



November 14, 2016

8584 Katy Freeway, Suite 420

Houston, TX 77024

Phone: 713-871-0005

Fax: 713-871-1358

**Partners**

Thomas E. Black, Jr.\*

Gregory S. Graham

Shawn P. Black \*\*

Regina M. Uhl\*\*\* ‡

**Senior Lawyers**

David F. Dulock

Diane M. Gleason

**Associates**

Peter B. Idziak \*\*

Daniel S. Engle\*\*

Nick Stevens

**Of Counsel**

David M. Tritter

Benjamin R. Idziak \*\*

Calvin C. Mann, Jr.

**Retired Partner(s)**

Calvin C. Mann, Jr.

\* Also Licensed in Iowa, New York,  
Washington and West Virginia

\*\* Also Licensed in New York

\*\*\* Also Licensed in Kentucky and Illinois

‡ Board Certified- Residential Real Estate  
Law- Texas Board of Legal Specialization

**To:** Clients and Friends

**From:** David F. Dulock

**Subject:** Loans in Areas Having Special Flood Hazards—Private Flood Insurance

In the November 7, 2016, *Federal Register* (81 FR 78063, [click here](#)) the Office of the Comptroller of the Currency (OCC), the Board of Governors of the Federal Reserve System (Board), the Federal Deposit Insurance Corporation (FDIC), the Farm Credit Administration (FCA), and the National Credit Union Administration (NCUA) jointly issued a proposed rule to amend their regulations regarding loans in areas having special flood hazards to implement the private flood insurance provisions of the Biggert-Waters Flood Insurance Reform Act of 2012 (Biggert-Waters Act). Specifically, the proposed rule would require regulated lending institutions to accept policies that meet the statutory definition of private flood insurance in the Biggert-Waters Act and permit regulated lending institutions to accept flood insurance provided by private insurers that does not meet the statutory definition of private flood insurance on a discretionary basis, subject to certain restrictions.

Comments on the proposed rule must be received by the above federal agencies (collectively the Agencies) on or before January 6, 2017 by any of the methods specified on page 78063-78064 of the above-identified *Federal Register*.

The Agencies each have issued regulations implementing the Federal flood insurance statutes that govern the National Flood Insurance Program (NFIP) for the lending institutions they supervise. The Biggert-Waters Act amended these NFIP statutory requirements. Among other things, the Biggert-Waters Act required the Agencies to issue a rule to direct regulated lending institutions to accept private flood insurance, as defined by the Biggert-Waters Act, and to notify borrowers of the availability of private flood insurance.

In October 2013, the Agencies jointly issued proposed rules to, among other things, implement the private flood insurance provisions of the Biggert-Waters Act (the October 2013 Proposed Rule). Based on comments received in response to the October 2013 Proposed Rule, the Agencies have by this proposed rule revised and re-proposed the private flood insurance provisions. Following is a brief summary of these re-proposed private flood insurance regulations by the Agencies.

*Definitions*

**Mutual aid society.** Under this proposed definition, to qualify as a mutual aid society, an organization would need to meet three criteria: (1) the members must share a common religious, charitable, educational, or fraternal bond; (2) the organization must cover losses caused by damage to members' property including damage caused by flooding, pursuant to an agreement, in accordance with this common bond; and (3) the organization must have a demonstrated history of fulfilling the terms of agreements to cover losses to members' property caused by flooding.

**Private flood insurance.** An insurance policy that:

1. Is issued by an insurance company that is licensed, admitted, or otherwise approved to

engage in the business of insurance by the insurance regulator of the State or jurisdiction in which the property to be insured is located; or, in the case of a policy of difference in conditions, multiple peril, all risk, or other blanket coverage insuring nonresidential commercial property, is recognized, or not disapproved, as a surplus lines insurer by the insurance regulator of the State or jurisdiction where the property to be insured is located;

2. Provides flood insurance coverage that is at least as broad as the coverage provided under a standard flood insurance policy issued under the NFIP (SFIP), including when considering deductibles, exclusions, and conditions offered by the insurer;
3. Includes a requirement for the insurer to give written notice 45 days before cancellation or non-renewal of flood insurance coverage to the insured and the regulated lending institution, or a servicer acting on the institution's behalf;
4. Includes information about the availability of flood insurance coverage under the NFIP;
5. Includes a mortgage interest clause similar to the clause contained in a SFIP;
6. Includes a provision requiring an insured to file suit not later than one year after the date of a written denial for all or part of a claim under a policy; and
7. Contains cancellation provisions that are as restrictive as the provisions contained in a SFIP.

#### *Mandatory Acceptance of Private Flood Insurance*

The proposed rule includes a new provision that would require a regulated lending institution to accept a private flood insurance policy that meets both: (1) the definition of private flood insurance, and (2) the private flood insurance is for the term of the loan and the coverage amount at least equals the lesser of the outstanding principal balance of the loan or the maximum limit of coverage available for the particular type of property under the National Flood Insurance Act of 1968 (*i.e.*, the mandatory coverage requirement).

