Loans in Areas Having Special Flood Hazards; Interagency Questions and Answers Regarding Flood Insurance

***Note: This document is extracted from the* Federal Register *publication at 74 FR 35914 (July 21, 2009). See the* Federal Register *document*[1] *for prefatory comments by the federal Agencies (OCC, FRB, FDIC, OTS, NCUA and Farm Credit Administration) that issued the Q&A. We have updated the Q&A to reflect final and proposed changes and proposed additional questions and answers published by the Agencies in the October 17, 2011,* Federal Register *at 76 FR 64175.*[2]**

The Interagency Questions and Answers are organized by topic. Each topic addresses a major area of the Act and Regulation. For ease of reference, the following terms are used throughout this document: "Act" refers to the National Flood Insurance Act of 1968 and the Flood Disaster Protection Act of 1973, as revised by the National Flood Insurance Reform Act of 1994 (codified at 42 U.S.C. 4001 et seq.). "Regulation" refers to each agency's current final rule.[3] The OCC, Board, FDIC, OTS, NCUA, and FCA (collectively, "the Agencies") are providing answers to questions pertaining to the following topics:

[1] http://www.bankersonline.com/topstory/74fedreg/74FR35912.pdf
[2] http://www.bankersonline.com/topstory/76fedreg/76FR64175.pdf
[3] The Agencies' rules are codified at 12 CFR part 22 (OCC), 12 CFR part 208 (Board), 12 CFR part 339 (FDIC), 12 CFR part 572 (OTS), 12 CFR part 614 (FCA), and 12 CFR part 760 (NCUA).

I. Determining When Certain Loans Are Designated Loans for Which Flood Insurance Is Required Under the Act and Regulation

1. Does the Regulation apply to a loan where the building or mobile home securing such loan is located in a community that does not participate in the National Flood Insurance Program (NFIP)?

Answer: Yes. The Regulation does apply; however, a lender need not require borrowers to obtain flood insurance for a building or mobile home located in a community that does not participate in the NFIP, even if the building or mobile home securing the loan is located in a Special Flood Hazard Area (SFHA). Nonetheless, a lender, using the standard Special Flood Hazard Determination Form (SFHDF), must still determine whether the building or mobile home is located in an SFHA. If the building or mobile home is determined to be located in an SFHA, a lender is required to notify the borrower. In this case, a lender, generally, may make a conventional loan without requiring flood insurance, if it chooses to do so. However, a lender may not make a government-guaranteed or insured loan, such as a Small Business Administration, Veterans Administration, or Federal Housing Administration loan secured by a building or mobile home located in an SFHA in a community that does not participate in the NFIP. See 42 U.S.C. 4106(a). Also, a lender is responsible for exercising sound risk management practices to ensure that it does not make a loan secured by a building or mobile home located in an SFHA where no flood insurance is available, if doing so would be an unacceptable risk.

2. What is a lender's responsibility if a particular building or mobile home that secures a loan, due to a map change, is no longer located within an SFHA?

Answer: The lender is no longer obligated to require mandatory flood insurance; however, the borrower can elect to convert the existing NFIP policy to a Preferred Risk Policy. For risk management purposes, the lender may, by contract, continue to require flood insurance coverage.

3. Does a lender's purchase of a loan, secured by a building or mobile home located in an SFHA in which flood insurance is available under the Act, from another lender trigger any requirements under the Regulation?

Answer: No. A lender's purchase of a loan, secured by a building or mobile home located in an SFHA in which flood insurance is available under the Act, alone, is not an event that triggers the Regulation's requirements, such as making a new flood determination or requiring a borrower to purchase flood insurance. Requirements under the Regulation, generally, are triggered when a lender makes, increases, extends, or renews a designated loan. A lender's purchase of a loan does not fall within any of those categories. However, if a lender becomes aware at any point during the life of a designated loan that flood insurance is required, the lender must comply with the Regulation, including force placing insurance, if necessary. Depending upon the circumstances, safety and soundness considerations may sometimes necessitate such due diligence upon purchase of a loan as to put the lender on notice of lack of adequate flood insurance. If the purchasing lender subsequently extends, increases, or renews a designated loan, it must also comply with the Regulation.

4. How do the Agencies enforce the mandatory purchase requirements under the Act and Regulation when a lender participates in a loan syndication or participation?

Answer: As with purchased loans, the acquisition by a lender of an interest in a loan either by participation or syndication after that loan has been made does not trigger the requirements of Act or Regulation, such as making a new flood determination or requiring a borrower to purchase flood insurance. Nonetheless, as with purchased loans, depending upon the circumstances, safety and soundness considerations may sometimes necessitate that the lender undertake due diligence to protect itself against the risk of flood or other types of loss. Lenders who pool or contribute funds that will be simultaneously advanced to a borrower or borrowers as a loan secured by improved real estate would all be subject to the requirements of Act or Regulation. Federal flood insurance requirements would also apply to those situations where such a group of lenders decides to extend, renew or increase a loan. Although the agreement among the lenders may assign compliance duties to a lead lender or agent, and include clauses in which the lead lender or agent indemnifies participating lenders against flood losses, each participating lender remains individually responsible for ensuring compliance with the Act and Regulation. Therefore, the Agencies will examine whether the regulated institution/participating lender has performed upfront due diligence to ensure both that the lead lender or agent has undertaken the necessary activities to ensure that the borrower obtains appropriate flood insurance and that the lead lender or agent has adequate controls to monitor the loan(s) on an ongoing basis for compliance with the flood insurance requirements. Further, the Agencies expect the participating lender to have adequate controls to monitor the activities of the lead lender or agent to ensure compliance with flood insurance requirements over the term of the loan.

5. Does the Regulation apply to loans that are being restructured or modified?

Answer: It depends. If the loan otherwise meets the definition of a designated loan and if the lender increases the amount of the loan, or extends or renews the terms of the original loan, then the Regulation applies.

6. Are table funded loans treated as new loan originations?

Answer: Yes. Table funding, as defined under HUD's Real Estate Settlement Procedure Act (RESPA) rule, 24 CFR 3500.2, is a settlement at which a loan is funded by a contemporaneous advance of loan funds and the assignment of the loan to the person advancing the funds. A loan made through a table funding process is treated as though the party advancing the funds has originated the loan. The funding party is required to comply with the Regulation. The table funding lender can meet the administrative requirements of the Regulation by requiring the party processing and underwriting the application to perform those functions on its behalf.

7. Is a lender required to perform a review of its, or of its servicer's, existing loan portfolio for compliance with the flood insurance requirements under the Act and Regulation?

Answer: No. Apart from the requirements mandated when a loan is made, increased, extended, or renewed, a regulated lender need only review and take action on any part of its existing portfolio for safety and soundness purposes, or if it knows or has reason to know of the need for NFIP coverage. Regardless of the lack of such requirement in the Act and Regulation, however, sound risk management practices may lead a lender to conduct scheduled periodic reviews that track the need for flood insurance on a loan portfolio.

II. Determining the Appropriate Amount of Flood Insurance Required Under the Act and Regulation

8. The Regulation states that the amount of flood insurance required "must be at least equal to the lesser of the outstanding principal balance of the designated loan or the maximum limit of coverage *available for the particular type of property under the Act." What is meant by the "maximum limit of coverage available for the particular type of property under the Act"?*

Answer: "The maximum limit of coverage available for the particular type of property under the Act" depends on the value of the secured collateral. First, under the NFIP, there are maximum caps on the amount of insurance available. For single-family and two-to-four family dwellings and other residential buildings located in a participating community under the regular program, the maximum cap is $250,000. For nonresidential structures located in a participating community under the regular program, the maximum cap is $500,000. (In participating communities that are under the emergency program phase, the caps are $35,000 for single-family and two-to-four family dwellings and other residential structures, and $100,000 for nonresidential structures).

In addition to the maximum caps under the NFIP, the Regulation also provides that "flood insurance coverage under the Act is limited to the overall value of the property securing the designated loan minus the value of the land on which the property is located," which is commonly referred to as the "insurable value" of a structure. The NFIP does not insure land; therefore, land values should not be included in the calculation.

An NFIP policy will not cover an amount exceeding the "insurable value" of the structure. In determining coverage amounts for flood insurance, lenders often follow the same practice used to establish other hazard insurance coverage amounts. However, unlike the insurable valuation used to underwrite most other hazard insurance policies, the insurable value of improved real estate for flood insurance purposes also includes the repair or replacement cost of the foundation and supporting structures. It is very important to calculate the correct insurable value of the property; otherwise, the lender might inadvertently require the borrower to purchase too much or too little flood insurance coverage. For example, if the lender fails to exclude the value of the land when determining the insurable value of the improved real estate, the borrower will be asked to purchase coverage that exceeds the amount the NFIP will pay in the event of a loss. (Please note, however, when taking a security interest in improved real estate where the value of the land, excluding the value of the improvements, is sufficient collateral for the debt, the lender must nonetheless require flood insurance to cover the value of the structure if it is located in a participating community's SFHA).

9. What is insurable value?

Answer: [Added as final by the October 17, 2011 *Federal Register* document] The insurable value of a building is the same as the overall value of a property minus the land on which the property is located. FEMA's *Mandatory Purchase of Flood Insurance Guidelines* state that the insurable value of a building is the same as 100 percent replacement cost value (RCV) of the insured building, which is defined as "[t]he cost to replace property with the same kind of material and construction without deduction for depreciation."[4] FEMA's guidelines, however, also provide that lenders should avoid creating a situation in which the insured pays for more coverage than the NFIP would pay in the event of a loss.[5] Strictly linking insurable value to RCV is not practical in all cases. In cases involving certain residential or condominium properties, insurance policies should be written to, and the insurance loss payout usually would be the equivalent of, RCV.[6] However, in cases

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[4] FEMA, *Mandatory Purchase of Flood Insurance Guidelines*, at GLS 10.

