

NCUA LETTER TO CREDIT UNIONS

**NATIONAL CREDIT UNION ADMINISTRATION
1775 Duke Street, Alexandria, VA 22314**

DATE: December 2004 **LETTER NO.:** 04-CU-16
TO: Federally Insured Credit Unions
SUBJ: Compliance with Federal Flood Insurance Requirements
ENCL: Flood Questionnaire

Dear Board of Directors:

All federally insured credit unions are required to comply with the requirements of the National Flood Insurance Program¹, as created by the National Flood Insurance Act of 1968. Part 760 of NCUA's Rules and Regulations implements these laws (Flood Act).

Typically, flooding causes more than \$1 billion in damage each year in the United States. The Federal Emergency Management Agency (FEMA) reports that despite the likelihood of flood damage in Special Flood Hazard Areas (SFHAs), less than half of the structures located in SFHAs are insured against such loss. The risk of loss by flooding in those areas is much higher than the risk of fire. Over the life of a 30-year mortgage, a property located in a SFHA has a 26 percent chance of being flooded compared to a 1 percent chance of loss by fire.

Compliance with the Flood Act protects credit unions and credit union members against catastrophic losses.

NCUA reviewed a compilation of recent examination findings and learned that some credit unions are not fully complying with the requirements of Part 760. This letter serves as a reminder of key provisions and provides references to public guidance, which may assist you in strengthening your Flood Act compliance program.

¹ The National Flood Insurance Program was created by the National Flood Insurance Act of 1968. This Act was amended by the Flood Disaster Protection Act of 1973, which authorizes NCUA to enforce compliance at federally insured credit unions. Further amendments were made through the Flood Insurance Reform Act of 1994 and the Bunning-Bereuter-Blumenauer Flood Insurance Reform Act of 2004. (42 U.S.C §4001 *et seq.*)

Review of your Flood Act compliance program is a required part of the Risk Focused Examination program. A copy of the AIREs questionnaire used by NCUA examiners is enclosed. NCUA may assess civil money penalties for failure to comply.

SUMMARY OF KEY FLOOD INSURANCE REQUIREMENTS

Flood Hazard Determinations (NCUA Regulations, Part 760.3, 760.6)

Subject to a few exceptions, a credit union cannot make, increase, extend, or renew any loan secured by personal property, a building, or mobile home on a permanent foundation, which is located in a special flood hazard area unless the collateral is covered by flood insurance for the term of the loan. Therefore, a flood hazard determination must be performed before the closing of the loan. The credit union or a servicer acting on its behalf must document the determination using the Standard Flood Hazard Determination Form provided by the Federal Emergency Management Agency. This form must be retained for the life of the loan.

Fees and Charges (NCUA Regulation, Part 760.8)

The credit union may charge borrowers a reasonable fee for determining whether the building or mobile home securing a loan is, or will be located, in a SFHA. The portion of the cost for the life-of-loan monitoring must be disclosed as a finance charge in accordance with the Truth-in-Lending Regulations. (12 CFR §226.4(c)(7)).

Notice to Borrowers (NCUA Regulation, Part 760.9)

If the Standard Flood Hazard Determination shows the building or mobile home securing the loan is in a SFHA, the credit union must mail or deliver a written notice to the borrower within a reasonable time (usually considered to be 10 days). The notice must inform the borrower that the property is in a SFHA, the requirement for purchase of flood insurance, whether flood insurance coverage is available from the National Flood Insurance Program, and whether Federal disaster relief assistance may be available in the event of flooding. A sample notice form is provided as an appendix to Part 760 of NCUA's Rules and Regulations.

Purchase Requirements (NCUA Regulation, Part 760.3)

If the building, mobile home, or personal property securing the loan is in a SFHA and flood insurance is available, the credit union must require the borrower to purchase insurance in an amount sufficient to cover the principal balance or the maximum limit of coverage for that property under the Flood Act, whichever is less. The insurance must be purchased before the loan is closed.

If the credit union or the borrower has reason to believe that an area has been improperly designated as a SFHA, the borrower may apply to FEMA for a Letter of Map Amendment. Unless the map is revised or a Letter of Map amendment is obtained, insurance must be purchased.

Escrowing Flood Insurance Premiums (NCUA Regulation, Part 760.5)

If the credit union requires an escrow for taxes, insurance premiums, fees or other charges, then it must also escrow for required flood insurance premiums.

