Introduction

Background and Summary

The National Flood Insurance Program (NFIP) is administered primarily under two statutes: the National Flood Insurance Act of 1968 (1968 Act) and the Flood Disaster Protection Act of 1973 (FDPA).[1] The 1968 Act made Federally subsidized flood insurance available to owners of improved real estate or mobile homes located in special flood hazard areas (SFHA) if their community participates in the NFIP. The NFIP is administered by a department of the Federal Emergency Management Agency (FEMA), the Federal Insurance Administration (FIA). The FDPA requires federal financial regulatory agencies to adopt regulations prohibiting their regulated lending institutions from making, increasing, extending or renewing a loan secured by improved real estate or a mobile home located or to be located in a SFHA in a community participating in the NFIP unless the property securing the loan is covered by flood insurance.

Title V of the Riegle Community Development and Regulatory Improvement Act of 1994[2] which is called the National Flood Insurance Reform Act of 1994 (Reform Act), comprehensively revised the Federal flood insurance statutes. The purpose of the Reform Act is to increase compliance with flood insurance requirements and participation in the NFIP in order to provide additional income to the National Flood Insurance Fund and to decrease the financial burden of flooding on the Federal government, taxpayers, and flood victims.[3] The Reform Act required the federal financial regulatory agencies[4] to revise their current flood insurance regulations and brought the Farm Credit Administration (FCA) under coverage of the Act. These agencies issued a joint final rule (final rule) on August 29, 1996, (61 FR 45684). On July 23, 1997, the FFIEC issued the Interagency Questions and Answers regarding Flood Insurance which are located in Appendix A of this section.

*Approved—FFIEC

The Reform Act also applied flood insurance requirements directly to the loans purchased by the Federal National Mortgage Association (Fannie Mae) and the Federal Home Loan Mortgage Corporation (Freddie Mac) and to agencies that provide government insurance or guarantees such as the Small Business Administration, Federal Housing Administration and the Veteran's Administration.

Objectives of the FDPA:

- Provide flood insurance to owners of improved real estate located in SFHAs of communities participating in the NFIP.
- Require communities to enact measures designed to reduce or avoid future flood losses as a condition for making federally subsidized flood insurance available.
- Require federal financial regulatory agencies to adopt regulations prohibiting their regulated lending institutions from making, increasing, extending or renewing a loan secured by improved real estate or a mobile home located or to be located in an SFHA of a community participating in the NFIP, unless the property securing the loan is covered by flood insurance.
- Require federal agencies, such as the Federal Housing Administration (FHA), Small Busi-

[1] These statutes are codified at 42 USC 4001-4129. FEMA administers the NFIP; its regulations implementing the NFIP appear at 44 CFR parts 59-77.

[2] Pub. L. 103-325, tit. V, 108 Stat. 2160, 2255-87 (September 23, 1994).

[3] H.R. Conf. Rep. No. 652, 103d Cong., 2d Sess. 195 (1994) (Conference Report).

[4] The agencies are the OCC, FDIC, OTS, NCUA and Federal Reserve.

ness Administration (SBA) and the Department of Veteran's Affairs (VA) not to subsidize, insure or guarantee any loan if the property securing the loan is in an SFHA of a community not participating in the NFIP.

Responsibilities of FIA:

- Identifying communities with SFHAs.
- Issuing flood boundary and flood rate maps for flood-prone areas.
- Making flood insurance available through the NFIP "Write Your Own" Program (WYO) which enables the public to purchase NFIP coverage from private companies that have entered into agreements with FIA.
- Assisting communities in adopting flood plain management requirements.
- Administering the insurance program. Licensed property and casualty insurance agents and brokers provide the primary connection between the NFIP and the insured party. Licensed agents sell flood insurance, complete the insured party's application form, report claims and follow-up with the insured for renewals of the policies.

National Flood Insurance Program

The NFIP has two distinct phases, the Emergency Program and the Regular Program.

- The Emergency Program is for communities that first enter the NFIP. It is an interim program that provides lower levels of flood insurance on eligible structures at subsidized rates. FEMA issues flood hazard boundary maps with this program to determine whether properties are located in a flood plain area. A community that is in the Emergency Program will be admitted to the Regular Program upon completion of specific requirements.
- A community enters the Regular Program once a detailed study has been completed and a flood insurance rate map for the area has been issued by FEMA. The maps delineate communities by degrees of probable flood hazard and include more specific area identification than do the flood hazard boundary maps. They also indicate base flood elevations depicting depth or elevation of flooding. The Regular Program provides full insurance coverage for eligible structures and it requires additional flood-plain management responsibilities for the community.

Eligible Structures for Flood Insurance

The NFIP covers improved real property or mobile homes located or to be located in an area identified by FEMA as having special flood hazards. Generally each insurable structure requires a separate insurance policy, although FEMA does provide special consideration for some nonresidential buildings. The following types of structures are eligible for coverage:

- Residential, industrial, commercial and agricultural buildings that are walled and roofed structures that are principally above ground.
- Buildings under construction where a development loan is made to construct insurable improvements on the land. Insurance can be purchased to keep pace with the new construction.
- Mobile homes that are affixed to a permanent site, including mobile homes that are part of a dealer's inventory and affixed to permanent foundations.
- Condominiums.
- Co-operative buildings.
- Flood insurance coverage is also available for personal property and other insurable contents contained in real property or mobile homes located in SFHAs. The property must be insured in order for the contents to be eligible.

Structures not eligible for flood insurance under the NFIP

- Unimproved land, bridges, dams and roads.
- Mobile homes not affixed to a permanent site.

- Travel trailers and campers.
- Converted buses or vans.
- Buildings entirely in, on, or over water into which boats are floated.
- Buildings newly constructed or substantially improved on or after October 1, 1983, in an area designated as an undeveloped coastal barrier with the Coastal Barrier Resource System established by the Coastal Barrier Resources Act (Public Law 97-348).

Flood Insurance Requirements for Lending Institutions

Basic Requirement

Flood insurance is required for the term of the loan on buildings or mobile homes when all three of the following factors are present:

- The institution makes, increases, extends or renews any loan(s) (commercial or consumer) secured by improved real estate or a mobile home that is affixed to a permanent foundation ("security property")
- The property securing the loan is located or will be located in an SFHA as identified by FEMA; and
- The community participates in the NFIP.

In the case of mobile homes, the criteria for coverage turns on whether the mobile home is affixed to a permanent foundation. An institution does not have to obtain a security interest in the underlying real estate in order for the loan to be covered by the final rule.

Institutions are not prohibited from making, increasing, extending or renewing a conventional loan if the community in which the security property is located has been mapped by FEMA but does not participate in the NFIP. However, federal flood insurance is not available in these communities. In addition, it should be noted that government guaranteed or insured loans (secured or unsecured) cannot be made if the community has been mapped by FEMA and does not participate in the NFIP.

Flood insurance requirements apply to loans where a security interest in improved real property is only taken "out of an abundance of caution." Section 102(b)(1) of the FDPA, as amended by the Reform Act,[5] provides that a regulated lending institution may not make, increase, extend <u>or renew any loan secured by improved real property</u> that is located in a special flood hazard area unless the improved real property is covered by the minimum amount of flood insurance required by statute.

