United States Government Accountability Office

Report to the Chairman, Subcommittee on Economic Policy, Committee on Banking, Housing, and Urban Affairs, U.S. Senate

July 2016

FLOOD INSURANCE

Potential Barriers Cited to Increased Use of Private Insurance

GAO-16-611

GAO Highlights

Highlights of GAO-16-611, a report to the Chairman, Subcommittee on Economic Policy, Committee on Banking, Housing, and Urban Affairs, U. S. Senate

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Why GAO Did This Study

NFIP was created, in part, because private insurers historically have been unwilling to insure against flood damage. The private flood insurance market remains small. The 2012 Biggert-Waters Act took steps to encourage private-sector participation by requiring regulators to direct lenders to accept private flood insurance to satisfy the mandatory purchase requirement—a federal requirement to purchase flood insurance on certain properties.

GAO was asked to examine if the regulatory environment posed barriers to private flood insurance. This report describes (1) lender and regulator implementation of provisions on private flood insurance; and (2) views on regulatory, or other, barriers to using private flood insurance to satisfy the mandatory purchase requirement. GAO reviewed laws, regulations and guidance and interviewed officials from FEMA, five federal regulators, government-sponsored enterprises, and the National Association of Insurance Commissioners. GAO interviewed various stakeholders, selected based on their flood insurance experience and size, among other factors: a nongeneralizable sample of eight lenders; 13 organizations; five state insurance regulators; and four private flood insurers.

What GAO Recommends

GAO recommends that FEMA reconsider allowing policyholders who cancel their NFIP policy to be refunded, on a prorated basis, when obtaining a non-NFIP policy and take any necessary steps to amend the NFIP standard policy to do so. FEMA agreed with our recommendation.

View GAO-16-611. For more information, contact Alicia Puente Cackley at (202) 512-8678 or cackleya@gao.gov.

What GAO Found

Lenders and their regulators have taken some action to implement provisions on private flood insurance in the Biggert-Waters Flood Insurance Reform Act of 2012 (Biggert-Waters Act). Specifically, lenders told GAO they send notifications to borrowers that encourage borrowers to compare private and National Flood Insurance Program (NFIP) policies. Lenders with whom GAO spoke accepted private policies and generally said they used Federal Emergency Management Agency (FEMA) guidelines and interagency guidance to evaluate private policies. Federal regulators (Board of Governors of the Federal Reserve System, Federal Deposit Insurance Corporation, Office of the Comptroller of the Currency, National Credit Union Administration, and Farm Credit Administration) issued interagency questions and answers on private insurance in 2009, which cite the FEMA guidelines. However, FEMA rescinded its guidelines in 2013, citing a lack of authority to rule on the acceptability of private insurance policies. Federal regulators have issued joint proposed rules to implement the Biggert-Waters Act definition of private flood insurance, but have not yet finalized them. Regulators stated that the information provided in the 2009 Questions and Answers remains in effect until final rules implementing the private flood insurance provisions of the Biggert-Waters Act are adopted.

Stakeholders cited a number of challenges as potentially inhibiting the use of private flood insurance to satisfy the mandatory purchase requirement.

- **Regulatory uncertainty**. Without final regulations implementing the Biggert-Waters Act requirement to accept private flood insurance, there was uncertainty among stakeholders about which private policies would satisfy the mandatory purchase requirement. Many stakeholders, including some lenders, emphasized that lenders needed discretion when evaluating policies and that ensuring policies met the Biggert-Waters Act definition would be challenging for lenders, in part due to their lack of insurance expertise.
- **Recent NFIP changes**. Stakeholders noted that a recent NFIP policy change could discourage consumers' use of private insurance. FEMA recently stopped allowing policyholders to obtain a refund of their unused NFIP premium if they obtained a non-NFIP policy. FEMA officials stated that, based on their recent review of NFIP cancellation policies, this practice was not explicitly permitted in the NFIP standard flood insurance policy terms and conditions. Due to this change, consumers who wish to obtain private coverage would forfeit any unused portion of their premium if they switched after the NFIP policy's effective date. While FEMA's standard policy terms do not specifically address refunds when a non-NFIP policy is obtained, FEMA could revise the standard policy to allow for such refunds. Allowing this type of refund would be in line with industry practice to allow refunds of paid premiums when cancelling insurance policies, as well as Congressional interest in transferring some of the federal government's exposure to flood insurance risk to the private sector.
- **Market challenges**. Many stakeholders noted that low private sector participation in flood insurance was also due to market challenges, some citing the inability to compete with discounted NFIP rates as a primary barrier—a finding that GAO also reported in previous work (GAO-14-127).

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Abbreviations

Biggert-Waters Act	Biggert-Waters Flood Insurance Reform Act of 2012
Fannie Mae	Federal National Mortgage Association
FCA	Farm Credit Administration
FDIC	Federal Deposit Insurance Corporation
FDPA	Flood Disaster Protection Act of 1973
Federal Reserve	Board of Governors of the Federal Reserve System
FEMA	Federal Emergency Management Agency
FHA	Federal Housing Administration
FIMA	Federal Insurance and Mitigation Administration
Freddie Mac	Federal Home Loan Mortgage Corporation
GSE	government-sponsored enterprise
HFIAA	Homeowner Flood Insurance Affordability Act of 2014
NAIC	National Association of Insurance Commissioners
NAPSLO	National Association of Professional Surplus Lines Offices
NCUA	National Credit Union Administration
NFIP	National Flood Insurance Program
OCC	Office of the Comptroller of the Currency
RESPA	Real Estate Settlement Procedures Act
SFHA	special flood hazard area
SFIP	Standard Flood Insurance Policy
Treasury	Department of the Treasury
VA	Department of Veterans Affairs
WYO	Write-Your-Own

U.S. GOVERNMENT ACCOUNTABILITY OFFICE
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July 14, 2016

The Honorable Dean Heller
Chairman
Subcommittee on Economic Policy
Committee on Banking, Housing, and Urban Affairs
United States Senate

Dear Chairman Heller:

Floods are the most common and destructive natural disaster in the United States. Created by the National Flood Insurance Act of 1968, the National Flood Insurance Program (NFIP) is designed to protect homeowners from flood losses, minimize the exposure of property to flood damage, and alleviate taxpayers' responsibility for flood losses paid out in the form of postdisaster relief.[1] NFIP—which is administered by the Federal Emergency Management Agency (FEMA)—was created, in part, because private insurers historically have been largely unwilling to insure against flood damage. As of April 2016, NFIP collected about $3.4 billion in annual premiums and insured about $1.2 trillion in property. Congress passed the Flood Disaster Protection Act of 1973 (FDPA) to increase flood insurance coverage among borrowers and encourage participation in NFIP.[2] FDPA, as amended, requires each federal entity for lending regulation to direct regulated lending institutions to ensure that borrowers with mortgages held by regulated lending institutions and secured by properties located in special flood hazard areas (SFHA) in communities

[1]Pub. L. No. 90-448, Tit. XIII, 82 Stat. 476, 572 (1968).

[2]Pub. L. No. 93-324, 87 Stat. 975 (1973).

participating in FEMA's NFIP purchase and maintain flood insurance (mandatory purchase requirement).[3]

After several years of catastrophic losses, primarily from Hurricane Katrina and other 2005 storms and Superstorm Sandy in 2012, NFIP's current debt to the Department of the Treasury (Treasury) was $23 billion as of April 2016.[4] Because of its premium structure, NFIP is unlikely to be able to repay this debt in the near future, if ever.[5] As a result of its financial exposure and management challenges, the program has been on GAO's High-Risk list since 2006.[6] Furthermore, some members of Congress and others have shown increased interest in reducing the federal role in flood insurance by transferring its exposure to the private sector. In addition, new technologies and a better understanding of flood risks may have increased the private sector's willingness to offer flood coverage. The Biggert-Waters Flood Insurance Reform Act of 2012

[3]The insurance must be in an amount at least equal to the outstanding principal balance of the loan or to the maximum limit of coverage made available under the National Flood Insurance Act of 1968 (as amended), whichever is less. 42 U.S.C. § 4012a(b)(1)(A). The term "federal entity for lending regulation" includes the Board of Governors of the Federal Reserve System (Federal Reserve), the Federal Deposit Insurance Corporation (FDIC), the Office of the Comptroller of the Currency (OCC), the National Credit Union Administration (NCUA), and the Farm Credit Administration (FCA). The term "regulated lending institution" means any bank, savings and loan association, credit union, farm credit bank, Federal land bank association, production credit association, or similar institution subject to the supervision of a Federal entity for lending regulation. With respect to a particular regulated lending institution, the federal entity for lending regulation is the entity primarily responsible for the supervision of that institution. 42 U.S.C. § 4003(a).

[4]FEMA has authority to borrow money from Treasury to pay losses that exceed premium revenue and any accumulated surplus. Treasury charges FEMA interest on the outstanding debt. Before Superstorm Sandy, this borrowing authority stood at $20.725 billion. In January 2013, Congress increased this authority to enable FEMA to pay flood claims related to Superstorm Sandy, raising FEMA's borrowing authority to a total of $30.425 billion. Pub. L. No. 113-1, § 1(a), 127 Stat. 3, 3 (2013).

[5]FEMA made a $1 billion principal prepayment at the end of December 2014—its first payment since 2010. The Biggert-Waters Flood Insurance Reform Act of 2012 amended the National Flood Insurance Act to require FEMA to develop a plan for repaying its debt to Treasury. Pub. L. No. 112-141, Div. F, Tit. II, Subtit. A, § 100213(a), 126 Stat. 916, 923 (2012) (codified at 42 U.S.C. § 4016(c)). In September 2014, FEMA's largest loan from Treasury was refinanced into three smaller loans with higher interest rates, and FEMA will have higher payments on its debt.

[6]Every 2 years, we provide Congress with an update on our High-Risk Program, which highlights major areas that are at high risk for fraud, waste, abuse, or mismanagement, or need broad reform. See GAO, *High-Risk Series: An Update*, GAO-15-290 (Washington, D.C.: Feb. 11, 2015).

(Biggert-Waters Act) reauthorized NFIP through September 30, 2017, and included changes related to the acceptance of private flood insurance to satisfy the mandatory purchase requirement.[7] In January 2014, we reported on conditions needed for private-sector involvement in flood insurance and strategies for increasing private-sector involvement.[8]

You requested that we revisit the issue of the private-sector involvement in flood insurance with a focus on the regulatory environment and whether it posed any barriers to private flood insurance policies being purchased by homeowners to satisfy the mandatory purchase requirement. This report describes (1) regulated lending institutions' and federal regulators' implementation of statutory provisions governing the use of private flood insurance to satisfy the mandatory purchase requirement; and (2) views on any regulatory, or other, barriers to the increased use of private flood insurance to satisfy the mandatory purchase requirement.

To address these objectives, we reviewed flood insurance laws and regulations, related agency guidance, congressional hearings, and studies, as well as past GAO reports on insurance markets and flood insurance.[9] To address the first objective, we reviewed relevant federal flood insurance laws to identify the requirements for federal entities for lending regulation (federal regulators) and how each regulator addresses the use and acceptability of private flood insurance to fulfill the mandatory purchase requirement. The federal regulators involved in implementing the provisions of the flood insurance laws governing the mandatory purchase requirement are the Office of the Comptroller of the Currency (OCC), the Board of Governors of the Federal Reserve System (Federal Reserve), the Federal Deposit Insurance Corporation (FDIC), the Farm Credit Administration (FCA), and the National Credit Union Administration (NCUA). We interviewed officials from each of these agencies, the Federal National Mortgage Association (Fannie Mae), Federal Home

[7]Pub. L. No. 112-141, Div. F, Tit. II, Subtit. A, 126 Stat. 916 (2012).

[8]GAO, *Flood Insurance: Strategies for Increasing Private Sector Involvement*, GAO-14-127 (Washington, D.C.: Jan. 22, 2014).

[9]For example, GAO-14-127; *Insurance Markets: Impacts of and Regulatory Response to the 2007-2009 Financial Crisis*, GAO-13-583 (Washington, D.C.: June 27, 2013); and *Flood Insurance: Extent of Noncompliance with Purchase Requirements Is Unknown*, GAO-02-396 (Washington, D.C.: June 21, 2002).

Loan Mortgage Corporation (Freddie Mac), and FEMA. We also obtained information from the Department of Housing and Urban Development's (HUD) Federal Housing Administration (FHA).

To understand how lenders are fulfilling the requirements, we identified and interviewed representatives from a nongeneralizable sample of eight mortgage lenders based on their volume of loans in counties with a high volume of NFIP policies, size and type of institution, and other factors.[10] To better understand how the federal regulators have implemented the statutory requirements, we compared their regulations with the statutes. We also reviewed guidance provided by the federal regulators and FEMA related to the use of private flood insurance to satisfy the mandatory purchase requirement. We reviewed and compared each of the regulators' examination manuals and flood insurance modules to understand how each examined the regulated lending institutions they supervise for compliance. Finally, we reviewed the policies of Fannie Mae, Freddie Mac, the Department of Veterans Affairs (VA), and FHA to understand their flood insurance requirements for mortgages they either purchase or insure.

To address the second objective on any barriers, we interviewed various stakeholders in the flood insurance industry: selected lenders (as discussed above), organizations in the insurance and lending industries, private flood insurance companies, and officials from selected state insurance regulatory agencies. We selected 13 organizations to interview based on the organization's type, purpose and relevance to private flood insurance, and membership. We identified these organizations based on previous and ongoing GAO work on flood insurance, and comment letters submitted by interested parties in response to federal regulators' proposed rules on private flood insurance.[11] We also selected and interviewed representatives from a nongeneralizable sample of four private insurance companies involved in the private market for flood insurance. We identified and selected these companies through news articles and our interviews with representatives of lenders and state

[10]Our sample included two nonbank mortgage lenders that are not directly subject to the requirements of FDPA as they do not fit within the statutory definition of regulated lending institutions. For the purposes of this report, we use "lenders" to refer to the eight lenders with whom we spoke. We spoke with the nonbank lenders to better understand practices related to private flood insurance among the full scope of mortgage market participants.