Notice to FEMA (NCUA Regulation, Part 760.10)

The credit union must notify FEMA of the identity of the loan servicer at the time the loan is made, increased, extended, renewed, sold, or transferred. The notice must be sent to the insurance carrier that issued the insurance policy so the mortgagee endorsement can be updated. This also helps the credit union ensure the policy is maintained in force.

Forced Placement of Flood Insurance (NCUA Regulation, Part 760.7)

If the credit union determines that the borrower allowed the flood insurance coverage to lapse, the credit union must notify the borrower that the borrower must obtain the insurance. If the borrower does not provide evidence of insurance coverage within 45 days, the credit union is required to purchase the insurance on the borrower's behalf. The credit union may charge the borrower for the cost of the premiums and fees.

The attached questionnaire has been developed for examiners to assess the credit union's compliance with the flood insurance regulation. It may also be helpful to you in evaluating your compliance program.

If you need additional information, the following resource listing may help you.

Flood Insurance Information Resources

- General Information about the National Flood Insurance Program:

Federal Emergency Management Agency
Federal Insurance Administration
500 C Street, S.W.
Washington, D.C. 20472
Fax: (202) 646-3362
Website: <http://www.fema.gov/nfip/>

- Lender compliance information: <http://www.fema.gov/nfip/infol.htm>

- nteragency Questions and Answers Regarding Flood Insurance: <http://www.fdic.gov/news/news/financial/1997/fil9777.html>
- Library of publications: <http://www.fema.gov/nfip/library.htm>
- To order Flood Hazard Boundary Maps or Flood Insurance Rate Maps, call or write:

Federal Emergency Management Agency
Map Service Center
PO Box 1038
Jessup, Maryland 20794-1038
Telephone: 1-800-358-9616
Fax: 1-800-358-9620

Or order maps online: <http://www.fema.gov.msc>

If you have questions concerning compliance with the flood insurance regulations, please discuss them with your examiner, your NCUA regional office, or, in the case of state chartered credit unions, your state supervisory authority.

Sincerely,

/s/

JoAnn Johnson
Chairman

Enclosure

FDPA - Flood Disaster Protection Act		
Loans - Real Estate and Mobile Homes		
INTRODUCTION AND PURPOSE		
APPLICABILITY		
PENALTIES		
RECORD RETENTION REQUIREMENTS		
	Yes/No	Comments
1. Does it appear the CU maintains sufficient records to indicate the method used to determine whether improved real estate or a mobile home offered as security for a loan is located in a special flood hazard area? (760.6)		
2. Is flood insurance required for the building, mobile home, or personal property securing a loan if located in an area identified as having special flood hazards and in which flood insurance has been made available? (760.3(a))		
3. If the CU uses a third party vendor to prepare flood zone determinations, does the vendor guarantee the accuracy of the information as part of the contract? (1994 Reform Act, 42 USC, Section 4104b(d))		
4. Does the CU rely on previous flood zone determinations only when all of the following conditions are met? The loan is not a new loan, the flood zone determination is less than 7 years old, no new flood maps issued since the original flood zone determination, and the original flood zone determination was recorded on the Special Flood Hazard Determination Form. (1994 Reform Act, 42 USC, Section 1365(e))		
5. Does it appear the CU provides the borrower with a Notice to Borrower in Special Flood Hazard Areas (SFHA) as least 10 days before closing? (760.9)		
6. Does it appear the CU receives an acknowledgment from the borrower before the loan closes? 760.9(d)		
7. Does it appear the CU requires evidence that sufficient flood insurance was purchased by the time the loan closes? (760.3(a))		
8. Does it appear the CU requires and monitors flood insurance coverage for the life of the loan? (760.3(a) and 760.7)		
9. If the CU requires escrowing for taxes, insurance premium fees or any other charges on subject loans, does it appear the CU established an escrow account for flood premiums as well? (760.5)		
10. Does the CU notify the Federal Emergency Management Agency (FEMA) in writing of the identity of the servicer of each loan requiring flood insurance? (760.10)		

Cell: A5

Comment: The Flood Disaster Protection Act of 1973 (FDPA) requires NCUA to ensure that federally insured credit unions do not make loans secured by real estate or mobile homes located in special flood hazard areas, unless adequate flood insurance is obtained. The exception is loans less than \$5,000 with terms less than one year; for these loans, flood insurance is not required.