Special Situation ¾ Table Funded Loans

In the typical table funding situation, the party providing the funding reviews and approves the credit standing of the borrower and issues a commitment to the broker or dealer to purchase the loan at the time the loan is originated. Frequently, all loan documentation and other statutorily mandated notices are supplied by the party providing the funding, rather than the broker or dealer. The funding party provides the original funding "at the table" when the broker or dealer and the borrower close the loan. Concurrent with the loan closing, the funding party acquires the loan from the broker or dealer. While the transaction is, in substance, a loan made by the funding party, it is structured as the purchase of a loan.

The final rule reflects the position that, for flood hazard determination purposes, the substance of the table funded transaction should control and that the typical table funded transaction should be considered a loan made, rather than purchased, by the entity that actually supplies the funds. Regulated institutions that provide table funding to close loans originated by a mortgage broker or mobile home dealer will be considered to be "making" a loan for purposes of the flood insurance requirements.

Treating table funded loans as loans made by the funding entity need not result in duplication of flood hazard determinations and borrower notices. The funding entity may delegate to the broker or dealer originating the transaction the responsibility for fulfilling the flood insurance requirements or may otherwise divide the responsibilities with the broker or dealer, as is currently done with respect

[5] See 42 USC 4012a(b)(1).

to the requirements under the Real Estate Settlement Procedures Act (RESPA).

Exemptions to the Purchase Requirement

The flood insurance purchase requirement does not apply to the following two loan situations:

- Loans on state-owned property covered under an adequate policy of self-insurance satisfactory to the Director of FEMA. The Director will periodically publish a list of state property falling within this exemption.
- Loans with an original principal balance of $5,000 or less, and having an original repayment term of one year or less.

Amount of Flood Insurance Required

The amount of flood insurance required must be at least equal to the outstanding principal balance of the loan, or the maximum amount available under the NFIP, whichever is less. Flood insurance coverage does not include the value of the land; rather, it only covers the amount of the insurable structure(s). Institutions may deduct the appraised value of the land from the total amount of the secured property to determine an estimated amount for insurance coverage. The amount of insurance coverage should not be less than the value of the improved structure(s).

Since March 1, 1995, the limits of coverage for flood policies are:

- $250,000 for residential property structures and $100,000 for personal contents
- $500,000 for non-residential structures and $500,000 for contents.

Waiting Period

Effective March 1, 1995, the Reform Act increased the waiting period for flood insurance coverage from five days to thirty days. FEMA through Policy Issuance 8-95, dated December 5, 1995, stated that increases in coverage amounts would be subject to the increased waiting period except in the following circumstances:

- When there is an existing policy and an additional amount of insurance is required in connection with the making, increasing, extension, or renewal of a loan, such as a second mortgage, home equity, or refinancing,
- When an additional amount of insurance is required as a result of a map revision
- When an additional amount of insurance is being obtained in connection with the renewal of an existing policy, and
- When flood insurance is required as a result of a lender determining that a loan which does not have flood insurance coverage should be protected by insurance (forced placement).

Special Situations ¾ Second Mortgages/Home Equity Loans

Both second mortgages and home equity loans are transactions that come within the purchase provisions of the FDPA. Since only one flood insurance policy can be issued for a building, an institution should not request that a new flood insurance policy if one already exists. Instead, the institution should have the borrower contact the insurance agent:

- To inform the agent of the intention to obtain a loan involving a subordinate lien
- To obtain verification of the existence of a flood insurance policy, and
- To check whether the amount of insurance covers all loan amounts.

After obtaining this information, the insurance agent should increase the amount of coverage if necessary and issue an endorsement that will reflect the institution as a lien holder.

For loans with approved lines of credit to be used in the future, it may be difficult to calculate the amount of insurance for the loan since the borrower will be drawing down differing amounts on the line at different times. In those instances where there is no policy on the collateral the borrower must, at a minimum, obtain a policy as a requirement for drawing on the line. As a matter of administrative convenience to ensure compliance with the requirements, an institution may take the following alternative approaches:

- Review its records periodically so that as draws are made against the line or repayments made to the account, the appropriate amount of insurance coverage can be maintained; or
- Upon origination, require the purchase of flood insurance for the total amount of the loan or the maximum amount of flood insurance coverage available, whichever is less.

Special Situations ¾ Condominium Policies

Effective October 1, 1994, FEMA issued a new condominium master policy called a Residential Condominium Building Association Policy (RCBAP). If the amount of the policy is 80% or more of the replacement value of the building, no co-insurance deductible is required by the policy. An institution can rely on a RCBAP as the required amount of flood insurance to support the loan if the policy meets the 80% requirement.

The amount of possible coverage available to a condominium association is $250,000 per unit multiplied by the total number of units. For instance, the maximum amount of coverage on a 50 unit condominium building would be $12,500,000 ($250,000 x 50). If the replacement value of the building was $10,000,000, the condominium association could purchase a policy of $8,000,000 (or more) and not be required to have a co-insurance payment in the event of a flood. This amount of insurance would meet the requirements of the final rule for any individual unit insurance requirement in the condominium.

Other Special Situations

- *Multiple Structures*. Multiple structures that secure a loan located in an SFHA generally must each be covered by flood insurance, even though the value of one structure may be sufficient to cover the loan amount. FEMA does permit borrowers to insure nonresidential buildings using one policy with a schedule separately listing each building. Loans secured by agricultural properties and improvements may be particularly assisted through this practice.
- *Other Real Estate Owned*. An institution with other real estate owned (OREO) in flood hazard areas should, as a prudent practice, purchase flood insurance policies on its OREO property, although it is not required to do so by the regulation.

Escrow Requirements

An institution must require the escrow of flood insurance premiums for loans secured by "residential improved real estate" if it requires the escrow of other funds to cover other charges associated with the loan, such as taxes, premiums for hazard or fire insurance, or any other fees. Depending on the type of loan, the escrow account for flood insurance premiums may be subject to section 10 of RESPA, 12 U.S.C. 2609,[6] which generally limits the amount that may be maintained in escrow accounts for consumer mortgage loans, and requires notices containing escrow account statements for those accounts. RESPA escrow requirements apply to "federally related mortgage loans," a category of loans that is narrower in scope than the Reform Act's "residential improved real estate." Therefore, escrow accounts established for federally related mortgage loans must comply with the requirements of section 10 of RESPA. However, an escrow account for "residential improved real estate" that is not also a "federally related mortgage loan" need not comply with section 10 of RESPA, even though the escrow requirements of the Reform Act apply.

The escrow provisions are designed to improve compliance with flood insurance requirements by ensuring that homeowners located in special flood hazard areas obtain and maintain flood insurance for the life of the loan. However, the Reform Act itself does not restrict the flood insurance escrow requirement to consumer mortgage loans. The de-

[6] The regulations of the Department of Housing and Urban Development (HUD) implementing section 10 appear at 24 CFR 3500.17 (1995); see also 60 FR 8812 (Feb. 15, 1995), 60 FR 24734 (May 9, 1995), 61 FR 13232 (Mar. 26, 1996) and 61 FR 29238 (June 7, 1996) (revising § 3500.17).

terminative factor in the coverage of the escrow requirement is not the purpose of the loan, but the purpose of the building-whether it is used primarily for residential purposes or for other purposes. Because the Reform Act defines “residential improved real estate” as “improved real estate for which the improvement is a residential building,” the escrow provisions cover, for example, multifamily properties containing five or more residential units.