[11]See 78 Fed. Reg. 65,108 (Oct. 30, 2013) (joint notice of proposed rulemaking).

regulatory agencies. We also interviewed insurance regulators and their representatives from Florida, Louisiana, Pennsylvania, Texas, and West Virginia and reviewed selected laws from those states. We selected these states based on the volume of NFIP policies written and flood insurance regulatory activity in each state. Information provided by the selected state insurance regulators is not generalizable to all states. In addition, we reviewed 44 comment letters submitted in response to proposed rules issued by the federal regulators in October 2013 on the acceptance of private flood insurance to satisfy the mandatory purchase requirement in order to identify comments pertaining to potential or actual regulatory barriers to the use of private flood insurance and potential effects of the proposed rules. We conducted a literature search for news articles and studies to determine what is known about any regulatory, or other, barriers to using private flood insurance to satisfy the mandatory purchase requirement. We also interviewed representatives of the National Association of Insurance Commissioners (NAIC) and the Department of the Treasury's Federal Insurance Office.[12]

We conducted this performance audit from May 2015 to July 2016 in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Background

Flooding disasters of the 1920s and 1930s led to federal involvement in protecting life and property from flooding, with the passage of the Flood Control Act of 1936.[13] Generally, the only available financial recourse to assist flood victims was postdisaster assistance. When flood insurance was first proposed in the 1950s, it became clear that private insurance companies could not profitably provide flood coverage at a price that

[12]NAIC is the U.S. standard-setting and regulatory support organization created and governed by the chief insurance regulators from the 50 states, the District of Columbia and the five U.S. territories. Through the NAIC, state insurance regulators establish standards and best practices, conduct peer review, and coordinate their regulatory oversight. NAIC members, together with the central resources of the NAIC, form the national system of state-based insurance regulation in the U.S.

[13]49 Stat. 1570 (1936).

consumers could afford, primarily because of the catastrophic nature of flooding and the difficulty of determining accurate rates.[14] In 1965, Congress passed the Southeast Hurricane Disaster Relief Act that provided financial relief for victims of flooding and mandated a feasibility study of a national flood insurance program, which helped provide the basis for the National Flood Insurance Act of 1968 that created NFIP.[15]

FEMA, through its Federal Insurance and Mitigation Administration (FIMA), manages the flood insurance program and sells and services NFIP policies primarily through private insurance companies in the Write-Your-Own (WYO) program.[16] Program participation takes place at the community and the property-owner level. To participate, communities must adopt and enforce land use and control measures to mitigate the effects of flooding on new or existing homes in SFHAs. Participation for property owners (borrowers) in participating communities initially was voluntary; however, due in part to low levels of borrower participation; Congress established the mandatory purchase requirement for properties located in SFHAs in participating communities.

Overview of Mandatory Purchase Requirement

Regulated lending institutions and loan servicers acting on their behalf must ensure that borrowers (1) purchase flood insurance for any building or a mobile home located or to be located in an SFHA in a participating community at the time a mortgage loan for that property is obtained, or at the time of increasing, extending or renewing the loan, and (2) maintain the insurance through the life of the loan, or add it if the property is remapped into an SFHA and the borrower is then required to purchase flood insurance under the mandatory purchase requirement.[17] Regulated

[14]Federal Emergency Management Agency, *National Flood Insurance Program: Program Description* (Washington, D.C.: Aug. 1, 2002).

[15]Pub. L. No. 89-339, 79 Stat. 1301 (1965); National Flood Insurance Act of 1968, Pub. L. No. 90-448, Title XIII, 82 Stat. 476, 572 (1968).

[16]Under the WYO program, private insurers sell and service policies and adjust claims for NFIP under an arrangement with FEMA. FEMA compensates the insurers for their services and also pays bonuses for expanding NFIP's policy base by increasing the number of policies they sell.

[17]A servicer is the entity responsible for receiving any scheduled, periodic payments from a borrower under the terms of a loan, including amounts for taxes, insurance premiums, and other charges relating to the property securing the loan, and making payments of principal and interest and any other payments with respect to the amounts received from the borrower as may be required under the terms of the loan. 42 U.S.C. § 4003(a)(11).

lending institutions may not make, increase, extend, or renew any loan secured by improved real estate or a mobile home located or to be located in an SFHA community participating in NFIP unless the building or mobile home and any personal property securing such loan is covered by flood insurance for the term of the loan, subject to certain exceptions.[18] Although FDPA did not define "flood insurance" to specifically include or exclude private insurance, guidance issued by the Federal Insurance Administration in 1974 stated that private flood insurance policies could satisfy the mandatory purchase requirement as long as they met specified criteria.[19]

The National Flood Insurance Reform Act of 1994 (1994 Act) further amended the statutory framework for the mandatory purchase requirement and its enforcement by federal regulators.[20] The 1994 Act directed that federal regulators issue regulations to require regulated

[18]Nonbank entities that provide mortgages to borrowers may not fall within the definition of regulated lending institutions for purposes of FDPA. However, these nonbanks may choose to comply with the requirements of government-sponsored enterprises (GSE) such as Fannie Mae to be able to sell the mortgage to one of the GSEs. As required by statute, GSEs have implemented procedures requiring flood insurance for loans that they purchase secured by improved real estate or manufactured homes in an SFHA. Nonbanks also may choose to require flood insurance to protect the property for which they are providing the loan.

[19]Mandatory Purchase of Flood Insurance, 39 Fed. Reg. 26,186, 26,190 (July 17, 1974). The Housing and Urban Development Act of 1968, of which the National Flood Insurance Act of 1968 was a part, created the Federal Insurance Administrator as a position within the Department of Housing and Urban Development. Pub. L. No. 90-448, § 1105, 82 Stat. 476, 567 (1968). In 1979, Executive Order 12127 merged the Federal Insurance Administration and a number of other disaster-related responsibilities into the Federal Emergency Management Agency. Exec. Order No. 12,127, 44 Fed. Reg. 19,367 (Mar. 31, 1979). The 1974 guidance stated that any flood insurance policy submitted in purported satisfaction of the mandatory purchase requirement should meet the following criteria: (a) the insurer is licensed to do business in the jurisdiction where the property is located; (b) the policy includes an endorsement that requires the insurer give 30 days written notice to both the insured and the lender of cancellation or nonrenewal and guarantees that coverage is at least as broad as the coverage offered by NFIP. The guidance also urges lenders, when flood insurance other than the Standard Flood Insurance Policy (SFIP) under NFIP is offered, to (1) advise borrowers of the availability of flood insurance under NFIP so that the borrower can make an appropriate comparison of the premium costs, and (2) satisfy themselves that the insurance policy contains a mortgagee interest clause similar to that in SFIP.

[20]The National Flood Insurance Reform Act of 1994 was passed as Title V of the Riegle Community Development and Regulatory Improvement Act of 1994. Pub. L. No. 103-325, Tit. V, 108 Stat. 2160, 2255 (1994).

lending intuitions to notify borrowers in SFHAs about the availability of flood insurance coverage under NFIP, and that such coverage is also available from private insurers.[21] Regulations implementing the 1994 Act require that regulated lending institutions mail or deliver a written notice to the borrower and servicer before completion of the transaction. The notice must contain the following information:

- a warning that the building or the mobile home is or will be located in an SFHA;
- a description of the flood insurance purchase requirements under FDPA, as amended;
- a statement, where applicable, that flood insurance coverage is available under NFIP and also may be available from private insurers; and
- a statement whether federal disaster relief assistance may be available if flooding (from a federally declared disaster) causes damage to the building or mobile home.[22]

The 1994 Act also requires regulators to assess civil monetary penalties against regulated lending institutions found to have a pattern or practice of violating certain federal flood insurance requirements. It also required Fannie Mae and Freddie Mac to implement procedures reasonably

[21]Some lenders do their own servicing, while others sell the servicing rights to loans in their portfolio. According to guidance provided by the federal regulators, in the event a regulated lender retains ownership of the loan but sells the servicing rights to a nonregulated servicer, the regulated lender remains ultimately liable for the fulfillment of flood insurance requirements. The federal regulators state that the servicing contract should require the servicer to comply with all the requirements that are imposed on the regulated lender as owner of the loan. If the regulated lender sells both the loan and the servicing rights, however, the lender has no further obligation regarding flood insurance. *See* 74 Fed. Reg. 35,914, 35,942 (July 21, 2009).

[22]61 Fed. Reg. 45,684 (Aug. 29, 1996). Regulated lending institutions must send the servicer the notice as promptly as practicable after it provides notice to the borrower and in any event no later than the time the regulated lending institution provides other similar notices to the servicer concerning hazard insurance and taxes. Regulated lending institutions also may obtain satisfactory written assurance from a seller or lessor that, within a reasonable time before the completion of the sale or lease transactions, the seller or lessor has provided such notice to the purchaser or lessee. Regulated lending institutions are required to retain a record of receipt of the notice by the borrower and the servicer, or written assurance from the seller or lessor for the period of time the regulated lending institution owns the loan.

designed to ensure that any mortgage they purchase (secured by improved real estate or a mobile home in an SFHA) has flood insurance.

More recently, in 2012, the Biggert-Waters Act reauthorized NFIP through September 30, 2017, and made some significant changes to FDPA.[23] For example, the Biggert-Waters Act increased the maximum penalties that may be assessed against a regulated lending institution. The Biggert-Waters Act also required regulators to issue regulations directing lending institutions to accept private flood insurance (as defined by the act) and modified the required notification of borrowers of the availability of private flood insurance.[24]

In 2013, the federal regulators issued a joint notice of proposed rulemaking to implement certain provisions of the Biggert-Waters Act, including the modified notification and required acceptance of private flood insurance.[25] In July 2015, the regulators issued a final rule implementing the modified notification provision and certain other provisions from the Biggert-Waters Act and HFIAA.[26] The July 2015 final rule did not include implementation of the Biggert-Waters Act's requirements on private flood insurance; the agencies noted that they planned to address those requirements in a separate rulemaking. See figure 1 for a summary timeline of selected federal flood insurance legislation.

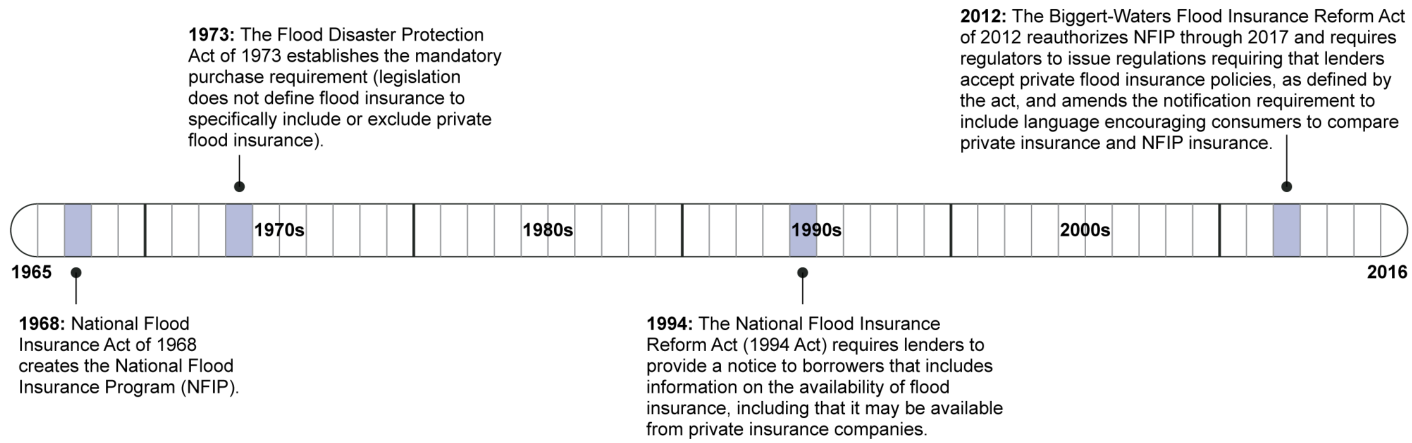
[23]Pub. L. No. 112-141, Div. F, Tit. II, Subtit. A, 126 Stat. 916 (2012).

[24]The Biggert-Waters Act also amended the Real Estate Settlement Procedures Act of 1974 (RESPA) to mandate a revision to required notices to include a notice to the borrower of the availability of flood insurance under NFIP or from a private insurance company, whether or not the real estate is located in an area having special flood hazards. Pub. L. No. 112-141, § 100222, 126 Stat. 916, 934 (codified at 12 U.S.C. § 2604(b)(14)). The requirement to revise the notices required under RESPA is the responsibility of the Bureau of Consumer Financial Protection.

[25]78 Fed. Reg. 65,108 (Oct. 30, 2013).

[26]For example, the July 2015 final rule implemented the escrow and detached structure provisions of HFIAA and the force-placement provisions of the Biggert-Waters Act. 80 Fed. Reg. 43,216 (July 21, 2015).