[5] FEMA, *Mandatory Purchase of Flood Insurance Guidelines*, at 27.

[6] A single-family dwelling, including a single-family unit in a building under a condominium form of ownership, used as the insured's primary residence is covered under the NFIP's Dwelling Policy and, upon loss, payment is settled at RCV if the dwelling is insured for at least the lesser of 80 percent of the dwelling's full RCV or the maximum limit of coverage under the NFIP. Losses on other residential properties are settled at actual cash value.

involving nonresidential properties, and even some residential properties, where the insurance loss payout would normally be based on actual cash value, which is RCV less physical depreciation,[7] insurance policies written at RCV may require an insured to pay for coverage that exceeds the amount the NFIP would pay in the event of a loss. Therefore, it is reasonable for lenders, in determining the amount of flood insurance required, to consider the extent of recovery allowed under the NFIP policy for the type of property being insured. This allows the lender to assist the borrower in avoiding situations in which the insured pays for coverage that exceeds the amount the NFIP will pay in the event of a loss. Lenders need to be equally mindful of avoiding situations in which, as a result of insuring at a level below RCV, they underinsure property.

In calculating the amount of insurance to require, the lender and borrower (either by themselves or in consultation with the flood insurance provider or other appropriate professional) may choose from a variety of approaches or methods to establish the insurable value. They may use an appraisal based on a cost-value (not market-value) approach, a construction-cost calculation, the insurable value used in a hazard insurance policy (recognizing that the insurable value for flood insurance purposes may differ from the coverage provided by the hazard insurance and that adjustments may be necessary; for example, most hazard policies do not cover foundations), or any other reasonable approach, so long as it can be supported.

10. Are there any alternatives to the definition of insurable value?

Answer: [Reserved]

11. What are examples of residential buildings?

Answer: Residential buildings include one-to-four family dwellings; apartment or other residential buildings containing more than four dwelling units; condominiums and cooperatives in which at least 75 percent of the square footage is residential; hotels or motels where the normal occupancy of a guest is six months or more; and rooming houses that have more than four roomers. A residential building may have incidental nonresidential use, such as an office or studio, as long as the total area of such incidental occupancy is limited to less than 25 percent of the square footage of the building, or 50 percent for single-family dwellings.

12. What are examples of nonresidential buildings?

Answer: Nonresidential buildings include those used for small businesses, churches, schools, farm activities (including grain bins and silos), pool houses, clubhouses, recreation, mercantile structures, agricultural and industrial structures, warehouses, hotels and motels with normal room rentals for less than six months' duration, nursing homes, and mixed-use buildings with less than 75 percent residential square footage.

13. How much insurance is required on a building located in an SFHA in a participating community?

Answer: The amount of insurance required by the Act and Regulation is the lesser of:

- The outstanding principal balance of the loan(s); or
- The maximum amount of insurance available under the NFIP, which is the lesser of:
    - The maximum limit available for the type of structure; or

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See FEMA, *Flood Insurance Manual*, at POL 3–20. Residential condominium buildings are covered under the NFIP's Residential Condominium Building Association Policy (RCBAP). Losses on residential condominium buildings are settled at RCV, unless subject to a co-insurance penalty, which applies when the building coverage is less than the lesser of 80 percent of full RCV or the maximum limit of coverage under the NFIP. See id. at POL 43–60.

[7] FEMA, *Mandatory Purchase of Flood Insurance Guidelines*, at GLS 1.

- The “insurable value” of the structure.

Example: (Calculating insurance required on a nonresidential building):

Loan security includes one equipment shed located in an SFHA in a participating community under the regular program.

- Outstanding loan principal is $300,000.
- Maximum amount of insurance available under the NFIP:
  - Maximum limit available for type of structure is $500,000 per building (nonresidential building).
  - Insurable value of the equipment shed is $30,000.

The minimum amount of insurance required by the Regulation for the equipment shed is $30,000.

14. Is flood insurance required for each building when the real estate security contains more than one building located in an SFHA in a participating community? If so, how much coverage is required?

Answer: Yes. The lender must determine the amount of insurance required on each building and add these individual amounts together. The total amount of required flood insurance is the lesser of:

- The outstanding principal balance of the loan(s); or
- The maximum amount of insurance available under the NFIP, which is the lesser of:
  - The maximum limit available for the type of structures; or
  - The “insurable value” of the structures.

The amount of total required flood insurance can be allocated among the secured buildings in varying amounts, but all buildings in an SFHA must have some coverage.

Example: Lender makes a loan in the principal amount of $150,000 secured by five nonresidential buildings, only three of which are located in SFHAs within participating communities.

- Outstanding loan principal is $150,000.
- Maximum amount of insurance available under the NFIP.
  - Maximum limit available for the type of structure is $500,000 per building (nonresidential buildings); or
  - Insurable value (for each nonresidential building for which insurance is required, which is $100,000, or $300,000 total).

Amount of insurance required for the three buildings is $150,000. This amount of required flood insurance could be allocated among the three buildings in varying amounts, so long as each is covered by flood insurance.

15. If the insurable value of a building or mobile home, located in an SFHA in which flood insurance is available under the Act, securing a designated loan is less than the outstanding principal balance of the loan, must a lender require the borrower to obtain flood insurance up to the balance of the loan?

Answer: No. The Regulation provides that the amount of flood insurance must be at least equal to the lesser of the outstanding principal balance of the designated loan or the maximum limit of coverage available for a particular type of property under the Act. The Regulation also provides that flood insurance coverage under the Act is limited to the overall value of the property securing the designated loan minus the value of the land on which the building or mobile home is located. Since the NFIP policy does not cover land value, lenders should determine the amount of insurance necessary based on the insurable value of the improvements.

16. Can a lender require more flood insurance than the minimum required by the Regulation?

Answer: Yes. Lenders are permitted to require more flood insurance coverage than required by the Regulation. The borrower or lender may have to seek such coverage outside the NFIP. Each lender has the responsibility to tailor its own flood insurance policies and procedures to suit its business needs and protect its ongoing interest in the collateral. However, lenders should avoid creating situations where a building is "over-insured."

17. Can a lender allow the borrower to use the maximum deductible to reduce the cost of flood insurance?

Answer: Yes. However, it is not a sound business practice for a lender to allow the borrower to use the maximum deductible amount in every situation. A lender should determine the reasonableness of the deductible on a case-by-case basis, taking into account the risk that such a deductible would pose to the borrower and lender. A lender may not allow the borrower to use a deductible amount equal to the insurable value of the property to avoid the mandatory purchase requirement for flood insurance.

III. Exemptions From the Mandatory Flood Insurance Requirements

18. What are the exemptions from coverage?

Answer: There are only two exemptions from the purchase requirements. The first applies to State-owned property covered under a policy of self-insurance satisfactory to the Director of FEMA. The second applies if both the original principal balance of the loan is $5,000 or less, and the original repayment term is one year or less.

IV. Flood Insurance Requirements for Construction Loans

19. Is a loan secured only by land that is located in an SFHA in which flood insurance is available under the Act and that will be developed into buildable lot(s) a designated loan that requires flood insurance?

Answer: No. A designated loan is defined as a loan secured by a building or mobile home that is located or to be located in an SFHA in which flood insurance is available under the Act. Any loan secured only by land that is located in an SFHA in which flood insurance is available is not a designated loan since it is not secured by a building or mobile home.

20. Is a loan secured or to be secured by a building in the course of construction that is located or to be located in an SFHA in which flood insurance is available under the Act a designated loan?

Answer: Yes. Therefore, a lender must always make a flood determination prior to loan origination to determine whether a building to be constructed that is security for the loan is located or will be located in an SFHA in which flood insurance is available under the Act. If so, then the loan is a designated loan and the lender must provide the requisite notice to the borrower prior to loan origination that mandatory flood insurance is required. The lender must then comply with the mandatory purchase requirement under the Act and Regulation.

21. Is a building in the course of construction that is located in an SFHA in which flood insurance is available under the Act eligible for coverage under an NFIP policy?

Answer: Yes. FEMA's Flood Insurance Manual, under general rules, states:

Buildings in the course of construction that have yet to be walled and roofed are eligible for coverage except when construction has been halted for more than 90 days and/or if the lowest floor used for rating purposes is below the Base Flood Elevation (BFE). Materials or supplies intended for use in such construction, alteration, or repair are not insurable unless they are contained within an enclosed building on the premises or adjacent to the premises. [FEMA, *Flood Insurance Manual* at p. GR 4 (FEMA's *Flood Insurance Manual* is updated every six months).]

The definition section of the *Flood Insurance Manual* defines "start of construction" in the case of new construction as "either the first placement of permanent construction of a building on site, such as the pouring of a slab or footing, the installation of piles, the construction of columns, or any work beyond the stage of excavation; or the placement of a manufactured (mobile) home on a foundation." [FEMA, *Flood Insurance Manual*, at p. DEF 9.] While an NFIP policy may be purchased prior to the start of construction, as a practical matter, coverage under an NFIP policy is not effective until actual construction commences or when materials or supplies intended for use in such construction, alteration, or repair are contained in an enclosed building on the premises or adjacent to the premises.

22. When must a lender require the purchase of flood insurance for a loan secured by a building in the course of construction that is located in an SFHA in which flood insurance is available?

Answer: Under the Act, as implemented by the Regulation, a lender may not make, increase, extend, or renew any loan secured by a building or a mobile home, located or to be located in an SFHA in which flood insurance is available, unless the property is covered by adequate flood insurance for the term of the loan. One way for lenders to comply with the mandatory purchase requirement for a loan secured by a building in the course of construction that is located in an SFHA is to require borrowers to have a flood insurance policy in place at the time of loan origination.

