

Lender Acceptance of the Natural Catastrophe Insurance Program is Mandatory

Summary

Poulton Associates, LLC created this document to help lenders and insurance producers recognize that the private flood insurance policies written through our Natural Catastrophe Insurance Program (the NCIP) must – mandatorily – be accepted in satisfaction of the flood insurance purchase requirement.

In January 2019 the federal banking regulators finalized their rule for lenders' mandatory acceptance of privately written coverage when borrowers need to buy flood insurance because their mortgaged property is in a flood zone. The rule is effective July 1, 2019. This document includes relevant excerpts from the regulation, as well as correlated information about the NCIP. Quoted language from the regulation, and the regulators' explanations of it, are written in blue font. The entirety of the regulation and the regulators' explanations can be found in the Joint Release, "New Rule Covers Private Flood Insurance," February 12, 2019 (cited as the "Joint Release"). The regulation is set out in each regulator's section of the Code of Federal Regulations as follows:

Department of the Treasury, Office of the Comptroller of the Currency, 12 CFR Part 22
Federal Reserve System, 12 CFR Part 208
Federal Deposit Insurance Corporation, 12 CFR Part 339
Farm Credit Administration, 12 CFR Part 614
National Credit Union Administration, 12 CFR 760

Background

The National Flood Insurance Act of 1968 (1968 Act) and the Flood Disaster Protection Act of 1973 (FDPA), as amended, (collectively referenced herein as the Federal flood insurance statutes) govern the National Flood Insurance Program (NFIP). These laws make Federally subsidized flood insurance available to owners of improved real estate or mobile homes located in participating communities and require the purchase of flood insurance in connection with a loan made by a regulated lending institution when the loan is secured by improved real estate or a mobile home located in a special flood hazard area (SFHA) in which flood insurance is available under the NFIP. The laws specify the amount of insurance that must be purchased, and also require such insurance be maintained for the term of the loan. (The requirement for flood insurance, and the term and amounts of such coverage, are hereinafter described as "the flood insurance purchase requirement.") The OCC, [Federal Reserve System], FDIC, FCA, and NCUA (collectively, the Agencies) each have issued regulations implementing these statutory requirements for the lending institutions they supervise.

The [Biggert-Waters Flood Insurance Reform Act of 2012] amends the Federal flood insurance statutes that the Agencies have authority to implement and enforce. Among other things, the

Biggert-Waters Act [...] requires the Agencies to issue a rule to direct regulated lending institutions to accept “private flood insurance,” as defined by the Biggert-Waters Act, and to notify borrowers of the availability of flood insurance coverage issued by private insurers. (Joint Release, pages 3-4).

Mandatory Acceptance of Private Flood Insurance

(1) Mandatory acceptance. [A regulated lending institution] must accept private flood insurance, as defined in [this regulation], in satisfaction of the flood insurance purchase requirement in [this regulation] if the policy meets the requirements for coverage [i.e., limits of insurance] in [this regulation]. (Note: Each regulator adopting the regulation has a version that includes cross-references to its part of the Code of Federal Regulations. In this document, such individualized cross-references are replaced with the generic words “this regulation.”)

(2) Compliance aid for mandatory acceptance. [A regulated lending institution] may determine that a policy meets the definition of private flood insurance in [this regulation], without further review of the policy, if the following statement is included within the policy or as an endorsement to the policy: **“This policy meets the definition of private flood insurance contained in 42 U.S.C. 4012a(b)(7) [added by the Biggert-Waters Act] and the corresponding regulation.”** (Joint Release, page 65).

The NCIP policy form includes such statement confirming that it meets the definition of private flood insurance, and therefore must be accepted by federally regulated lenders.

Definition of Private Flood Insurance for Purposes of Mandatory Acceptance

The Biggert-Waters Act defines private flood insurance as any policy that meets seven total criteria, as set out in 42 U.S.C. § 4012a(b)(7). Those criteria, and how the NCIP meets them, are as follows:

- 1) The policy is issued by an insurer that is licensed, admitted, or otherwise approved to engage in the business of insurance in the State or jurisdiction in which the property to be insured is located, by the insurance regulator of that State or jurisdiction, or in the case of a policy of difference in conditions, multiple peril, all risk, or other blanket coverage insuring nonresidential commercial property, is recognized, or not disapproved, as a surplus lines insurer by the insurance regulator of the State or jurisdiction where the property to be insured is located;
 - NCIP reference: The underwriters of the NCIP are insurers that are either admitted or otherwise approved to engage in the business of insurance via the surplus lines market in all states.

