FEMA IMPLEMENTS RISK RATING 2.0

FEMA is updating the National Flood Insurance Program's ("NFIP") risk rating algorithms through the implementation of a new premium pricing methodology called Risk Rating 2.0. The methodology leverages industry best practices and technology to enable FEMA to deliver rates that are actuarily sound and equitable to better reflect a property's flood risk.

FEMA's Risk Rating 2.0 is being implemented in two phases:

Phase I

New **policies beginning October 1, 2021**, will be subject to the new rating methodology. Also beginning October 1, existing policyholders eligible for renewal and subject to lower premiums based on Risk Rating 2.0 will be able to take advantage of immediate decreases in their premiums.

Phase 2

All remaining policies **renewing on or after April 1, 2022**, will be subject to the new rating methodology.

Why FEMA is Undertaking Risk Rating 2.0

- Since the 1970s, rates have been predominantly based on relatively static measurements, emphasizing a property's elevation within a zone on a Flood Insurance Rate Map ("FIRM").
- The historical approach does not incorporate as many flood behavior variables as Risk Rating 2.0. Risk Rating 2.0 enables FEMA to set rates that are actuarially and intuitively fairer, plus ensures rate increases and decreases are both equitable. For example, with Risk Rating 2.0, FEMA now has the capability and tools to address rating disparities by incorporating more flood risk variables such as flood frequency, multiple flood types—river overflow, storm surge, coastal erosion, heavy rainfall—and distance to water source along with property characteristics such as elevation and the cost to rebuild.
- Currently, policy holders with lower-valued homes are typically paying more than their share of the risk while policyholders with higher-valued homes are paying less than their fair share of the risk. Because Risk Rating 2.0 considers current rebuilding costs, FEMA can better spread premium rates across all policyholders based on home value and a property's unique flood risk.

What's Not Changing Under Risk Rating 2.0

- Annual Premium Increases: Existing statutory limits on rate increase require that most rates not increase more than 18% per year. That remains in place.
- Using Flood Insurance Rate Maps (FIRMs) for Mandatory Purchase and Floodplain Management: FEMA's flood map data populates the catastrophe models used in the development of rates under Risk Rating 2.0. Flood mapping data is necessary and essential for communities to promulgate floodplain management building requirements and the mandatory purchase requirement. However, flood zones will not be used in determining flood risk.

- FEMA will continue to offer premium discounts for pre-FIRM subsidized and newly mapped properties.
- Policyholders will still be able to transfer their discount to a new owner by assigning their flood insurance policy when their property changes ownership.

Flood Zone Discrepancies

Risk Rating 2.0 will not use flood zones as the primary rating component for NFIP policies but rather in the determination of mandatory purchase requirements and for floodplain management that communities impose on buildings in a special flood hazard area. For example, how high a building may need to be elevated in order to meet the community's floodplain ordinance.

Congruently with Risk Rating 2.0, Federal bank regulatory agencies ("Agencies") through proposed Interagency Questions and Answers have offered revised guidance regarding a lender's involvement in resolving flood zone discrepancies. More specifically, the guidance is proposing to alleviate the lender's need to attempt to resolve the discrepancy for when the flood zone on the flood determination form is different than the flood zone on the policy declaration page. The Agencies propose that the lenders only document the loan file of the discrepancy. The Agencies note in the proposed guidance that the issue of flood zone discrepancies is an insurance rating issue, not an insurance coverage issue. This clarifies that a lender is not in violation when the flood zone on the flood determination form differs from that on the flood insurance declaration page.

Based on the implementation of Risk Rating 2.0 with the elimination of the flood zones as the primary factor is determining flood risk, coupled with the Agencies' proposed stance on flood zone discrepancies, lenders' flood zone discrepancy procedures currently in place may need revised once final regulatory guidance is approved, and implementation of Risk Rating 2.0 occurs.

Lenders should contact their OSC Client Service Managers or SUI Client Managers for any needed revisions to flood zone discrepancy procedures.

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