Alternatively, a lender may allow a borrower to defer the purchase of flood insurance until either a foundation slab has been poured and/or an elevation certificate has been issued or, if the building to be constructed will have its lowest floor below the Base Flood Elevation, when the building is walled and roofed. [FEMA, *Mandatory Purchase of Flood Insurance Guidelines*, at 30.] However, the lender must require the borrower to have flood insurance in place before the lender disburses funds to pay for building construction (except as necessary to pour the slab or perform preliminary site work, such as laying utilities, clearing brush, or the purchase and/or delivery of building materials) on the property securing the loan. If the lender elects this approach and does not require flood insurance to be obtained at loan origination, then it must have adequate internal controls in place at origination to ensure that the borrower obtains flood insurance no later than when the foundation slab has been poured and/or an elevation certificate has been issued.

23. Does the 30-day waiting period apply when the purchase of the flood insurance policy is deferred in connection with a construction loan?

Answer: No. The NFIP will rely on an insurance agent's representation on the application for flood insurance that the purchase of insurance has been properly deferred unless there is a loss during the first 30 days of the policy period. In that case, the NFIP will require documentation of the loan transaction, such as settlement papers, before adjusting the loss.

V. Flood Insurance Requirements for Nonresidential Buildings

24. Some borrowers have buildings with limited utility or value and, in many cases, the borrower would not replace them if lost in a flood. Is a lender required to mandate flood insurance for such buildings?

Answer: Yes. Under the Regulation, lenders must require flood insurance on real estate improvements when those improvements are part of the property securing the loan and are located in an SFHA and in a participating community.

The lender may consider "carving out" buildings from the security it takes on the loan. However, the lender should fully analyze the risks of this option. In particular, a lender should consider whether it would be able to market the property securing its loan in the event of foreclosure. Additionally, the lender should consider any local zoning issues or other issues that would affect its collateral.

25. What are a lender's requirements under the Regulation for a loan secured by multiple buildings located throughout a large geographic area where some of the buildings are located in an SFHA in which flood insurance is available and other buildings are not? What if the buildings are located in several jurisdictions or counties where some of the communities participate in the NFIP and others do not?

Answer: A lender is required to make a determination as to whether the improved real property securing the loan is in an SFHA. If secured improved real estate is located in an SFHA, but not in a participating community, no flood insurance is required, although a lender can require the purchase of flood insurance (from a private insurer) as a matter of safety and soundness. Conversely, where secured improved real estate is located in a participating community but not in an SFHA, no insurance is required. A lender must provide appropriate notice and require the purchase of flood insurance for designated loans located in an SFHA in a participating community.

VI. Flood Insurance Requirements for Residential Condominiums

26. Are residential condominiums, including multi-story condominium complexes, subject to the statutory and regulatory requirements for flood insurance?

Answer: Yes. The mandatory flood insurance purchase requirements under the Act and Regulation apply to loans secured by individual residential condominium units, including those located in multi-story condominium complexes, located in an SFHA in which flood insurance is available under the Act. The mandatory purchase requirements also apply to loans secured by other condominium property, such as loans to a developer for construction of the condominium or loans to a condominium association.

27. What is an NFIP Residential Condominium Building Association Policy (RCBAP)?

Answer: The RCBAP is a master policy for residential condominiums issued by FEMA. A residential condominium building is defined as having 75 percent or more of the building's floor area in residential use. It may be purchased only by condominium owners associations. The RCBAP covers both the common and individually owned building elements within the units, improvements within the units, and contents owned in common (if contents coverage is purchased). The maximum amount of building coverage that can be purchased under an RCBAP is either 100 percent of the replacement cost value of the building, including amounts to repair or replace the foundation and its supporting structures, or the total number of units in the condominium building times $250,000, whichever is less. RCBAP coverage is available only for residential condominium buildings in Regular Program communities.

28. What is the amount of flood insurance coverage that a lender must require with respect to residential condominium units, including those located in multi-story condominium complexes, to comply with the mandatory purchase requirements under the Act and the Regulation?

Answer: To comply with the Regulation, the lender must ensure that the minimum amount of flood insurance covering the condominium unit is the lesser of:

- The outstanding principal balance of the loan(s); or
- The maximum amount of insurance available under the NFIP, which is the lesser of:
  - The maximum limit available for the residential condominium unit; or
  - The "insurable value" allocated to the residential condominium unit, which is the replacement cost value of the condominium building divided by the number of units.

Effective October 1, 2007, FEMA required agents to provide on the declaration page of the RCBAP the replacement cost value of the condominium building and the number of units. Lenders may rely on the replacement cost value and number of units on the RCBAP declaration page in determining insurable value unless they have reason to believe that such amounts clearly conflict with other available information. If there is a conflict, the lender should notify the borrower of the facts that cause the lender to believe there is a conflict. If the lender believes that the borrower is underinsured, it should require the purchase of a Dwelling Policy for supplemental coverage.

Assuming that the outstanding principal balance of the loan is greater than the maximum amount of coverage available under the NFIP, the lender must require a borrower whose loan is secured by a residential condominium unit to either:

- Ensure the condominium owners association has purchased an NFIP Residential Condominium Building Association Policy (RCBAP) covering either 100 percent of the insurable value (replacement cost) of the building, including amounts to repair or replace the foundation and its supporting structures, or the total number of units in the condominium building times $250,000, whichever is less; or
- Obtain a dwelling policy if there is no RCBAP, as explained in question and answer 29, or if the RCBAP coverage is less than 100 percent of the replacement cost value of the building or the total number of units in the condominium building times $250,000, whichever is less, as explained in question and answer 30.

Example: Lender makes a loan in the principal amount of $300,000 secured by a condominium unit in a 50-unit condominium building, which is located in an SFHA within a participating community, with a replacement cost of $15 million and insured by an RCBAP with $12.5 million of coverage.

- Outstanding principal balance of loan is $300,000.
- Maximum amount of coverage available under the NFIP, which is the lesser of:
  - Maximum limit available for the residential condominium unit is $250,000; or
  - Insurable value of the unit based on 100 percent of the building's replacement cost value ($15 million ÷ 50 = $300,000).

The lender does not need to require additional flood insurance since the RCBAP's $250,000 per unit coverage ($12.5 million ÷ 50 = $250,000) satisfies the Regulation's mandatory flood insurance requirement. (This is the lesser of the outstanding principal balance ($300,000), the maximum coverage available under the NFIP ($250,000), or the insurable value ($300,000)).

The guidance in this question and answer will apply to any loan that is made, increased, extended, or renewed after the effective date of this revised guidance. This revised guidance will not apply to any loans made prior to the effective date of this guidance until a trigger event occurs (that is, the loan is refinanced, extended, increased, or renewed) in connection with the loan. Absent a new trigger event, loans made prior to the effective date of this new guidance will be considered compliant if they complied with the Agencies' previous guidance, which stated that an RCBAP that provided 80 percent RCV coverage was sufficient.

29. What action must a lender take if there is no RCBAP coverage?

Answer: If there is no RCBAP, either because the condominium association will not obtain a policy or because individual unit owners are responsible for obtaining their own insurance, then the lender must require the individual unit owner/borrower to obtain a dwelling policy in an amount sufficient to meet the requirements outlined in Question 28.

A dwelling policy is available for condominium unit owners' purchase when there is no or inadequate RCBAP coverage. When coverage by an RCBAP is inadequate, the dwelling policy may provide individual unit owners with supplemental building coverage to the RCBAP. The RCBAP and the dwelling policy are coordinated such that the dwelling policy purchased by the unit owner responds to shortfalls on building coverage pertaining either to improvements owned by the insured unit owner or to assessments. However, the dwelling policy does not extend the RCBAP limits, nor does it enable the condominium association to fill in gaps in coverage.

Example: The lender makes a loan in the principal amount of $175,000 secured by a condominium unit in a 50-unit condominium building, which is located in an SFHA within a participating community, with a replacement cost value of $10 million; however, there is no RCBAP.

- Outstanding principal balance of loan is $175,000.
- Maximum amount of coverage available under the NFIP, which is the lesser of:
  - Maximum limit available for the residential condominium unit is $250,000; or
  - Insurable value of the unit based on 100 percent of the building's replacement cost value ($10 million ÷ 50 = $200,000).

The lender must require the individual unit owner/borrower to purchase a flood insurance dwelling policy in the amount of at least $175,000, since there is no RCBAP, to satisfy the Regulation's mandatory flood insurance requirement. (This is the lesser of the outstanding principal balance ($175,000), the maximum coverage available under the NFIP ($250,000), or the insurable value ($200,000).)

30. What action must a lender take if the RCBAP coverage is insufficient to meet the Regulation's mandatory purchase requirements for a loan secured by an individual residential condominium unit?

Answer: If the lender determines that flood insurance coverage purchased under the RCBAP is insufficient to meet the Regulation's mandatory purchase requirements, then the lender should request that the individual unit owner/ borrower ask the condominium association to obtain additional coverage that would be sufficient to meet the Regulation's requirements (see question and answer 28). If the condominium association does not obtain sufficient coverage, then the lender must require the individual unit owner/borrower to purchase a dwelling policy in an amount sufficient to meet the Regulation's flood insurance requirements. The amount of coverage under the dwelling policy required to be purchased by the individual unit owner would be the difference between the RCBAP's coverage allocated to that unit and the Regulation's mandatory flood insurance requirements (see question and answer 29).

Example: Lender makes a loan in the principal amount of $300,000 secured by a condominium unit in a 50-unit condominium building, which is located in an SFHA within a participating community, with a replacement cost value of $10 million; however, the RCBAP is at 80 percent of replacement cost value ($8 million or $160,000 per unit).

- Outstanding principal balance of loan is $300,000.
- Maximum amount of coverage available under the NFIP, which is the lesser of:
  - Maximum limit available for the residential condominium unit is $250,000; or
  - Insurable value of the unit based on 100 percent of the building's replacement value ($10 million ÷ 50 = $200,000).

