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CHAPTER 21. INSURANCE AND LOSS DRAFTS

SECTION 1. INTRODUCTION

21-1. General

HUD regulation 24 CFR 207.10 requires that HUD-insured mortgages contain a covenant (acceptable to HUD) binding the mortgagor to keep the project insured against fire and other hazards. The insurance policy is required to be in an amount established by HUD, and contain a clause making any loss payable to the mortgagee and HUD, as their interest may appear. Handbook 4571.1 Rev 2, Section 202 Processing requires the same guarantee from Section 202 mortgagors. As the terms of the Regulatory Agreement remain in effect in projects with HUD-held mortgages, the mortgagor continues to be responsible for assuring that required insurance is maintained. In the case of HUD-held mortgages, mortgagee responsibilities described in this chapter are assumed by Loan Management staff. The documents which describe mortgagee/mortgagor requirements in HUD-insured and HUD-held projects are: Form FHA-2447, Property Insurance Requirements and Form HUD-92329, Property Insurance Schedule. For Section 202 projects, Handbook 4571.1 Rev.2, Appendices 28 and 29 prescribe the requirements.

This chapter provides guidance for all HUD-insured, coinsured, and HUD-held (including Section 202) projects on insurance, both required and optional, and provides procedures for HUD monitoring of mortgagor compliance. Also included are instructions for processing loss settlement drafts issued in settlement of insurance claims.

21-2. Chapter Highlights

This Chapter has five sections. A brief summary of each section follows.

Section 1. Introduction

This section provides a description of the Chapter's applicability, controlling documents, and regulatory references. Also included is a glossary of insurance industry terms and other terms used throughout the chapter.

Section 2. Required Insurance for All HUD-Insured, Coinsured, and HUD-Held Multifamily Projects

In this section, HUD requirements for mortgagees to maintain certain property and other kinds of insurance are discussed in detail.

Section 3. Optional Insurance or Additional Levels of Coverage Which May be Considered for All HUD-Insured, Coinsured, or HUD-held Projects

Other kinds and amounts of insurance, in addition to required insurance, which may protect the mortgagee, mortgagor, or HUD are discussed in this section.

Section 4. Assuring Continuing and Adequate Coverage

This section provides procedures for Loan Management staff to use in monitoring a mortgagor's maintenance of required insurance. Also discussed are methods for addressing increased insurance costs.

Section 5. Loss Settlement Drafts

In this section, procedures are provided for endorsement of loss settlement drafts by the mortgagee, mortgagor, and HUD. For HUD-held projects, procedures for Loan Management staff monitoring of restoration work following property damage also are included in this section.

21-3. Glossary

Definitions of commonly used insurance industry terms are provided below.

Actual Cash Value - Cost to replace damaged or destroyed property with comparable new property adjusted for depreciation and obsolescence.

Additional Insured - A person, firm or entity added to an insurance policy that is not the insured person or entity named in the policy and that has an insurable interest in the property. The additional insured enjoys the same protection as the insured.

Agreed Amount (Stipulated Amount) - An endorsement to a coinsurance clause in an insurance policy which states that the underwriter agrees that the value established for

the insured property is correct. The value is then used to set coinsurance requirements for the policy. The endorsement also states that in a partial loss, the insurer will not invoke any coinsurance penalty. will not invoke any coinsurance penalty.

All Risk insurance - Covers losses from each and every risk except those that are specifically excluded under the policy.

Apportionment (Clause) - When more than one policy has been purchased to cover a property, this clause divides a loss among the policies in the proportion that each policy bears to the entire covered loss.

As Their Interests May Appear (ATIMA) - Refers to the financial interest in a mortgaged property. For a HUD-insured mortgage, HUD and the mortgagee hold as their interest the unpaid principal amount of the mortgage note. The mortgagor's interest is the equity in the property.

Benefit - Amount of money paid or payable to a recipient from an insurance company.

Blanket Insurance (Coverage) - A single policy on the insured's property providing coverage for two or more different kinds of property on the same location; the same kind of property at two or more locations; or two or more different kinds of property at two or more different locations.

Bodily Injury - Physical damage to one's person.

Boiler and Machinery Insurance - Covers losses (including losses to business property, other property and legal fees, if any) resulting from the malfunction of boilers and machinery. (See special multi-peril, insurance)

Builder's Risk Form - Insures building contractors for bodily injury or damage to property while it is under construction. Insures against losses from fire, lightning, vandalism, malicious mischief, riot and civil commotion, smoke, sprinkler leakage, water damage and windstorm and hail perils. The insurance comes in two basic types:

- a. The Completed Value Form - Requires 100% coinsurance because it covers the full cost of the completed structure.

- b. The Reporting Form - Coverage that corresponds to the value of the structure at various stages of construction.

