



Flood Insurance

IV. Frequently Asked Questions

Frequently Asked Questions - Determination

§ When is a bank required to get a new determination?

- Part 339 requires that each time a bank makes, increases, extends, or renews a loan that it must determine whether or not the improved property is in a special flood hazard area.
- An existing flood determination can be relied upon in certain circumstances if the determination is less than seven years old, the flood map and flood status haven't changed, and it was prepared on the standard flood hazard determination form.

Frequently Asked Questions - Remapping

§ **The area has been remapped; now what?**

- If the property is now located in a special flood hazard area, the bank must start force-placement procedures.
- If the property has been removed from the special flood hazard area, flood insurance is no longer required.

Frequently Asked Questions - Discrepancies

- § **What should a bank do if there are discrepancies in the flood zone determinations?**
- Federal Emergency Management Agency (FEMA) has instructed insurance companies to use the more hazardous flood zone for rating the policy unless the policy qualifies for the “grandfather rule”.
 - A bank should ensure the discrepancy hasn’t resulted from a simple mistake, such as an incorrect street address on the determination.

Frequently Asked Questions - Disputes

- § **What are the bank's responsibilities if the borrower disputes the property is in a special flood hazard area?**
- There is no flexibility in the flood insurance requirements. If the determination shows the improvements are in a special flood hazard area, flood insurance is required.
 - The borrower can pursue a Letter of Map Amendment (LOMA) from FEMA. Until a LOMA is obtained, insurance is required.

Frequently Asked Questions – Detached Structures

§ What does it mean for a structure to be “*part of a residential property*” and to be “*detached*”?

- ***Residential Property:*** A property that is used primarily for personal, family or household purposes, and not used primarily for agricultural, commercial, industrial or other business purposes.
- ***Detached:*** A structure is “detached” from the primary residential structure if it is not joined by any structural connection to the residential structure.

Frequently Asked Questions – Detached Structures

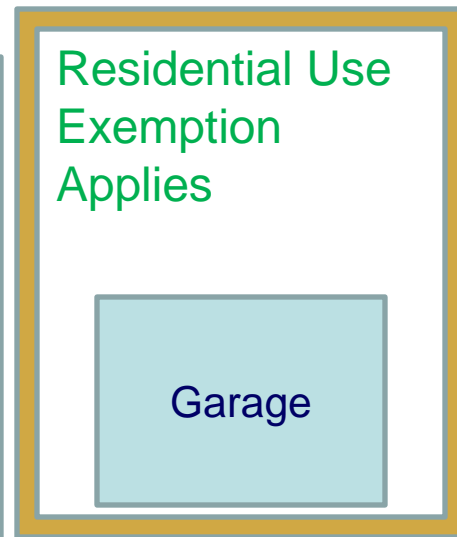
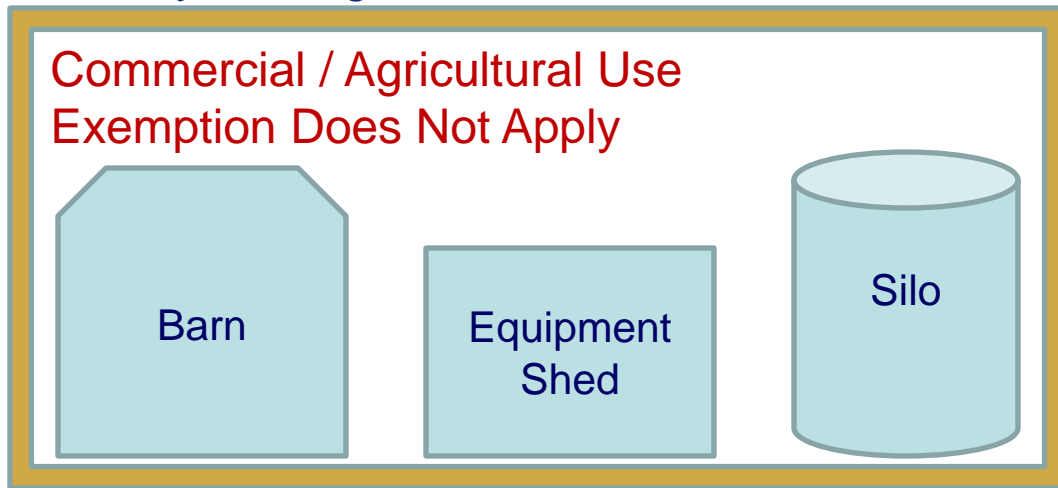
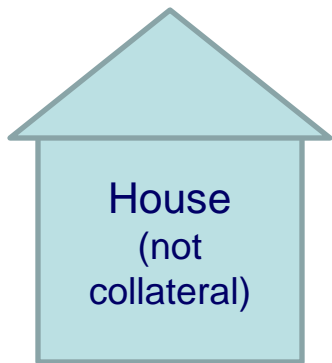
§ How to determine when a structure “*does not serve as a residence*”:

- Structure could serve as a residence if it includes sleeping, bathroom or kitchen facilities, but not all three facilities are necessary.
- Lender should focus on the structure’s intended use.
- Lender must make good faith determination as to whether detached structure serves as a residence.

