context, it is worthwhile to recall the role of PIA and insurance agents in the history of the flood insurance program. Insurance agents have been integrally involved in NFIP since its inception. NFIP was originally a direct-written program and agents dealt directly with FIA, FEMA's predecessor in administering NFIP. In the early 1980s, after an attempt at out-sourcing administration of the program to EDS, the agents convinced reluctant insurance carriers to participate in NFIP. The insurers would issue policies, adjust claims, collect premiums and work with their agent force to sell and service policies in much the same way other lines of insurance are sold. The government would remain responsible for setting rates, coverage limits and eligibility requirements, and for paying losses. Thus, the "write-your-own" program was born and an entirely new phase of the flood insurance program began. Today, approximately 95% of flood insurance policies are sold through 86 private insurers working through their agents to sell billions [?] of dollars worth of flood insurance policies.

The flood insurance program was built in large part by independent insurance agents and owes a great deal of its success to their involvement and hard work. In light of this history, the changes proposed in section 61.5(f) are not only problematic from a legal and practical standpoint, but they are disheartening, as well.

Analysis

1. Procedurally Deficient Rulemaking

As an initial matter, this rulemaking has three procedural deficiencies: (i) the 30-day comment period is too short, in violation of FEMA rules and an Executive Order; (ii) the proposed rule raises novel legal and policy issues and should be reviewed by the Office of Management and Budget (OMB); and (iii) the proposed will have a significant economic impact on small business and should be subject to the provisions of the Regulatory Flexibility Act.

Abbreviated Comment Period: FEMA has not followed its own procedures in undertaking this rulemaking and has contravened a binding Executive Order.¹ FEMA's Policies

¹ Exec. Order No. 12,886, 50 Fed. Reg. 51,735 (October 4, 1993).

and Procedures require that notices of proposed rulemaking provide for at least sixty days for submission of public comments.² Shorter comment periods are permitted if (i) the Director makes an exception and sets forth the reasons for the exception in the preamble to the notice of proposed rulemaking and (ii) the “procedural transgression” is in response to an emergency situation and a statement setting forth the reasons the agency cannot follow the requisite procedures is published in the Federal Register.³ Executive order 12886 additionally recommends that “not less than 60 days” be allocated for public comment on a proposed rulemaking.⁴

The proposed rule in question, dated October 14, 2003, requires submission of comments on or before November 13, 2003. This allows interested parties only 30 days to review and prepare evidentiary submissions. Although as noted above, FEMA’s policies and procedures allow for exceptions to the 60-day comment period rule, the proposed comments do not qualify for the exception because the preamble to the proposed rule does not include any discussion of the reasons for the shortened comment period. Similarly, the proposed comments do not qualify as an “emergency situation” because no rationale for such a determination was published in the Federal Register.

Given the significant impact of the proposed rule, it is imperative that interested parties be given adequate time to analyze the proposal and prepare their comments. The shortened comment period has caused real harm, resulting in insufficient time to collect and submit a complete evidentiary record and to solicit support more broadly from affected parties.⁵ We therefore object to the abbreviated comment period permitted for the proposed rule, which is in clear violation of FEMA’s policies and procedures and Executive Order 12886.

The Proposed Rule Should be Reviewed By OMB: Because the proposed rule will have a significant impact on the insurance industry, it must be submitted to the Office of Management and Budget (OMB) for review and approval pursuant to Executive Order 12886.

² 44 C.F.R. § 1.4(e) (2002).

³ *See id.* § 1.4(h).

⁴ Exec. Order No. 12,886, § 6(a)(1), 50 Fed. Reg. 51,735 (October 4, 1993), “...In addition, each agency shall afford the public a meaningful opportunity to comment on any proposed regulation, which in most cases should include a comment period of not less than 60 days.”

⁵ For example, Harold T. Duryee, former Director of the Ohio Department of Insurance and Executive Deputy Administrator of the Federal Insurance Administration (FIA), intended to file comments supporting PIA’s position on the proposed rule. Unfortunately, he was unable to dedicate the time and resources necessary to do so during the shortened comment period. Mr. Duryee, who is currently a consultant in private practice, was part of the team that developed and implemented the WYO program in the early 1980s.