Special situation involving condominium units

In the case of a condominium unit where the association has purchased an RCBAP that meets the 80% requirement of FEMA, the payments made by the borrower to the condominium association for the policy will constitute compliance with the requirements of the final rule for the escrow provisions.

Types of escrow accounts covered

The escrow requirement does not apply if the institution does not require other escrows to be maintained. An escrow arrangement is generally considered voluntary if the policies of the institution do not require the establishment of an escrow account in connection with the particular type of loan, even if permitted by the loan documents. In determining whether an escrow account arrangement is voluntary, it is appropriate to look to the loan policies and practices of the institution and the contractual agreement underlying the loan. If the loan documentation permits the institution to require an escrow account, and its loan policies normally would require an escrow account for a loan with particular characteristics, an escrow account in connection with such a loan generally would not be considered to be voluntary.

In the preamble to their final rule, the agencies noted that HUD takes the position that voluntary payments for credit life insurance do not constitute escrows for purposes of RESPA.[7] Therefore, the agencies have also determined that payments for credit life insurance and similar types of contracts should not trigger the escrow of flood insurance premiums.

Standard Flood Hazard Determination Form

Note: FEMA has revised the Standard Flood Hazard Determination Form effective April 20, 1999. The updated form and instructions can be obtained by contacting FEMA at the address below or from FEMA’s website at http://www.fema-.gov/library/fform.html.

When an institution makes, increases, extends, or renews any loan secured by improved real estate or by a mobile home, it must use the standard flood hazard determination form (SFHDF) developed by FEMA[8] to determine whether the building or mobile home offered as security property is or will be located in an SFHA in which flood insurance is available under the Act.

An institution can use a printed, computerized or electronic form. It must retain a copy of the completed form, in either hard copy or electronic format, for the period of time it owns the loan. FEMA has stated that if an electronic format is used, the format and exact layout of the SFHDF is not required, but the fields and elements listed on the form are required. Any electronic format used by an institution must contain all mandatory fields indicated on the SFHDF.

Decisions as to the applicability of flood insurance may not be based on an institution's unilateral determination of elevations at which floods may occur. Official elevation determinations and, therefore, map revisions or amendments (LOMAs or LOMRs) may only be performed by FEMA.

Flood maps and Standard Flood Hazard Determination forms may be obtained from FEMA by writing to:

Federal Emergency Management Agency
Flood Map Distribution Center
6930 (A-F) San Tomas Road
Baltimore, MD 21227-6227

or calling:

1-800-358-9616 or 1-800-611-6125

[7] See 60 FR 24733 (May 9, 1995) (revising 24 CFR 3500.17).

Community status information is no longer published in the Federal Register. To obtain information on a community's participation status, telephone a FEMA representative at 1-800-358-9616 to request a community status book. Information on community status is also available on the World Wide Web at http://www.fema.gov/fema /finifp.html.

Reliance on prior determination

The Reform Act permits an institution to rely on a prior determination, whether or not the security property is located in an SFHA, and it is exempt from liability for errors in the previous determination if:

- The previous determination is not more than seven years old, and
- The basis for it was recorded on the SFHDF mandated by the Reform Act.

There are, however, two circumstances in which an institution may not rely on a previous determination:

- If FEMA's map revisions or updates show that the security property is now located in an SFHA, or
- If the lender contacts FEMA and discovers that map revisions or updates affecting the security property have been made after the date of the previous determination.

The Reform Act also states that an institution cannot rely on a previous determination set forth on an SFHDF when it makes a loan; only when it increases, extends, renews or purchases a loan. However, the preamble to the final rule indicates that the agencies will treat subsequent transactions by the same institution with respect to the same property, such as assumptions, refinancings and second lien loans, as renewals. A new determination would, therefore, not be required in those limited circumstances, assuming the other requirements are met.

Forced Placement Requirements

The Reform Act does not require an institution to monitor for map changes, and the final rule does not require that determinations be made at any time other than when a loan is made, increased, extended, or renewed. If, however, at any time during the life of the loan the institution or its servicer determines that required flood insurance is deficient, the final rule requires initiation of forced placement procedures.

The Reform Act imposed the requirement on an institution or a servicer acting on its behalf to purchase or "force place" flood insurance for the borrower if the institution or the servicer determines that coverage is lacking. The final rule, therefore, provides that an institution, or servicer acting on its behalf, upon discovering that security property is not covered by an adequate amount of flood insurance, must, after providing notice and an opportunity for the borrower to obtain the necessary amount of flood insurance, purchase flood insurance in the appropriate amount on the borrower's behalf.

An institution or its servicer continues to be responsible for ensuring that where flood insurance was required at origination, the borrower renews the flood insurance policy and continues to renew it for as long as flood insurance is required for the security property. If a borrower allows a policy to lapse when insurance is required the institution or its servicer is required to commence force placement procedures.[8]

Forced placement should not be necessary at the time an institution makes, increases, extends or renews a loan, when it is obligated to require that flood insurance be in place prior to closing. Rather, forced placement authority is designed to be used if, over the term of the loan, the institution or its servicer determines that flood insurance coverage on the security property is deficient; that is,

[8] The insurance carrier should notify the institution or its servicer, along with the borrower, when the insurance contract is due for renewal. The insurance carrier also notifies these parties if it has not received the policy renewal.

whenever the amount of coverage in place is not equal to the lesser of the outstanding principal balance of the loan or the maximum stipulated by statute for the particular category of structure securing the loan. The amount that must be force placed is equal to the difference between the present amount of coverage and the lesser of the outstanding principal balance or the maximum coverage limit.

There is no required specific form of notice to borrowers for use in connection with the forced placement procedures. An institution or its servicer may choose to send the notice directly or may use the insurance company that issues the forced placement policy to send the notice. FEMA has developed the Mortgage Portfolio Protection Program (MPPP) to assist lenders in connection with forced placement procedures. For information concerning the contents of the notification letters used under the MPPP, lenders and others should consult FEMA's MPPP Notice.[9]

Determination Fees

An institution or its servicer may charge a reasonable fee to the borrower for the costs of making a flood hazard determination under the following circumstances:

- The borrower initiates a transaction (making, increasing, extending or renewing a loan) that triggers a flood hazard determination;
- There is a revision or updating of floodplain areas or risk zones by FEMA;
- The determination is due to FEMA's publication of a notice that affects the area in which the loan is located; or
- The determination results in the purchase of flood insurance under the forced placement provision.

The preamble to the final rule indicates that the authority to charge a borrower a reasonable fee for a flood hazard determination extends to a fee for life-of-loan monitoring by either the institution, its servicer, or by a third party, such as a flood hazard determination company.