The lender must require the individual unit owner/borrower to purchase a flood insurance dwelling policy in the amount of $40,000 to satisfy the Regulation's mandatory flood insurance requirement of $200,000. (This is the lesser of the outstanding principal balance ($300,000), the maximum coverage available under the NFIP ($250,000), or the insurable value ($200,000).) The RCBAP fulfills only $160,000 of the Regulation's flood insurance requirement.

While the individual unit owner's purchase of a separate dwelling policy that provides for adequate flood insurance coverage under the Regulation will satisfy the Regulation's mandatory flood insurance requirements, the lender and the individual unit owner/borrower may still be exposed to additional risk of loss. Lenders are encouraged to apprise borrowers of this risk. The dwelling policy provides individual unit owners with supplemental building coverage to the RCBAP. The policies are coordinated such that the dwelling policy purchased by the unit owner responds to shortfalls on building coverage pertaining either to improvements owned by the insured unit owner or to assessments. However, the dwelling policy does not extend the RCBAP limits, nor does it enable the condominium association to fill in gaps in coverage.

The risk arises because the individual unit owner's dwelling policy may contain claim limitations that prevent the dwelling policy from covering the individual unit owner's share of the co-insurance penalty, which is triggered when the amount of insurance under the RCBAP is less than 80 percent of the building's replacement cost value at the time of loss. In addition, following a major flood loss, the insured unit owner may have to rely upon the condominium association's and other unit owners' financial ability to make the necessary repairs to common elements in the building, such as electricity, heating, plumbing, and elevators. It is incumbent on the lender to understand these limitations.

31. What must a lender do when a loan secured by a residential condominium unit is in a complex whose condominium association allows its existing RCBAP to lapse?

Answer: If a lender determines at any time during the term of a designated loan that the loan is not covered by flood insurance or is covered by such insurance in an amount less than that required under the Act and the Regulation, the lender must notify the individual unit owner/borrower of the requirement to maintain flood insurance coverage sufficient to meet the Regulation's mandatory requirements. The lender should encourage the individual unit owner/borrower to work with the condominium association to acquire a new RCBAP in an amount sufficient to meet the Regulation's mandatory flood insurance requirement (see question and answer 28). Failing that, the lender must require the individual unit owner/borrower to obtain a flood insurance dwelling policy in an amount sufficient to meet the Regulation's mandatory flood insurance requirement (see questions and answers 29 and 30). If the borrower/unit owner or the condominium association fails to purchase flood insurance sufficient to meet the Regulation's mandatory requirements within 45 days of the lender's notification to the individual unit owner/borrower of inadequate insurance coverage, the lender must force place the necessary flood insurance.

32. How does the RCBAP's co-insurance penalty apply in the case of residential condominiums, including those located in multi-story condominium complexes?

Answer: In the event the RCBAP's coverage on a condominium building at the time of loss is less than 80 percent of either the building's replacement cost or the maximum amount of insurance available for that building under the NFIP (whichever is less), then the loss payment, which is subject to a co-insurance penalty, is determined as follows (subject to all other relevant conditions in this policy, including those pertaining to valuation, adjustment, settlement, and payment of loss):

A. Divide the actual amount of flood insurance carried on the condominium building at the time of loss by 80 percent of either its replacement cost or the maximum amount of insurance available for the building under the NFIP, whichever is less.

B. Multiply the amount of loss, before application of the deductible, by the figure determined in A above.

C. Subtract the deductible from the figure determined in B above.

The policy will pay the amount determined in C above, or the amount of insurance carried, whichever is less.

Example 1: (Inadequate insurance amount to avoid penalty).
Replacement value of the building: $250,000.
80% of replacement value of the building: $200,000.
Actual amount of insurance carried: $180,000.
Amount of the loss: $150,000.
Deductible: $ 500.
Step A: 180,000 ÷ 200,000 = .90
(90% of what should be carried to avoid co-insurance penalty)
Step B: 150,000 × .90 = 135,000
Step C: 135,000 ¥ 500 = 134,500

The policy will pay no more than $134,500. The remaining $15,500 is not covered due to the co-insurance penalty ($15,000) and application of the deductible ($500). Unit owners' dwelling policies will not cover any assessment that may be imposed to cover the costs of repair that are not covered by the RCBAP.

Example 2: (Adequate insurance amount to avoid penalty).
Replacement value of the building: $250,000.
80% of replacement value of the building: $200,000.
Actual amount of insurance carried: $200,000.
Amount of the loss: $150,000.
Deductible: $ 500.
Step A: 200,000 ÷ 200,000 = 1.00
(100% of what should be carried to avoid co-insurance penalty)
Step B: 150,000 × 1.00 = 150,000
Step C: 150,000 ¥ 500 = 149,500

In this example there is no co-insurance penalty, because the actual amount of insurance carried meets the 80 percent requirement to avoid the co-insurance penalty. The policy will pay no more than $149,500 ($150,000 amount of loss minus the $500 deductible). This example also assumes a $150,000 outstanding principal loan balance.

33. What are the major factors involved with the individual unit owner's dwelling policy's coverage limitations with respect to the condominium association's RCBAP coverage?

Answer: The following examples demonstrate how the unit owner's dwelling policy may cover in certain loss situations:

Example 1: (RCBAP insured to at least 80 percent of building replacement cost).

- If the unit owner purchases building coverage under the dwelling policy and if there is an RCBAP covering at least 80 percent of the building replacement cost value, the loss assessment coverage under the dwelling policy will pay that part of a loss that exceeds 80 percent of the association's building replacement cost allocated to that unit.
- The loss assessment coverage under the dwelling policy will not cover the association's policy deductible purchased by the condominium association.
- If building elements within units have also been damaged, the dwelling policy pays to repair building elements after the RCBAP limits that apply to the unit have been exhausted. Coverage combinations cannot exceed the total limit of $250,000 per unit.

Example 2: (RCBAP insured to less than 80 percent of building replacement cost).

- If the unit owner purchases building coverage under the dwelling policy and there is an RCBAP that was insured to less than 80 percent of the building replacement cost value at the time of loss, the loss assessment coverage cannot be used to reimburse the association for its co-insurance penalty.
- Loss assessment is available only to cover the building damages in excess of the 80-percent required amount at the time of loss. Thus, the covered damages to the condominium association building must be greater than 80 percent of the building replacement cost value at the time of loss before the loss assessment coverage under the dwelling policy becomes available. Under the dwelling policy, covered repairs to the unit, if applicable, would have priority in payment over loss assessments against the unit owner.

Example 3: (No RCBAP),

- If the unit owner purchases building coverage under the dwelling policy and there is no RCBAP, the dwelling policy covers assessments against unit owners for damages to common areas up to the dwelling policy limit.
- However, if there is damage to the building elements of the unit as well, the combined payment of unit building damages, which would apply first, and the loss assessment may not exceed the building coverage limit under the dwelling policy.

VII. Flood Insurance Requirements for Home Equity Loans, Lines of Credit, Subordinate Liens, and Other Security Interests in Collateral Located in an SFHA

34. Is a home equity loan considered a designated loan that requires flood insurance?

Answer: Yes. A home equity loan is a designated loan, regardless of the lien priority, if the loan is secured by a building or a mobile home located in an SFHA in which flood insurance is available under the Act.

35. Does a draw against an approved line of credit secured by a building or mobile home, which is located in an SFHA in which flood insurance is available under the Act, require a flood determination under the Regulation?

Answer: No. While a line of credit secured by a building or mobile home located in an SFHA in which flood insurance is available under the Act is a designated loan and, therefore, requires a flood determination before the loan is made, draws against an approved line do not require further determinations. However, a request made for an increase in an approved line of credit may require a new determination, depending upon whether a previous determination was done. (See response to question 68 in Section XIII. Required use of Standard Flood Hazard Determination Form.)

36. When a lender makes, increases, extends or renews a second mortgage secured by a building or mobile home located in an SFHA, how much flood insurance must the lender require?

Answer: The lender must ensure that adequate flood insurance is in place or require that additional flood insurance coverage be added to the flood insurance policy in the amount of the lesser of either the combined total outstanding principal balance of the first and second loan, the maximum amount available under the Act (currently $250,000 for a residential building and $500,000 for a nonresidential building), or the insurable value of the building or mobile home. The junior lienholder should also ensure that the borrower adds the junior lienholder's name as mortgagee/loss payee to the existing flood insurance policy. Given the provisions of NFIP policies, a lender cannot comply with the Act and Regulation by requiring the purchase of an NFIP flood insurance policy only in the amount of the outstanding principal balance of the second mortgage without regard to the amount of flood insurance coverage on a first mortgage.

A junior lienholder should work with the senior lienholder, the borrower, or with both of these parties, to determine how much flood insurance is needed to cover improved real estate collateral. A junior lienholder should obtain the borrower's consent in the loan agreement or otherwise for the junior lienholder to obtain information on balance and existing flood insurance coverage on senior lien loans from the senior lienholder.

Junior lienholders also have the option of pulling a borrower's credit report and using the information from that document to establish how much flood insurance is necessary upon increasing, extending or renewing a junior lien, thus protecting the interests of the junior lienholder, the senior lienholders, and the borrower. In the limited situation where a junior lienholder or its servicer is unable to obtain the necessary information about the amount of flood insurance in place on the outstanding balance of a senior lien (for example, in the context of a loan renewal), the lender may presume that the amount of insurance coverage relating to the senior lien in place at the time the junior lien was first established (provided that the amount of flood insurance relating to the senior lien was adequate at the time) continues to be sufficient.

Example 1: Lender A makes a first mortgage with a principal balance of $100,000, but improperly requires only $75,000 of flood insurance coverage, which the borrower satisfied by obtaining an NFIP policy. Lender B issues a second mortgage with a principal balance of $50,000. The insurable value of the residential building securing the loans is $200,000. Lender B must ensure that flood insurance in the amount of $150,000 is purchased and maintained. If Lender B were to require additional flood insurance only in an amount equal to the principal balance of the second mortgage ($50,000), its interest in the secured property would not be fully protected in the event of a flood loss because Lender A would have prior claim on $100,000 of the loss payment towards its principal balance of $100,000, while Lender B would receive only $25,000 of the loss payment toward its principal balance of $50,000.