The Executive Order requires that all proposed rulemakings that involve “significant regulatory action” receive approval from OMB.

The Order stipulates that OMB review is required for any action that is likely to result in a rule that may:

- (i) Have an annual effect on the economy of \$100 million or more or adversely affect in a material way the economy, a sector of the economy, productivity, competition, jobs, the environment, public health or safety, or State, local, or tribal governments or communities;
- (ii) Create a serious inconsistency or otherwise interfere with an action taken or planned by another agency;
- (iii) Materially alter the budgetary impact of entitlements, grants, user fees, or loan programs or the rights and obligations of recipients thereof; or
- (iv) Raise novel legal or policy issues arising out of legal mandates, the President’s priorities, or the principles set forth in this Executive order.⁶

Although the proposed change has been characterized as a clarification of current rules, the effect of the change cannot be overstated. By changing the status of insurance agents participating in the flood insurance program, it essentially transforms agents, whose duties are to the insurer, into brokers, whose duties are to the insured. As discussed below, this transformation is not permitted by the governing statute and creates new legal and practical issues for producers. Thus, it clearly raises novel legal and policy issues warranting OMB review. Accordingly, the proposed rule should be submitted to OMB for its analysis and approval.

The Proposed Rule will have a significant economic impact on small business and should be subject to the Regulatory Flexibility Act: The preamble to the proposed rule contains a certification that the rulemaking will not have a significant economic impact on a substantial number of small entities. This certification permits FEMA to avoid the requirement, otherwise mandated by the Regulatory Flexibility Act⁷, that the agency prepare and make available for public comment an initial regulatory flexibility analysis.

The determination that this rulemaking would not have significant economic impact on a substantial number of small businesses is clearly erroneous. Many of the local independent agents servicing the flood insurance program are small insurance agencies and the burdens imposed by the proposed rule will have substantial economic impact on their operations, their expenses and their competitiveness in the market. The proposed rule should be subject to the provisions of the Regulatory Flexibility Act and the initial regulatory flexibility analysis should

⁶ See Exec. Order No. 12,886, § 3(f), 50 Fed. Reg. 51,735 (October 4, 1993).

⁷ Regulatory Flexibility Act of 1980, Pub. L. No. 96-354 (1980), 5 U.S.C § 601 *et seq.*

be published for public comment and transmitted to the Chief Counsel for Advocacy of the Small Business Administration pursuant to the requirements of 5 U.S.C. § 603.

2. **The Proposed Rule Substantively Changes the Status of Agents Under NFIP, Significantly Burdening Agents in Violation of Current Law and Established Business Practices**

A. The Proposed Rule Interferes with the Contractual Relationship between Agents and Insurers and Violates the National Flood Insurance Act

The new Section 61.5 (f) has been explained as a “minor clarification” of current policy undertaken to reduce litigation costs for WYO insurers. In reality, this language does much more than clarify. The regulatory intervention by FEMA into private contractual relationships between insurers and their agents is a sea change in the way NFIP functions and has functioned since 1983 when private insurers were brought into the program and in the relationship between insurers and their agents. Moreover, it overrides long-established legal and practical distinctions between agents and brokers, placing significant new burdens on agents.

The new paragraph (f) of Section 61.5 provides that:

(f) Any duly licensed property or casualty agent selling and servicing NFIP policies acts for the insured, and does not act as agent for the Federal Government, the Federal Emergency Management Agency, the Federal Insurance Administration, the servicing agent, or the Write-Your-Own Company.

In essence, this provision transforms an agent into a broker for all sales and servicing under NFIP. This is unprecedented. Significantly, by transforming all agents who market flood insurance through WYO insurers into brokers, a host of legal and practical problems are raised because the agent’s connection to the WYO insurer is statutorily severed. This statutory severing of the insurer-agent relationship undermines the well-defined and commonly-understood business and legal concepts of the insurer-agent relationship.

