

Compliance Insights

Your monthly compliance news roundup

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Agencies Release Final Rule on Private Flood Insurance Policies

On January 25, 2019, the financial regulatory agencies released a **final rule** governing the acceptance of private flood insurance policies. This final rule, which will become effective on July 1, 2019, implements section 100239 of the Biggert-Waters Flood Insurance Reform Act of 2012 (Biggert Waters Act), which mandates that federally regulated lending institutions accept private flood insurance policies to satisfy mandatory flood insurance purchase requirements if the policy meets certain criteria. Under the current regulation, institutions are permitted to accept private flood insurance policies that meet certain requirements established by the Federal Emergency Management Agency (FEMA) but are not required to do so.

The final rule establishes the minimum criteria that a private flood insurance policy must meet to satisfy the mandatory flood insurance purchase requirement; these include the following:

- Be issued by an insurance company that is approved to engage in the business of insurance by the insurance regulator of the State or jurisdiction where the property is located and be recognized as a surplus lines insurer by that same regulator under certain circumstances;
- Provide flood insurance coverage that is at least as broad as the coverage provided by a standard flood insurance policy (SFIP) issued under the National Flood Insurance Program (NFIP), the minimum standards for which are provided within the regulation;
- Include policy provisions that require the insurer to provide written notice 45 days before cancellation or non-renewal to the insured and the financial institution, a mortgage interest clause similar to the SFIP, a provision restricting the insured from

filing suit not later than one year after the denial of a claim, as well as information about the availability of flood insurance coverage under the NFIP; and

- Cancellation provisions that are as restrictive as the provisions contained in an SFIP.

In addition to defining private flood insurance, the final rule establishes standards for when a private flood insurance policy must be accepted as well as standards for when a policy issued by a private insurer may be accepted at the discretion of the institution.

A financial institution is required to accept a private flood insurance policy in satisfaction of the mandatory flood insurance purchase requirement if the policy meets the definition of a private flood insurance policy set forth in the regulation. The final rule also provides a “compliance aid” or streamlined approach to assist financial institutions in determining whether a policy meets the minimum criteria. If a private flood insurance policy contains the statement, “This policy meets the definition of private flood insurance contained in 42 U.S.C. 4012a(b)(7) and the corresponding regulation,” then an institution may rely on this compliance aid statement alone in order to accept the policy. However, it is important to note that the absence of the phrase cannot be relied upon for non-acceptance of a policy that otherwise meets the statutory definition of “private flood insurance.”

In addition to the mandatory acceptance requirement, the final rule establishes a discretionary acceptance standard which, if met, permits but does not require acceptance of a flood insurance policy. The minimum criteria for discretionary acceptance are as follows:

- The policy must provide coverage in the amount required by the flood insurance purchase requirement;
- The policy must be issued by an insurer that meets the aforementioned standards for issuing a private flood insurance policy;
- The policy must cover both the mortgagors(s) and the mortgagee(s) as loss payees, except in the case of a policy that is provided by a condominium association, cooperative, homeowners association or other applicable group, and for which the premium is paid by the group as a common expense; and
- The policy must provide sufficient protection of the designated loan consistent with general safety and soundness principles, and the regulated institution must document its conclusion regarding sufficiency of the protection of the loan in writing.

If a policy meets all four of these criteria, an institution may accept the policy in satisfaction of the flood insurance purchase requirement.

The final rule also provides for the discretionary acceptance of plans provided by mutual aid societies (such as Amish communities) to satisfy the mandatory flood insurance purchase requirement. A mutual aid society is defined as an organization that meets three criteria: (1) The members must share a common religious, charitable, educational or fraternal bond; (2) the organization must cover losses caused by damage to members' property pursuant to an agreement, including damage caused by flooding, in accordance with this common bond; and (3) the organization must have a demonstrated history of fulfilling the terms of agreements to cover losses to members' property caused by flooding. Below are the criteria that must be considered for acceptance:

- The institution's primary federal supervisory agency has determined that such plans qualify as flood insurance;
- The plan must provide coverage in the amount required by the flood insurance purchase requirement;
- The plan must cover both the mortgagor(s) and the mortgagee(s) as loss payees; and
- The plan must provide sufficient protection of the designated loan, consistent with general safety and soundness principles, and the institution must document its conclusion regarding sufficiency in writing.