Figure 1: Selected Flood Legislation, Including that Related to Private Flood Insurance, 1965-July 2016



Source: GAO review of relevant flood legislation. | GAO-16-611

Overview of Insurance Regulation and Markets

Insurance is primarily regulated by the states, unless federal law specifically relates to the business of insurance (as in the cases of flood and terrorism insurance).[27] Federal regulators generally have authority over the activities of regulated lending institutions that relate to the flood insurance requirements under FDPA. The Federal Reserve, FDIC, OCC, NCUA, and FCA are the regulators responsible for overseeing the federal flood insurance requirements, including the mandatory flood insurance purchase requirement, for their institutions (see table 1).

[27]McCarran-Ferguson Act, 15 U.S.C §§ 1011-1015. Two federal insurance programs are the National Flood Insurance Program and the Terrorism Risk Insurance Program.

Table 1: Federal Regulators and the Lending Institutions They Supervise for Flood Insurance Activities, 2016

Federal agency	Regulated entities
Board of Governors of the Federal Reserve System (Federal Reserve)	State-chartered banks that opt to be members of the Federal Reserve System, and subsidiaries of those institutions
Farm Credit Administration (FCA)	Farm Credit System institutions
Federal Deposit Insurance Corporation (FDIC)	State-chartered banks that are not members of the Federal Reserve System and federally insured state savings banks and thrifts
National Credit Union Administration (NCUA)	All federally insured credit unions
Office of the Comptroller of the Currency (OCC)	National banks, federal savings associations, and any service corporation thereof, and federal branches or agencies of foreign banks

Source: GAO analysis of agency information. | GAO-16-611

Requirements and processes for regulating insurance may vary from state to state, but state regulators generally license insurance companies and agents, review insurance products and premium rates, and examine insurers' financial solvency and market conduct. According to NAIC, state regulators monitor an insurers' compliance with laws and regulations, and a company's financial condition through solvency surveillance and examination mechanisms. Insurance regulators use insurance companies' financial statements and other information as part of their continuous financial analysis, which is performed at least quarterly, to identify issues that could affect solvency. State insurance regulators typically conduct on-site financial solvency examinations every 3–5 years, although they may do so more frequently for some insurers, and may perform additional examinations as needed. Through NAIC, the regulators also collect financial information from insurers for ongoing monitoring of financial solvency.[28]

Admitted Insurance Market

Admitted insurers can sell insurance in one or more states but must be licensed to operate in every state in which they sell coverage. Admitted

[28]While NAIC does not regulate insurers, according to NAIC officials, it provides services designed to make certain interactions between insurers and regulators more efficient. According to NAIC, these services include providing detailed insurance data to help regulators analyze insurance sales and practices; maintaining a range of databases useful to regulators; and coordinating regulatory efforts by providing guidance, model laws and regulations, and information-sharing tools. Generally, a model act or law is meant as a guide for subsequent legislation. State legislatures may adopt model acts in whole or in part, and modify them to fit their needs.

insurers can be licensed to sell several lines or types of coverage to individuals or families, including personal lines (such as homeowners, renters, and automobile insurance) and commercial lines (such as general liability, commercial property, and product liability insurance). Their activities are regulated primarily by the states. State regulators require admitted insurance companies to maintain specific levels of capital to continue to conduct business.[29]

Admitted insurers provide coverage for numerous risks, but they may not be willing to cover some risks. These include risks that are difficult to assess, occur too frequently to be acceptable to admitted insurers, are specialized or unusual, or require coverage that exceeds the capacity of admitted carriers. In these cases, potential insureds may turn to the nonadmitted market.

Nonadmitted Market and Surplus Lines Insurance

The nonadmitted market offers insurance products for risks for which coverage is unavailable in the admitted market. Among the nonadmitted insurers are surplus lines insurers.[30] These insurers provide coverage for general, management, and professional liabilities and commercial, automobile, environmental, and property risks, among other things, and tailor their products to meet the needs of the insured. For example, they may write policies to cover personal lines of insurance such as homeowners insurance in flood-prone areas. In 2014, the total surplus

[29]In addition, in the event that an insurer becomes insolvent, states have guaranty funds to help ensure that policyholders continue to receive coverage. Guaranty funds (separate for life and property/casualty insurance), are funded by assessments on insurers doing business in their state. Guaranty funds pay covered claims within limits set by individual state laws and the insurance contract. For instance, the overall benefit cap in most states for an individual life or property/casualty policy is $300,000, although some states have higher maximums. Certain products, such as some variable annuities, financial guaranty insurance, and mortgage guaranty insurance, are not covered by state guaranty funds.

[30]All states have laws that permit surplus lines insurers to sell coverage in their states, but do not cover their policies with state guaranty funds. According to NAIC, while policyholders may not have as much protection as they would under a guaranty fund, state insurance receivership laws provide a mechanism for marshaling the assets of the insurer if the company fails. Also, states generally require a disclosure to policyholders that the surplus lines policy is not subject to state guaranty fund coverage. Furthermore, according to NAIC, surplus lines insurers are regulated for financial solvency by their state of domicile in the same manner as are licensed companies. Congress passed the Nonadmitted and Reinsurance Reform Act of 2010, which included regulatory reforms to, among other things, make it easier to access the surplus lines market and create uniform standards for regulating surplus lines insurers. Pub. L. No. 111-203, Tit. V, Subtit. B, 124 Stat. 1376, 1589 (2010).

lines direct premiums written in the U.S. market totaled more than $40 billion.[31]

While admitted insurers must be licensed in the states in which they sell insurance, surplus lines insurers must be licensed in only one state but may sell in others in which they are not licensed, provided they are eligible according to the states' surplus lines laws.[32] Surplus lines insurers also must sell their insurance through a state-licensed broker. The brokers typically represent insurance buyers and place coverage with surplus lines insurers.[33] According to NAIC, on a surplus lines placement, the insurance regulator of the policyholder's home state has authority over the placement of the insurance by a surplus lines broker and can sanction the surplus lines broker, revoke their license, and hold them liable for the full amount of the policy. To place coverage in the surplus lines market, brokers must follow state due diligence requirements. Although they vary from state to state, according to an association representing surplus lines insurers and brokers, these requirements generally call for a "diligent search" of the admitted market before turning to a surplus lines insurer. The diligent search generally requires brokers to establish that three admitted companies licensed to write the kind and type of insurance being requested had declined to provide it.[34]

[31]A.M. Best, *U.S. Surplus Lines: Record Levels Reached* (Oldwick, New Jersey: August 2015).

[32]Surplus lines coverage is the largest component of the nonadmitted market. An insured also can access the nonadmitted market by purchasing insurance out of state from a carrier not licensed to sell insurance where the risk is located or through a broker not licensed by the jurisdiction where the risk is located.

[33]Brokers are responsible for (1) selecting an eligible surplus lines insurer, (2) reporting the surplus lines transaction to insurance regulators, (3) remitting the premium tax due on the transaction to state tax authorities, and (4) assuring compliance with all the requirements of state regulations for the surplus lines.

[34]For additional information on the admitted and nonadmitted insurance markets and regulation, see GAO, *Property and Casualty Insurance: Effects of the Nonadmitted and Reinsurance Reform Act of 2010*, GAO-14-136 (Washington, D.C.: Jan. 16, 2014).

Lenders' and Regulators' Implementation of Provisions Relating to Private Flood Insurance

Lenders Told Us They Rely on Existing Guidance and Criteria When Assessing Private Policies

All eight of the lenders with whom we spoke stated that they accept or would accept private flood insurance as satisfaction of the mandatory purchase requirement. Moreover, all but one stated that they have policies and procedures that use one or more sources of guidance when determining if a private policy satisfies the mandatory purchase requirement.[35] All but one of the lenders referenced the criteria in FEMA's (now rescinded) *Mandatory Purchase of Flood Insurance Guidelines* (Guidelines) as one set of guidance—the Guidelines provided lenders with six criteria to evaluate private flood insurance policies for compliance with the mandatory purchase requirement. The Guidelines also provided that to the extent the policy differs from the NFIP standard policy, the differences should be examined before the policy is accepted. (See table 2 and app. II for more detailed information on the criteria.) Half of the lenders with whom we spoke also referenced the July 2009 Interagency Questions and Answers Regarding Flood Insurance (2009 Questions and Answers) provided by the federal regulators, which cite FEMA's Guidelines as criteria for evaluating private flood insurance policies.[36] One lender cited the requirements of Fannie Mae and Freddie Mac as a primary source of guidance.[37] The same lender also added that when

[35]One bank indicated that it had no experience with private flood insurance because, to date, none of its customers had attempted to use such insurance to satisfy the mandatory purchase requirement.

[36]74 Fed. Reg. 35,914 at 35,944 (July 21, 2009).

[37]Fannie Mae's and Freddie Mac's requirements state that the terms and conditions of the flood insurance coverage must be at least equivalent to the terms and conditions of coverage under a standard NFIP policy for the appropriate property type. The requirements also state that any private flood insurance must be written by a carrier that meets certain financial strength ratings requirements. For additional information on Fannie Mae and Freddie Mac's requirements, see their respective selling guides. *Selling Guide: Fannie Mae Single Family, Fannie Mae, June 28, 2016; Single-Family Seller/Servicer Guide, Freddie Mac, March 9, 2016.*

working with loans insured by FHA and VA, they use their requirements and guidance on the use of private flood insurance.[38]

Table 2: FEMA's Criteria for Evaluating Private Flood Insurance Policies, 2007 (Rescinded in February 2013)

Criteria	Summary
Licensure	The insurer must be licensed, admitted, or otherwise approved to do business in the jurisdiction where the building is located, by the insurance regulator of that jurisdiction, except for surplus lines recognition (see next row).
Surplus lines recognition	In the case of nonresidential commercial property insurance issued under a policy of difference in conditions, multiple peril, all risk, or other blanket coverage, the insurer should be recognized, or not disapproved, as a surplus lines insurer by the insurance regulator of the jurisdiction where the building is located.
Requirement of 45-day cancellation/nonrenewal notice	The policy should include a requirement for the insurer to give 45 days' written notice of cancellation or nonrenewal of flood insurance coverage to the insured, with respect to the flood insurance coverage. The policy should also state that, to be effective, such notice must be mailed to both the insured and the lender or federal agency lender, and must include information about the availability of NFIP insurance. The policy should be as restrictive in its cancellation provisions as the NFIP standard policy.
Breadth of policy coverage	The policy must guarantee that the flood insurance coverage, considering deductibles, exclusions, and conditions offered by the insurer, is at least as broad as the coverage under the NFIP standard policy.
Strength of mortgage interest clause	Lenders must ensure that the private policy contains a mortgage interest clause similar to that contained in the general conditions section of the NFIP standard policy.
Legal recourse	The policy must contain a provision that the insured must file suit within 1 year after the date of written denial of all or part of the claim.

Legend:

FEMA – Federal Emergency Management Agency

NFIP – National Flood Insurance Program

Source: FEMA's Mandatory Purchase of Flood Insurance Guidelines. | GAO-16-611

FEMA issued Guidelines in 1989 to promote greater uniformity and understanding of the requirements of mandatory purchase provisions among federal regulators of lenders, government-sponsored enterprises (such as Fannie Mae or Freddie Mac), federal agency lenders, and

[38]FHA is not a federal agency lender and therefore is not directly subject to the Biggert-Waters Act requirement for federal agency lenders. Currently, its Single Family Handbook states that properties in SFHAs are only eligible for FHA insurance if NFIP insurance is obtained. However, FHA has determined that revisions to its Handbook are necessary and plans to go through the rulemaking process to revise its regulations to allow for the acceptance of private flood insurance for FHA-insured loans. VA is a federal agency lender and is therefore subject to the Biggert-Waters Act provisions on private insurance for federal agency lenders. VA regulations provide that when making, increasing, extending, or renewing loans, it must provide the borrower a notice that includes the statement that flood insurance may be available from private insurers that do not participate in NFIP.

applicable lending institutions.[39] In February 2013, FEMA rescinded the Guidelines, stating that the six elements listed in the guidance were intended to provide assistance to regulated lending institutions in determining the acceptability of private flood insurance and were not meant to be exclusive. Furthermore, FEMA stated, as it had in the Guidelines, that it had no authority to rule on the acceptability of private insurance policies.[40]

However, federal regulators told us that until they finalize regulations requiring regulated lending institutions to accept private flood insurance under the Biggert-Waters Act, regulated lending institutions should continue to use the 2009 Questions and Answers as guidance when determining if a private flood insurance policy satisfies the purchase requirement.[41] In these Questions and Answers, the regulators state that a private flood insurance policy may be an adequate substitute for an NFIP policy if it meets the criteria set forth by FEMA in its Guidelines.[42] The 2009 Questions and Answers also state that regulated lending institutions may rely on a private policy that does not meet the FEMA

[39]FEMA officials told us that the earliest documentation of the Guidelines that they were able to find was from 1989 but could not confirm this was the earliest version of the Guidelines.

[40]In the Guidelines, FEMA stated that the Guidelines are intended to augment, not replace, a review of the applicable statutes and regulations, and that FEMA does not have statutory responsibility for enforcing the mandate to purchase flood insurance. FEMA also states that the implementation of the mandatory purchase requirements is the responsibility of the federal agencies that oversee lenders.

[41]More specifically, regulators stated that regulated lending institutions should continue to use the requirements set forth in the answers to questions 63 and 64 when determining if a private flood insurance policy meets the regulated lending institutions' obligations.

[42]FCA also issued an Informational Memorandum stating that, pending issuance of a regulation on private insurance, FCA will not bring an enforcement action against any institution that accepts a private flood insurance policy in satisfaction of the mandatory purchase requirement, provided the policy meets certain minimum criteria set forth in the memorandum.

criteria only in limited circumstances.[43] Officials for each of the regulators acknowledged that the 2009 Questions and Answers cite the rescinded FEMA Guidelines but stated that the overall guidance remains in effect. They noted that regulated lending institutions continue to have discretion in determining whether a private flood insurance policy meets regulated lending institutions' obligations under the mandatory purchase requirement.