The Proposed Rule’s Effective Elimination of Agents from NFIP Would Violate the National Flood Insurance Act: Historically, the National Flood Insurance Act⁸ (the “Act”) and rules promulgated thereunder have defined the relationships between the federal government – through FEMA – and the private parties with which the government deals directly under NFIP. For example, in the Supplementary Information to the Proposed Rule, FEMA correctly points out that agents utilized by FEMA in the direct-written portion of the program act “for the insured.” This is not a change from the current rule. The disturbing change in the proposed rule is the extension of this concept to private parties. Under the proposed rule, agents that currently act for WYO insurers will be deemed to act “for the insured,” in effect making them brokers.

⁸ 42 U.S.C. § 4001 *et seq.* (2003).

This is the first time FEMA has attempted to define the relationships of non-governmental parties with each other. Although we recognize that FEMA can and does define its relationship with agents that sell and service policies for FEMA directly, there is no statutory or regulatory authority for changing the role of the agent when they are selling for private-sector WYO insurers.⁹

The Act clearly contemplates active agent involvement in NFIP.¹⁰ In fact, the Act specifically recognizes the existence and participation of both insurance agents and insurance brokers. Because the Act clearly refers to “agents and brokers” several times,¹¹ Congress clearly contemplated that both agents and brokers could be involved in the program. If the proposed change is adopted, FEMA will be in violation of the Act because of its effective elimination of agents from participation in NFIP.

B. The Proposed Rule Overrides Long-Established Legal and Practical Distinctions between Agents and Brokers

The change in the proposed rule would effectively convert state-licensed property and casualty insurance agents, specifically appointed and authorized by WYO insurers to place flood insurance coverage, into insurance “brokers” acting solely on behalf of the insureds. The purported purpose of the change is to shield WYO insurers from potential liability for the actions or omissions of their appointed and contracted agents, but the actual impact would be far greater, unfairly imposing additional burdens and responsibilities on agents.

The categorization of an insurance producer as an “agent” or “broker” has important legal and practical ramifications.

Status as an Insurance Agent Determined by Existence of Contract with Insurer:

Traditionally, an insurance “agent” is a producer who represents an insurer under contract in anticipation of an ongoing and continuous relationship. The agent is deemed to have a fixed and permanent relationship with the insurance company and thus has certain duties and responsibilities to that company defined by statute, common law and the agency contract the producer signed with the insurance company.¹²

⁹ Only 5-7% of NFIP policies are directly written by FEMA. Pursuant to the regulation, the small number of agents who sell and service those policies act as agent for the insured. This can be distinguished from agents selling and servicing under WYO, however, because of the statutory indemnification provision at CITE.

¹⁰ See 42 U.S.C. §§ 4011, 4018, 4081, 4121 (2003).

¹¹ Cite statute

¹² See *Lazzara v. Howard A. Esser, Inc.*, 802 F.2d 260, 264 (7th Cir. 1986); *Royal Maccabes Life Ins. Co. v. Malachinski*, 161 F.Supp.2d 847, 851 (N.D. Ill. 2001); *Benevento v. Life USA Holding, Inc.*, 61 F.Supp.2d 407 (E.D. Pa. 1999); *Rich Maid Kitchens v. Penn Lumbermens Mut.*

(...continued)

The agency contract with the insurance carrier sets forth the duties and responsibilities of the parties to one another, confirming the responsibility of the agent to place coverage within company-approved underwriting standards and the consequences if the agent fails to do so. Such agency agreements also provide for indemnification between the parties. The appointed agent will be required to indemnify the insurer in those instances where the carrier is held liable for damages arising out of the errors or omissions of the agent or where conduct of the agent exceeds his or her contractual authority. Similarly, the insurer will be required to indemnify the appointed agent in instances where the company is at fault.¹³

In the case of NFIP coverage written through the WYO insurers, insurance agents placing coverage for the WYO carriers are required to sign and adhere to the terms of an agency agreement administered by the particular WYO carrier. Moreover, the agent must be a state licensed property and casualty agent acting under written appointment of a WYO insurer, specifically authorized to place the flood coverage as agents of the WYO company.

Thus, the contractual relationship between the producer and insurer is the defining element of the producer's status as an agent. The proposed rules, by dictating that an agent is, essentially, a broker for purposes of NFIP, undermine the producer's ability to establish such a contractual relationship. This violates the spirit and goal of the WYO program, which was designed to take advantage of the exiting insurance marketplace and the industry's well-established company/agent structure.