Truth in Lending Act Issues

The Official Staff Commentary to Regulation Z states that a fee for services that will be performed periodically during the loan term is a finance charge, regardless of whether the fee is imposed at closing, or when the service is performed. This would include the fee for life-of-loan coverage. The fee for the determinations of whether a security property is in a SFHA is excluded from the finance charge. The Commentary further indicates that any portion of a fee that does not relate to the initial decision to grant credit must be included in the finance charge.[10] If creditors are uncertain about what portion of a fee is related to the initial decision to grant credit, the entire fee may be treated as a finance charge.

Notice Requirements

The final rule requires that when the security property is or will be located in a SFHA, the institution must provide a written notice to the borrower and the servicer. This notice must be provided regardless of whether the security property is located in a participating or non-participating community. The written notice must contain the following information:

- A warning that the building or mobile home is or will be located in a SFHA.
- A description of the flood purchase requirements contained in §102(b) of the FDPA, as amended.
- A statement whether flood insurance coverage is available under the NFIP and may also be available from private insurers.
- A statement whether Federal disaster relief assistance may be available in the event of

[9] Notice by FEMA, 60 FR 44881 (August 29, 1995).

[10] See 12 CFR part 226, supplement 1 comment 4(c)(7)-3.

damage to the building or mobile home, caused by flooding in a Federally declared disaster.

The final rule permits an institution to use the sample form to comply with the notice requirements. The sample form is an example of an acceptable form that notice may take and it does contain additional information not required under the regulation. Lenders may also personalize, change the format of, and add information to the sample form if they wish to do so. However, to ensure compliance with the notice requirements, a lender-revised notice form must provide the borrower, at a minimum, with the information required by the regulation.

The final rule permits an alternate notice provision by which an institution may rely on assurances from a seller or lessor that the seller or lessor has provided the requisite notice to the purchaser or lessee. This alternate form of notice might arise in a situation where the lender is providing financing through a developer for the purchase of condominium units by multiple borrowers. The lender may not deal directly with the individual condominium unit purchaser and need not provide notice to each purchaser but may instead rely on the developer/seller's assurances that the developer/seller has given the required notice. The same may be true for a cooperative conversion, where the sponsor of the conversion may be providing the required notice to the purchasers of the cooperative shares. A purchaser of shares in a cooperative may be considered to be a "lessee" rather than a purchaser with respect to the underlying real property. The final rule provides that delivery of notice must take place within a "reasonable time" before the completion of the transaction. What constitutes "reasonable" notice will necessarily vary according to the circumstances of particular transactions. An institution should bear in mind, however, that a borrower should receive notice timely enough to ensure that:

- The borrower has the opportunity to become aware of the borrower's responsibilities under the NFIP; and
- Where applicable, the borrower can purchase flood insurance before completion of the loan transaction.

The preamble to the final rule states that the agencies generally continue to regard ten days as a "reasonable" time interval.

Notice to Servicer

The Reform Act added loan servicers to the entities that must be notified of special flood hazards. In many cases the servicer's identity will not be known until well after the closing; consequently, notification to the servicer in advance of the closing would not be possible or would serve no purpose. In recognition that the servicer is often not identified prior to closing, the preamble to the final rule requires notice to the servicer as promptly as practicable after the institution provides notice to the borrower, and provides that notice to the servicer must be given no later than at the time the lender transmits to the servicer other loan data concerning hazard insurance and taxes. The final rule explicitly states that delivery of a copy of the borrower's notice to the servicer suffices as notice to the servicer.

Notice to Director of FEMA

An institution must notify the Director of FEMA, or the Director's designee, of the identity of the loan servicer and of any change in the servicer. FEMA has designated the insurance carrier as its designee to receive notice of the servicer's identity and of any change therein, and at FEMA's request this designation is stated in the final regulation. Notice of the identity of the servicer will enable FEMA's designee to provide notice to the servicer of a loan 45 days before the expiration of a flood insurance contract. The final rule requires the notice to be sent within 60 days of the effective date of the transfer of servicing. No standard form of notice is required to be used, however, in the preamble to the final rule, the agencies stated that the information should be sufficient for the Director, or the Director's designee, to identify the security property and the loan, as well as the new servicer and its address.

Record-keeping Requirements

The record-keeping requirements of the final rule include retention of:

- Copies of completed SFHD forms, in either hard copy or electronic form, for as long as the institution owns the loan; and
- Records of the receipt of the notice to the borrower and the servicer for as long as the institution owns the loan.

The final rule does not prescribe a particular form for the record of receipt, however, it should contain a statement from the borrower indicating that the borrower has received the notification. Examples of records of receipt may include:

- A borrower's signed acknowledgment on a copy of the notice,
- A borrower-initialed list of documents and disclosures that the lender provided the borrower, or
- A scanned electronic image of a receipt or other document signed by the borrower.

An institution may keep the record of receipt provided by the borrower and the servicer in the form that best suits the institution's business. Institutions who retain these records electronically must be able to retrieve them within a reasonable time.

Penalties and Liabilities

The Reform Act revised the FDPA to provide penalties for violations of:

- Escrow requirements;
- Notice requirements; and
- Forced placement requirements.

If an institution is found to have a pattern or practice of committing violations, the agencies shall assess civil penalties in an amount not to exceed $350 per violation with a total amount against any one regulated institution not to exceed $115,000[1] in any calendar year. Any penalty assessed will be paid into the National Flood Mitigation Fund. Liability for violations cannot be transferred to a subsequent purchaser of a loan. Liability for penalties expires four years from the time of the occurrence of the violation.

[1] Although the Reform Act provided for a maximum $100,000 yearly assessment against any one regulated institution, that amount was increased to $115,000 pursuant to the Federal Civil Money Penalty Inflation Adjustment Act of 1990. The Act requires all Federal agencies with statutory authority to impose Civil Money Penalties to evaluate and adjust those CMPs every four years. This CMP inflation adjustment appears at OTS Rules of Practice and Procedure, 12 C.F.R 509.103(c), 65 Federal Register 61260 (October 17, 2000).

Federal Emergency Management Agency (FEMA) and
National Flood Insurance Program (NFIP) Regional Offices

FEMA administers the National Flood Insurance Program through the Federal Insurance Administration located at:

Federal Emergency Management Agency
Federal Insurance Administration
500 C Street, S.W.
Washington, DC 20472

Federal Emergency Management Regional Offices:

Region I
(CT, MA, ME, NH, RI, VT)
442 J.W. McCormack Post Office
and Court House Building, Room 462
Boston, Massachusetts 02109-4595
(617) 223-9540

Region II
(NJ, NY)
26 Federal Plaza,
Room 1338
New York, New York 10278-0002
(212) 225-7209

Caribbean Area Office
(Puerto Rico, Virgin Islands)
P.O. Box 70105
San Juan, PR 00936
(809) 729-7624

Region III
(DC, DE, MD, PA, VA, WV)
Liberty Square Building
Second Floor
105 South Seventh Street
Philadelphia, Pennsylvania 19106-3316
(215) 931-5500

Region IV
(AL, FL, GA, KY, MS, NC, SC, TN)
1371 Peachtree Street, N.E.
Suite 700
Atlanta, Georgia 30309-3108
(404) 853-4200