Furthermore, in their interagency statement as well as their 2013 joint notice of proposed rulemaking, the regulators stated that the Biggert-Waters Act provision requiring the acceptance of private flood insurance, as defined by the act, will be implemented through rulemaking. Both documents noted that the regulators considered this provision not effective until final regulations are issued.[44] The 2013 joint notice of proposed rulemaking further stated that regulated lending institutions currently continue to have the discretion to accept flood insurance issued by private insurers.[45] According to federal regulators, while they are working on finalizing these regulations, they currently do not have a timetable for issuing final regulations implementing these requirements.

According to most of the lenders with whom we spoke, each exercises some level of discretion when determining whether a private policy meets the guidance they currently follow. For example, two lenders stated that if a private policy does not exactly match the FEMA criteria, they use their judgement in determining if the policy provides sufficient protection under the law. Four lenders stated that if a policy does not meet the criteria they may determine not to accept the policy or ask the borrower to obtain a policy that more closely meets the criteria. Most lenders described

[43]For example, the 2009 questions and answers state that when force placing a policy, regulated lending institutions may not rely on a private insurance policy that does not meet the criteria set forth by FEMA on an ongoing basis. Force-placed insurance, also known as "lender-placed" or "creditor-placed" insurance, is an insurance policy purchased by a mortgage lender or servicer on a home to ensure continuous coverage when the borrower's homeowners or flood insurance lapses or otherwise becomes inadequate. GAO, *Lender-Placed Insurance: More Robust Data Could Improve Oversight*, GAO-15-631 (Washington, D.C.: Sept. 8, 2015).

[44]Joint notice of proposed rulemaking, 78 Fed. Reg. 65,108, 65,110 (Oct. 30, 2013); "Interagency Statement on the Impact of Biggert-Waters Act," CA 13-2 (Federal Reserve), FIL 14-2013 (FDIC), Bulletin 2013-10 (OCC), 13-RA-03 (NCUA), Informational Memorandum (FCA) (Mar. 29, 2013).

[45]78 Fed. Reg. at 65,114 (Oct. 30, 2013).

currently having procedures for evaluating a private flood insurance policy that generally require greater judgement and resources than required when the borrower presents an NFIP policy. For example, half of the lenders stated that procedures for assessing a private flood insurance policy generally include obtaining the entire policy and evaluating it against the FEMA Guidelines. In contrast, one lender stated that the company only obtains the NFIP policy declaration page. A representative of another lender said the company has specialists to conduct reviews of private flood insurance policies and a centralized flood insurance function that reviews NFIP policies.

Finally, according to most of the lenders with whom we spoke, they deal with a relatively small number of private policies. For example, while most of the lenders did not specifically track data on the use of private flood insurance, six of the eight lenders roughly estimated that less than 5 percent of the residential mortgages in their portfolios that require flood insurance were insured by a private policy. While stakeholders with whom we spoke did not have data on the use of private flood insurance, they generally agreed that most private flood insurance written is in the surplus lines market for commercial properties or for coverage in excess of what NFIP offers.[46] We were not able to identify any currently available information on the amount of flood insurance written by admitted carriers. According to NAIC officials, NAIC has begun to collect information on private flood insurance from various associations to inform state insurance regulators of the current interest and activity in the private market for flood insurance. NAIC also has been developing a requirement for insurance companies to include a line item in their annual financial statements that highlights their private flood insurance activity.

[46]One trade association estimates that in 2014 total surplus lines flood insurance premiums (commercial and residential) in six states that collect such data (California, Florida, Mississippi, New York, Texas, and Utah), were $126.6 million. Of this total, they estimate that 8 percent ($9.9 million) was in primary residential, and 59 percent ($74.4 million) was in primary commercial. In the same year, NFIP total residential and commercial premiums were $3.5 billion.

Lenders Told Us They Send Notifications to Borrowers That Include Language Encouraging Comparison of NFIP and Private Insurance

According to all of the lenders we interviewed, their notices to borrowers include language that encourages the comparison of NFIP and private insurance policies. More specifically, they said they use sample language provided in the final rule that implemented Biggert-Waters Act changes to the notification requirement, or something generally similar. (The statutory requirements and the sample language are described in more detail below.)

All of the lenders with whom we spoke also stated that other than providing the required notice to borrowers, they generally did not communicate with borrowers about flood insurance, either private or NFIP. A few lenders stated that borrowers likely make insurance decisions with their insurance agent.

As noted previously, the Biggert-Waters Act amended the notification requirement in the 1994 Act to revise and add information pertaining to private flood insurance.[47] The Biggert-Waters Act requires that regulated lending institutions disclose to a borrower that

- flood insurance is available from private insurance companies that issue standard flood insurance policies on behalf of NFIP or directly from NFIP;
- flood insurance that provides the same level of coverage as a standard flood insurance policy under NFIP may be available from a private insurance company that issues policies on behalf of the company; and
- the borrower is encouraged to compare the flood insurance coverage, deductibles, exclusions, conditions, and premiums associated with flood insurance policies issued on behalf of NFIP and policies issued on behalf of private insurance companies and to direct inquiries on the availability, cost, and comparisons of flood insurance coverage to an insurance agent.

In July 2015, the federal regulators issued a final rule that provides that the revised and additional disclosures be included in the notification to

[47]Pub. L. No. 112-141, § 100239(a)(4), 126 Stat. 916, 958 (2012) (codified as amended at 42 U.S.C. § 4012a(b)(6)).

borrowers.[48] The regulators also amended an existing sample form (Sample Form of Notice of Special Flood Hazards and Availability of Federal Disaster Relief Assistance) with language to reflect the additional disclosures (see app. III). Since the sample form was first provided in 1996, regulations have provided that a regulated lending institution will be considered in compliance with the notice requirement if the regulated lending institution provides a written notice to the borrower containing the language found in the sample form (within a reasonable time before the completion of the transaction).

Federal Regulators Have Jointly Implemented Flood Insurance Regulations

Our review of the regulations issued to implement the various flood insurance statutes found that since the passage of the 1994 Act, as amended, the federal regulators have issued joint regulations implementing most of the statutory requirements.

Most recently, in July 2015 the regulators issued final rules implementing numerous provisions of the Biggert-Waters Act and the Homeowner Flood Insurance Affordability Act of 2014 (HFIAA) related to the escrow of flood insurance payments on residential properties, exemptions from the mandatory purchase requirement, and, as stated earlier, revised disclosures in the notification to borrowers, among other provisions.[49] The regulators did not implement the Biggert-Waters Act provision requiring the acceptance of private flood insurance, as defined by the act.

The federal regulators in our review—FDIC, Federal Reserve, NCUA, OCC, and FCA—also have developed consistent examination guidance for regulated lending institutions' activities related to flood insurance. All five of the federal regulators currently responsible for lending regulation use risk-based examinations in their oversight of their institutions. When examining institutions, each has procedures for reviewing a regulated lending institution's compliance with the requirements of the National

[48]80 Fed. Reg. 43,216 (July 21, 2015). Some portions of the final rule became effective on October 1, 2015, and the rest on January 1, 2016.

[49]80 Fed. Reg. 43,216 (July 21, 2015). HFIAA amended some of the changes mandated by the Biggert-Waters Act, but did not revise the private flood insurance requirements. See Pub. L. No. 113-89, 128 Stat. 1020 (2014).

Flood Insurance Act, as amended.[50] To assist examiners in executing these examinations, each federal regulator has developed a general examination manual that details examination policies and procedures as well as flood insurance examination procedures that were developed on an interagency basis under the direction of the Federal Financial Institutions Examination Council.[51] According to federal regulators' examination guidance, an examination team is to review a regulated lending institution's policies, procedures, and controls for ensuring compliance with the flood insurance requirements. Two federal regulators stated and the other three regulators' examination guidance states that examiners generally review a sample of loans to determine compliance with regulatory requirements, potentially including flood insurance requirements.

We reviewed the examination manuals and flood insurance modules or checklists for each of the federal regulators and found that the relevant flood insurance portions of each manual were substantially similar and addressed the flood insurance-related requirements for the regulated lending institutions.[52] For example, all five regulators' modules or checklists include, reviewing loan documentation to ensure that a flood zone determination was made, notices were provided to the borrower and servicer, premiums were properly escrowed, and the property was covered by an insurance policy in the appropriate amount. Based on our review, the flood insurance examination procedures did not differentiate between private flood insurance policies and NFIP policies. The focus of the manuals was to assist examiners in assessing regulated lending

[50]For every examination, examiners are required to determine whether the regulated lending institution is complying with the federal flood insurance statutes. 12 U.S.C. §§ 1784(e), 1820(d), (i), 2254(a).

[51]According to FCA officials, while FCA is not a member of, or subject to the direction of, the Federal Financial Institutions Examination Council, FCA does look to it for guidance on matters involving flood insurance.

[52]We reviewed regulators' examination procedures, available as of May 2016. In April 2016, the Federal Financial Institutions Examination Council approved revised examination procedures for FDPA. The procedures reflect the July 2015 interagency rulemaking addressing force placement of flood insurance, escrow of flood insurance premiums and fees, and the exemption to the mandatory purchase of flood insurance requirement for certain detached structures. As of May 2016, the Federal Reserve and FDIC had updated their individual examination procedures to reflect the new procedures. Officials from NCUA, OCC, and FCA stated they were in the process of doing so.

institutions' compliance with flood insurance requirements, including notice and mandatory purchase of flood insurance.

Regulatory Uncertainty, Certain NFIP Changes, and Market Challenges Cited as Potentially Inhibiting Use of Private Flood Insurance

Stakeholders cited regulatory uncertainty, such as the lack of final implementing regulations and the scope of the definition of private flood insurance in the Biggert-Waters Act, as some of the potential barriers lenders may face in fulfilling their responsibilities regarding private flood insurance and the mandatory purchase requirement. Stakeholders also cited recent changes made by FEMA to certain NFIP policies as potential barriers to consumers' use of private flood insurance. Finally, stakeholders identified certain market challenges as barriers to increased use of private insurance. Congress has been considering legislation to address some of the concerns raised by stakeholders and some states have enacted legislation to make private flood insurance more accessible.

Lack of Final Regulations and Scope of Statutory Definition of Private Flood Insurance Cited by Stakeholders as Potential Barriers for Lenders

Stakeholders cited the lack of final implementing regulations, the scope of the Biggert-Waters Act definition of private flood insurance, and limited insurance expertise as potential barriers lenders face to evaluating and accepting private policies in satisfaction of the mandatory purchase requirement. The Biggert-Waters Act requires regulators to issue regulations requiring that regulated lending institutions accept private flood insurance, as defined in the statute, to meet the mandatory purchase requirement; however, regulators have yet to issue the final regulations to make this provision effective.[53]

Lack of final rules. Various stakeholders with whom we spoke cited the lack of final rules as creating regulatory uncertainty among lenders and insurers about the use of private flood insurance to satisfy the mandatory purchase requirement. For example, one association noted that while a law has been passed requiring regulated lending institutions to accept private flood insurance, without final rules implementing this requirement, it is unknown what the regulations will be and how lenders and private insurers will comply. Officials from two lenders also stated that the lack of

[53]Pub. L. No. 112-141, § 100239, 126 Stat. 916, 958 (2012); 78 Fed. Reg. 65,108 (Oct. 30, 2013) (joint notice of proposed rulemaking).

final regulations and the lenders' reliance on FEMA guidance puts them in an uncertain and uncomfortable position, as this guidance has been rescinded and is not current. Furthermore, according to a private insurer with whom we spoke, there is uncertainty about whether private policies that lenders have accepted as satisfying the mandatory purchase requirement, may retroactively be deemed noncompliant if they do not meet the requirements of the new regulations, after they are finalized. This insurer added that the issuance of final rules on the acceptance of and definition of private flood insurance would lead to more clarity. They added that public acceptance and use of private flood insurance also may increase. Finally, a state insurance regulator and federal regulator noted that the lack of final rules has led to uncertainty among lenders about which private policies should be accepted.

Scope of definition and flexibility. Stakeholders we interviewed, as well as many comment letters in response to the regulators' October 2013 proposed rules on private flood insurance, expressed concerns about the scope of the definition of private flood insurance in the Biggert-Waters Act, also discussed later in this section.[54] They also noted the need for regulated lending institutions to retain some discretion when evaluating private flood policies. The Biggert-Waters Act codified the rescinded FEMA criteria (which the regulators and lenders considered as guidance), into law as the definition of private flood insurance. See app. II for a side-by-side comparison of the FEMA criteria and the Biggert-Waters Act definition.

According to some stakeholders, to be compliant with the Biggert-Waters Act provisions, regulated lending institutions only may be able to accept private policies meeting all the criteria in the law. They added that evaluating private policies to meet all elements of the statutory definition would reduce the discretion regulated lending institutions currently have when evaluating and accepting private policies. As discussed previously, some lenders stated that they currently use their judgement in determining whether to accept a private policy even if it does not meet all the criteria but still covers their risk. Furthermore, two lenders stated that, under the Biggert-Waters Act requirement, their evaluation of private policies would focus on compliance with the statutory definition, as

[54]We analyzed 44 comment letters submitted by interested parties on the regulators' October 2013 joint proposed rules, as of May 2016.

opposed to focusing on ensuring the policies met the lender's own risk requirements. These lenders, as well as associations and lenders that submitted comment letters, emphasized the need for regulated lending institutions to have a certain level of flexibility and discretion in evaluating and accepting policies.