An Insurance Broker: Under common law, an insurance "broker" is traditionally defined as one who, acting as an intermediary between the insured and the insurer, solicits insurance from the public and upon securing an order for insurance from the client, places the coverage with a company selected by the insured or by the broker.¹⁴ Absent some special condition or circumstance in a particular case, a broker is not an agent of the insurer and may not be converted into an agent for the insurer without some action on the part of the insurer, or the existence of some facts by which the broker's authority to represent the insurance company may be reasonably inferred.¹⁵

(...continued)

Ins. Co., 641 F.Supp. 2d at 303; *Production Credit Ass'n of Southeast Wisconsin v. Gorton Farms*, 573 N.W.2d 549 (Wisc. Ct. App. 1997).

¹³ Insurers are generally responsible for training their agents with respect to the company's policies and procedures and regarding the particular lines of insurance that the company sells. If a company provides incorrect or insufficient training to an agent, the company may be found liable for damages.

¹⁴ COUCH ON INSURANCE 3d, § 45.1; *Royal Maccabees Life Ins. Co. v. Malachinski*, 161 F.Supp.2d at 851; *Galiher v. Spates*, 262 N.E.2d 626, 628 (Ill. App. Ct. 1970).

¹⁵ *Travelers Indem. Co. v. National Indem.Co.*, 292 F.2d 214 (8th Cir. 1961).

Any determination of whether an insurance producer is acting as an agent of the insurer or a broker for the insured must take into consideration not only what he or she is referred to by statute or contract, but also the producer's activities with respect to the insurer and the insured. Factors frequently cited in determining if an insurance producer is acting as the agent of the insurer or the broker for the insured include: 1) who put the producer in motion; 2) who controls the producer's actions; 3) who pays the producer; and 4) whose interest does the producer represent.¹⁶

Applying these four factors to the placement of NFIP flood insurance policies by insurance producers clearly indicates that such producers are agents of the WYO insurance carriers and not the brokers of the insureds. While in most cases it is probably the insured who, pursuant to a lender or other requirement, seeks out the agent to secure flood insurance coverage, the agent's conduct and duties are nevertheless tightly constrained by: (i) the agent's WYO agent appointment and the terms of the producer agreement put forth by the WYO carrier, (ii) strictly construed flood insurance policy provisions, and (iii) the regulations that govern the operation of the NFIP, participating WYOs, and their agents. Agents authorized and appointed by WYO carriers to sell and service flood coverage are subject to strict control by the carriers and receive commissions from these same insurers for placement of NFIP flood policies. To contend that the agent does not represent the interests of the WYO carrier would be to ignore the very strict appointment and authority criteria specifically granted to the agent under his or her contract with the WYO carrier and the limitations placed upon the agent's conduct in soliciting and selling the coverage. The NFIP is not a program that easily lends itself to the exercise of discretion on the part of WYO insurers or their appointed agents.

It is legally unsound to declare for all purposes that an insurance agent in the flood insurance setting is the "agent" of the insured and not the agent of the WYO carrier with whom the producer is authorized and appointed to place flood coverage. It ignores a significant body of common and statutory law that has developed to ensure that the determination of agent status is based upon the facts of each case, including contractual appointments, applicable statutes, and the specific conduct of the agent, insurer and the insured.

C. The Proposed Rule Would Impose New Obligations and Additional Burdens on Insurance Agents:

As "Brokers," Agents will be Subject to Significant New Burdens: As we have indicated, if the proposed rule is adopted, agents selling and servicing flood insurance policies under NFIP will effectively become brokers. As "brokers," they will be subject to significant additional obligations and responsibilities under state law, heightened fiduciary duties, increased liability exposure, and increased difficulty securing errors and omission coverage.

Producers Face Additional State Law Requirements as Brokers: Most state

¹⁶ *Lazzara v. Howard A. Esser, Inc.*, 802 F.2d 260, 264 (7th Cir. 1986).

insurance codes include provisions defining the respective roles and responsibilities of insurance agents and brokers.