Example 2: Lender A, who is not directly covered by the Act or Regulation, makes a first mortgage with a principal balance of $100,000 and does not require flood insurance. Lender B, who is directly covered by the Act and Regulation, issues a second mortgage with a principal balance of $50,000. The insurable value of the residential building securing the loans is $200,000. Lender B must ensure that flood insurance in the amount of $150,000 is purchased and maintained. If Lender B were to require flood insurance only in an amount equal to the principal balance of the second mortgage ($50,000) through an NFIP policy, then its interest in the secured property would not be protected in the event of a flood loss because Lender A would have prior claim on the entire $50,000 loss payment towards its principal balance of $100,000.

Example 3: Lender A made a first mortgage with a principal balance of $100,000 on improved real estate with a fair market value of $150,000. The insurable value of the residential building on the improved real estate is $90,000; however, Lender A improperly required only $70,000 of flood insurance coverage, which the borrower satisfied by purchasing an NFIP policy. Lender B later takes a second mortgage on the property with a principal balance of $10,000. Lender B must ensure that flood insurance in the amount of $90,000 (the insurable value) is purchased and maintained on the secured property to comply with the Act and Regulation. If Lender B were to require flood insurance only in an amount equal to the principal balance of the second mortgage ($10,000), its interest in the secured property would not be protected in the event of a flood loss because Lender A would have prior claim on the entire $70,000 loss payment towards the insurable value of $90,000.

37. If a borrower requesting a loan secured by a junior lien provides evidence that flood insurance coverage is in place, does the lender have to make a new determination? Does the lender have to adjust the insurance coverage?

Answer: It depends. Assuming the requirements in Section 528 of the Act (42 U.S.C. 4104b) are met and the same lender made the first mortgage, then a new determination may not be necessary, when the existing determination is not more than seven years old, there have been no map changes, and the determination was recorded on an SFHDF. If, however, a lender other than the one that made the first mortgage loan is making the junior lien loan, a new determination would be required because this lender would be deemed to be “making” a new loan. In either situation, the lender will need to determine whether the amount of insurance in force is sufficient to cover the lesser of the combined outstanding principal balance of all loans (including the junior lien loan), the insurable value, or the maximum amount of coverage available on the improved real estate. This will hold true whether the subordinate lien loan is a home equity loan or some other type of junior lien loan.

38. If the loan request is to finance inventory stored in a building located within an SFHA, but the building is not security for the loan, is flood insurance required?

Answer: No. The Act and the Regulation provide that a lender shall not make, increase, extend, or renew a designated loan, that is a loan secured by a building or mobile home located or to be located in an SFHA, “unless the building or mobile home and any personal property securing such loan” is covered by flood insurance for the term of the loan. In this example, the collateral is not the type that could secure a designated loan because it does not include a building or mobile home; rather, the collateral is the inventory alone.

39. Is flood insurance required if a building and its contents both secure a loan, and the building is located in an SFHA in which flood insurance is available?

Answer: Yes. Flood insurance is required for the building located in the SFHA and any contents stored in that building.

Example: Lender A makes a loan for $200,000 that is secured by a warehouse with an insurable value of $150,000 and inventory in the warehouse worth $100,000. The Act and Regulation require that flood insurance coverage be obtained for the lesser of the outstanding principal balance of the loan or the maximum amount of flood insurance that is available under the NFIP. The maximum amount of insurance that is available for both building and contents is $500,000 for each category. In this situation, Federal flood insurance requirements could be satisfied by placing $150,000 worth of flood insurance coverage on the warehouse, thus insuring it to its insurable value, and $50,000 worth of contents flood insurance coverage on the inventory, thus providing total coverage in the amount of the outstanding principal balance of the loan. Note that this holds true even though the inventory is worth $200,000.

40. If a loan is secured by Building A, which is located in an SFHA, and contents, which are located in Building B, is flood insurance required on the contents securing a loan?

Answer: No. If collateral securing the loan is stored in Building B, which does not secure the loan, then flood insurance is not required on those contents whether or not Building B is located in an SFHA.

41. Does the Regulation apply where the lender takes a security interest in a building or mobile home located in an SFHA only as an "abundance of caution"?

Answer: Yes. The Act and Regulation look to the collateral securing the loan. If the lender takes a security interest in improved real estate located in an SFHA, then flood insurance is required.

42. If a borrower offers a note on a single-family dwelling as collateral for a loan but the lender does not take a security interest in the dwelling itself, is this a designated loan that requires flood insurance?

Answer: No. A designated loan is a loan secured by a building or mobile home. In this example, the lender did not take a security interest in the building; therefore, the loan is not a designated loan.

43. If a lender makes a loan that is not secured by real estate, but is made on the condition of a personal guarantee by a third party who gives the lender a security interest in improved real estate owned by the third party that is located in an SFHA in which flood insurance is available, is it a designated loan that requires flood insurance?

Answer: Yes. The making of a loan on condition of a personal guarantee by a third party and further secured by improved real estate, which is located in an SFHA, owned by that third party is so closely tied to the making of the loan that it is considered a designated loan that requires flood insurance.

VIII. Flood Insurance Requirements in the Event of the Sale or Transfer of a Designated Loan and/or Its Servicing Rights

44. How do the flood insurance requirements under the Regulation apply to regulated lenders under the following scenarios involving loan servicing?

Scenario 1: A regulated lender originates a designated loan secured by a building or mobile home located in an SFHA in which flood insurance is available under the Act. The regulated lender makes the initial flood determination, provides the borrower with appropriate notice, and flood insurance is obtained. The regulated lender initially services the loan; however, the regulated lender subsequently sells both the loan and the servicing rights to a nonregulated party. What are the regulated lender's requirements under the Regulation? What are the regulated lender's requirements under the Regulation if it only transfers or sells the servicing rights, but retains ownership of the loan?

Answer: The regulated lender must comply with all requirements of the Regulation, including making the initial flood determination, providing appropriate notice to the borrower, and ensuring that the proper amount of insurance is obtained. In the event the regulated lender sells or transfers the loan and servicing rights, the regulated lender must provide notice of the identity of the new servicer to FEMA or its designee. Once the regulated lender has sold the loan and the servicing rights, the lender has no further obligation regarding flood insurance on the loan.

If the regulated lender retains ownership of the loan and only transfers or sells the servicing rights to a nonregulated party, the regulated lender must notify FEMA or its designee of the identity of the new servicer. The servicing contract should require the servicer to comply with all the requirements that are imposed on the regulated lender as owner of the loan, including escrow of insurance premiums and force placement of insurance, if necessary.

Generally, the Regulation does not impose obligations on a loan servicer independent from the obligations it imposes on the owner of a loan. Loan servicers are covered by the escrow, force placement, and flood hazard determination fee provisions of the Act and Regulation primarily so that they may perform the administrative tasks for the regulated lender, without fear of liability to the borrower for the imposition of unauthorized charges. It is the Agencies' longstanding position, as described in the preamble to the Regulation that the obligation of a loan servicer to fulfill administrative duties with respect to the flood insurance requirements arises from the contractual relationship between the loan servicer and the regulated lender or from other commonly accepted standards for performance of servicing obligations. The regulated lender remains ultimately liable for fulfillment of those responsibilities, and must take adequate steps to ensure that the loan servicer will maintain compliance with the flood insurance requirements.

Scenario 2: A nonregulated lender originates a designated loan, secured by a building or mobile home located in an SFHA in which flood insurance is available under the Act. The nonregulated lender does not make an initial flood determination or notify the borrower of the need to obtain insurance. The nonregulated lender sells the loan and servicing rights to a regulated lender. What are the regulated lender's requirements under the Regulation? What are the regulated lender's requirements if it only purchases the servicing rights?

Answer: A regulated lender's purchase of a loan and servicing rights, secured by a building or mobile home located in an SFHA in which flood insurance is available under the Act, is not an event that triggers any requirements under the Regulation, such as making a new flood determination or requiring a borrower to purchase flood insurance. The Regulation's requirements are triggered when a regulated lender makes, increases, extends, or renews a designated loan. A regulated lender's purchase of a loan does not fall within any of those categories. However, if a regulated lender becomes aware at any point during the life of a designated loan that flood insurance is required, then the regulated lender must comply with the Regulation, including force placing insurance, if necessary. Depending upon the circumstances, safety and soundness considerations may sometimes necessitate that the lender undertake sufficient due diligence upon purchase of a loan as to put the lender on notice of lack of adequate flood insurance. If the purchasing lender subsequently extends, increases, or renews a designated loan, it must also comply with the Act and Regulation.

Where a regulated lender purchases only the servicing rights to a loan originated by a nonregulated lender, the regulated lender is obligated only to follow the terms of its servicing contract with the owner of the loan. In the event the regulated lender subsequently sells or transfers the servicing rights on that loan, the regulated lender must notify FEMA or its designee of the identity of the new servicer, if required to do so by the servicing contract with the owner of the loan.

45. When a regulated lender makes a designated loan and will be servicing that loan, what are the requirements for notifying the Director of FEMA or the Director's designee?

Answer: FEMA stated in a June 4, 1996, letter that the Director's designee is the insurance company issuing the flood insurance policy. The borrower's purchase of a policy (or the regulated lender's force placement of a policy) will constitute notice to FEMA when the regulated lender is servicing that loan.

In the event the servicing is subsequently transferred to a new servicer, the regulated lender must provide notice to the insurance company of the identity of the new servicer no later than 60 days after the effective date of such a change.

46. Would a RESPA Notice of Transfer sent to the Director of FEMA (or the Director's designee) satisfy the regulatory provisions of the Act?