Importance of guidance. Comment letters and representatives of banking trade associations with whom we spoke also stated their desire for additional guidance on how to evaluate private flood insurance policies once the final rule is implemented. Some stakeholders want additional guidance because regulated lending institutions could face civil monetary penalties (for noncompliance) for policies that did not meet the statutory criteria.[55] A few lenders we interviewed and comment letters to the proposed rules also noted that additional guidance that clearly states what is required of private flood insurance policies to comply with the Biggert-Waters Act would make lenders more comfortable in reviewing and accepting such policies. Citing a need for clear and comprehensive guidance, several stakeholders urged the federal regulators and FEMA to work together to update and reinstate FEMA's rescinded Guidelines to reflect changes from the Biggert-Waters Act. In addition, in their comment letters, a few stakeholders noted that additional guidance would help promote uniformity across mortgage lenders and the private flood insurance industry.

Lender expertise. Some lenders and other stakeholders from the insurance and banking industries stated their concern about evaluating policies for compliance with one criterion in particular: that private flood insurance provide coverage be "at least as broad as" the coverage NFIP

[55]The National Flood Insurance Act, as amended, provides that any regulated lending institution found to have a pattern or practice of committing certain violations, including violations of regulations (when implemented) requiring the acceptance of private flood insurance, shall be assessed a civil monetary penalty by the appropriate federal entity for lending regulation. Prior to the Biggert-Waters Act, the maximum civil monetary penalty that could be assessed for each violation was $350, with an annual cap of $135,000. The Biggert-Waters Act increased the maximum civil monetary penalty for each violation to $2,000 and eliminated the annual penalty cap. Pub. L. No. 112-141, § 100208, 126 Stat. 916, 919 (2012) (codified as amended at 42 U.S.C. § 4012a(f)).

offers.[56] A lender, two insurers, FEMA officials, and a regulatory official all noted that matching the elements of a private policy to an NFIP policy would be difficult. For example, FEMA officials said that NFIP's policy terms and rates do not reflect prior flood losses and that private insurers likely would not be able to develop their rates without taking prior losses into consideration. Two private insurers told us that in their experience, some lenders find it difficult to compare private policies with NFIP policies. One insurer added that if a lender was not familiar with private flood insurance, the company would need to educate the lender on their policy's coverage and show how it matched that of an NFIP policy. More generally, some lenders and banking associations with whom we spoke, as well as many comment letters on the proposed rule, noted that lenders might not have the expertise to evaluate private flood policies against the statutory criteria. In addition, a FEMA-commissioned study on privatization concluded that an increased use of private insurance would necessitate increased resources on the part of regulated lending institutions to assess whether private policies complied with the mandatory purchase requirement and met their needs.[57]

In their October 2013 proposed rule, the federal regulators acknowledged concerns about the ability of regulated lending institutions to evaluate whether private policies met the statutory definition because some regulated lending institutions lacked the necessary technical expertise. Recognizing that regulating insurance is generally the domain of state regulators, the regulators suggested that the state regulators might be the appropriate parties to determine whether a flood insurance policy met all the criteria in the statutory definition of private flood insurance. Therefore, the proposed rule includes a safe harbor to allow regulated lending institutions to rely on a written determination of the state insurance regulator that a policy issued by a private insurer met the federal statutory definition of private flood insurance.

[56]Specifically, under the Biggert-Waters Act definition, a private flood insurance policy must provide "flood insurance coverage which is at least as broad as the coverage provided under a standard flood insurance policy under the national flood insurance program, including when considering deductibles, exclusions, and conditions offered by the insurer." 42 U.S.C. § 4012a(b)(7)(B).

[57]Federal Emergency Management Agency, *National Flood Insurance Program: Report to Congress on Reinsuring NFIP Insurance Risk and Options for Privatizing the NFIP* (Washington, D.C.: Aug. 13, 2015). This report was compiled pursuant to requirements in the Biggert-Waters Act. Pub. L. No. 112-141, § 100232(a), (c), 126 Stat. 916, 953 (2012).

Concerns about state interpretations. While some comment letters and stakeholders with whom we spoke acknowledged that state insurance regulators have authority and experience in approving and overseeing property/casualty insurance, and can do the same with private flood insurance, some also noted challenges with the proposed safe harbor. Specifically, in their comment letters, NAIC and other stakeholders questioned the authority and ability of state insurance regulators to be solely responsible for interpreting or enforcing federal law generally, and in particular, the federal statutory definition of private flood insurance. Representatives of one state insurance regulator with whom we spoke noted that even with their experience and regulatory structure for approving insurance policies, state regulators would find it challenging to determine if private policies were at least as broad as NFIP policies.

FEMA's report on privatization acknowledges that with greater use of private flood insurance, state insurance regulators would have an increased role and need to become more familiar with how flood insurance is modeled, priced, and managed. The FEMA report also noted that the involvement of different state regulators could result in many different regulatory systems. Some comment letters also raised this concern, and added that varying state laws could result in inconsistencies in states' determinations of acceptable flood insurance policies. Due to the challenges with the statutory definition of private flood insurance described earlier, comment letters from some lenders and banking associations, and a few lenders with whom we spoke, noted the need for an additional option for a safe harbor provision (that is, in addition to the one discussed in the proposed rule), which they could rely on for approving private policies as meeting the statutory criteria. They suggested that insurance companies provide their own written determination that their policy complies with the definition of private flood insurance in the Biggert-Waters Act. One private insurer we interviewed has been asked by lenders to attest in writing that its flood insurance policy meets the requirements in the Biggert-Waters Act.

Recent NFIP Policy Changes May Discourage Consumers' Use of Private Flood Insurance

Stakeholders cited certain changes made by FEMA to NFIP policies on flood insurance, which may affect consumers financially, as potential barriers to consumers' ability or willingness to switch from NFIP and use private flood insurance to satisfy the mandatory purchase requirement.

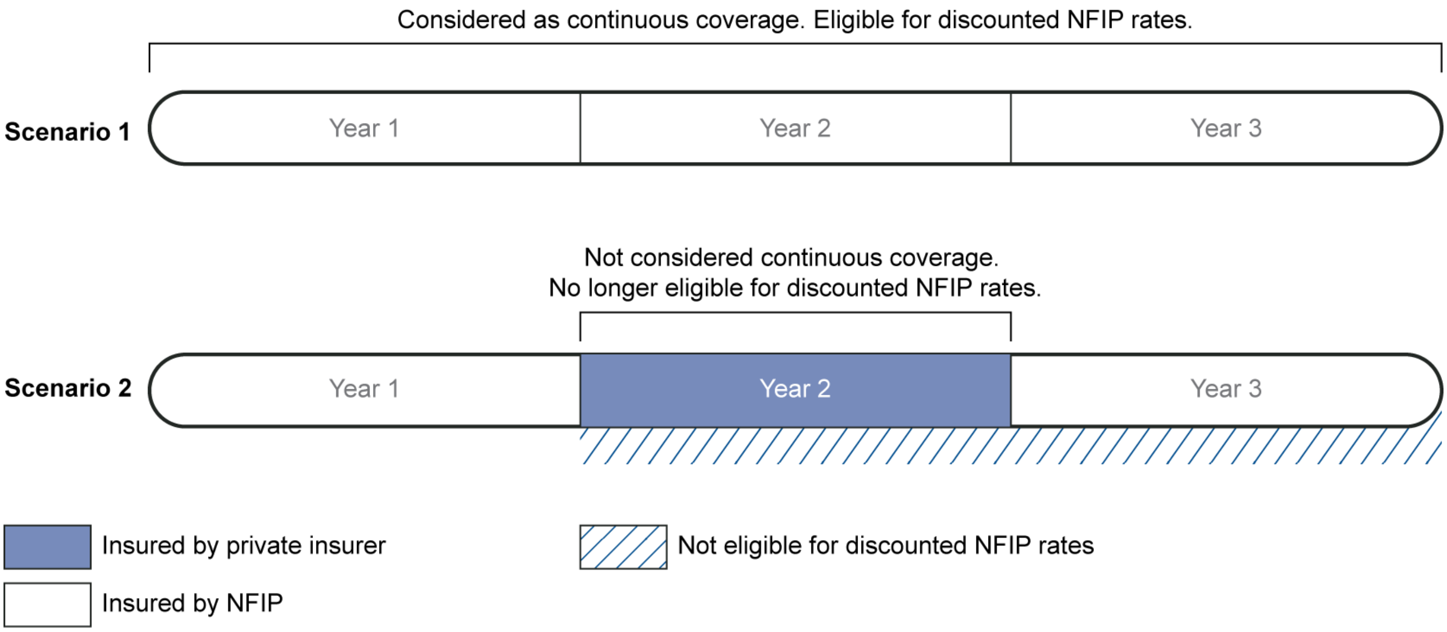
Continuous coverage. NAIC and stakeholders cited FEMA's interpretation of the continuous coverage requirement in connection with private flood insurance and the effect on consumers' ability to qualify for

NFIP discounted rates. Effective April 1, 2016, FEMA prohibits the use of discounted rates (subsidized or “grandfathered” rates) for policies when there has been a lapse in NFIP coverage of more than 90 days (see fig. 2).[58] FEMA officials noted that excluding non-NFIP policies from constituting continuous coverage was due to FEMA’s interpretation of the HFIAA provision on policy lapses.[59]

[58]Effective April 1, 2016, FEMA prohibits the use of discounted rates for policies that reinstate coverage for buildings previously insured by NFIP when the NFIP coverage is reinstated by means of a payment received more than 90 days after expiration or cancellation of the policy. Federal Emergency Management Agency, *NFIP Flood Insurance Manual*, RATE 21 (March 2016). Discounted insurance premiums (rates) include both subsidized and grandfathered policies. Generally, subsidized policies cover properties in high-risk locations that otherwise would have been charged higher premiums and that were built before Flood Insurance Rate Maps became available and their flood risk was clearly understood. Further, NFIP allows other property owners to continue to pay “grandfathered” rates. These rates do not reflect reassessments of properties’ flood risk that occur when the properties are remapped into higher-risk flood zones; instead the policies continue to be classified with other policies from lower-risk zones.

[59]Section 1307(g) of the National Flood Insurance Act, as amended by HFIAA, states, in part, that “[t]he Administrator shall not provide flood insurance to prospective insureds at [subsidized rates]… for any policy under the flood insurance program that has lapsed in coverage, unless the decision of the policy holder to permit a lapse in flood insurance was as a result of the property covered by the policy no longer being required to retain such coverage.” Pub. L. No. 113-89, § 3, 128 Stat. 1020, 1021 (2014) (codified at 42 U.S.C. § 4014(g)).

Figure 2: Example of Effect of NFIP Continuous Coverage Policy on Consumers Who Purchase Private Flood Insurance



Source: GAO analysis of National Flood Insurance Program (NFIP) documentation. | GAO-16-611

Note: Discounted insurance premiums (rates) include both subsidized and grandfathered NFIP policies.

Some stakeholders, including private insurers, noted that FEMA's decision to exclude private flood insurance policies from constituting continuous coverage could have financial repercussions for consumers seeking to reinstate their previously discounted NFIP coverage (after using a private policy to insure their properties from flood losses). So, if a NFIP policyholder who qualified for subsidized rates switched to a private flood policy, and then switched back to an NFIP policy, the policyholder would no longer qualify for subsidized rates and would be charged full-risk rates based on the elevation of the property. A single-family primary residence with $200,000 in building coverage and $50,000 in contents coverage would pay a subsidized premium of $2,880, but their full-risk rate would be based on elevation. For example if this building's elevation was 1 foot below base flood elevation, the full-risk premium would be

$4,650. If it was 2 feet below, the full-risk premium would be $6,890.[60] Two private insurers and an association representing insurers told us that due to the risk of losing their discounted NFIP rates, consumers may avoid the private market as an option to insure against flood losses.

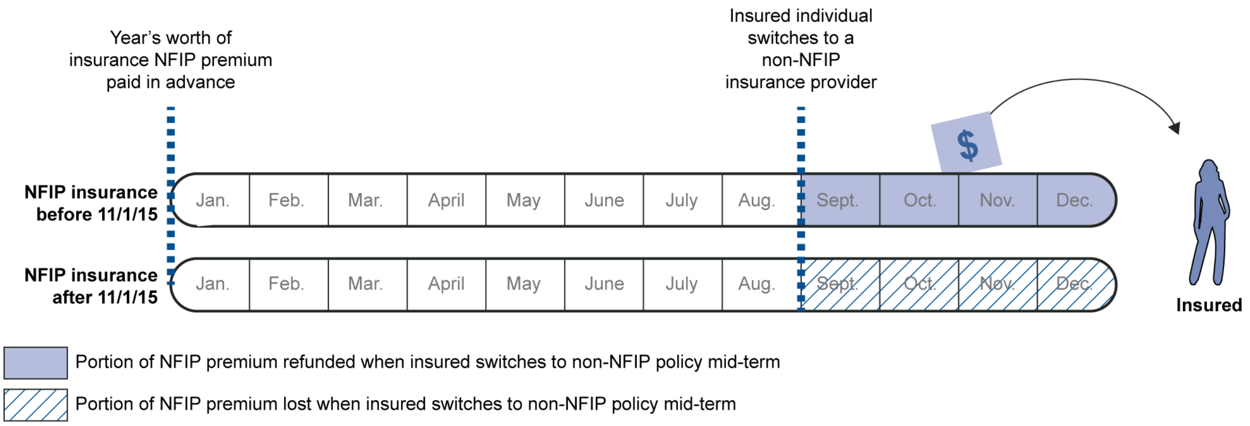
Narrowed opportunities for premium refunds. According to NAIC and the private flood insurance companies with whom we spoke, another recent regulatory change—a FEMA guidance revision related to policy cancellations—could discourage the use of private flood insurance by consumers. FEMA allows NFIP coverage to be terminated in accordance with its stated cancellation reasons. If coverage is terminated for a valid cancellation reason, the insured may be entitled to a full or partial refund of the paid NFIP premium. Effective November 1, 2015, FEMA no longer allows policyholders to cancel their NFIP policy and obtain a refund if they obtained a non-NFIP policy (private flood insurance policy).[61] However, FEMA had allowed for refunds under this scenario previously (see fig. 3). According to NAIC officials, if the reason for cancellation of an insurance policy is the request of the policyholder, the policyholder generally would receive a refund of the paid premium, which may be less than the prorated premium, if stipulated by the insurance policy. Two organizations that represent private insurers also stated that policyholders generally would receive a refund of their paid premium when cancelling a policy after the effective date of the policy. FEMA officials told us that this change came about due to a review of cancellation allowances conducted to incorporate any necessary changes from flood insurance legislation (Biggert-Waters Act and HFIAA). Specifically, FEMA officials said that FEMA only can allow cancellation of policies and refunds according to the terms and conditions of NFIP's Standard Flood Insurance Policy (SFIP). They stated that while the NFIP policy allows for the cancellation of a policy and refund of a premium, on a prorated basis, when a duplicate NFIP policy is obtained on the same property, there is not a similar

[60] If the building was above base elevation, the full-risk premium would be significantly lower than the subsidized premium. We based this example on a single-family primary residence in flood zone AE with no basement or enclosure and no deductible or discounts. See Federal Emergency Management Agency, *NFIP Flood Insurance Manual*, RATING, (April 2016).