- *Licensing Requirements:* California and New York, the two largest insurance markets in the country, impose separate licensing obligations on agents and brokers.¹⁷ Although many other states are foregoing separate brokers licenses in favor of a single “insurance producer” license, many of the states require producers to indicate on license applications if they are acting as a broker. This helps the states determine if the producer has a higher duty of care to consumers.
- *Bonding Requirements:* In addition to a brokers license, California requires brokers to post a \$10,000 bond to secure broker authority.¹⁸ This is a significant financial burden for a small business such as an insurance agency.
- *Producers Deemed to be Agents Under State Laws:* Many, if not all, states have retained a frequently drawn statutory distinction between agents and brokers providing that in any controversy between the insured and the insurer, the insurance “agent” is deemed the agent of the insurance company when he or she is engaged in the sale, solicitation, or negotiation of the carrier’s insurance policy.¹⁹ For example, in Tennessee, the statute defining the role of the agent provides:

“Any person who shall solicit an application for insurance shall be in all matters relating to such application and the policy issued in consequence thereof be regarded as an agent of the company issuing the policy, and not the agent of the insured, and all provisions in the application and policy to the contrary are void and of no effect whatever.”

Texas Insurance Code Section 21.02(a) defines “agents” broadly as:

“(a) Any person who solicits insurance on behalf of any insurance company,....or who takes or transmits other than for himself any application for insurance or any policy of insurance to or from such company, or who advertises or otherwise gives notice that he will receive or transmit the same, or who shall receive or deliver a policy of insurance of any such company, or who shall examine or inspect any risk, or receive, or collect or transmit any premium of insuranceshall be held to be the agent of the company for which the act is

¹⁷ N.Y. INS. LAW §§ 2101(a), 2101(c), 2104 (2003).

¹⁸ CAL. INS. CODE §§ 1662-1665 (2003).

¹⁹ VA. CODE ANN. § 38.2-1801 (2003); D.C. CODE ANN. § 31-802; S.C. Code Ann. §§ 38-1-20, 38-43-10; W.VA. CODE ANN. § 33-12-22; TENN. CODE ANN. § 56-705; TEX. INS. CODE ANN. § Art. 21.02(a).

done.

The Proposed Rule Imposes a Heightened Duty of Care on Agents: The scope of an insurance producer's duties to the insured are dramatically affected by whether the agent is found to be an agent of the insurance company or a broker for the insured. A broker's duty to the insured is significantly greater than that of an agent.

The most basic legal duty imposed on all insurance producers is to exercise the skill and care which a "reasonably prudent person engaged in the insurance business would use under similar circumstances."²⁰ An insurance producer's duty to the insured is ordinarily limited to the duties imposed in any agency relationship, to act in good faith and to follow instructions or requests of the insured.²¹

As mentioned above, the principal determinant of a producer's status as "agent" is the existence of a contractual relationship with the insurer. If the producer is considered to be the "agent" of the insurer, he or she may have little in the way of duties to a policyholder. For example, a federal court, applying Oregon law, granted summary judgment to an agent who allegedly failed to include specific property in a policy schedule in accordance with the insured's instructions. The court concluded that neither the evidence nor the pleadings were sufficient to establish an agency relationship between the agent and the insured.²²

Absent an agreement to the contrary or prior course of dealing with the insured, an insurance agent has no duty beyond what he or she has specifically undertaken to perform for the insured, nor does an agent have a duty to advise, guide or direct the client regarding additional or future coverage changes. The agent need only exercise reasonable care by transmitting the information secured from the insured and necessary to obtain the requested coverage.²³

By contrast, a broker, as the "agent" of the insured, is liable for any loss sustained by the insured principal (i) if the broker fails to procure insurance or does not follow instructions when obligated to do so, (ii) if the policy obtained is void or materially defective through the broker's fault, or (iii) if the insured principal suffers damage through the act or omission of the broker. In his or her relationship with the insured, the broker is under a continuous and affirmative duty to

²⁰ *Johnson v. Farmers & Merchants State Bank of Balaton*, 320 N.W.2d 892, 898 (Minn. 1982).

²¹ 16 A J. APPLEMAN, INSURANCE LAW AND PRACTICE, § 8836 (1981); *Graham v. Milky Way Barge, Inc.*, 923 F.2d 1100, 1105-06 (5th Cir. 1991); *Madsen v. Allstate Ins. Co.*, 760 F. Supp. 1389, 1393 (D. Or. 1991).