Answer: Yes. The delivery of a copy of the Notice of Transfer or any other form of notice is sufficient if the sender includes, on or with the notice, the following information that FEMA has indicated is needed by its designee:

- Borrower's full name;
- Flood insurance policy number;
- Property address (including city and State);
- Name of lender or servicer making notification;
- Name and address of new servicer; and
- Name and telephone number of contact person at new servicer.

47. Can delivery of the notice be made electronically, including batch transmissions?

Answer: Yes. The Regulation specifically permits transmission by electronic means. A timely batch transmission of the notice would also be permissible, if it is acceptable to the Director's designee.

48. If the loan and its servicing rights are sold by the regulated lender, is the regulated lender required to provide notice to the Director or the Director's designee?

Answer: Yes. Failure to provide such notice would defeat the purpose of the notice requirement because FEMA would have no record of the identity of either the owner or servicer of the loan.

49. Is a regulated lender required to provide notice when the servicer, not the regulated lender, sells or transfers the servicing rights to another servicer?

Answer: No. After servicing rights are sold or transferred, subsequent notification obligations are the responsibility of the new servicer. The obligation of the regulated lender to notify the Director or the Director's designee of the identity of the servicer transfers to the new servicer. The duty to notify the Director or the Director's designee of any subsequent sale or transfer of the servicing rights and responsibilities belongs to that servicer. For example, a financial institution makes and services the loan. It then sells the loan in the secondary market and also sells the servicing rights to a mortgage company. The financial institution notifies the Director's designee of the identity of the new servicer and the other information requested by FEMA so that flood insurance transactions can be properly administered by the Director's designee. If the mortgage company later sells the servicing rights to another firm, the mortgage company, not the financial institution, is responsible for notifying the Director's designee of the identity of the new servicer.

50. In the event of a merger or acquisition of one lending institution with another, what are the responsibilities of the parties for notifying the Director's designee?

Answer: If an institution is acquired by or merges with another institution, the duty to provide notice for the loans being serviced by the acquired institution will fall to the successor institution in the event that notification is not provided by the acquired institution prior to the effective date of the acquisition or merger.

IX. Escrow Requirements

51. Are multi-family buildings or mixed-use properties included in the definition of “residential improved real estate” under the Regulation for which escrows are required?

Answer: “Residential improved real estate” is defined under the Regulation as “real estate upon which a home or other residential building is located or to be located.” A loan secured by residential improved real estate located or to be located in an SFHA in which flood insurance is available is a designated loan. Lenders are required to escrow flood insurance premiums and fees for mandatory flood insurance for such loans if the lender requires the escrow of taxes, hazard insurance premiums or any other charges for loans secured by residential improved real estate. A lender is not required to escrow flood insurance premiums and fees for a particular loan if it does not require escrowing of any other charges for that loan.

Multi-family buildings. For the purposes of the Act and the Regulation, the definition of residential improved real estate does not make a distinction between whether a building is single- or multi-family, or whether a building is owner- or renter-occupied. Single-family dwellings (including mobile homes), two-to-four family dwellings, and multi-family properties containing five or more residential units are covered under the Act’s escrow provisions. If the building securing the loan meets the Regulation’s definition of residential improved real estate and the lender requires the escrow of any other charges such as taxes or hazard insurance premiums, then the lender is required to also escrow premiums and fees for flood insurance.

Mixed-use properties. The lender should look to the primary use of a building to determine whether it meets the definition of “residential improved real estate.” (See questions and answers 11 and 12 for guidance on residential and nonresidential buildings.) If the primary use of a mixed-use property is for residential purposes, the Regulation’s escrow requirements apply.

52. When must escrow accounts be established for flood insurance purposes?

Answer: If a lender requires the escrow of taxes, insurance premiums, fees, or any other charges for a loan secured by residential improved real estate or a mobile home, the lender must also require the escrow of all flood insurance premiums and fees. When administering loans secured by one-to-four family dwellings, lenders should look to the definition of “Federally related mortgage loan” contained in the Real Estate Settlement Procedures Act (RESPA) to see whether a particular loan is subject to the escrow requirements in Section 10 of RESPA. (This includes individual units of condominiums. Individual units of cooperatives, although covered by Section 10 of RESPA, are not insurable under the NFIP and are not covered by the Regulation.) Loans on multi-family dwellings with five or more units are not covered by RESPA requirements. Pursuant to the Regulation, however, lenders must escrow premiums and fees for any required flood insurance if the lender requires escrows for other purposes, such as hazard insurance or taxes.

53. Do voluntary escrow accounts established at the request of the borrower trigger a requirement for the lender to escrow premiums for required flood insurance?

Answer: No. If escrow accounts for other purposes are established at the voluntary request of the borrower, the lender is not required to establish escrow accounts for flood insurance premiums. Examiners should review the loan policies of the lender and the underlying legal obligation between the parties to the loan to determine whether the accounts are, in fact, voluntary. For example, when a lender’s loan policies require borrowers to establish escrow accounts for other purposes and the contractual obligation permits the lender to establish escrow accounts for those other purposes, the lender will have the burden of demonstrating that an existing escrow was made pursuant to a voluntary request by the borrower.

54. Will premiums paid for credit life insurance, disability insurance, or similar insurance programs be viewed as escrow accounts requiring the escrow of flood insurance premiums?

Answer: No. Premiums paid for these types of insurance policies will not trigger the escrow requirement for flood insurance premiums.

55. Will escrow-type accounts for commercial loans, secured by multi-family residential buildings, trigger the escrow requirement for flood insurance premiums?

Answer: It depends. Escrow-type accounts established in connection with the underlying agreement between the buyer and seller, or that relate to the commercial venture itself, such as “interest reserve accounts,” “compensating balance accounts,” “marketing accounts,” and similar accounts are not the type of accounts that constitute escrow accounts for the purpose of the Regulation. However, escrow accounts established for the protection of the property, such as escrows for hazard insurance premiums or local real estate taxes, are the types of escrow accounts that trigger therequirement to escrow flood insurance premiums.

56. Which requirements for escrow accounts apply to properties adequately covered by RCBAPs?

Answer: RCBAPs (Residential Condominium Building Association Policies) are policies purchased by the condominium association on behalf of itself and the individual unit owners in the condominium. A portion of the periodic dues paid to the association by the condominium owners applies to the premiums on the policy. When a lender makes, increases, renews, or extends a loan secured by a condominium unit that is adequately covered by an RCBAP and dues to the condominium association apply to the RCBAP premiums, an escrow account is not required. However, if the RCBAP coverage is inadequate and the unit is also covered by a dwelling form policy, premiums for the dwelling form policy would need to be escrowed if the lender requires escrow for other purposes, such as hazard insurance or taxes. Lenders should exercise due diligence with respect to continuing compliance with the insurance requirements on the part of the condominium association.

X. Force Placement of Flood Insurance

57. What is the requirement for the force placement of flood insurance under the Act and Regulation?

Answer: [Reserved]

[Note: The Agencies included a proposed revised answer to Question 57 in the October 17, 2011 *Federal Register* document.]

Answer: [Proposed revision] The Act and Regulation require a lender to force place flood insurance, if *all* of the following circumstances occur:

- The lender determines at any time during the life of the loan that the property securing the loan is located in an SFHA;
- Flood insurance under the Act is available for improved property securing the loan;
- The lender determines that flood insurance coverage is inadequate or does not exist; and
- After required notice, the borrower fails to purchase the appropriate amount of coverage within 45 days.

The Act and Regulation require the lender, or its servicer, to send notice to the borrower upon making a determination that the improved real estate collateral’s insurance coverage has expired or is less than the amount required for that particular property, such as upon receipt of the notice of cancellation or expiration from the insurance provider. The Act and Regulation also require the lender, or its servicer, to give notice and force-place such insurance, if necessary, when a lender learns that a property requires flood insurance coverage because it is in an SFHA as a result of a flood map change (which is occurring in many communities as a result of FEMA's map modernization program).

The notice to the borrower must clearly state that the borrower should obtain, at the borrower's expense, flood insurance in an amount at least equal to the amount required under the NFIP, for the remainder of the loan's term. The notice should also state that if the borrower does not obtain the insurance within 45 days, the lender will purchase the insurance on behalf of the borrower and may charge the borrower for the cost of premiums and fees to obtain the coverage, which are likely to be more expensive than if the borrower purchases it. The Agencies encourage institutions to explain their force-placement policies to borrowers (including, where applicable, that they charge for force-placement coverage for the 45-day period and the timing of that charge). In situations where a borrower has not previously been required to have flood insurance (such as a map change), it is a best practice to also provide the Notice of Special Flood Hazards and Availability of Federal Disaster Assistance, which give borrowers important information about the implications of being in an SFHA.

If adequate insurance is not obtained by the borrower within the 45-day notice period, then the lender must purchase insurance on the borrower's behalf. Standard Fannie Mae/Freddie Mac documents permit the servicer or lender to add those charges to the principal amount of the loan.

FEMA developed the Mortgage Portfolio Protection Program (MPPP) to assist lenders in connection with force-placement procedures. FEMA published these procedures in the *Federal Register* on August 29, 1995 (60 FR 44881). Appendix A of FEMA's September 2007 *Mandatory Purchase of Flood Insurance Guidelines* sets out the MPPP Guidelines and Requirements, including force-placement procedures and examples of notification letters to be used in connection with the MPPP.

58. Can a servicer force place on behalf of a lender?

Answer: Yes. Assuming the statutory prerequisites for force placement are met, and subject to the servicing contract between the lender and the servicer, the Act clearly authorizes servicers to force place flood insurance on behalf of the lender, following the procedures set forth in the Regulation.

