ABA Staff Analysis: Interagency Questions and Answers Regarding Flood Insurance
76 Fed. Reg. 64175 (October 17, 2011)\(^1\)

Background.
On March 21, 2008, the OCC, FDIC, Federal Reserve, FCA, and NCUA (collectively, the Agencies) initiated an update of the interagency guidance on Flood Insurance compliance, soliciting comment on proposed revisions to the Interagency Questions and Answers Regarding Flood Insurance (Q & As).\(^2\) On July 21, 2009, the Agencies published 77 final Q & As and proposed five additional Q & As, two seeking to define “insurable value” and three on force placement.\(^3\) ABA filed comments to both proposals.\(^4\)

Almost 28 months later, on October 17, 2011, the Agencies have finally published two final Q & As, one defining insurable value (#9), and one addressing force placement (# 61). In addition, they have withdrawn question 10 and have re-proposed for comment three questions and answers on force placement (# 57, 60, and 62). Comments are due on December 1, 2011.

Summary and Discussion Questions:

**Question 9 (final):** Responding to some of ABA’s comments, the Agencies have backed away from their previous suggestion that “insurable value” should equate with 100% replacement cost value (RCV) for all properties. They recognize that adherence to 100% RCV is inappropriate in those instances in which the NFIP loss payout would be at actual cash value (ACV) as this would result in a borrower paying for coverage that would exceed the amount the NFIP will pay in the event of a loss. In effect, the Agencies establish two measures of insurable value:

1. For single-family dwellings (covered under the NFIP Dwelling form that pays losses at RCV) and single-family condominium units (also settled at RCV, assuming there is no coinsurance penalty for a RCBAP insured for less than 80% of RCV), insurable value should be the equivalent of 100% RCV.

2. For “other” residential and commercial buildings, there is no obligation to tie insurable value to RCV; instead, the lender is directed “to consider the extent of recovery allowed under the applicable NFIP policy.”

In addition, the rule gives lenders the flexibility to choose from a number of methods to determine and document insurable value, including:

- a cost-based appraisal (not a market value),
- a construction-cost calculation,

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the insurable value stated in a hazard insurance policy (recognizing that adjustments to include the cost of the foundation may be necessary), or
any other reasonable approach so long as it can be supported.

Discussion Questions:
1. What do you use to document RCV for a single-family dwelling?
2. If you are relying on hazard insurance, how do you calculate the cost of the foundation?
3. For commercial properties, should we comment that the parenthetical “not a market value” conflicts with the fourth alternative, “any other reasonable approach so long as it can be supported?”
4. Interest in urging the Agencies to work with FEMA to require NFIP and WYO agents to determine and document insurable value?

Question 10 (withdrawn) proposing alternate insurable value calculations for certain non-residential buildings used for ranching, farming or industrial purposes.

Question 57 (proposed): states that force placement is required if all of the following occur:
- The lender determines at any time during the life of the loan that property securing the loan is in a SFHA;
- Flood insurance is available;
- The lender determines that flood insurance coverage does not exist or is inadequate; and
- After required notice, the borrower fails to purchase the required amount.

The Q & A also outlines what the force placement notice must state:
- The borrower’s obligation to purchase and maintain for the life of the loan flood insurance in an amount at least equal to the amount required under the NFIP.
- If the borrower does not purchase it within 45 days, the lender will purchase it and charge the borrower for the premium and fees of a force placement policy, which are likely to be more expensive than if the borrower purchases it.

In addition, it “encourages” institutions:
- To explain their force placement policies, including, if applicable, that they charge for force placement coverage within the 45-day period and the timing of that charge.
- To send the Notice of Special Flood Hazards and Availability of Federal Disaster Assistance (the Flood Notice) in situation when a borrower had not previously been notified that a property is in a special flood hazard area such as when an area has been re-mapped.

Discussion question:
1. This is new, and goes beyond the regulatory requirements since a change in flood zone is not a triggering event that requires the Flood Notice under the regulations. The Agencies couch this as a best practice and speak only of "providing" the Flood Notice; they say nothing about obtaining a signature to confirm receipt of such notice. Query whether in the field, it will be "required" by examiners. If so, will this be a problem?

Question 60 (proposed): This question addresses when a force placement notice must be provided, explaining that it should be provided:
• “upon making the determination” that flood insurance has expired or is inadequate in amount; and
• when a lender learns that a property is in a SFHA due to map revisions.

The Agencies also add a recommendation that lenders advise borrowers when policies are about to expire, but they do not provide any guidelines on how far in advance such notice should be made.

**Question 61** (final): This question and answer addresses how quickly lenders must force place flood insurance if a flood policy is not obtained (or renewed) within the 45-day period. The Agencies refuse to assign a specific time period that would be acceptable; instead, they state that any delay beyond the 45th day must be “brief” and “reasonably explained” – i.e., documented. The Q&A also states that a lender should have a policy and procedures in place to ensure that force placement begins after conclusion of the 45-day notice period.

**Question 62** (proposed): This question and answer addresses when force placed flood insurance may be obtained, allowing an institution to purchase a force placed policy prior to the expiration of the 45-day period, *provided that* the borrower agrees to allow the lender to obtain such coverage as a contractual condition of the loan. It also reiterates that a force placed policy must be the equivalent of an NFIP policy, and it must protect the borrower and lender equally.

Finally, it “encourages” lenders to:
• explain their force placement policies to borrowers (including their policy on charging for coverage during the 45-day notice period)
• escrow flood insurance premiums.

Discussion questions:
1. Is the requirement for a contract provision governing force placement an issue?
2. Do institutions currently explain their force placement policy?
3. In your letter reminding the borrower of the obligation to maintain flood insurance, do you explain the following:
   • Force placement may occur within the 45-day notice period?
   • Force placed policies are more expensive than NFIP policies?
   *Note: in the request for comments, the Agencies specifically request comment on how to ensure that borrowers have this information.*
4. Recalling that mortgagee coverage under a NFIP policy extends for 30 days following lapse, the Agencies also ask whether the final Q & A should bar a lender from charging for overlapping lender-placed coverage during this 30-day period. Is our response that the borrower is not protected during this 30-day period?
5. Concerns about the suggestion that institutions escrow for flood, even when not required?