[T]he Agencies confirm that policies issued by surplus lines insurers for noncommercial properties already are covered in the definition of “private flood insurance” as policies that are issued by insurance companies that are

“otherwise approved to engage in the business of insurance by the insurance regulator of the State or jurisdiction in which the property to be insured is located.” (Joint Release, page 12).

Note: Under the Nonadmitted & Reinsurance Reform Act of 2010 (15 U.S.C. § 8201 et seq.), insurers that are domiciled outside the United States and listed on the Quarterly Listing of Alien Insurers maintained by the NAIC are approved to write surplus lines insurance in all states.

- 2) The policy provides flood insurance coverage which is at least as broad as the coverage provided under a standard flood insurance policy under the national flood insurance program;
 - NCIP reference: The NCIP policy form is broader than the NFIP form, including a broader definition of a flood, broader contents coverage, available additional living expense coverage, higher available limits, etc.
- 3) The policy includes:
 - i. A requirement for the insurer to give 45 days’ written notice of cancellation or non-renewal of flood insurance coverage to the insured and the regulated lending institution or Federal agency lender;
 - NCIP reference: “Where this Policy is subject to the [National Flood Insurance Act’s] Mandatory Purchase Requirement for Flood insurance, this Policy may be cancelled by or on behalf of the Underwriters by delivery to the First Named Insured and first mortgagee(s), if any shown in the Policy, by registered, certified, or other first-class mail written notice not less than 45 days from the date cancellation shall become effective.”
 - ii. Information about the availability of flood insurance coverage under the national flood insurance program;
 - NCIP reference: “Should this private placement Policy be cancelled or non-renewed, coverage may be available under the National Flood Insurance Program.”
 - iii. A mortgage interest clause similar to the clause contained in a standard flood insurance policy under the national flood insurance program;
 - NCIP reference: “Whenever a mortgagee is noted on any individual Policy issued hereunder, the following Mortgagee/Loss Payee Clause shall apply but only to building property:

Loss or damage, if any, under this Policy shall be payable to the mortgagee (or trustee) named in the first page of this Policy or named on an endorsement attached hereto, as interest may appear, under all present or future mortgages on the property herein described in which the aforesaid may have an interest, and this insurance, as to the interest of the mortgagee (or trustee), only therein

shall not be invalidated by any act of neglect of the mortgagee or owner of the within described property, by any foreclosure or other proceedings or notice of sale relating to the property, nor the occupation of the premises for purposes more hazardous than are permitted by this Policy, provided that in case the mortgagor or owner shall neglect to pay any premium due under this Policy, the mortgagee (or trustee) shall, on demand, pay the same.”

iv. A provision requiring an insured to file suit not later than 1 year after the date of a written denial of all or part of a claim under the policy; and

- NCIP reference: “No suit, action, or proceeding for the recovery of any claim under this Policy shall be sustainable in any court of law or equity unless:

- a. You have fully complied with all the requirements of this Policy, and

- b. The suit, action, or proceeding is commenced within twelve (12) months after the written denial of the claim or any amount claimed to be due hereunder. Where the law of the state where the premises is located requires that the period of time extend beyond twelve (12) months, this Policy shall conform to the length of time most favourable to the insured.”

4) The policy contains cancellation provisions that are as restrictive as the provisions contained in a standard flood insurance policy under the national flood insurance program.

- NCIP reference: “We reserve the right to cancel this Policy at any time as provided by its terms, but in such case notice must be given simultaneously to you and the mortgagee (or trustee) named herein. If we decide to cancel or not renew this Policy, other than for non-payment of premium, coverage hereunder for the peril of flood only will continue in effect for the benefit of the mortgagee only for 45 days from the date that cancellation or non-renewal is sent to the mortgagee....

This insurance contract may be cancelled at any time. The following conditions may apply:

- a. After submission of an acceptable and complete Cancellation Request Form(s) executed by both the Named Insured and the mortgagee(s) shown as such in the mortgagee or loss payee section of the Coverage Declarations; or

- b. By us or on our behalf for non-payment of premium by delivering to you or by mailing to you at your address as shown in the Coverage Declarations, written notice stating when not less than ten (10) days thereafter the cancellation shall be effective.”