59. When force placement occurs, what is the amount of insurance required to be placed?

Answer: The amount of flood insurance coverage required is the same regardless of how the insurance is placed. (See Section II. Determining the appropriate amount of flood insurance required under the Act and Regulation and also Section VII. Flood Insurance Requirements for Home Equity Loans, Lines of Credit, Subordinate Liens, and Other Security Interests in Collateral Located in an SFHA.)

60. When should a lender send the force placement notice to the borrower? [Note: This question and answer are *proposed* in the October 17, 2011 *Federal Register document.*]

Answer: [Proposed] To ensure that adequate flood insurance coverage is maintained throughout the term of the loan, a lender or its servicer must notify a borrower whenever flood insurance on the collateral has expired or is less than the amount required for the property. The lender must send this notice upon making a determination that the flood insurance coverage is inadequate or has expired, such as upon receipt of the notice of cancellation or expiration from the insurance provider or as a result of an internal flood policy monitoring system. Notice is also required when a lender learns that a property requires flood insurance coverage because it is in an SFHA as a result of a flood map change (which is occurring in many communities as a result of FEMA's map modernization program). To avoid the expiration of insurance, the Agencies recommend that the lender also advise the borrower when flood insurance on the collateral is about to expire.

61. [As revised in October 17, 2011 Federal *Register document] When must the lender have flood insurance in place if the borrower has not obtained adequate insurance within the 45-day notice period?*

Answer: [Added as final in October 17, 2011 *Federal Register* document] The Regulation provides that the lender or its servicer shall purchase insurance on the borrower's behalf if the borrower fails to obtain flood insurance within 45 days after notification. However, where there is a brief delay in force placing required insurance, the Agencies will expect the lender to provide a reasonable explanation for the delay, for example, where a lender uses batch processing to purchase force-placed flood insurance policies.

62. When may a lender or its servicer charge a borrower for the cost of insurance that covers collateral during the 45-day notice period? [Note: This question and answer are *proposed* in the October 17, 2011 *Federal Register document.*]

Answer: [Proposed] A lender or its servicer may charge a borrower for insurance coverage for any part of the 45-day notice period in which no adequate borrower-purchased flood insurance coverage is in effect, if the borrower has given the lender or its servicer the express authority to charge the borrower for such coverage as a contractual condition of the loan being made. Any policy that is obtained by a lender or its servicer, the premium of which is charged to the borrower pursuant to a contractual right, should be equivalent in coverage and exclusions to an NFIP policy and cover the interests of both the borrower and the lender.

The Agencies encourage institutions to explain their force-placement policies to borrowers (including their policy on charging for force-placement coverage for the 45-day period and the timing of that charge) and encourage lenders and servicers to escrow flood insurance premiums. Following these recommendations could result in less force placement of flood insurance. Further, Regulation Z requires lenders to establish an escrow account for the payment of property taxes and mortgage-related insurance required by the lender, including flood insurance, for all "higher priced" first-lien mortgage loans. See 12 CFR 226.35(b)(3).[8]

XI. Private Insurance Policies

63. May a lender rely on a private insurance policy to meet its obligation to ensure that its designated loans are covered by an adequate amount of flood insurance?

Answer: It depends. A private insurance policy may be an adequate substitute for NFIP insurance if it meets the criteria set forth by FEMA in its *Mandatory Purchase of Flood Insurance Guidelines*. Similarly, a private insurance policy may be used to supplement NFIP insurance for designated loans where the property is underinsured if it meets the criteria set forth by FEMA in its *Mandatory Purchase of Flood Insurance Guidelines*. FEMA states that, to the extent that a private policy differs from the NFIP Standard Flood Insurance Policy, the differences should be carefully examined before the policy is accepted as sufficient protection under the law. FEMA also states that the suitability of private policies need only be considered when the mandatory purchase requirement applies.

64. When may a lender rely on a private insurance policy that does not meet the criteria set forth by FEMA?

[8] Institutions should note that upcoming rules to implement section 1461 of the Dodd-Frank Wall Street Reform and Consumer Protection Act (Pub. L. 111–203) (Dodd-Frank Act), may affect the portion of the answer referencing mandatory escrow requirements for flood insurance.

Answer: A lender may rely on a private insurance policy that does not meet the criteria set forth by FEMA only in limited circumstances. For example, when a flood insurance policy has expired and the borrower has failed to renew coverage, private insurance policies that do not meet the criteria set forth by FEMA, such as private insurance policies providing portfolio-wide blanket coverage, may be useful protection for the lender for a gap in coverage in the period of time before a force placed policy takes effect. However, the lender must still force place adequate coverage in a timely manner, as required, and may not rely on a private insurance policy that does not meet the criteria set forth by FEMA on an ongoing basis.

XII. Required Use of Standard Flood Hazard Determination Form (SFHDF)

65. Does the SFHDF replace the borrower notification form?

Answer: No. The SFHDF is used by the lender to determine whether the building or mobile home offered as collateral security for a loan is or will be located in an SFHA in which flood insurance is available under the Act. The notification form, on the other hand, is used to notify the borrower(s) that the building or mobile home is or will be located in an SFHA and to inform them about flood insurance requirements and the availability of Federal disaster relief assistance.

66. May a lender provide the SFHDF to the borrower?

Answer: Yes. While not a statutory requirement, a lender may provide a copy of the flood determination to the borrower so the borrower can provide it to the insurance agent in order to minimize flood zone discrepancies between the lender's determination and the borrower's policy. A lender would also need to make the determination available to the borrower in case of a special flood hazard determination review, which must be requested jointly by the lender and the borrower. In the event a lender provides the SFHDF to the borrower, the signature of the borrower is not required to acknowledge receipt of the form.

67. May the SFHDF be used in electronic format?

Answer: Yes. In the final rule adopting the SFHDF, FEMA stated: "If an electronic format is used, the format and exact layout of the Standard Flood Hazard Determination Form is not required, but the fields and elements listed on the form are required. Any electronic format used by lenders must contain all mandatory fields indicated on the form." It should be noted, however, that the lender must be able to reproduce the form upon receiving a document request by its Federal supervisory agency.

68. May a lender rely on a previous determination for a refinancing or assumption of a loan or multiple loans to the same borrower secured by the same property?

Answer: It depends. Section 528 of the Act, 42 U.S.C. 4104b(e), permits a lender to rely on a previous flood determination using the SFHDF when it is increasing, extending, renewing, or purchasing a loan secured by a building or a mobile home. Under the Act, the "making" of a loan is not listed as a permissible event that permits a lender to rely on a previous determination. When the loan involves a refinancing or assumption by the same lender who obtained the original flood determination on the same property, the lender may rely on the previous determination only if the original determination was made not more than seven years before the date of the transaction, the basis for the determination was set forth on the SFHDF, and there were no map revisions or updates affecting the security property since the original determination was made. A loan refinancing or assumption made by a lender different from the one who obtained the original determination constitutes a new loan, thereby requiring a new determination. Further, if the same lender makes multiple loans to the same borrower secured by the same improved real estate, the lender may rely on its previous determination if the original determination was made not more than seven years before the date of the transaction, the basis for the determination was set forth on the SFHDF, and there were no map revisions or updates affecting the security property since the original determination was made.

XIII. Flood Determination Fees

69. When can lenders or servicers charge the borrower a fee for making a determination?

Answer: There are four instances under the Act and Regulation when the borrower can be charged a specific fee for a flood determination:

- When the determination is made in connection with the making, increasing, extending, or renewing of a loan that is initiated by the borrower;
- When the determination is prompted by a revision or updating by FEMA of floodplain areas or flood-risk zones;
- When the determination is prompted by FEMA's publication of notices or compendia that affect the area in which the security property is located; or
- When the determination results in force placement of insurance.

Loan or other contractual documents between the parties may also permit the imposition of fees.

70. May charges made for life-of-loan reviews by flood determination firms be passed along to the borrower?

Answer: Yes. In addition to the initial determination at the time a loan is made, increased, renewed, or extended, many flood determination firms provide a service to the lender to review and report changes in the flood status of a dwelling for the entire term of the loan. The fee charged for the service at loan closing is a composite one for conducting both the original and subsequent reviews. Charging a fee for the original determination is clearly within the permissible purpose envisioned by the Act. The Agencies agree that a determination fee may include, among other things, reasonable fees for a lender, servicer, or third party to monitor the flood hazard status of property securing a loan in order to make determinations on an ongoing basis.

However, the life-of-loan fee is based on the authority to charge a determination fee and, therefore, the monitoring fee may be charged only if the events specified in the answer to Question 69 occur. Further, a lender may not charge a composite determination and life-of-loan fee if the loan does not close, because the life-of-loan fee would be an unearned fee in violation of the Real Estate Settlement Procedures Act.

XIV. Flood Zone Discrepancies

71. What should a lender do when there is a discrepancy between the flood hazard zone designation on the flood determination form and the flood insurance policy?

[**Answer**:] A lender should only be concerned about a discrepancy on the Standard Flood Hazard Determination Form (the SFHDF) and the one on the flood insurance policy if the discrepancy is between a high-risk zone (A or V) and a low- or moderate-risk zone (B, C, D, or X). In other words, a lender need not be concerned about subcategory differences between flood zones on these two documents. Once in possession of a copy of the flood insurance policy, a lender should systematically compare the flood zone designation on the policy with the zone shown on the SFHDF. If the flood insurance policy shows a lower risk zone than the SFHDF, then lender should investigate. As noted in FEMA's *Mandatory Purchase* *of Flood Insurance Guidelines*, Federal law sets the ultimate responsibility to place flood insurance on the lender, with limited reliance permitted on third parties to the extent that the information that those third parties provide is guaranteed.

A lender should first determine whether the difference results from the application of the NFIP's "Grandfather Rule." This rule provides for the continued use of a rating on an insured property when the initial flood insurance policy was issued prior to changes in the hazard rating for the particular flood zone where the property is located. The Grandfather Rule allows policyholders who have maintained continuous coverage and/or who have built in compliance with the Flood Insurance Rate Map to continue to benefit from the prior, more favorable rating for particular pieces of improved property. A discrepancy resulting from application of the NFIP's Grandfather Rule is reasonable and acceptable, but the lender should substantiate these findings.