Frequently Asked Questions – Detached Structures

Does a lender need to take a security interest in the primary residential structure for detached structures to be eligible for the exemption?

§ No, but the lender needs to evaluate the uses of detached structures to determine if they are eligible.



Frequently Asked Questions - Coverage

§ How does a bank calculate the appropriate amount of insurance?

- Compare three values: (1) The maximum amount of insurance available under the NFIP, (2) the insurable value of the property, and (3) the principal loan amount(s) outstanding. The lesser of the three is the minimum required amount of coverage.

<u>Property Type</u>	<u>NFIP Limits</u>
Residential	\$250,000
Residential – Multi-Family	\$500,000
Commercial	\$500,000
Personal Contents	\$100,000
Commercial Contents	\$500,000

First Lien Home Loan Examples

	Example 1	Example 2
Loan Amount	\$100,000	\$200,000
Insurable Value	\$150,000	\$150,000
Maximum Available Insurance	\$250,000	\$250,000
Minimum Required Flood Insurance Coverage	\$100,000	\$150,000

Commercial Building Example

Loan Amount	\$1,000,000
Insurable Value	\$1,000,000
Maximum Available Insurance	\$500,000
Minimum Required Flood Insurance Coverage	\$500,000

Example - Subordinate Lien Transaction

Lender A

First lien home loan = \$100,000

Lender B

Second lien home loan = \$50,000

Minimum
Required
Insurance
\$150,000



NFIP Insurance
Available
\$250,000

Frequently Asked Questions - Coverage

- § **How does a bank determine appropriate coverage for multiple buildings?**
- The calculation is the same as for a single building; however, the bank must spread the coverage among all of the buildings in the special flood hazard area. Each building must have some coverage.

Multi-building Coverage Example



Required Coverage
\$200,000



Commercial Buildings and Home Example

Structure	(A) Insurable Value	(B) Max NFIP Available	(C) <u>Lesser</u> of A and B
Single-Family	\$200,000	\$250,000	\$200,000
Commercial #1	\$1,000,000	\$500,000	\$500,000
Commercial #2	\$300,000	\$500,000	\$300,000
Aggregate of Maximum Building Coverage			\$1,000,000
Loan Amount			\$2,000,000
<u>Lesser</u> of Aggregate Coverage and Loan Amount			\$1,000,000

Frequently Asked Questions - Value

§ **How does a bank determine insurable value?**

- A reasonable, consistent valuation method should be used, such as an appraisal based on the cost value (not market value), a construction-cost calculation, or the insurable value from a hazard insurance policy.
- Other reasonable valuation methods can be used as long as they can be supported.

Frequently Asked Questions - Value

FEMA benefits are paid based on property type.

Primary Residence:

Benefits paid based on replacement cost value (RCV).

All Other Structures:

Benefits paid based on actual cash value (ACV).

Formula: $ACV = RCV - Depreciation$

Frequently Asked Questions - Proof

§ How can a bank prove that flood insurance coverage is in place?

- For a new policy, proof of insurance consists of a copy of the written application and the method of premium payment, for example, a copy of the check.
- For an existing policy, proof of insurance consists of the declarations page which includes the policy number and certain information about the insurance company or agent.

Frequently Asked Questions - Blanket Policy

- § **The bank has a blanket insurance policy in place from a private insurance company. Why does the bank still need the borrower to get a flood insurance policy to comply with the flood insurance regulation?**
- Flood insurance regulations are designed to protect the property owner's interest. When a customer buys a flood insurance policy, or when a bank force-places a policy, that policy shows the customer as the "insured" party. Conversely, blanket policies usually protect only the bank's interest. As a result, most blanket insurance policies do not meet Part 339 requirements.

Frequently Asked Questions - Force-Place

§ **When does a bank have to force-place insurance?**

- A bank must force-place insurance upon determining that it does not have adequate insurance in place. This means beginning force-placement procedures immediately upon discovery of the deficiency.