[61] Federal Emergency Management Agency, *National Flood Insurance Program: Flood Insurance Manual* (Washington, D.C.: June 2014, revised November 2015). In May 2015, FEMA issued a memorandum to WYOs and NFIP servicing agents stating that the insured obtaining a non-NFIP policy (private flood insurance policy) no longer represented a valid cancellation reason.

provision when a non-NFIP policy is obtained. FEMA did not provide any additional analysis or offer further explanation for this change. However, FEMA could have taken steps to revise the SFIP to allow for such refunds. Allowing this type of refund would be in line with industry practice to allow for refunds of paid premiums as well as Congress's interest in transferring some of the federal government's exposure to flood insurance risk to the private sector.

Figure 3: Comparison of Former and Current Refund Policy for When Policyholders Switch from NFIP to a Non-NFIP Provider



Source: GAO analysis of National Flood Insurance Program (NFIP) documentation. | GAO-16-611

According to most of the private flood insurers with whom we spoke, this change to the cancellation policy further complicates the situation for consumers who wish to opt for private flood insurance when coupled with the requirement that regulated lending institutions establish escrow accounts for flood insurance premiums and fees for loans made after January 1, 2016.[62] Generally, according to some insurers with whom we spoke, lenders will use escrow accounts to pay for flood insurance from 30 to 90 days in advance of the effective date of insurance policies. The combination of factors may present a challenge to consumers because

[62]*See* 42 U.S.C. § 4012a(d); 80 Fed. Reg. 43,216 (July 21, 2015). Prior to the implementation of the escrow requirement from the Biggert-Waters Act and HFIAA, the regulators' escrow provisions provided that each regulated lending institution was required to escrow all premiums and fees for required flood insurance if the institution required the escrow of taxes, insurance premiums, fees, or other charges. Amended regulations implementing the statutory requirements to require regulated lending institutions, or servicers acting on their behalf, to escrow premiums and fees for flood insurance, subject to exception, became effective on December 31, 2015.

they may not know when escrowed payments are made or because of the limited time frame in which they could cancel their NFIP policies to avoid forfeiting their premium, which could result in the following scenarios.

- According to one private insurer, policyholders may not be aware that the bank already renewed their NFIP policy and made the payment from the escrow account. Because FEMA will no longer refund premiums to policyholders who switch to a non-NFIP policy, consumers must cancel their NFIP policy in advance of their NFIP renewal date to avoid forfeiting their premium.

- A representative of another private insurer added that consumers who wish to obtain a private insurance policy must consider making this change well in advance of the NFIP policy effective date (or renewal date) and that generally consumers do not address their insurance needs that far in advance or realize when their insurance has been paid from their escrow account.

Limited Use of Private Flood Insurance Also Due to Market Challenges

Many stakeholders with whom we spoke said that low private-sector participation in the flood insurance market also was due to certain market challenges that presented barriers to the private sector such as NFIP's discounted rates, a topic on which we reported previously and also have ongoing work.[63] For example, in our January 2014 report, we noted that according to stakeholders, insurers needed to be able to charge premium rates that reflect the full risk of potential flood losses, but with NFIP charging rates that were not actuarially sound, private companies found it difficult to compete in the market.[64] Stakeholders with whom we spoke for this report (including insurance trade associations, several state

[63]For GAO-14-127, we hosted a roundtable in August 2013 that included stakeholders from FEMA, the insurance and reinsurance industries, and state insurance regulators.

[64]Actuarial Standards of Practice note that "actuarial soundness" has different meanings in different contexts, and these practices state that if an actuary identifies a process or result as actuarially sound, the actuary should define the meaning of actuarially sound in that context. In referring to NFIP as not actuarially sound, we mean that its aggregate premiums, after providing for program expenses, are not at a sufficient level to cover actuarial estimates of the program's long-term expected losses. For more information on FEMA's methods for setting NFIP rates, see GAO, *NFIP: Continued Progress Needed to Fully Address Prior GAO Recommendations on Rate-Setting Methods*, GAO-16-59 (Washington, D.C.: Mar. 17, 2016). For more information on affordability issues related to NFIP rate increases, see GAO, *NFIP: Options for Providing Affordability Assistance*, GAO-16-190 (Washington, D.C.: Feb. 10, 2016).

insurance regulatory agencies, and another organization with flood insurance expertise) also noted this concern. Several stakeholders, including private insurers, and NAIC emphasized that having to compete with NFIP's discounted rates is one of the primary barriers to increased use of private flood insurance rather than any regulatory issues. Similarly, our review of literature related to the involvement of the private sector in flood insurance found that the ability to charge actuarially sound rates was a strong factor in market participation.[65]

Many stakeholders (including insurance trade associations, a private insurer, and officials from two state regulatory agencies) also noted the lack of access to NFIP data on flood losses and claims as a barrier to more private companies offering flood insurance. Stakeholders added that access to such data would allow private insurance companies to better estimate losses and price flood insurance premiums. In our previous work, stakeholders told us that access to NFIP policy and claims data would help private insurers assess flood risks and determine which properties they might be willing to insure.[66]

However, in our previous report we also noted that according to FEMA officials, the agency would need to address privacy concerns to provide property-level information to insurers, because the Privacy Act prohibits the agency from releasing detailed NFIP policy and claims data. The Privacy Act governs how federal agencies may use the personal information that individuals supply when obtaining government services or fulfilling obligations.[67] FEMA officials said that while the agency could release data in the aggregate, some information could not be provided in detail. For example, FEMA could provide ZIP code-level information to communities but would need to determine how to release property-level information while protecting the privacy of individuals. FEMA officials added that recent data breaches in the federal government's information technology controls have led to additional concerns about the secure

[65]For example, Carolyn Kousky and Leonard Shabnam, "Pricing Flood Insurance: How and Why the NFIP Differs from a Private Insurance Company," *Resources for the Future* (October 2014); and Erwann O. Michel-Kerjan, "Catastrophe Economics: The National Flood Insurance Program," *Journal of Economic Perspectives*, vol. 24, no. 4 (Fall 2010): 165–186.

[66]GAO-14-127.

[67]Pub. L. No. 93-579, 88 Stat. 1896 (1974) (codified, as amended, at 5 U.S.C. § 552a).

storage and sharing of NFIP data. According to NAIC officials, after receiving a request from a state insurance regulator for NFIP data on flood losses and claims in their state, FEMA officials approached NAIC to discuss options for sharing such data. NAIC officials told us that its catastrophe insurance working group is coordinating with FEMA actuaries to determine how FEMA could share specific data with states, without disclosing personally identifiable information.

Our previous work on private-sector involvement in flood insurance also cited other concerns raised by stakeholders.[68] Stakeholders we interviewed for that work noted several conditions that must be present to increase private-sector involvement in the sale of flood insurance, including that insurers need sufficient consumer participation to properly manage and diversify their risk. They also identified several strategies that could help create conditions that would promote the sale of flood insurance by the private sector, such as Congress eliminating discounted rates and NFIP charging full-risk rates, or NFIP providing residual insurance. In addition, we have an ongoing review examining the policy goals that have led to NFIP's debt to Treasury—for example, providing subsidies to certain policyholders—and how the program can be reformed under different circumstances (for example, if there is increased participation in flood insurance by the private sector.)

Finally, some stakeholders also told us that certain FEMA restrictions on WYOs may be an impediment to increasing the availability of private flood insurance in the market. Specifically, the NFIP Financial Assistance/Subsidy Arrangement (Arrangement) with WYOs restricts WYOs from selling stand-alone flood insurance coverage outside of NFIP.[69] Officials from two state insurance agencies and one insurance trade association said that the FEMA restriction limits companies with the most experience in flood insurance from entering the private market. FEMA officials stated that, despite this restriction, a number of companies have found ways to offer flood insurance while remaining compliant with the Arrangement. For example, if a subsidiary of a large insurance

[68] GAO-14-127.

[69] Financial Assistance/Subsidy Arrangement, Art. XIII (Oct. 1, 2015) (codified at 44 C.F.R. pt. 62, app. A). This restriction applies solely to policies providing only flood insurance; WYOs are not restricted from selling flood insurance as part of multiple peril policies or policies that are over and above the limits NFIP allows.

company is a WYO, the parent company could offer stand-alone flood coverage. Alternatively the WYO could offer flood coverage as part of a multiperil policy.

Recent Legislative Proposals to Amend the Biggert-Waters Act and State Actions to Help Increase Accessibility of Private Flood Insurance

Since the passage of the Biggert-Waters Act, new legislation has been introduced in Congress that could help address some of the regulatory issues and a recent change made to NFIP that stakeholders cited as barriers. The proposed legislation would amend the statutory definition of private flood insurance that would satisfy the mandatory purchase requirement.[70] That is, the definition of private flood insurance in the proposed legislation would replace the specific criteria in the Biggert-Waters Act and instead define private flood insurance as an insurance policy that

(1) is issued by an insurance company that is

(I) licensed, admitted, or otherwise approved to engage in the business of insurance in the state in which the insured building is located, by the insurance regulator of that state; or

(II) eligible as a nonadmitted insurer to provide insurance in the home state of the insured;

(2) is issued by an insurance company that is not otherwise disapproved as a surplus lines insurer by the insurance regulator of the state in which the property to be insured is located; and

(3) provides flood insurance coverage that complies with the laws and regulations of that state.

Some stakeholders with whom we spoke supported the proposed legislation because it relies on the expertise of state insurance regulators rather than individual regulated lending institutions. According to these stakeholders, the changes to the statutory definition of private flood insurance clarify that flood insurance approved by state insurance regulators is acceptable in satisfying the mandatory purchase

[70]Flood Insurance Market Parity and Modernization Act, H.R. 2901, 114th Cong. (2015) (as passed by House, Apr. 28, 2016).

requirement. But according to a consumer advocate's January 2016 testimony to Congress, facilitating the sale of flood insurance by surplus lines carriers could create problems for consumers because surplus lines policies are subject to fewer consumer protections than admitted policies. For example, surplus lines policies are not backed by state guaranty funds and states do not regulate surplus lines policy forms, which may contain exclusions that regulators would not approve for an admitted carrier.[71] At the same hearing, NAIC stated its support for the proposed legislation and noted that as the private flood insurance market grew, they expected state insurance regulation would continue to evolve to meet the size of the market as well as the needs of consumers.[72] NAIC officials also told us that the proposed legislation would alleviate their concerns that the Biggert-Waters Act allows federal regulators to regulate the solvency of private flood insurers. However, Fannie Mae officials stated that the proposed legislation (H.R. 2901 as adopted by the House on April 28, 2016) would weaken its risk-management practices to the extent that it would impair Fannie Mae from maintaining or taking prudent actions to protect homeowners and collateral.[73] Furthermore, while noting that creating a viable private flood insurance market is in the interest of the housing finance system and taxpayers, Freddie Mac officials stated that they have concerns that the proposed legislation could shift the risk of

[71]Birny Birnbaum, Executive Director, Center for Economic Justice, *How to Create a More Robust and Private Flood Insurance Market Place*, testimony before the House Subcommittee on Housing and Insurance, Committee on Financial Services, 114th Cong., January 13, 2016.

[72]Teresa D. Miller, Commissioner, Pennsylvania Insurance Department, on behalf of the National Association of Insurance Commissioners, *How to Create a More Robust and Private Flood Insurance Market Place*, testimony before the House Subcommittee on Housing and Insurance, Committee on Financial Services, 114th Cong., January 13, 2016.