Region V
(IL, IN, MI, MN, OH, WI)
175 West Jackson Boulevard, Fourth Floor
Chicago, Illinois 60604-2698

Region VI
(AR, LA, NM, OK, TX)
Federal Regional Center
800 North Loop 288, Room 206
Denton, Texas 76201-3698
(817) 898-5104

Region VII
(IA, KS, MO, NE)
911 Walnut Street, Room 200
Kansas City, Missouri 64106-2085
(816) 283-7061

Region VIII
(CO, MT, ND, SD, UT, WY)
Denver Federal Center, Building 710 A
P.O. Box 25267
Denver, Colorado 80225-0267
(303) 235-4800

Region IX
(AZ, CA, Guam, HI, NV)
Presidio of San Francisco
Building 105
San Francisco, California 94129-1250
(415) 923-7100

Region X
(AK, ID, OR, WA)
Federal Regional Center
130 228th Street, S.W.
Bothell, Washington 98021-9796
(206) 481-8800

NFIP offices are field offices of the Federal Insurance Administration's servicing contractor for the National Flood Insurance Program. Although they do not coincide with the areas served by FEMA regional offices, NFIP offices supplement the work of the regional offices.

National Flood Insurance Program Bureau and Statistical Agent Regional Offices

Region I
(CT, MA, ME, NH, RI, VT)
140 Wood Road
Suite 200
Braintree, Massachusetts 02184
(617) 848-1908

Region II
(NJ, NY)
33 Wood Avenue, South
Suite 600
Iselin, NJ 08830
(908) 603-3875

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Examination Objectives

To determine whether an institution performs required flood determinations for loans secured by improved real estate or a mobile home affixed to a permanent foundation in accordance with the final rule.

To determine if the institution requires flood insurance in the correct amount when it makes, increases, extends, or renews a loan secured by improved real estate or a mobile home located or to be located in a SFHA.

To determine if the institution provides the required notices to the borrower, servicer and to the Director of FEMA whenever flood insurance is required as a condition of the loan.

To determine if the institution requires flood insurance premiums to be escrowed when flood insurance is required on a residential building and other items are required to be escrowed.

To determine if the institution complies with the forced placement provisions if at any time during the term of a loan it determines that flood insurance on the loan is not sufficient to meet the requirements of the regulation.

To initiate corrective action when policies or internal controls are deficient, or when violations of law or regulation are identified.

Examination Procedures

The following procedures should be performed, as appropriate:

- by reviewing previous examinations and supervisory correspondence;
- by obtaining and reviewing the institution's policies, procedures and other pertinent information;
- by reviewing the institution's system of internal controls;
- through discussions with management; and
- by reviewing a sample of loan files.

Coverage and Internal Control

1. Determine the method(s) used by the institution to ascertain whether improved real estate or mobile homes are or will be located in a special flood hazard area.

2. Verify that the process used accurately identifies special flood hazard areas.

3. For those special flood hazard areas identified, determine if the communities in which they are located participate in the National Flood Insurance Program (NFIP).

4. If the institution provides “affordable funding” to close loans originated by mortgage brokers or dealers, verify that it complies with regulatory requirements.

5. If the institution purchases servicing rights, review the contractual obligations placed on the institution as servicer by the owner of the loans to ascertain if flood insurance requirements are identified and compliance responsibilities are adequately addressed.

6. If the institution utilizes a third party to service loans, review the contractual obligations between the parties to ascertain that flood insurance requirements are identified and compliance responsibilities are adequately addressed.

Property Determination Requirements

1. Verify that flood zone determinations are accurately prepared on the Standard Flood Hazard Determination Form (SFHDF).

2. Verify that the institution only relies on a previous determination if it is not more than seven years old, is recorded on the SFHDF and that it is not in a community that has been remapped.

3. If the institution utilizes a third party to prepare flood zone determinations, review the contractual obligations between the parties to ascertain that flood insurance requirements are identified and compliance responsibilities are adequately covered, including the extent of the third party's guarantee of work and the procedures in place to resolve disputes relating to determinations.

4. Verify that the institution retains a copy of the completed SFHDF, in either hard copy or electronic form, for as long as it owns the loan.

Purchase Requirements

1. For loans that require flood insurance, determine that sufficient insurance was obtained prior to loan closing and is maintained for the life of the loan.

2. If the institution makes loans insured or guaranteed by a government agency (SBA, VA or FHA) determine how it complies with the requirement not to make these loans if the security property is in a SFHA within a nonparticipating community.

Determination Fee Requirements

1. Determine that any fees charged to the borrower by the institution for flood zone determinations (absent some other authority such as contract language) are charged only when a loan :

   - is made, increased, renewed or extended;
   - is made in response to a remapping by FEMA; or
   - results in the purchase of flood insurance under the forced placement provisions.

2. If other authority permits the institution to charge fees for determinations in situations other than the ones listed above, determine if the institution is consistent in this practice.

3. Determine the reasonableness of any fees charged to a borrower for flood determinations by evaluating the method used by the institution to determine the amount of the charge. Consider, for example, the relationship of the fees charged to the cost of services provided.

Notice Requirements

1. Ascertain that written notice is mailed or delivered to the borrower within a reasonable time prior to loan closing.

2. Verify that the notice contains:

   - a warning that the property securing the loan is or will be located in a SFHA;
   - a description of the flood insurance purchase requirements;
   - a statement, where applicable, that flood insurance coverage is available under the NFIP and may also be available from private insurers, if applicable; and
   - a statement whether Federal disaster relief assistance may be available in the event of damage to the property caused by flooding in a Federally declared disaster, if applicable.

3. If the seller or lessor provided the notice to the purchaser or lessee, verify that the institution obtained satisfactory written assurance that the notice was provided within a reasonable time before the completion of the sale or lease transaction.

4. Verify that the institution retains a record of receipt of the notice provided to the borrower for as long as it owns the loan.

5. If applicable, verify that the institution provided written notice to the servicer of the loan within the prescribed time frames and that the institution retains a record of receipt of the notice for as long as it owns the loan.

6. If the institution transfers servicing of loans to another servicer, ascertain whether it provides notice of the new servicer's identity to the flood insurance carrier (Director of FEMA's designee) within prescribed time frames.

Escrow Requirements

1. If the institution's policies or loan documents require the escrow of funds to cover charges such as taxes, premiums for hazard insurance or other fees, verify that the institution requires the escrow of funds for loans secured by residential improved real estate to cover premiums and other charges associated with flood insurance.

2. For loans closed after October 1, 1996, where flood insurance is required and where the loan is subject to RESPA, verify that the institution's escrow procedures comply with Section 10 of RESPA.

Forced Placement Requirements

1. If the institution determines that flood insurance coverage is less than the amount required by the FDPA, ascertain that is has appropriate policies and procedures in place to exercise its forced placement authority.

2. If the institution is required to force place insurance, verify:

   - That it provides written notice to the borrower that flood insurance is required, and
   - That if the required insurance is not purchased by the borrower within 45 days from the time that the institution provides the written notice, that the institution purchases the required insurance on the borrower's behalf.