The flood insurance provided under an NCIP policy on residential and commercial structures qualifies for mandatory acceptance by lenders in satisfaction of the mandatory purchase of flood insurance requirement.

Discretionary Acceptance

Even though the NCIP policy form must be accepted by lenders via the mandatory acceptance requirement, we have included the following information regarding the regulation's suggested approach to discretionary acceptance.

(3) Discretionary acceptance. A [regulated lending institution] may accept a flood insurance policy issued by a private insurer that is not issued under the NFIP and that does not meet the definition of private flood insurance in [this regulation] in satisfaction of the flood insurance purchase requirement in [this regulation] if the policy:

(i) Provides coverage in the amount required by [the flood insurance purchase requirement];

(ii) Is issued by an insurer that is licensed, admitted, or otherwise approved to engage in the business of insurance by the insurance regulator of the State or jurisdiction in which the property to be insured is located; or in the case of a policy of difference in conditions, multiple peril, all risk, or other blanket coverage insuring nonresidential commercial property, is issued by a surplus lines insurer recognized, or not disapproved, by the insurance regulator of the State or jurisdiction where the property to be insured is located;

(iii) Covers both the mortgagor(s) and the mortgagee(s) as loss payees, except in the case of a policy that is provided by a condominium association, cooperative, homeowners association, or other applicable group and for which the premium is paid by the condominium association, cooperative, homeowners association, or other applicable group as a common expense; and

(iv) Provides sufficient protection of the designated loan, consistent with general safety and soundness principles, and the [regulated lending institution] documents its conclusion regarding sufficiency of the protection of the loan in writing. (Joint Release, pages 65-66).

Elements 2 and 3 are met within the plain language of the NCIP policy form. Elements 1 and 4 are straightforward numerical evaluations that the lender can perform based on the specific limits of a given policy.

In summary, the NCIP policy form must be accepted because it includes the regulation's statement that it meets the definition of private flood insurance—specifically, it satisfies the criteria in the Biggert-Waters Act. The NCIP policy form also meets the regulation's outline for discretionary acceptance. Under any circumstance, federally regulated lenders can, and must, accept the NCIP policy form when the structure is mandated by law to have flood insurance.

Our service team can be reached at 801-268-2600 Option #2.

For reference, the following is a specimen of the certification contained in at least one NCIP policy form as of March 1, 2019 which confirms that it meets the definition of a private flood insurance policy that must be accepted:

Certification of Conformity

Interagency Final Rule: Loans in Areas Having Special Flood Hazards

This Policy meets the definition of private flood insurance contained in 42 U.S.C. § 4012a(b)(7) and the corresponding regulation.

Per:

FEDERAL LENDING REGULATOR

DEPARTMENT OF THE TREASURY

FEDERAL RESERVE SYSTEM

FEDERAL DEPOSIT INSURANCE CORPORATION

FARM CREDIT ADMINISTRATION

NATIONAL CREDIT UNION ADMINISTRATION

REFERENCE

12 CFR Parts 22 and 172 [Docket ID OCC-2014-0016]

12 CFR Part 208 [Reg. H, Docket No R-1498]

12 CFR Part 339

12 CFR Part 614

12 CFR Part 760

This policy must be accepted by federally regulated lenders as satisfying the mandatory purchase of flood insurance requirement for structures that reside in a special flood hazard area.

We Certify This Policy:

- 1) Is issued by an insurer that is licensed, admitted, or otherwise approved to engage in the business of insurance in the State or jurisdiction in which the property to be insured is located, by the insurance regulator of that State or jurisdiction;
- 2) Provides flood insurance coverage which is at least as broad as the coverage provided under a standard flood insurance policy under the national flood insurance program;
- 3) Includes:
 - a) A requirement for the insurer to give 45 days' written notice of cancellation or non-renewal of flood insurance coverage to the insured and the regulated lending institution or Federal agency lender;
 - b) Information about the availability of flood insurance coverage under the national flood insurance program;
 - c) A mortgage interest clause similar to the clause contained in a standard flood insurance policy under the national flood insurance program;
 - d) A provision requiring an insured to file suit not later than 1 year after the date of a written denial of all or part of a claim under the policy; and
- 4) Contains cancellation provisions that are as restrictive as the provisions contained in a standard flood insurance policy under the national flood insurance program.