A lender should also determine whether a difference in flood zone designations is the result of a mistake. To do so, a lender should facilitate communication between itself or the third-party service provider that performed the flood hazard determination for the lender. If it appears that the discrepancy is the result of a mistake, a lender should recheck its determination. If there still appears to be a discrepancy after this step has been taken, a lender and borrower may jointly request that FEMA review the determination to confirm or review the accuracy of the original determination performed by a lender or on the lender's behalf. However, FEMA will only conduct this review if the request is submitted within 45 days of the date the lender notified the borrower that a building or manufactured home is in an SFHA and flood insurance is required.

If, despite these efforts, the discrepancy is not resolved, or in the course of attempting to resolve a discrepancy, a borrower or an insurance company or its agent is uncooperative in assisting a lender in this attempt, the lender should notify the insurance agent about the insurer's duty pursuant to FEMA's letter of April 16, 2008 (W–08021), to write a flood insurance policy that covers the most hazardous flood zone. When providing this notification, the lender should include its zone information and it should also notify the insurance company itself. The lender should substantiate these communications in its loan file.

72. Can a lender be found in violation of the requirements of the Regulation if, despite the lender's diligence in making the flood hazard determination, notifying the borrower of the risk of flood and the need to obtain flood insurance, and requiring mandatory flood insurance, there is a discrepancy between the flood hazard zone designation on the flood determination form and the flood insurance policy?

Answer: As noted in question and answer 71 above, lenders should have a process in place to identify and resolve flood zone discrepancies. A lender is in the best position to coordinate between the various parties involved in a mortgage loan transaction to resolve any flood zone discrepancy. If a lender is able to substantiate in its loan file a bona fide effort to resolve a discrepancy, either by finding a legitimate reason for such discrepancy or by attempting to resolve the discrepancy, for example, by contacting FEMA to review the determination, no violation will be cited. If a pattern or practice of unresolved discrepancies is found in a lender's loan portfolio due to a lack of effort on the lender's part to resolve such discrepancies, the Agencies may cite the lender for a violation of the mandatory purchase requirements.

XV. Notice of Special Flood Hazards and Availability of Federal Disaster Relief

73. Does the notice have to be provided to each borrower for a real estate related loan?

Answer: No. In a transaction involving multiple borrowers, the lender need only provide the notice to any one of the borrowers in the transaction. Lenders may provide multiple notices if they choose. The lender and borrower(s) typically designate the borrower to whom the notice will be provided. The notice must be provided to a borrower when the lender determines that the property securing the loan is or will be located in an SFHA.

74. Lenders making loans on mobile homes may not always know where the home is to be located until just prior to, or sometimes after, the time of loan closing. How is the notice requirement applied in these situations?

Answer: When it is not reasonably feasible to give notice before the completion of the transaction, the notice requirement can be met by lenders in mobile home loan transactions if notice is provided to the borrower as soon as practicable after determination that the mobile home will be located in an SFHA. Whenever time constraints can be anticipated, regulated lenders should use their best efforts to provide adequate notice of flood hazards to borrowers at the earliest possible time. In the case of loan transactions secured by mobile homes not located on a permanent foundation, the Agencies note that such “home only” transactions are excluded from the definition of mobile home and the notice requirements would not apply to these transactions.

However, as indicated in the preamble to the Regulation, the Agencies encourage a lender to advise the borrower that if the mobile home is later located on a permanent foundation in an SFHA, flood insurance will be required. If the lender, when notified of the location of the mobile home subsequent to the loan closing, determines that it has been placed on a permanent foundation and is located in an SFHA in which flood insurance is available under the Act, flood insurance coverage becomes mandatory and appropriate notice must be given to the borrower under those provisions. If the borrower fails to purchase flood insurance coverage within 45 days after notification, the lender must force place the insurance.

75. When is the lender required to provide notice to the servicer of a loan that flood insurance is required?

Answer: Because the servicer of a loan is often not identified prior to the closing of a loan, the Regulation requires that notice be provided no later than the time the lender transmits other loan data, such as information concerning hazard insurance and taxes, to the servicer.

76. What will constitute appropriate form of notice to the servicer?

Answer: Delivery to the servicer of a copy of the notice given to the borrower is appropriate notice. The Regulation also provides that the notice can be made either electronically or by a written copy.

77. In the case of a servicer affiliated with the lender, is it necessary to provide the notice?

Answer: Yes. The Act requires the lender to notify the servicer of special flood hazards and the Regulation reflects this requirement. Neither contains an exception for affiliates.

78. How long does the lender have to maintain the record of receipt by the borrower of the notice?

Answer: The record of receipt provided by the borrower must be maintained for the time that the lender owns the loan. Lenders may keep the record in the form that best suits the lender’s business practices. Lenders may retain the record electronically, but they must be able to retrieve the record within a reasonable time pursuant to a document request from their Federal supervisory agency.

79. Can a lender rely on a previous notice if it is less than seven years old, and it is the same property, same borrower, and same lender?

Answer: No. The preamble to the Regulation states that subsequent transactions by the same lender with respect to the same property will be treated as a renewal and will require no new determination. However, neither the Regulation nor the preamble addresses waiving the requirement to provide the notice to the borrower. Therefore, the lender must provide a new notice to the borrower, even if a new determination is not required.

80. Is use of the sample form of notice mandatory?

Answer: No. Although lenders are required to provide a notice to a borrower when it makes, increases, extends, or renews a loan secured by an improved structure located in an SFHA, use of the sample form of notice provided in Appendix A of the Regulation or in Appendix 4 of FEMA's *Mandatory Purchase of Flood Insurance Guidelines* is not mandatory. It should be noted that the sample form includes other information in addition to what is required by the Act and the Regulation. Lenders may personalize, change the format of, and add information to the sample form of notice, if they choose. However, a lender-revised notice must provide the borrower with at least the minimum information required by the Act and Regulation. Therefore, lenders should consult the Act and Regulation to determine the information needed.

XVI. Mandatory Civil Money Penalties

81. Which violations of the Act can result in a mandatory civil money penalty?

Answer: A pattern or practice of violations of any of the following requirements of the Act and their implementing Regulation triggers a mandatory civil money penalty:

- Purchase of flood insurance where available (42 U.S.C. 4012a(b));
- Escrow of flood insurance premiums (42 U.S.C. 4012a(d));
- Force placement of flood insurance (42 U.S.C. 4012a(e));
- Notice of special flood hazards and the availability of Federal disaster relief assistance (42 U.S.C. 4104a(a)); and
- Notice of servicer and any change of servicer (42 U.S.C. 4101a(b)).

The Act states that any regulated lending institution found to have a pattern or practice of certain violations "shall be assessed a civil penalty" by its Federal supervisor in an amount not to exceed $350 per violation, with a ceiling per institution of $100,000 during any calendar year (42 U.S.C. 4012a(f)(5)). Each Agency adjusts these limits pursuant to the Federal Civil Penalties Inflation Adjustment Act of 1990, as amended by the Debt Collection Improvement Act of 1996, 28 U.S.C. 2461 note.[9] Lenders pay the penalties into the National Flood Mitigation Fund held by the Department of the Treasury for the benefit of FEMA.

82. What constitutes a "pattern or practice" of violations for which civil money penalties must be imposed under the Act?

Answer: The Act does not define "pattern or practice." The Agencies make a determination of whether a pattern or practice exists by weighing the individual facts and circumstances of each case. In making the determination, the Agencies look both to guidance and experience with determinations of pattern or practice under other regulations (such as Regulation B (Equal Credit Opportunity) and Regulation Z (Truth in Lending)), as well as Agencies' precedents in assessing civil money penalties for flood insurance violations.

[9] Please refer to 12 CFR 19.240(a) (OCC); 12 CFR 263.65(b)(10) (Board); 12 CFR 308.132(c)(xvi) (FDIC); 12 CFR 509.103(c) (OTS); 12 CFR 622.61(b) (FCA); and 12 CFR 747.1001(a) (NCUA) for the Agencies' current civil penalty limits.

The *Policy Statement on Discrimination in Lending* (Policy Statement) provided the following guidance on what constitutes a pattern or practice:

> *Isolated, unrelated, or accidental occurrences will not constitute a pattern or practice. However, repeated, intentional, regular, usual, deliberate, or institutionalized practices will almost always constitute a pattern or practice. The totality of the circumstances must be considered when assessing whether a pattern or practice is present.*

In determining whether a financial institution has engaged in a pattern or practice of flood insurance violations, the Agencies' considerations may include, but are not limited to, the presence of one or more of the following factors:

- Whether the conduct resulted from a common cause or source within the financial institution's control;
- Whether the conduct appears to be grounded in a written or unwritten policy or established practice;
- Whether the noncompliance occurred over an extended period of time;
- The relationship of the instances of noncompliance to one another (for example, whether the instances of noncompliance occurred in the same area of a financial institution's operations);
- Whether the number of instances of noncompliance is significant relative to the total number of applicable transactions. (Depending on the circumstances, however, violations that involve only a small percentage of an institution's total activity could constitute a pattern or practice);
- Whether a financial institution was cited for violations of the Act and Regulation at prior examinations and the steps taken by the financial institution to correct the identified deficiencies;
- Whether a financial institution's internal and/or external audit process had not identified and addressed deficiencies in its flood insurance compliance; and
- Whether the financial institution lacks generally effective flood insurance compliance policies and procedures and/or a training program for its employees.

Although these guidelines and considerations are not dispositive of a final resolution, they do serve as a reference point in assessing whether there may be a pattern or practice of violations of the Act and Regulation in a particular case. As previously stated, the presence or absence of one or more of these considerations may not eliminate a finding that a pattern or practice exists.