[73]Fannie Mae also stated that the legislation could adversely affect existing contractual rights in Uniform Security Instruments. Uniform Security Instruments are Fannie Mae's and Freddie Mac's standard contracts recommended to be used by lenders when originating single-family residential mortgage loans whenever possible, and required for mortgages the GSEs purchase.

flood loss to Freddie Mac; they have been addressing these concerns with the Federal Housing Finance Agency.[74]

The proposed legislation also would amend the flood insurance statute to explicitly allow for private flood insurance coverage to satisfy any continuous coverage requirements, reversing a recent change that FEMA made to NFIP (coverage is not considered continuous if supplied through a non-NFIP policy for more than 90 days). As discussed earlier, some stakeholders cited FEMA's change to this policy as a potential barrier to the use of private insurance. Specifically, the proposed legislation states that any period during which a property was continuously covered by private flood insurance, as defined by the proposed legislation, should be considered to be a period of continuous coverage for purposes of applying any statutory, regulatory, or administrative continuous coverage requirement. However, the proposed legislation does not directly address NFIP's recent change in cancellation reasons, which can preclude refunds of premiums when coverage was supplied by a non-NFIP policy, or the restriction on WYOs offering stand-alone flood insurance products.

Whether a state permits a particular private flood insurance policy to be offered to consumers is a different question from whether the regulated lending institution or federal regulator finds the private policy sufficient to satisfy the mandatory purchase requirement. More specifically, regulated lending institutions and federal regulators, rather than states, are responsible for ensuring compliance with the mandatory purchase requirements under federal law. However, according to the state officials with whom we spoke, states have the authority to regulate the flood insurance offered by private insurance companies in their states and some have taken steps to try to make private flood insurance more accessible.

For example, Florida and West Virginia recently passed legislation that outlines the regulatory structure for insurance companies that choose to sell private flood insurance in those states.[75] Specifically,

[74]The Housing and Economic Recovery Act of 2008 established the Federal Housing Finance Agency (FHFA) as an independent agency to supervise and regulate Fannie Mae, Freddie Mac, and the Federal Home Loan Bank System. FHFA has a statutory responsibility to ensure that Fannie Mae and Freddie Mac operate in a safe and sound manner and that the operations and activities of each regulated entity foster liquid, efficient, competitive, and resilient national housing finance markets. Pub. L. No. 110-289, § 1101, 122 Stat. 2654, 2661 (codified at 12 U.S.C. § 4511).

- Both states allow insurance companies to write flood insurance policies in a more customized way and charge rates in accordance with state laws.[76]

- Both state laws reduce the barriers to accessing the surplus lines market for some flood insurance by not requiring an agent to attempt to place a policy with an admitted company or attempt to find a comparable admitted product.[77] Before the enactment of these laws, the agent would have had to make a “diligent effort” to seek such coverage in the admitted market before placing a flood insurance policy with a surplus lines carrier.

According to officials from both states, these laws were not necessarily needed to allow private insurers to offer flood insurance as officials from both states believed prior statutes permitted the state insurance regulator to allow for flood insurance. However, officials noted that these laws publicly encourage private companies to sell flood insurance in these states, with the intent of offering consumers more options.

Similarly, according to the National Association of Professional Surplus Lines Offices (NAPSLO), 18 states have made private flood insurance more accessible by providing for easier access to the surplus lines insurance market.[78] Furthermore, 12 of these states allow direct access to the surplus lines market with no restrictions for flood, which means that generally an insurance agent would not need to perform a diligent search. According to representatives of NAPSLO, this generally includes not having to first seek coverage with NFIP. NAPSLO officials also stated that

[75]2014 Fla. Laws ch. 80 (codified as amended at FLA. STAT. § 627.715); 2014 W. Va. Acts ch. 96 (codified at W. VA. CODE § 33-49-1 to 33-49-10).

[76]In addition to the legislation passed in 2014, in 2015 Florida passed legislation that amended its statute to (1) allow insurers to issue flood insurance policies on a flexible flood insurance basis, and (2) allow an insurer to request from Florida’s Office of Insurance Regulation a certification that acknowledges that the insurer provides a policy, contract, or endorsement for flood insurance that provides coverage equaling or exceeding the flood coverage offered by the NFIP. 2015 Fla. Laws ch. 69.

[77]West Virginia’s allowance for accessing the surplus lines market directly is restricted to flood coverage of $1 million or more and expires on July 1, 2019. W. Va. Code § 33-49-3(b). The Florida allowance does not contain that restriction, but expires on July 1, 2017. Fla. Stat. § 627.715(4).

[78]According to NAPSLO officials, in the remaining 32 states and the District of Columbia, flood insurance can only be placed with the surplus lines market after the diligent search requirements are met.

the other six states allow for access to the surplus lines insurance market under specific circumstances, such as when a community does not participate in NFIP.

Conclusions

The Biggert-Waters Act took steps to encourage greater participation by the private sector in flood insurance, but aspects of the act's provisions on private flood insurance have created some regulatory uncertainty among insurers and lenders. As a result, Congress has been considering some steps designed to address potential regulatory barriers to the use of private-sector insurance to satisfy the mandatory purchase requirement, including considering legislation that would amend the statutory definition of private flood insurance. The proposed legislation also would explicitly allow for private flood insurance coverage to satisfy any continuous coverage requirements, reversing a recent change that FEMA made to NFIP cited by some stakeholders as a potential barrier to the use of private insurance.

However, a recent policy change made by FEMA might discourage the use of private flood insurance. FEMA no longer allows policyholders to cancel their NFIP policy and obtain a refund, on a prorated basis, if they obtained a non-NFIP policy (private flood insurance policy). FEMA made the change based on a review of its policies brought about by the enactment of the Biggert-Waters Act and HFIAA. FEMA officials stated that FEMA can only allow the cancellation of policies and refunds according to the terms and conditions of NFIP's standard policy, which does not directly address the refunds of premiums when a non-NFIP policy is obtained. However, FEMA could have taken steps to revise the SFIP to allow for such refunds. It is generally industry practice to refund policyholders a portion of premium that is unused if they decide to cancel their insurance policies. Allowing this type of refund would be in line with congressional interest in transferring some of the federal government's exposure to flood insurance risk to the private sector.

Recommendation

To address a potential challenge for consumers who wish to opt for private flood insurance and who must have insurance under the mandatory purchase requirement, we recommend that the FEMA Administrator should consider reinstating the cancellation reason code allowing policyholders to cancel their NFIP policy and be eligible for premium refunds, on a prorated basis, if they obtain a non-NFIP policy after their NFIP policy became effective. If changes are needed to NFIP's standard flood insurance policy to allow such refunds, FEMA should take the necessary steps to amend its standard flood insurance policy.

Agency Comments

We provided a draft of this report to FCA, FDIC, Federal Reserve, FEMA within the Department of Homeland Security, HUD, NCUA, OCC, Treasury, Fannie Mae, Freddie Mac, and NAIC for review and comment.

FCA, FDIC, Federal Reserve, OCC, Fannie Mae, Freddie Mac, and NAIC provided technical comments, which we incorporated, as appropriate. DHS provided a written response, reproduced in appendix IV, in which FEMA agreed with our recommendation and plans to reinstate their previous policy allowing policyholders to cancel their NFIP policy and obtain a prorated refund if they obtain a comparable non-NFIP policy. The response also stated that the policy change will be included in an April 2017 program bulletin, with an effective date of October 1, 2017, and followed up with a subsequent rulemaking. NCUA also provided written comments, reproduced in appendix V, in which agency officials stated that the agency plans to, as noted in the report, update examination policies and procedures to reflect recent changes in flood insurance regulation and work with the other regulators to finalize private flood insurance regulations.

We are sending copies of this report to the appropriate congressional committee, and other interested parties. In addition, the report is available at no charge on the GAO website at http://www.gao.gov.

If you or your staff have any questions about this report, please contact me at (202) 512-8678 or cackleya@gao.gov. Contact points for our Offices of Congressional Relations and Public Affairs may be found on the last page of this report. GAO staff who made key contributions to this report are listed in appendix VI.

Sincerely yours,

Alicia Puente Cackley

Alicia Puente Cackley
Director, Financial Markets
and Community Investment

Appendix I: Objectives, Scope, and Methodology

We were asked to revisit the issue of the private-sector involvement in flood insurance with a focus on the regulatory environment and whether it posed any barriers to private flood insurance policies being purchased by homeowners to satisfy the mandatory purchase requirement. This report describes (1) regulated lending institutions' and federal regulators' implementation of statutory provisions governing the use of private flood insurance to satisfy the mandatory purchase requirement; and (2) views on any regulatory, or other barriers, to the increased use of private flood insurance to satisfy the mandatory purchase requirement. To address these objectives, we reviewed flood insurance laws and regulations, related agency guidance, congressional hearings, and studies, as well as past GAO reports on insurance markets and flood insurance.[1]

Regulator and Lender Implementation

We reviewed relevant federal flood insurance laws, including the Flood Disaster Protection Act, National Flood Insurance Reform Act, Biggert-Waters Flood Insurance Reform Act, and the Homeowner Flood Insurance Affordability Act, to identify requirements placed on federal entities responsible for lending regulation (federal regulators) and how each has addressed the use and acceptability of private flood insurance to fulfill the mandatory purchase requirement. The federal regulators involved in implementing the provisions of the flood insurance laws governing the mandatory purchase requirement are the Office of the Comptroller of the Currency (OCC), Board of Governors of the Federal Reserve System (Federal Reserve), Federal Deposit Insurance Corporation (FDIC), Farm Credit Administration (FCA), and National Credit Union Administration (NCUA). We also reviewed the rules implementing these statutes to determine what requirements are placed on regulated lending institutions.

To understand how lenders have been fulfilling the requirements, we interviewed representatives from eight lending institutions consisting of banks and nonbanks. To identify lenders likely to have experience with private flood insurance, we used National Flood Insurance Program (NFIP) and SNL's Mortgage Market Share data to identify the largest

[1]For example, GAO, *Flood Insurance: Strategies for Increasing Private Sector Involvement*, GAO-14-127 (Washington, D.C.: Jan. 22, 2014); *Insurance Markets: Impacts of and Regulatory Response to the 2007-2009 Financial Crisis*, GAO-13-583 (Washington, D.C.: June 27, 2013); and *Flood Insurance: Extent of Noncompliance with Purchase Requirements Is Unknown*, GAO-02-396 (Washington, D.C.: June 21, 2002).

lenders (by volume of mortgages originated) in those counties with the largest number of NFIP flood insurance policies. To further categorize the lending institutions, we then used criteria such as the type of institution, regulatory agency responsible for supervising the institution, and size by total assets (selecting lenders from large, medium, and small asset categories). We selected a purposive sample of eight lenders with one or two institutions supervised by each regulator and took care to ensure a balanced representation of the different types and sizes of institutions. For the purposes of this report we use the term “lenders” to refer to the eight lenders with whom we spoke. Our sample included two nonbank mortgage lenders that are not directly subject to the requirements of the Flood Disaster Protection Act as they do not fit within the statutory definition of regulated lending institutions. We spoke with these nonbank lenders to better understand practices related to private flood insurance among the full scope of mortgage market participants. This selection of mortgage lenders is not generalizable to all mortgage lenders. We determined that the data used were reliable for the purpose of identifying and selecting mortgage lenders for a nongeneralizable sample.

To better understand how the federal regulators have implemented the statutory requirements, we compared their regulations with the statutes. We also reviewed guidance provided by the federal regulators and the Federal Emergency Management Agency (FEMA) related to the use of private flood insurance to satisfy the mandatory purchase requirement. We reviewed and compared each of the regulator’s examination manuals and flood insurance modules to understand how they examined the regulated lending institutions they supervise for compliance. For example, we reviewed each regulator’s flood insurance examination module to determine what specific aspects of the regulations examiners were reviewing. We also interviewed officials from OCC, Federal Reserve, FDIC, FCA, NCUA, and FEMA. Finally, we reviewed the policies of the Federal National Mortgage Association (Fannie Mae), Federal Home Loan Mortgage Corporation (Freddie Mac), Department of Veterans Affairs, and Federal Housing Administration to understand their flood insurance requirements for mortgages they either purchase or insure. We also followed up with the Department of Housing and Urban Development’s Federal Housing Administration to understand any potential changes to its policies.

Regulatory and Other Barriers

We interviewed various stakeholders—including selected lenders, organizations in the insurance and lending industries, private flood insurance companies, and state insurance regulatory agencies—about any regulatory barriers to the increased use of private flood insurance. We interviewed representatives of the eight selected lenders on barriers they encounter in evaluating and accepting private flood insurance policies and their views on enacted and proposed legislation on private flood insurance. To obtain other views on private flood insurance, we selected a diverse group of 13 organizations to interview based on the type of organization, the organization's purpose and relevance to private flood insurance, and membership. We identified these organizations based on previous and ongoing GAO work on flood insurance and comment letters submitted in response to federal regulators' proposed rules on private flood insurance.

We also selected and interviewed representatives of four private insurance companies involved in the private market for flood insurance. To identify these companies, we reviewed news articles; interviewed selected lenders, state insurance officials, and other industry stakeholders; reviewed comment letters submitted in response to proposed rules issued by the federal regulators on private flood insurance; and reviewed prior GAO work. To select the insurance companies to interview, we focused on those that were identified as currently writing flood insurance in the admitted or nonadmitted insurance markets. This selection of private insurance companies is not generalizable to all private insurance companies.

To understand selected states' regulation of flood insurance and obtain the perspectives of state insurance regulators on regulatory barriers related to private flood insurance, we interviewed insurance regulators and their representatives from Florida, Louisiana, Pennsylvania, Texas, and West Virginia and reviewed selected laws from Florida and West Virginia. We selected these states based on the volume of NFIP policies written and flood insurance regulatory activity in each state. The information provided by the representatives of the state insurance regulators is not generalizable to how all states oversee flood insurance.