²² *Albany Insurance Co. v. Rose-Tillman, Inc.*, 883 F.Supp. 1458 (D. Or. 1995).

²³ *Farmers Ins. Co. v. McCarthy*, 871 S.W.2d 82 (Mo. Ct. App. 1994); HOLMES/APPLEMAN ON INSURANCE 2D, § 47.2.

provide responsive and competent advice to the insured.²⁴ Section 2120 of the New York Insurance Law reflects the codification of the long-standing common law that as the agent of the insured, a broker holds a fiduciary duty to the insured requiring the highest levels of loyalty, skill, and obligation.²⁵ As the “agent” of the insured, the scope of the broker’s duties and obligations to his or her principal client and the attendant liabilities for failing in those duties are significantly greater than those placed upon the agent of the insurer.

The Proposed Change Would Absolve WYO Insurers from Liability for their Errors and the Change is Unnecessary to Shield Insurers from Agent Errors: The proposed designation of all insurance producers as “agents of the insured” for all purposes is being sought by the WYO insurers for the sole purpose of shielding themselves from liability for claimed errors or omissions on the part of their duly appointed agents. The simple fact is that such a blanket designation is entirely unnecessary and unwise. It would unfairly absolve insurers from liability for their errors, and has the potential to cause significant problems for insurance agents.

As explained above, agency contracts between agents and insurers contain indemnification provisions requiring the parties to indemnify each other for their errors. Thus, if an agent, in reliance on the insurer, makes an error and is sued, the agent can look to the company for indemnification. The proposed change would effectively nullify the agency contracts and, therefore, the right of indemnification between an agent and an insurer. The effect would be to absolve the company of their errors, leaving the agent fully liable for errors for which they are not fully responsible.

The need to resolve liability for errors and agent-insurer disputes is common to all lines of insurance; flood insurance is not unique in this respect. There exists ample case law to support the finding that where an insurance producer breaches a duty owed to his or her principal, be that the insurer, insured, or both, the producer will be held accountable for damages resulting from that breach.²⁶ Agency contracts in place between property and casualty agents and their respective carriers all mandate that the agent indemnify the carrier in the event of a liability imposed upon the insurer as a result of the agent’s error or omission or breach of the terms of the agency agreement. Nothing more is needed to ensure that the WYO carriers are held harmless from the errors or omissions of their appointed agents.

²⁴ *AAS-DMP Management, L.P. Liquidating Trust v. Acordia Northwest, Inc.*, 63 P.3d 860,864 (Wash. Ct. App. 2003); Bertram Harnett, RESPONSIBILITIES OF INSURANCE AGENTS AND BROKERS § 3.07 (4), 3-76.

²⁵ *Evvtex Co., Inc. v. Hartley Cooper Associates Ltd.*, 911 F.Supp. 732, 738 (S.D.N.Y. 1996); *Lake County Grading Co. of Libertyville, Inc. v. Great Lakes Agency, Inc.*, 589 N.E.2d 1128 (Ill. App. Ct. 1992).

²⁶ *See Gulf Ins. Co. v. Kolub Corp., Inc.*, 404 F.2d 115 (10th Cir. 1968); *Insurance Company of North America v. J.L. Hubbard Co.*, 318 N.E.2d 289 (Ill. App. Ct. 1974); *Trinity Universal Insurance Company v. Fuller*, 524 S.W.2d 335 (Tx. Ct. App. 1975); Clarence E. Hagglund, INSURANCE PRODUCER LIABILITY 61-70 (Common Law Publishing 1991).

In the NFIP setting, if a WYO carrier is brought into litigation as a result of the conduct of one of its appointed agents, there is nothing that would preclude the insurer from pursuing indemnification or contribution from the agent through the agent's errors and omissions professional liability carrier. Simply put, there is no need for the proposed change. The protection being sought by the WYO insurers from unwarranted liability stemming from the errors or omissions of their appointed agents is already established and in place.