Frequently Asked Questions - Force-Place

- § **Can a bank send the 45-day notice about force-placing insurance prior to the policy's expiration date?**
- No. However, some banks choose to send a courtesy notice to customers prior to expiration as a reminder.

Frequently Asked Questions - Force-Place

- § **May a lender commence a force-placed insurance policy on the day the previous policy expires, or must the new policy begin the day after?**
- If the previous policy expires at midnight at the end of Day 1, the lender's new force-placed policy should not begin to provide coverage until just after midnight at the beginning of Day 2. If the lender did force place on Day 1 and the policy provided overlapping coverage, the lender could not charge and collect premiums and fees from the borrower for the period of overlapping coverage on Day 1.

Frequently Asked Questions - Applicability

§ Are condominiums and mobile homes covered by the flood insurance regulations?

- Yes, usually.
- FEMA issues a Residential Condominium Building Association Policy to condominium associations to cover the entire complex.
- Section VI of the 2009 Interagency Questions and Answers addresses condominium questions.
- Mobile homes, if permanently affixed to the foundation, are generally subject to the flood insurance requirements.

Frequently Asked Questions - Contents

§ **When is contents insurance required?**

- Contents insurance is required when:
 1. Contents are taken as collateral; AND
 2. The bank also takes the building where the contents are located as collateral; AND
 3. The building is located in a special flood hazard area.

Examples - Building or Contents Coverage?

Chef Goodcook loan examples

Example 1: Collateral = GBSA

(no flood insurance required)

Example 2: Collateral = Mortgage on building in SFHA

(flood insurance required on building only, not the contents)

Example 3: Collateral = GBSA and Mortgage on building in SFHA and contents are in the building

(flood insurance required on building and contents)

GBSA = General Business Security Agreement

SFHA = Special Flood Hazard Area

Frequently Asked Questions - Escrows

When does a bank meet the small lender exemption?

- § Institution may qualify for the small lender exemption if it had total assets of less than \$1 billion as of December 31 of either of the two prior calendar years.
- § Examples:
 1. Lender A has assets of \$998 million on December 31, 2014 and \$1.01 billion on December 31, 2015. Lender A may qualify for the exemption for 2016.
 2. Lender B has assets of \$1.01 billion on December 31, 2014 and \$1.02 billion on December 31, 2015. Lender B does not qualify for the exemption for 2016.

Frequently Asked Questions - Escrows

When must a bank begin escrowing if it no longer qualifies as a small lender?

- § A bank must escrow flood insurance premiums and fees for any loans made, increased, extended, or renewed on or after July 1 of the succeeding calendar year after it has a change in status.
- § Example:

Lender C qualifies for the small lender exemption at the beginning of 2017. That lender has assets of \$1.3 billion on December 31, 2017, and \$1.4 billion on December 31, 2018. Lender C will be required to escrow flood insurance premiums and fees for any loans made, increased, extended, or renewed on or after July 1, 2019.

Frequently Asked Questions - Escrows

- § A bank that no longer qualifies for the small lender exemption must also provide notice of the option to escrow by September 30th of the first calendar year in which it has a change in status.
- § It must begin escrowing as soon as reasonably practicable after receiving the borrower's request to escrow.
- § Example:

Lender C qualifies for the small lender exemption at the beginning of 2017. That lender has assets of \$1.3 billion on December 31, 2017, and \$1.4 billion on December 31, 2018. Lender C must provide notices of the option to escrow by September 30, 2019.

Frequently Asked Questions - Escrows

If a bank meets the other requirements, is it still eligible for the small lender exemption if:

§ It offers escrows at the request of the borrower?

Ø Yes

§ It collects escrow funds at closing at the request of a third party and then transfers the escrow funds to the third party servicing the loan?

Ø Yes

§ It collects escrow funds at closing and services the loan?

Ø No

Frequently Asked Questions - Escrows

If a lender was required to escrow for taxes and hazard insurance under the HPML rules on or before July 6, 2012, is such a lender, who otherwise qualifies for the small lender exemption, required to escrow the premiums and fees for flood insurance?

§ No, HPML escrow requirements should not result in the loss of the escrow exemption for a small lender that made an HPML-covered loan prior to enactment of the Biggert-Waters Act because the lender was not required to escrow for the entire term of the loan. In addition, if a lender required escrow for an HPML solely to comply with Federal law, a lender complying with that law did not have its own separate policy of consistently and uniformly requiring escrow.