

NATIONAL FLOOD INSURANCE PROGRAM

Regulatory Considerations

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THE NATIONAL FLOOD INSURANCE PROGRAM

A voluntary program based on a mutual agreement between the Federal government and the local community:

In exchange for **adopting and enforcing** a floodplain management ordinance, Federally-backed flood insurance is made available to property owners throughout the community.

Why is it Important:

- Bank Regulators focusing on Flood Insurance requirements during compliance and/or safety and soundness examinations;
- Requirement to Purchase Flood Insurance was Federal Reserve, OTS, and OCC's top regulatory compliance violation for 2005;
- Institutions are subject to mandatory Civil Money Penalties which are formal public actions for pattern or practice of Flood violations;

Why is it Important: (cont.)

- Since 2005, Federal Bank Regulatory Agencies have taken over 60 public enforcement actions in which CMPs have been assessed for flood insurance violations;
- Failure to adhere with Flood Insurance requirements could result in other bank regulatory administrative actions.

Why is it Important: (cont.)

It is a real business risk on many levels for all of these reasons!

Flood Risk Probabilities

- For a house located within the Special Flood Hazard Area, there is a **26% chance** that it will be inundated by a 100-year flood during the life of a 30-year mortgage...
- There is a 1-2% chance that a house will catch fire during the life of a 30-year mortgage.
- Over a 50 year period, the probability increases to 39%.

It won't flood here!

Southern New Hampshire - October 2005



It won't flood here!

Southern New Hampshire - October 2005



It won't flood here!

Whittenton Mills Dam, Taunton- October 2005



It won't flood here!

Merrimack Valley - May 2006



It won't flood here!

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Enough Coverage?

New England has fairly low participation in the flood insurance program*

- Massachusetts - 6.4 million people
 - 44,731 policies (as of Feb 2006)
- New Hampshire - 6,692 policies
- Maine - 7,396 policies

* May 2006 Insurance Journal

Key Controls

- Bank/Corporate-wide Flood Insurance policies, procedures and other controls including controls relating to condos, commercial loans, construction loans, second mortgages and cross collateralized properties;
- Automated flood determination and loan conditioning requirements;
- Consistent standards and tools for determining required Flood Insurance amounts;

Key Controls (cont.)

- Controls to ensure appropriate escrowing of flood insurance;
- Pre-closing review of proof of sufficiency of flood insurance amount;
- Regular flood insurance compliance monitoring and testing activities;
- Life of loan review and loan servicing flood insurance controls including processes for force placement.

Trouble Spots

Life of Loan Monitoring

- Borrower reduces coverage amount
 - Policy is checked for existence, not for accuracy - loan is insufficiently insured
- Insurance agent changes zone coverage
 - Tries to "save" the customer money - borrower purchases coverage outside of a flood zone

Trouble Spots

Commercial Lending

- Ensure consistent coverage/monitoring policies exist throughout all business lines
- Watch out for "contents" coverage
 - Typically found in commercial lending - take inventory as security

On the Horizon...

H.R. 4973 "Flood Insurance Reform and Modernization Act" (FIRM)

- Increase max coverage from \$250K to \$335K - residential , \$500K to \$670K - commercial
- Increases max CMPs from \$350 each violation to \$2000
- Notification that flood insurance available to ALL RE borrowers
- Improve flood map system
- Change force place wait period from 45 to 30 days





FOR MORE INFORMATION

- www.fema.gov
- www.floodsmart.gov
- www.federalreserve.gov
- www.bankersonline.com