Notice to Director of FEMA

1. Does the institution provide the appropriate notice to the carrier of the insurance policy (the Director of FEMA's designee) regarding the identity of the servicer of a designated loan?

2. If the institution sells or transfers the servicing of designated loans to another party, does it have procedures in place to provide the appropriate notice to the Director's designee within 60 days of the effective date of the transfer of the servicing?

Interagency Questions and Answers Regarding Flood Insurance - July 23, 1997

Background

The National Flood Insurance Reform Act of 1994 (the Reform Act) (Title V of the Riegle Community Development and Regulatory Improvement Act of 1994) comprehensively revised the two federal flood insurance statutes, the National Flood Insurance Act of 1968 and the Flood Disaster Protection Act of 1973. The Reform Act required the OCC, Board, FDIC, OTS, and NCUA to revise their current flood insurance regulations and required the FCA to promulgate flood insurance regulations for the first time. The agencies fulfilled these requirements by issuing a joint final rule in the summer of 1996. See 61 FR 45684 (August 29, 1996).

Purpose

The purpose of these Interagency Questions and Answers is to consolidate, to the extent possible, useful flood insurance information into a comprehensive document. These Interagency Questions and Answers supplement other documents that the agencies are not superseding, including, for example, interagency staff flood insurance interpretive letters.

Interagency Questions and Answers Regarding Flood Insurance

Table of Contents

I. Definitions.

Designated Loan - A loan secured by a building or mobile home that is located or to be located in a special flood hazard area (SFHA) in which flood insurance is available under the Act.

1. Is an interim loan to construct a commercial building included in this definition?

Answer: Yes. If the purpose of the loan is to construct a building (assuming the loan is secured by that building), the Regulation applies. If the community in which the property is located participates in the National Flood Insurance Program (NFIP), then NFIP policies, subject to certain conditions and restrictions, can be purchased to provide coverage during the construction period for a building that will be located in an SFHA.

2. Are loans secured by raw land that will be developed into buildable lots subject to the Regulation?

Answer: No. Acquisition and development loans would not be subject to the Regulation because they do not meet the definition of a "designated loan." However, when the final construction phase of an ADC (acquisition, development, construction) project commences, the Regulation becomes applicable. This will require lenders to determine whether the property is located in an SFHA. If the building securing the loan is located or to be located in an SFHA, the other requirements of the Regulation will also apply. As noted above, the NFIP permits policies (subject to certain conditions and restrictions) to be purchased prior to the actual construction of a building.

3. Is a home equity loan considered a "designated loan?"

Answer: Yes, a home equity (or other) loan can be a designated loan, regardless of the lien priority, if: the loan is secured by a building or a mobile home; the collateral is located in an SFHA; and, the community where the property is located participates in the NFIP.

4. Are draws against approved lines of credit a "triggering event" requiring a flood determination under the Regulation or is it only the original application for the line of credit that triggers a determination?

Answer: Assuming that the line of credit is secured by a building and is thereby a "designated loan," a determination is required when application is made for the loan. Draws against an approved line would not require further determinations. However, a request for an increase in the line of approved credit is a triggering event and might require a new determination, depending upon whether a previous determination was done. (See the response to Question 4 in Section V, Required use of Standard Flood Hazard Determination Form)

5. 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 looks to the collateral securing the loan. In this example, the collateral does not meet the definition of a "designated loan" because it is not a building or mobile home.

6. If the building and contents both secure the loan, and the building is located in an SFHA, in a community that participates in the NFIP, what are the requirements for flood insurance? What if the contents securing the loan are located in buildings other than the building securing the loan?

Answer: Flood insurance is required for the building located in the SFHA and any contents stored in that building. If collateral securing the loan is stored in buildings that do not secure the loan and these buildings are not located in an SFHA, then flood insurance is not required on those contents.

7. Does the Regulation apply where the lender is taking a security interest only as an "abundance of caution?"

Answer: Yes. The Act looks to the collateral securing the loan, not to the purpose of the loan. If the lender takes a security interest in improved real estate, the Regulation applies without regard to the purpose of the loan.

8. If a borrower offers a note on a single family dwelling as collateral for a personal loan but the lender does not take a security interest in the dwelling itself, is this a "designated loan?"

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."

9. Does the Regulation apply to loans that are being restructured because of the borrower's default on the original loan?

Answer: Yes, assuming that 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.

10. A lender makes a loan (not secured by real estate) on the condition that a third party personally guarantees the loan and permits the lender to take a security interest in improved real estate owned by the third party. Is this a "designated loan" to which the Regulation applies if the guarantor's property is located in an SFHA in a community that participates in the NFIP?

Answer: Yes. The making of a loan on condition of a personal guarantee by a third party and further secured by improved real estate owned by that third party is so closely tied to the making of the loan that it is considered a "designated loan" under the Regulation.

II. Requirement to purchase flood insurance where available.

1. If flood insurance is not available because the community in which the property securing the loan is located is a non-participating community in the NFIP, does the Regulation apply?

Answer: Yes. The Regulation still applies, although it does not require the borrower to obtain flood insurance. The lender must make a determination on the Special Flood Hazard Determination Form (SFHDF) to determine if the property is located in an SFHA and notify the borrower. The lender may make a conventional loan in an SFHA in a non-participating community if it chooses to do so. Government-guaranteed or insured loans (e.g., SBA, VA, FHA), however, are not permitted to be made in non-participating communities (see 42 USC §4106(a)).

Nevertheless, institutions should exercise good risk management practices to ensure that making loans on properties that are in an SFHA where no flood insurance is available does not create unacceptable risks in an institution's loan portfolio.

2. Does the Regulation apply loans purchased from others?

Answer: No. The Regulation lists certain events that trigger its requirements: making, increasing, extending or renewing a designated loan. The purchase of a loan is not an event that requires a purchaser to make a new determination at the time of purchase. However, if the lender becomes aware at some point during the life of the loan that flood insurance is required, then the lender must comply with the Regulation. Similarly, if the lender extends, increases or renews the loan, the Regulation applies.

3. What about table funding programs? Are they treated as originations or as loans purchased from others?

Answer: Loans made through a table funding process will be treated as though the party providing the funds has originated the loan. The funding party must 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.

4. How are loans that are now under-insured because of previous insurance limitations to be handled?

Answer: In accordance with the Act, the Federal Insurance Administration has increased the amount of insurance available under the NFIP. Consequently, loans that previously had principal balances in excess of the program limits may now be underinsured. The new insurance limitations went into effect on March 1, 1995. Lenders and servicers must adjust coverage limits at the first renewal date or the first anniversary date following March 1, 1995, if the policy is a multi-year policy. Loans made after March 1, 1995, are subject to the new limits.

5. If the insurable value of the building securing the loan is less than the outstanding balance of the loan, can a lender require the borrower to obtain flood insurance up to the balance of the loan?

Answer: No. The insurable value of the improvements to the real estate that secures the loan governs the amount of insurance that is required. The amount of required insurance coverage is the lesser of the principal balance of the loan(s) or the maximum coverage available under the NFIP. An NFIP policy will not provide insurance coverage for losses in excess of the value of the improvements. Since the NFIP policy does not cover land value, lenders should determine the amount of insurance necessary based on the value of the improvements.

