



TEMENOS

PRIVATE FLOOD RULE SUMMARY RULE EFFECTIVE 7/1/19

Courtesy of the Temenos Compliance Advisory Team

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PRIVATE FLOOD RULE – EFFECTIVE 7/1/19

May continue to accept private flood policies as currently permitted by each Agency until this date.

I. Must accept private policies that meet definition of “private flood insurance” (page 19), which is defined as follows:

1. Issued by an insurance company that is:

- **Licensed**, admitted, or otherwise approved to engage in the business of issuance in the State or jurisdiction in which the property to be insured is located
- Recognized, or not disapproved, as a surplus lines insurer by the insurance regulator of the State or jurisdiction where the property is located in the case of a policy of difference of conditions, multiple peril, all risk, or other blanket coverage insuring nonresidential commercial property.
- Includes surplus lines insurers for noncommercial properties. (page 20)

2. Provides coverage “at least as broad as” under an SFIP – must consider deductibles, exclusions, and conditions offered by insurer:

- SFIP – Definition: Standard flood insurance policy issued under the NFIP in effect as of the date the private policy is provided to a regulated lending institution.
 - ✓ Should compare like policies based on type – single family dwelling, condo, etc.
- Defines the term “flood” to include the events defined as “flood” under the SFIP¹; **See Appendix A**
- Contains the coverage and provision specified in an SFIP, including those relating to building property coverage, personal property coverage (if purchased), other coverages, and the increased cost of compliance²; **See Appendix A**
- Deductibles no higher than the specified NFIP max for the same type of property, and includes similar non-applicability provisions as under SFIP, for any total policy coverage amount up to the max available under the NFIP at the time the policy is provided to the lender;
 - ✓ For policies with coverage exceeding that available under the NFIP, the policy must only meet the deductible for the amount of coverage available in an SFIP.

Example: commercial structure with coverage of \$1M need only have deductible that matches the \$500,000 max available under NFIP. Acceptable for policy to have higher deductible for the coverage over \$500,000.
- Provides coverage for direct physical loss caused by a flood³; **See Appendix A**
 - ✓ May exclude other causes of loss identified in an SFIP
 - ✓ Any additional exclusions than those in an SFIP may only pertain to coverage that is in addition to the amount and type of coverage that could be provided by an SFIP; AND
 - ✓ Need not accept policies with additional exclusions unless the exclusions have the effect of providing broader coverage.
- Does not contain conditions that narrow the coverage that would be provided in an SFIP.

- Anti-concurrent causation clauses: if two perils cause loss, one of which is excluded and one of which is covered, the loss is not covered— Okay, as long as clause excludes losses to no greater degree than an SFIP.
- 3. Includes a requirement for insurer to give *45 days written notice* before cancellation or non-renewal to both insured and lender (or servicer acting on lender's behalf);**
- The Agencies understand this requirement is broader than in the SFIP, but this is the final rule. (Page 21)
- 4. Includes info about *availability of NFIP* coverage;**
- 5. Includes a *mortgage interest clause* similar to SFIP⁴; See Appendix A**
- Agencies understand that this might create an issue for condo policies as those do not typically include this, but this must be complied with. (Page 21)
- 6. Includes provision requiring insured to *file suit no later than one year* after the date of written denial for all or part of a claim under policy; AND**
- We understand this might disqualify private policies with different or no statute of limitations.
- 7. Contains *cancellation provisions* that are as restrictive as those in SFIP⁵; See Appendix A.**
- **Force Placement – Under existing force placement rules, a declarations page is sufficient to demonstrate borrower's purchase of flood insurance.**
 - For private flood insurance, a declarations page does not provide sufficient detail. Lender will need to request additional policy pages from borrower to determine whether policy meets definition of private flood insurance.
 - **Conflicts with State Law**
 - It's possible that some state laws will prevent private policies from meeting the definition of private flood insurance. In those states, a lender will not be required to accept private policies that do not meet the above definition, but may exercise their discretion to optionally accept them.
 - **Compliance Aid – Allows lender to conclude that a policy meets the definition of “private flood insurance” without further review, if policy or endorsement from insurer:**
 - Includes the following statement - “This policy meets the definition of private flood insurance contained in 42 U.S.C. 4012a(b)(7) and the corresponding regulation.”
 - A Lender can optionally choose not to rely on the statement and instead make its own determination based on the above criteria.
 - The Agencies do not regulate the insurers. If the insurer does not choose to include this statement, the lender will be required to make a determination about whether the policy meets the definition of “private flood insurance” and therefore whether the lender is required to accept the policy.
 - **You can't reject a policy simply because it doesn't have the statement. (page 34)**

II. Option to accept private policies that do not meet definition of “private flood insurance” issued by private insurers:

1. Policy must meet the following requirements:

- Issued by an insurance company that is:
 - **Licensed**, admitted, or otherwise approved to engage in the business of issuance in the State or jurisdiction in which the property to be insured is located
 - **Recognized**, or not disapproved, as a surplus lines insurer by the insurance regulator of the State or jurisdiction where the property is located in the case of a policy of difference of conditions, multiple peril, all risk, or other blanket coverage insuring nonresidential commercial property.
- Must provide coverage in the amount required by the flood insurance purchase requirement;
- Covers both the mortgagor and the mortgagee as loss payees;
 - Exception: not required for policy provided by condo association, cooperative, homeowners association, or other applicable group for which premium is paid by such organization.
- Must provide sufficient protection of the loan, consistent with general safety and soundness principles.
 - Lender must document conclusion regarding sufficiency of the protection in writing.
 - Some factors to consider:
 - ✓ Whether the insurer provide adequate notice of cancellation to the mortgagor and mortgagee to ensure timely force placement if necessary;
 - ✓ Whether the terms and conditions of the policy with respect to payment per loss or payment per occurrence and aggregate limits are adequate to protect the lender's interest in the collateral;
 - ✓ Whether the policy complies with State insurance laws; and
 - ✓ Whether the provider has the financial strength, solvency, and ability to satisfy claims.