As financial institutions plan for implementing the final rule into their business practices, they should consider what processes and controls need to be developed to properly evaluate whether a flood insurance policy issued by a private insurer meets the regulatory standards for acceptance. The level of effort and time period necessary to make such a determination should also be considered carefully and may impact the extent to which an institution chooses to rely on the compliance aid statement and the discretionary acceptance standard. An additional factor to be considered is the relative risk of accepting an impermissible private flood insurance policy versus rejecting a private flood insurance policy that, in fact, meets the regulatory standard. The credit risk associated with the loss of collateral should also be incorporated into the overall analysis.

EU Money Laundering Blacklist Evokes Strong Reaction

On February 13, 2019, the European Commission (the Commission) adopted a [provisional list](#) of 23 non-European jurisdictions, identified as having strategic deficiencies in their anti-money laundering (AML) and countering the financing of terrorism (CFT) frameworks. The list was established pursuant to the European Union's (EU) Fourth and Fifth Anti-Money Laundering Directives, which require that the Commission identify high-risk third countries in order to protect the EU financial system. However, in late February 2019, the provisional list of high-risk third countries was rejected by 27 of the 28 EU member states, which will now require the Commission to re-evaluate its list and the methodology for deriving it.

The new list of high-risk third countries adopted by the Commission included 12 countries also identified by the Financial Action Task Force (FATF) as being high-risk jurisdictions. The Commission considers jurisdictions on the FATF high-risk list as a starting point when developing its list of high-risk third countries. The Commission also added 11 additional jurisdictions to its list of high-risk third countries which it identified according to its own [methodology](#). These 11 additional jurisdictions included four U.S. territories (American Samoa, Guam, Puerto Rico and the U.S. Virgin Islands) as well as Saudi Arabia. The inclusion of a jurisdiction on the Commission's high-risk third country list would mean an enhanced level of scrutiny over transactions associated with such jurisdictions and the financial institutions located there.

The updates to the Commission's high-risk third country list evoked strong reactions from many of the countries that appear on the list – in particular, the United States. The U.S. Treasury Department [stated](#) that the method for creating the blacklist was flawed and specifically criticized the inclusion of the four U.S. territories. The Treasury Department also emphasized that the FATF is the organization primarily responsible for setting global AML standards and suggested that the Commission's list could undermine the FATF's central role in the AML/CFT regulatory landscape. The Treasury Department stated that it did not expect U.S. financial institutions to take the updated list into account in their AML/CFT policies and procedures.

Since the provisional list was rejected by the EU member states, the Commission's existing list of high-risk third countries will remain in effect and financial institutions will have no new obligations with respect to the new jurisdictions included within the provisional list. However, financial institutions should continue to monitor the activities of the European Commission for an updated high-risk third country list in the future.

CFPB Proposes to Rescind Provisions of Payday Lending Rule

On February 6, 2019, the CFPB [announced](#) a proposed rule to rescind certain provisions of the [2017 Payday Lending Rule](#). The provisions the CFPB proposes to rescind are the mandatory underwriting provisions that require lenders to make specific underwriting decisions before issuing certain high-cost installment, single-payment vehicle title and payday loans. The CFPB's proposal suggests there was insufficient evidence and legal support for these provisions. While the 2017 final rule is scheduled to go into effect on August 19, 2019, the CFPB issued an additional [proposed rule](#) on February 6, 2019, which would delay the mandatory compliance date for the underwriting provisions it proposes to eliminate. We will keep you informed of further developments related to the rule in future issues of *Compliance Insights*.

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