6. How do the flood insurance requirements apply in situations involving loan servicing?

Scenario 1- Loan is originated by a regulated lender and secured by a building on property located in an SFHA in a community in which flood insurance is available under the Act. Borrower is provided appropriate notice and insurance is obtained. Lender services the loan. Loan is subsequently sold to a non-regulated party and servicing is transferred to that party. What responsibilities are imposed on the regulated lender? What if the regulated lender only transfers or sells the servicing rights?

Answer: The lender must comply with all requirements of the Regulation, including making the initial determination, providing appropriate notice to the borrower, and ensuring that the proper amount of insurance is obtained. When the loan is sold and servicing is transferred to the new servicer, the lender must provide notice of the identity of the new servicer to FEMA or its designee.

If the lender retains ownership of the loan and only transfers or sells servicing rights to a non-regulated party, the 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 lender as owner of the loan, including escrow of insurance premiums and forced placement (if necessary).

More 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, forced placement and flood hazard determination fee provisions of the Act and Regulation primarily to ensure that they may perform the administrative tasks for the lender, without fear of liability to the borrower for the imposition of unauthorized charges. In addition, the preamble to the Regulation emphasizes 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 lender or from other commonly accepted standards for performance of servicing obligations. The 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 - Loan is originated by a non-regulated lender. Property is located in an SFHA but the lender did not make an initial determination or notify borrower of the need to obtain insurance. Loan is purchased by regulated lender who also services the loan. What are the responsibilities of the regulated lender? What if the regulated lender only purchases the servicing rights?

Answer: If the loan is purchased by the regulated lender, no determination is necessary at that point nor is any notice to FEMA required. If, at some time in the future, the lender becomes aware that the property is located in an SFHA in a community in which flood insurance is available under the Act, it must notify the borrower of that fact and require the borrower to purchase flood insurance. If the borrower does not voluntarily comply, the lender must force place the insurance. If servicing is subsequently sold or transferred, the lender must also notify FEMA or its designee of the identity of the new servicer.

If the regulated lender purchases only the servicing rights to the loan, the lender is only obligated to follow the terms of its servicing contract with the owner of the loan.

7. A loan is secured by multiple agricultural buildings located throughout a large geographic area. Some of the properties are located in an SFHA and others are not. In addition, the buildings are located in several jurisdictions or counties where some of the communities participate in the NFIP, and others do not. What are the flood insurance requirements for security properties in this scenario?

Answer: Flood insurance would be required only on those buildings located in an SFHA in which the community participates in the NFIP. A notice of special flood hazards is required for those buildings located in an SFHA whether or not the community participates in the NFIP. The amount of insurance required will depend upon the principal amount of the loan, the value of the buildings located in participating communities and the amount of insurance available under the NFIP.

For example, a loan in the principal amount of $150,000 is secured by 5 buildings, 3 of which are located in SFHAs within participating communities. The properties are non-residential in nature, therefore the maximum amount of insurance available under the NFIP is $500,000 per building. Each of the three buildings located in an SFHA must be covered by flood insurance. The total required amount of insurance for the three buildings would be the lesser of $150,000 or the value of the three buildings with each building insured separately from the other. The amount of required flood insurance could be allocated among the three buildings in varying amounts, so long as each is covered by flood insurance.

8. What is the appropriate amount of coverage under federal flood insurance legislation with respect to condominiums, in particular, multi-story condominium complexes?

Answer: Effective October 1, 1994, the Federal Insurance Administration issued a new form of Master Policy for condominiums - the Residential Condominium Building Association Policy (RCBAP). To meet federal flood insurance requirements, an RCBAP should be purchased in the amount of at least 80% of the replacement value of the building or the maximum amount available under the NFIP (currently $250,000 multiplied by the number of units), whichever is less. For instance, the maximum amount of coverage on a 50 unit condominium building could be up to $12,500,000 ($250,000 x 50). However, if the replacement value of the building was only $10,000,000, the condominium association could purchase a policy of $8,000,000 and not be required to have a co-insurance payment in the event of a flood. The $8,000,000 of coverage would meet the requirements of the Regulation for all the units within the condominium. A lender should make a similar analysis to determine the amount of coverage for other condominium complexes where flood insurance is required.

When making a loan on a condominium unit located in an SFHA, lenders should determine whether a master policy or similar product, provides adequate flood insurance coverage and is in place at the time the loan is made. Lenders should further ensure that a mechanism is in place (possibly a covenant on the part of the condominium association) that provides for adequate flood insurance coverage for the term of the loan.

9. A lender has a loan secured by a condominium unit in a multi-unit complex whose condominium association allows its existing flood insurance policy to lapse. As a result, there is no flood insurance coverage for the condominium unit. What recourse does the lender have?

   Answer: The NFIP does make an individual condominium unit policy available (the Dwelling Form), in addition to association master policies. In this instance, the lender after receiving notice that the association policy has lapsed, must notify the unit owner according to the forced placement procedures to obtain a policy (within 45 days) for the amount of the loan or the maximum amount of coverage available, whichever is less.

III. Exemptions.

1. 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 the original principal balance of the loan is $5,000 or less, and the original repayment term is one year or less. Both of these conditions must be present for the second exemption to apply.

IV. Escrow requirements.

1. The effective date of the escrow requirement was October 1, 1996. Does the escrow requirement apply to applications received before October 1, 1996?

   Answer: No. The escrow requirement applies only to loans closed on or after October 1, 1996.

2. Are multi-family buildings or mixed-use properties included in the definition of “residential improved real estate?” Are escrows required?

Answer: The Regulation states that if the collateral securing the loan meets the definition of "residential improved real estate" and the lender requires escrows for other items (e.g., hazard insurance or taxes), then the lender is required to also escrow flood insurance premiums.

Multi-family buildings. Neither the Act nor the Regulation distinguishes whether residential improved real estate is single or multi-family, or whether it is owner or renter-occupied. The preamble to the Regulation indicates that 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 other items, such as taxes or hazard insurance premiums, 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 if it meets the definition of "residential improved real estate." For example, a building having a retail store on the ground level with a small upstairs apartment used by the store's owner is generally considered a commercial enterprise and consequently would not constitute a residential building under the definition. Even though the Regulation does not require escrows for flood insurance, the lender may impose such a requirement through contract.

On the other hand, if the primary use of a mixed-use property is for residential purposes, the Regulation's escrow requirements apply.

3. When must escrow accounts established for flood insurance purposes be administered in accordance with the escrow rules under Section 10 of RESPA?

Answer: Lenders should look to the definition of "federally related mortgage loan" contained in RESPA to see if a particular loan is subject to Section 10. Generally, only loans on one to four family dwellings will be subject to the escrow requirements of RESPA. Consequently, only those escrow accounts established for loans subject to RESPA are required to conform with Section 10 of RESPA. 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. This requirement pertains to any loan, including those subject to RESPA. The preceding paragraph addresses the requirement for administering loans covered by RESPA. The preamble to the Regulation contains a more detailed discussion of the escrow requirements.

4. 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, if the loan policies of the lending institution 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.

5. 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.