We also reviewed comment letters submitted to the regulators (OCC, Federal Reserve, FDIC, FCA, and NCUA) in response to proposed federal rules on the acceptance of private flood insurance. We obtained these comment letters by downloading each from www.regulations.gov, docket ID OCC-2013-0015. We analyzed 44 comment letters submitted by interested parties regarding the regulators' joint proposed rules as of

May 2016.[2] We reviewed each comment letter to identify comments pertaining to potential or actual regulatory barriers to the use of private flood insurance and effects of the proposed rules. One analyst created a summary of common themes from the comment letters, which were verified by a second analyst.

We also conducted a literature search for news articles and studies to determine what is known about any regulatory barriers to using private flood insurance to satisfy the mandatory purchase requirement. To identify news articles and studies, we conducted searches of various databases, such as EconLit and ProQuest, using search terms such as “private” and “flood insurance.” From these searches, we identified and reviewed 19 studies and articles since 2005 that were relevant to barriers to private flood insurance. We reviewed these studies and articles to identify regulatory barriers to the use of private flood insurance. We found that these studies and articles generally did not identify regulatory barriers but identified other relevant barriers related to increasing involvement of the private sector in flood insurance.[3]

We also interviewed representatives from the Department of the Treasury’s Federal Insurance Office and the National Association of Insurance Commissioners (NAIC) to obtain their views on regulatory barriers, enacted and proposed legislation and regulations, and NAIC’s views on states’ laws and regulations related to private flood insurance.

[2]Forty-four comment letters were submitted in response to the October 2013 joint proposed rules; four comment letters contained no comments related to the private insurance provisions of the proposed rule and were excluded from our analysis.

[3]Our previous work on the conditions needed for private-sector involvement in flood insurance and strategies for increasing private-sector involvement addressed some of these other relevant barriers. See GAO-14-127.

Appendix II: Private Flood Insurance Criteria in FEMA's Guidelines (2007) and the Biggert-Waters Act Definition (2012)

The following table compares the guidance provided by Federal Emergency Management Agency (FEMA) in the 2007 Mandatory Purchase of Flood Insurance Guidelines (rescinded in February 2013) for use of private flood insurance to satisfy the mandatory purchase requirement with the statutory definition of private flood insurance in the Biggert-Waters Flood Insurance Reform Act of 2012 (Biggert-Waters Act).

Table 3: Private Flood Insurance Criteria in FEMA Guidelines and the Biggert-Waters Act

Policy areas	FEMA guidelines	Biggert-Waters Act definition
	The Guidelines state a private flood insurance policy that meets all six of the FEMA criteria conforms to the mandatory flood insurance purchase requirements of the 1994 Act. The Guidelines further provide that to the extent that the private policy differs from the NFIP standard flood insurance policy, the differences should be carefully examined before the policy is accepted as sufficient protection under the law.	The term "private flood insurance" means an insurance policy that:
Licensure	The insurer must be licensed, admitted, or otherwise approved to do business in the jurisdiction where the building is located, by the insurance regulator of that jurisdiction, except for surplus lines recognition, below.	Is issued by an insurance company that is licensed, admitted, or otherwise approved to engage in the business of insurance in the state or jurisdiction in which the insured building is located, by the insurance regulator of that state or jurisdiction, or surplus lines recognition, below.
Surplus lines recognition	In the case of nonresidential commercial property insurance issued under a policy of difference in conditions, multiple peril, all risk, or other blanket coverage, the insurer should be recognized, or not disapproved, as a surplus lines insurer by the insurance regulator of the jurisdiction where the building is located.	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.
Requirement of 45-day cancellation/nonrenewal notice	The policy should include a requirement for the insurer to give 45 days' written notice of cancellation or nonrenewal to the insured with respect to the flood insurance coverage. The policy should also state that to be effective, such notice must be mailed to both the insured and the lender or federal agency lender, and must include information about the availability of NFIP flood insurance. The policy should be as restrictive in its cancellation provisions as the NFIP standard policy.	Includes a requirement for the insurer to give 45 days' written notice of cancellation or nonrenewal of flood insurance coverage to the insured and the regulated lending institution or federal agency lender. Includes information about the availability of flood insurance coverage under NFIP. Contains cancellation provisions that are as restrictive as the provisions contained in a standard flood insurance policy under NFIP.

Policy areas	FEMA guidelines	Biggert-Waters Act definition
Breadth of policy coverage	The policy must guarantee that the flood insurance coverage, considering deductibles, exclusions, and conditions offered by the insurer, is at least as broad as the coverage under the NFIP standard flood insurance policy.	Provides flood insurance coverage that is at least as broad as the coverage provided under a standard flood insurance policy under NFIP, including when considering deductibles, exclusions, and conditions offered by the insurer.
Strength of mortgage interest clause	Lenders must ensure that the private policy contains a mortgage interest clause similar to that contained in the general conditions section of the NFIP standard flood insurance policy.	Includes a mortgage interest clause similar to the clause contained in a standard flood insurance policy under NFIP.
Legal recourse	The policy must contain a provision that the insured must file suit within 1 year after the date of written denial of all or part of the claim.	Includes a provision requiring an insured to file suit not later than 1 year after date of a written denial of all or part of a claim under the policy.

Legend:

1994 Act – National Flood Insurance Reform Act of 1994

Biggert- Waters Act – Biggert-Waters Flood Insurance Reform Act of 2012

FEMA – Federal Emergency Management Agency

NFIP – National Flood Insurance Program

Source: FEMA and Biggert-Waters Act, Pub. L. No. 112-141, § 100239(a)(4), 126 Stat. 916, 960 (codified at 42 U.S.C. § 4012a(b)(7)). | GAO-16-611

Appendix III: Sample Form of Notice of Special Flood Hazards and Availability of Federal Disaster Relief Assistance

The following sample notice is included as an appendix in the regulators' respective flood insurance regulations.[1]

Figure 4: Sample Form of Notice of Special Flood Hazards and Availability of Federal Disaster Relief Assistance

Notice of Special Flood Hazards and Availability of Federal Disaster Relief Assistance

We are giving you this notice to inform you that:

The building or mobile home securing the loan for which you have applied is or will be located in an area with special flood hazards.

The area has been identified by the Administrator of the Federal Emergency Management Agency (FEMA) as a special flood hazard area using FEMA's *Flood Insurance Rate Map* or the *Flood Hazard Boundary Map* for the following community: ____________. This area has a one percent (1%) chance of a flood equal to or exceeding the base flood elevation (a 100-year flood) in any given year. During the life of a 30-year mortgage loan, the risk of a 100-year flood in a special flood hazard area is 26 percent (26%).

Federal law allows a lender and borrower jointly to request the Administrator of FEMA to review the determination of whether the property securing the loan is located in a special flood hazard area. If you would like to make such a request, please contact us for further information.

The community in which the property securing the loan is located participates in the National Flood Insurance Program (NFIP). Federal law will not allow us to make you the loan that you have applied for if you do not purchase flood insurance. The flood insurance must be maintained for the life of the loan. If you fail to purchase or renew flood insurance on the property, Federal law authorizes and requires us to purchase the flood insurance for you at your expense.

- At a minimum, flood insurance purchased must cover *the lesser of*:
  (1) the outstanding principal balance of the loan; *or*
  (2) the maximum amount of coverage allowed for the type of property under the NFIP.
  Flood insurance coverage under the NFIP is limited to the building or mobile home and any personal property that secures your loan and not the land itself.
- Federal disaster relief assistance (usually in the form of a low-interest loan) may be available for damages incurred in excess of your flood insurance if your community's participation in the NFIP is in accordance with NFIP requirements.
- Although you may not be required to maintain flood insurance on all structures, you may still wish to do so, and your mortgage lender may still require you to do so to protect the collateral securing the mortgage. If you choose not to maintain flood insurance on a structure and it floods, you are responsible for all flood losses relating to that structure.

Availability of Private Flood Insurance
Flood insurance coverage under the NFIP may be purchased through an insurance agent who will obtain the policy either directly through the NFIP or through an insurance company that participates in the NFIP. Flood insurance that provides the same level of coverage as a standard flood insurance policy under the NFIP may be available from private insurers that do not participate in the NFIP. You should compare the flood insurance coverage, deductibles, exclusions, conditions, and premiums associated with flood insurance policies issued on behalf of the NFIP and policies issued on behalf of private insurance companies and contact an insurance agent as to the availability, cost, and comparisons of flood insurance coverage.
[Escrow Requirement for Residential Loans: Federal law may require a lender or its servicer to escrow all premiums and fees for flood insurance that covers any residential building or mobile home securing a loan that is located in an area with special flood hazards. If your lender notifies you that an escrow account is required for your loan, then you must pay your flood insurance premiums and fees to the lender or its servicer with the same frequency as you make loan payments for the duration of your loan. These premiums and fees will be deposited in the escrow account, which will be used to pay the flood insurance provider.]

Flood insurance coverage under the NFIP is not available for the property securing the loan because the community in which the property is located does not participate in the NFIP. In addition, if the non-participating community has been identified for at least one year as containing a special flood hazard area, properties located in the community will not be eligible for Federal disaster relief assistance in the event of a Federally-declared flood disaster.

Source: 12 C.F.R. pt. 22, app. A (OCC); 12 C.F.R. § 208.25, app. A (Federal Reserve); 12 C.F.R. pt. 339, app. A (FDIC); 12 C.F.R. pt. 614, subpt. S, app. A (FCA); 12 C.F.R. pt. 760, app. A (NCUA). | GAO-16-611

[1] 12 C.F.R. pt. 22, app. A (OCC); 12 C.F.R. § 208.25, app. A (Federal Reserve); 12 C.F.R. pt. 339, app. A (FDIC); 12 C.F.R. pt. 614, subpt. S, app. A (FCA); 12 C.F.R. pt. 760, app. A (NCUA).

Appendix IV: Comments from the Department of Homeland Security

U.S. Department of Homeland Security
Washington, DC 20528

Homeland Security

July 7, 2016

Alicia Puente Cackley
Director, Financial Markets and Community Investment
U.S. Government Accountability Office
441 G Street, NW
Washington, DC 20548

Re: Management's Response to Draft Report GAO-16-611, "FLOOD INSURANCE: Potential Barriers Cited to Increased Use of Private Insurance"

Dear Ms. Cackley:

Thank you for the opportunity to comment on this draft report. The U.S. Department of Homeland Security (DHS) appreciates the U.S. Government Accountability Office's (GAO) work in planning and conducting its review and issuing this report.

The Department is pleased to note GAO's positive recognition of the actions lenders, regulators, and the Federal Emergency Management Agency (FEMA) have taken to implement provisions of the Flood Insurance Reform Act of 2012 (Biggert-Waters Act). Many provisions of the Biggert-Waters Act and subsequent follow-on legislation have already been implemented and others are still being implemented. FEMA is committed to ensuring that barriers to insurance are minimized and that flood insurance is accessible to protect homeowners and others.

It is also important to note that while FEMA actively works to implement new flood-related laws, FEMA encourages policy holders to maintain and keep current flood insurance policies. FEMA does NOT recommend cancelling a flood insurance policy. Cancelling flood insurance policies can leave policy holders unprotected during flooding and may cause policy holders to lose important discounts on their rate if they reinstate in the future.

Thank you for the opportunity to comment on this draft report. Technical comments were previously provided under separate cover. Please feel free to contact me if you have any questions. We look forward to working with you in the future.

Sincerely,

Jim H. Crumpacker, CIA, CFE
Director
Departmental GAO-OIG Liaison Office

Attachment: DHS Management Response to Recommendation Contained in GAO-16-611

GAO recommended that the FEMA Administrator:

Recommendation 1: Consider reinstating the cancellation reason code allowing policyholders to cancel their NFIP [National Flood Insurance Policy] policy and be eligible for premium refunds, on a pro-rated basis, if they obtain a non-NFIP's SFIP [Standard Flood Insurance Policy] to allow such refunds, then FEMA should take the necessary steps to amend the SFIP.

Response: Concur. Article VII, Paragraph U of the SFIP provides that a policyholder cannot be insured under more than one NFIP policy at the same time, requires the cancellation of one of the policies, and authorizes a refund of the cancelled NFIP policy. GAO's recommendation to reinstate the cancellation reason code when a comparable non-NFIP (private) insurance policy is obtained with a pro-rated premium refund aligns with the intent of Paragraph U.

FEMA has already considered reinstating this cancellation code and will be reinstating the policy and following it up with a subsequent rulemaking. The policy change will be included in the April 2017 bulletin sent to Write Your Own (WYO) companies, announcing NFIP changes that will be effective as of October 1, 2017. Estimated Completion Date: September 30, 2017.

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Appendix V: Comments from the National Credit Union Administration

National Credit Union Administration
Office of the Executive Director

June 27, 2016

SENT BY E-MAIL

Alicia Puente Cackley
Director, Financial Markets and Community Investment
U.S. Government Accountability Office
441 G Street, NW
Washington, DC 20548
cackleya@gao.gov

Dear Director Cackley:

We have reviewed the GAO's draft report entitled *Flood Insurance: Potential Barriers Cited to Increased Use of Private Insurance* (GAO-16-611). As noted in the report, NCUA is updating our examination policies and procedures to reflect recent changes to the flood insurance regulation. Our staff is also working with the other regulators to finalize regulations regarding private flood insurance.

Thank you for the opportunity to comment.

Sincerely,

Mark Treichel
Executive Director

1775 Duke Street – Alexandria, VA 22314-3428 – 703-518-6320

Appendix VI: GAO Contact and Staff Acknowledgments

GAO Contact

Alicia Puente Cackley, (202) 512-8678 or at cackleya@gao.gov

Staff Acknowledgments

In addition to the contact named above, Allison Abrams (Assistant Director), Anar Jessani (Analyst-in-Charge), Pamela Davidson, Matthew Keeler, Marc Molino, Patricia Moye, and Barbara Roesmann made key contributions to this report.

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