#### *Compliance Aid for Mandatory Acceptance of Private Flood Insurance*

The proposed rule includes a compliance aid provision, which provides that a policy is deemed to meet the definition of private flood insurance if : (1) the policy includes, or is accompanied by, a written summary that demonstrates how the policy meets the definition of private flood insurance by identifying the provisions of the policy that meet each criterion in the definition, and confirms that the insurer is regulated in accordance with that definition; (2) the regulated lending institution verifies in writing that the policy includes the provisions identified by the insurer in the written summary and that these provisions satisfy the criteria included in the definition; and (3) the policy includes the following assurance clause within the policy or as an endorsement to the policy: “This policy meets the definition of private flood insurance contained in 42 U.S.C. 4012a(b)(7) and the corresponding regulation.”

In the preamble to the proposed rule the Agencies state that this proposed compliance aid provision does not relieve a regulated lending institution of the requirement to accept a policy that

meets the definition of private flood insurance and the mandatory coverage requirement, even if the policy is not accompanied by a written summary and does not include the assurance clause.

*Discretionary Acceptance of Private Flood Insurance*

The proposed rule would expressly permit a regulated lending institution to exercise its discretion to accept certain types of flood insurance policies issued by private insurers other than the private flood insurance policies that an institution is required to accept, provided the following criteria are met.

1. The flood insurance policy would be required to meet the mandatory coverage requirement described above.
2. The flood insurance policy would be required to be issued by an insurer that is licensed, admitted, or otherwise approved to engage in the business of insurance by the insurance regulator of the State or jurisdiction in which the property to be insured is located. In the case of a policy of difference in conditions, multiple peril, all risk, or other blanket coverage insuring nonresidential commercial property, the flood insurance policy would be required to be issued by a surplus lines insurer recognized, or not disapproved, by the insurance regulator of the State or jurisdiction where the property to be insured is located.
3. The flood insurance policy would be required to cover both the mortgagor(s) and the mortgagee(s) as loss payees.
4. The flood insurance policy would be required to provide for cancellation following reasonable notice to the borrower only for reasons permitted by FEMA for a SFIP on the Flood Insurance Cancellation Request/Nullification Form, or in any case of nonpayment, or when cancellation is mandated by State law.
5. The flood insurance policy would be required to either be “at least as broad” as the coverage provided under a SFIP or provide coverage that is “similar” to coverage provided under a SFIP, including when considering deductibles, exclusions, and conditions offered by the insurer. In determining whether the coverage is similar to coverage provided under a SFIP, the regulated lending institution would be required to: (1) compare the private flood insurance policy with a SFIP to determine the differences between the private flood insurance policy and a SFIP; (2) reasonably determine that the private flood insurance policy provides sufficient protection of the loan secured by the property; and (3) document its findings.

*Exception for Mutual Aid Societies.*

The proposed rule would expressly permit a regulated lending institution to accept a private flood insurance policy issued by a mutual aid society, provided the following criteria are met.

1. The institution’s primary supervisory agency determines that such policy or types of policies meet the requirement for flood insurance for purposes of the Federal flood insurance statutes.
2. The policy meets the amount of coverage for losses and term requirements in the mandatory

coverage requirement.

3. The policy covers both the mortgagor(s) and the mortgagee(s) as loss payees.
4. The regulated lending institution has determined that the policy provides sufficient protection of the loan secured by the property by: (1) verifying that the policy is consistent with general safety and soundness principles, such as whether deductibles are reasonable based on the borrower's financial condition; (2) considering the policy provider's ability to satisfy claims, such as whether the policy provider has a demonstrated record of covering losses; and (3) documenting its conclusions.

For ease of reference: (1) those clients whose primary supervisory agency is the OCC will find the text of the proposed rule applicable to them starting on page 78073 of the above *Federal Register* under 12 CFR Part 22; (2) those clients whose primary supervisory agency is the Board will find the text of the proposed rule applicable to them starting on page 78074 of the above *Federal Register* under 12 CFR Part 208; (3) those clients whose primary supervisory agency is the FDIC will find the text of the proposed rule applicable to them starting on page 78076 of the above *Federal Register* under 12 CFR Part 339; (4) those clients whose primary supervisory agency is the FCA will find the text of the proposed rule applicable to them starting on page 78077 of the above *Federal Register* under 12 CFR Part 614; and (5) those clients whose primary supervisory agency is the NCUA will find the text of the proposed rule applicable to them starting on page 78079 of the above *Federal Register* under 12 CFR Part 760.

We advise those clients that will be affected by the proposed rule to send written comments to the Agencies as noted on page 1 of this memorandum. We also them not to rely solely on the brief summary contained in this memorandum but to read the proposed rule and its preamble in their entirety by clicking on the hyperlink [click here](#) in the first paragraph on page 1.

**This Memorandum is provided as general information in regard to the subject matter covered, but no representations or warranty of the accuracy or reliability of the content of this information are made or implied. Opinions expressed in this memorandum are those of the author alone. In publishing this information, neither the author nor the law firm of Black, Mann & Graham L.L.P. is engaged in rendering legal services. While this information concerns legal and regulatory matters, it is not legal advice and its use creates no attorney-client relationship or any other basis for reliance on the information. Readers should not place reliance on this information alone, but should seek independent legal advice regarding the law applicable to matters of interest or concern to them. The law firm of Black, Mann & Graham L.L.P. expressly disclaims any obligation to keep the content of this information current or free of errors.**