2. Can include other forms of insurance including captive insurance, self-insurance, and other types of alternative insurance policies.

III. Option to accept private policies that do not meet definition of “private flood insurance” issued by Mutual Aid Societies:

1. Mutual Aid Society – an organization:

- Whose members share a common religious, charitable, educational, or fraternal bond;
- That covers losses caused by damage to members’ properties pursuant to an agreement, including damage caused by flooding, in accordance with this common bond; and
- That has demonstrated a history of fulfilling the terms of the agreement to cover the losses to members’ property caused by flooding.

2. May accept policy issued by MAS, if criteria are met:

- The institution’s primary supervisory agency has determined that such plans qualify as flood insurance for purposes of the Federal flood insurance statutes;
 - The Board, FDIC, and NCUA expect that cases in which they approve policies issued by MSA’s will be rare and limited. (Page 50)
 - There could be some inconsistency in which regulators accept MSA’s.
- The policy meets the amount of coverage for losses specified in the flood insurance purchase requirement;
- The policy covers both the mortgagor and the mortgagee as loss payees; AND
- The regulated lending institution has determined that the policy provide sufficient protection of the loan.
 - Must be consistent with safety and soundness principles. Some considerations might include:
 - ✓ Whether deductibles are reasonable based on borrower’s financial condition;
- Lender must document its conclusion.
- Remember the definition of MSA has a requirement that the MSA has a demonstrated history of paying such claims.

3. Escrow – Flood escrow requirement only applies if borrower is paying for policy. If MSA is paying for policy, no escrow required. (Page 49)

IV. Reality

1. *“...most existing flood policies issued by private insurers would not meet the definition of “private flood insurance” under the Biggert-Waters Act and that insurers would most likely request that lenders accept the policies under the more flexible discretionary acceptance provisions. The provisions on discretionary acceptance, including acceptance of plans issued by mutual aid societies, do not impose affirmative obligations upon lenders. Accordingly, regulated lending institutions may choose not to accept policies under those provisions and therefore would have no associated compliance burdens.”*
 - BUT, you still need to be able to recognize a private flood insurance policy in order to know whether you are required to accept it. And if insurer doesn't include the compliance aid, then you are obligated to do your own analysis.
2. Those lenders currently accepting private flood insurance policies already have experience evaluating those private policies under the current criteria in Biggert-Waters, and this new criteria is almost identical, so the compliance burden should not be that challenging.
3. However, there will be small entities that don't currently accept private flood that will have a compliance burden when it comes to determining whether a policy meets the definition of “private flood insurance”, if the insurer fails to include the compliance aid.
 - These entities will need to be prepared to make this determination, as necessary.

Appendix A

¹Events defined as “flood” on current SFIP:

Flood, as used in this flood insurance policy, means:

1. A general and temporary condition of partial or complete inundation of two or more acres of normally dry land area or of two or more properties (one of which is your property) from:
 - Overflow of inland or tidal waters
 - Unusual and rapid accumulation or runoff of surface waters from any source
 - Mudflow
2. Collapse or subsidence of land along the shore of a lake or similar body of water as a result of erosion or undermining caused by waves or currents of water exceeding anticipated cyclical levels that result in a flood as defined in A.1.a. above.

²Coverages specified in SFIP: see pages 3-9 of SFIP

³Exclusions specified in SFIP: see Page 12-14 of SFIP - Also see other types of exclusions by type of coverage in SFIP

⁴Mortgage Clause from SFIP

The word “mortgagee” includes trustee. Any loss payable under Coverage A—Building Property will be paid to any mortgagee of whom we have actual notice, as well as any other mortgagee or loss payee determined to exist at the time of loss, and you, as interests appear. If more than one mortgagee is named, the order of payment will be the same as the order of precedence of the mortgages. If we deny your claim, that denial will not apply to a valid claim of the mortgagee, if the mortgagee:

1. Notifies us of any change in the ownership or occupancy, or substantial change in risk of which the mortgagee is aware;
2. Pays any premium due under this policy on demand if you have neglected to pay the premium; and
3. Submits a signed, sworn proof of loss within 60 days after receiving notice from us of your failure to do so.

All of the terms of this policy apply to the mortgagee. The mortgagee has the right to receive loss payment even if the mortgagee has started foreclosure or similar action on the building.

If we decide to cancel or not renew this policy, it will continue in effect for the benefit of the mortgagee only for 30 days after we notify the mortgagee of the cancellation or non-renewal.

If we pay the mortgagee for any loss and deny payment to you, we are subrogated to all the rights of the mortgagee granted under the mortgage on the property. Subrogation will not impair the right of the mortgagee to recover the full amount of the mortgagee's claim.

⁵Cancellation clause from SFIP:

E. CANCELLATION OF THE POLICY BY YOU

1. You may cancel this policy in accordance with the applicable rules and regulations of the NFIP.
2. If you cancel this policy, you may be entitled to a full or partial refund of premium also under the applicable rules and regulations of the NFIP