6. Will escrow-type accounts for multi-family building commercial loans trigger the escrow requirement for flood insurance premiums?

Answer: Various types of accounts are established in connection with commercial purpose real estate loans. These loans typically involve multi-family properties and are substantially different in purpose and type from escrow accounts on single family residences. These involve accounts such as "interest reserve accounts," "compensating balance accounts," "marketing accounts," and similar accounts that may be established by contract between the purchaser and seller of the building (although administered by the lender in some cases). Accounts established in connection with the underlying agreement between the buyer and seller, or that relate to the commercial venture itself are not the type of accounts that constitute escrow accounts for the purpose of the Regulation. Escrow accounts for the protection of the property, such as escrows for hazard insurance premiums or local real estate taxes, are the types of escrows that trigger the requirement to escrow flood insurance premiums.

7. What requirements for escrow accounts apply to properties covered by Residential Condominium Building Association Policies?

Answer: RCBAPs are policies purchased by the condominium association on behalf of the individual unit owners in the condominium. The premiums on the policy are paid by a portion of the periodic dues paid to the association by the condominium owners. When a lender makes a loan on the purchase of a condominium over which a RCBAP is in place and the premiums are paid by dues to the condominium association, the escrow requirement is satisfied. Lenders should exercise due diligence with respect to continuing compliance with the insurance requirements on the part of the condominium association.

V. Required use of Standard Flood Hazard Determination Form (SFHDF).

1. Does the SFHDF replace the borrower notification form?

Answer: No. The notification form is used to notify the borrower(s) that they are purchasing improved property located in an SFHA. The financial regulatory agencies, in consultation with FEMA, included a revised version of the sample borrower notification form in Appendix A to the Regulation. The SFHDF is used by the lender to determine whether the property securing the loan is located in an SFHA.

2. Must the SFHDF be provided to the borrower? If so, must the borrower sign the form acknowledging receipt?

Answer: While it may be a common practice in some areas for lenders to provide a copy of the SFHDF to the borrower to give to the insurance agent, lenders are neither required to, nor prohibited from, providing the borrower with a copy of the form. Signature of the borrower is not required on the SFHDF.

3. May the SFHDF be used in electronic format?

Answer: Yes. FEMA, in the final rule adopting the SFHDF 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.

4. Section 528 of the Act permits a lender to rely on a previous determination using the SFHDF when it is increasing, extending, renewing or purchasing a loan secured by a building or a mobile home. The Act omits the "making" of a loan as a permissible event to rely on a previous determination. May a lender rely on a previous determination for a refinancing or assumption of a loan?

Answer: It depends. If a subsequent loan involving a refinancing or assumption is made on the same property by the same lender who obtained the original determination, and the other requirements contained in Section 528 are met, the lender may rely on the previous determination. Section 528 of the Act requires that a lender may rely on a previous determination only if the original determination was recorded on the SFHDF within the previous seven years and there were no map revisions or updates affecting the security property since the original determination was made. However, a loan refinancing or assumption made by a lender other than the lender who obtained the original determination would constitute "making" a new loan, thereby requiring a new determination.

5. If a borrower requesting a home equity 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 are met and the lender made the first mortgage, then a new determination would not be necessary. If, however, a lender other than the one that made the first mortgage loan is making the home equity loan, a new determination would be required because this lender would be deemed to be "making" a new loan. In any event, the institution will need to determine if the amount of insurance in force is sufficient to cover either the principal balance of all loans (including the home equity loan) or the maximum amount of coverage available on the improved real estate, whichever is less.

VI. Forced placement of flood insurance.

1. Is forced placement allowed? What are the procedures?

Answer: 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;
- The community in which the property is located participates in the NFIP;

- Flood insurance coverage is inadequate or does not exist; and
- The borrower fails to purchase the appropriate amount of coverage.

In order to force place, a lender must notify the borrower of the required amount of flood insurance that must be obtained within 45 days after notification. The notice must also state that if the borrower does not obtain the insurance within the 45 day period, the lender will purchase the insurance on behalf of the borrower and may charge the borrower the cost of premiums and fees to obtain the coverage. Standard FNMA/FHLMC 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 forced placement procedures. FEMA published these procedures in the Federal Register on August 29, 1995 (60 FR 44881). Appendix A of the FEMA publication contains examples of notification letters to be used in connection with the MPPP.

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

Answer: Yes. Assuming the statutory prerequisites for forced 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.

3. When forced 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. Requirement to purchase flood insurance where available.)

VII. Determination fees.

1. 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 a notice or compendia that affects the area in which the security property is located; or
- When the determination results in forced placement of insurance.
- Loan or other contractual documents between the parties may also permit the imposition of fees.

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

Answer: Yes. Many flood determination firms provide a service to the lender for conducting a periodic review of the loan during the time it is outstanding to ascertain whether the original determination remains valid. This service is sometimes coupled with the making of the original determination and the fee charged 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.

Consequently, the agencies also believe that a fee for a life of loan service may be passed along to the borrower. However, because the life of loan fee is based on the ability to charge a determination fee, the monitoring fee may be charged only if the events specified in the answer to question VII.1 occur.

VIII. Notice of special flood hazards and availability of Federal disaster relief.

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

Answer: The notice must be provided to a borrower only when the lender determines that the property securing the loan is or will be located in an SFHA. In a transaction involving multiple borrowers, the agencies believe it is only necessary to 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.

2. 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: 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 and, if possible, before completion of the loan transaction. In circumstances where 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.

3. 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.

4. 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.

5. 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.

6. 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.

IX. Notice of servicer's identity.

1. When a lender makes a designated loan and it 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 lender's forced placement of a policy), will constitute notice to FEMA when the lender is servicing that loan. In the event the servicing is subsequently transferred to a new servicer, the lender must provide notice to the insurance company of the identity of the new servicer.

2. 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: 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 bank or servicer making notification
- Name and address of new servicer
- Name and telephone number of contact person at new servicer

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

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

4. If the loan and its servicing rights are sold by the lender, is the 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.

5. Is the lender required to provide notice when a servicer other than the lender sells or transfers the servicing rights to another servicer?

Answer: No. The obligation of the 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, First Financial Institution makes and services the loan. It then sells the loan in the secondary market and also sells the servicing rights to First Financial Mortgage Company. First Financial Institution notifies the Director's designee of the identity of the new servicer and the other information requested by FEMA so that FEMA can track the loan. If First Financial Mortgage Company later sells the servicing rights to another firm, First Financial Mortgage Company is responsible for notifying the Director's designee of the identity of the new servicer, not First Financial Institution.

6. In the event of a merger 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.

X. Appendix A to the Regulation - Sample Form of Notice of Special Flood Hazards and Availability of Federal Disaster Relief Assistance.

1. Is use of the sample form of notice mandatory? Can it be revised to accommodate a lender's needs?

Answer: Although lenders are required to provide a notice to a borrower who is purchasing property secured by an improved structure located in an SFHA, use of the sample form of notice provided in Appendix A 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 if they choose. However, a lender-revised form must provide the borrower with at least the minimum information required by the Regulation. Therefore, lenders should consult the Regulation to determine the information needed.