Loss of Indemnification Could Cause Loss of E&O Coverage: Although the proposed change might make litigation simpler for the WYO companies by cutting them off from liability through their agents, the negative effects of the change on agents far outweigh any benefits to the insurers. As stated above, the proposed change would effectively absolve insurers from their errors and leave agents fully liable for errors for which they are not fully responsible. This will greatly increase agents' liability exposures. Agents are already having difficulty finding errors and omissions (E&O) coverage. If this change becomes effective, such coverage could become completely inaccessible: E&O carriers could exit the market completely, or choose to price the coverage out of reach of most agencies. Loss of E&O coverage would force agents to drop out of NFIP or leave the business completely.

3. Other Practical Implications

The Proposed Change Could Cause Agent Confusion and Ultimately Mislead Consumers: Agents are accustomed to selling flood insurance in the same manner that they sell other property and casualty insurance – that is, on behalf of an insurer, under the control and guidance of that insurer. Agents, particularly small agencies lacking extensive resources, rely on their carriers for guidance and information as to particular lines of insurance and as to their carrier's specific policies and procedures. Loss of the contractual relationship between the agent and insurer could harm communications between agent and insurer and lead to confusion and misunderstanding. Many agents work for multiple insurers. Without direct, clear guidance from each insurer, the agent is left to determine the best course of action. This places a heavy burden on agents, who must choose among the “best practices” of many carriers and are left open to second-guessing and, ultimately, liability. This harms agents and insurers, but in the long run the greatest harm is done to the consumer.

The proposed change also poses potential harm to consumers because of the way in which flood insurance is sold. Flood insurance generally is packaged with other lines of insurance – homeowners, auto, and others. An agent offering such insurance will be subject to different requirements and responsibilities depending upon which line the agent is talking about at a particular moment. This will not only cause the agent confusion – a “broker” one minute, an “agent” the next – but it will potentially mislead consumers who may wonder why the information and advice they receive regarding flood insurance differs so greatly from the information and advice they receive on the other lines they are purchasing. Consumers are not looking for different levels of advice and information from their “agent.” They are seeking consistent treatment so they are able to determine and analyze their options.

The potential for confusion and inconsistent treatment of insurance producers can be

extended to instances in which an insured makes claims for a flood related loss under both a homeowners policy and a WYO-issued flood policy. If the proposed change were to go into effect, the producing agent could be deemed the “agent” of the insurer for purposes of the homeowners policy portion of the litigated claim and the “agent” of the insured (the “broker”) on the WYO issued flood policy. As previously discussed, different relationships give rise to different duties owed by the producer to his or her principal.

The Proposed Change Could Decrease Agent Participation and Harm NFIP: The combined effects of the legal and practical burdens imposed by the proposed rule could damage the long-term prospects for the flood insurance program.

The NFIP is currently operational in over 19,000 communities across the country. In a majority of those communities, flood insurance is optional. There are only a few thousand communities where flood insurance is required. For the most part, flood insurance is purchased by homeowners and businesses who are prudently managing their risks. The placement of such policies is made easier by the ready availability of agents to sell and service flood insurance.

The heavy burdens imposed by the proposed rule – the loss of E&O coverage; the complete liability for all errors and omissions; the uncertain new responsibilities and obligations under state law – may cause agents to leave the program. Agents might determine that the extra costs and responsibilities are simply not worth the small percentage of their business that they derive from selling flood insurance. This is particularly likely in those communities where flood insurance is not mandated – representing a majority of the communities where flood is currently sold and the future expansion of the flood insurance program. Without convenient access to flood insurance coverage through their agents, consumers are less likely to take the affirmative steps necessary to secure coverage unless they are required to. Thus, the number of policies will decrease and the expansion of the program will be severely hampered.

Conclusion

In conclusion, we oppose the addition of section 61.5(f) because of the burdens it will impose on agents and the harm it will cause agents, consumers and the National Flood Insurance Program. As we stated above, however, we support the goal of the proposed rule and the removal of flood insurance program lawsuits to federal court. We believe this will lessen the confusion that currently exists in determining jurisdiction of lawsuits related to NFIP and will help mitigate the costs of litigating such suits. We also believe federal court jurisdiction is a more narrowly-focused way of discouraging frivolous lawsuits, one that does not unduly favor the WYO insurers at the expense of their agents.

Thank you for your consideration.

Sincerely,

Pat Borowski
PIA National
Senior Vice President
Government Relations