The National Flood Insurance Reform Act of 2004, also called the Bunning-Bereuter-Blumenauer Flood Insurance Reform Act of 2004, amends the National Flood Insurance Act of 1968. This Act was previously amended by the Flood Disaster Protection Act of 1973 and the National Flood Insurance Reform Act of 1994. Sections of all of these Acts remain relevant. Together, they create, reform, and reauthorize the National Flood Insurance Program.

Because the 2004 amendment does not repeat the text of prior amendments, this questionnaire provides pertinent guidance from applicable sections of the various Acts.

Cell: A6

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

1. The institution makes, increases, extends, or renews any loan(s) (commercial or consumer) secured by improved real estate or a mobile home affixed to a permanent foundation ("security property");
2. The property securing the loan is located or will be located in an SFHA as identified by FEMA; and
3. 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. A permanent foundation includes mobile home parks where a mobile home is connected to utilities. An institution does not have to obtain a security interest in their underlying real estate in order for the loan to be covered by the requirements of the national flood insurance program.

Flood insurance requirements also apply to loans where a security interest in improved real property is only taken "out of an abundance of caution." A regulated lending institution may not make, increase, extend, or renew any loan secured by improved real property located in a special flood hazard area unless the improved real property is covered by the minimum amount of flood insurance required by statute.

Flood insurance requirements do not apply to property securing a loan with an original balance of \$5,000 or less and a term of one year or less.

Cell: A7

Comment: NCUA can assess civil money penalties of \$385 per violation and up to \$110,000 annually.

If a CU has not met all the requirements of the Act and the borrower sustains a loss due to flooding, the CU may run the risk of being held liable in a negligence suit.

Cell: A8

Comment: Credit unions must maintain sufficient records to indicate the method used to determine whether improved real estate or a mobile home is in a Special Flood Hazard Area. You should find in every loan file subject to FDPA a Standard Flood Determination Form and the acknowledgement from the borrower that they received the required flood insurance notice.

Although not required, a credit union may wish to retain copies of any other notices sent to the borrower and a copy of the flood insurance policy.

Cell: A10

Comment: CUs must maintain sufficient records to indicate the method used to determine whether loans require flood insurance. Effective 1/2/96, CUs are required to use and maintain the "Standard Flood Hazard Determination Form" in determining whether property offered as collateral on a loan is located in a SFHA. The most current Standard Flood Hazard Determination Form can be found on the Federal Emergency Management Agency's (FEMA) web site at <http://www.fema.gov>

The credit union is required to maintain a record of the Standard Flood Hazard determination Form either in hard copy or electronic form for as long as it owns the loan.

For loans made before 1/2/96, the records must include (a) copies of official maps, including the date and complete panel number of the FEMA map used to determine whether the collateral is located in or out of a flood hazard zone; (b) written statements in each file indicating a flood determination was performed and the result; and (c) copies of any written contracts between the CU and the appraiser performing flood assessments.

Cell: A14

Comment: When a loan is secured by property located in a SFHA, the CU must mail or deliver a written notice to the borrower at least 10 days before closing. The notice must state (a) that the property is located in a flood hazard area; and (b) whether federal disaster relief assistance will be available for such property in the event of damage caused by flooding in a federally declared disaster area.

Cell: A15

Comment: The CU must obtain a written acknowledgment from the borrower that the property is located in an SFHA and the borrower has received the mandatory notice regarding federal disaster relief assistance.

Cell: A16

Comment: The borrower should present evidence of flood insurance at least equal to the amount of the loan, or the maximum amount available if the property is in a community insured under FEMA's National Flood Insurance Program (NFIP), was purchased.

Cell: A17

Comment: Flood insurance is written annually. The CU is responsible for ensuring coverage is renewed and maintained for the duration of the loan. When designated as mortgagee, the CU should receive copies of the policy and all renewal notices. If the borrower does not renew the policy, the CU has the responsibility to force place it or call the loan.

Cell: A18

Comment: Flood premium escrow accounts are only required when escrow accounts are established for other items such as property taxes or fire hazard insurance. The regulation does not require an institution establish escrow accounts if it is not their policy to do so. This requirement only applies to loan transactions after September 23, 1995.

Cell: A19

Comment: CUs are also required to notify FEMA of any change in the servicer of a loan requiring flood insurance within 60 days of the effective date of the change of the servicer.