Building Laws. Most metropolitan areas have building codes that govern repair of buildings damaged by fire and other perils. These codes may require that buildings damaged to a certain degree be rebuilt to current code requirements. The current codes might be more stringent than those in effect when the building was first constructed. Costs associated with such requirements are not covered by ordinary insurance because the loss was incurred not as a result of a provision of law. The following endorsements provide protection from law-caused losses:

- a. Contingent Liability from Operation of Building Laws - Provides for reconstruction of the undamaged portion of a building in the event that local laws require it to be rebuilt after a partial insured loss. Does not cover the cost of demolition, clearing the site or increased costs of construction resulting from building laws. These expenses must be insured separately.
- b. Demolition Cost (Undamaged Portion) - Covers the cost of demolition of the undamaged portion of a building, if the demolition is required by law. A demolition cost endorsement can only be purchased in conjunction with contingent liability coverage.
- c. Increased Cost of Construction - Covers the cost of repair or reconstruction of a damaged insured property when, due to building codes or other laws, the repair costs exceed normal replacement costs.

Burglary Insurance - Part of special multi-peril insurance or mercantile open stock burglary insurance that covers against loss as a result of burglary. Coverage extends to loss of merchandise, furniture, equipment and fixtures due to forced or violent entry to the premises. Also covers damage to the building premises as a result of the burglary.

Casualty Insurance - Coverage for an individual or organization for liability for bodily injury or property damage to a third party which results from the negligent acts or omissions of the insured party.

Certificate of Insurance - Document issued to a policy holder or additional insured that gives evidence of the existence and terms of a given insurance policy.

Certified Duplicate Copy of Policy - A copy of an original insurance policy which is certified by the insurer as being the same as the original policy. Such copies must be safeguarded as the insurer or insured generally may not cancel or amend a policy unless all certified duplicate copies are accounted for by the insurer. If a certified duplicate copy of a policy is not available, that policy can still be canceled if all parties sign a Cancellation Request/Policy Release form and submit it to the insurer.

Coinsurance (Reduced Rate Average ) Clause - Developed to encourage owners to carry adequate amounts of fire and extended coverage insurance. Insurers offer lower rates to owners maintaining coverage of at least 80% of the actual cash value of an insured property. Because replacement costs for a building increase over time, the required coinsurance amount also increases. If coinsurance requirements (a % of value stipulated in the policy) are met, the insurer pays 100% of a loss, up to the policy limits and subject to any deductible. If the insured carries less than the stipulated coinsurance percentage, then the insurer only pays the percentage of the loss stated in the policy; the insured must make up any difference.

Coinsurance Formula:

Amount of Insurance Carried		= % of loss paid by insurer
Amount of Insurance That Should be Carried		(up to policy limit)

Example (\$20,000 Loss):

Amount Carried	\$240,000				
Should be Carried	\$240,000	=	100%	of loss	covered or
					\$20,000 (less deductible)
Amount Carried	\$240,000				
Should be Carried	\$320,000	=	75%	of loss	covered or
					\$15,000 (less deductible)

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Comprehensive General Liability Insurance (CGL) (a/k/a "Commercial General Liability"). Provides coverage against all liability exposures of a business unless specifically excluded.

Depreciated Value. The value of property at a point in time. An actual or accounting recognition of the decrease in value of an asset over time according to a predetermined schedule.

Directors and Officers Liability Insurance - Coverage for a business for liability due to a director/officer's breach of duty resulting from negligence, error, or omission. The insurer will not pay damages for libel, slander, dishonesty, fraud nor for personal profits illegally received by a director or officer.

Earthquake Insurance - Endorsement to a policy covering losses due to earthquake or volcano. Excludes losses from fire, flood, or tidal wave.

Endorsement - A written agreement attached to a basic policy to add to or subtract from the insurance coverage stated in the policy. Takes precedence over the policy's original provisions.

Explosion - Part of an extended coverage endorsement to a standard fire policy. The term explosion is not defined in the endorsement. Instead, the endorsement lists those perils that are not considered explosions.

Extended Coverage - Endorsement extending coverage under a standard fire policy to loss from riot, riot attending a strike, civil commotion, smoke, aircraft and vehicle damage to the property, windstorm, hail, and explosion.

FAIR Plan (Fair Access to Insurance Requirements) : Established by Federal government after the riots of the late 1960s to provide insurance to those living or doing business in deteriorated areas. If insurance cannot be obtained because of a property's location, an owner may make application to a company in the FAIR program. The FAIR Plan is based on the stop loss insurance method in which risk is spread by giving a portion of any loss to several companies.

Fidelity Bond - Covers the insured for money or property lost because of dishonest acts of its bonded employees. The bond lists employees either by name or position.

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Fire (standard Fire Policy) - A standard form used in most states. Written to cover numerous direct and indirect risks, it is a 165 line basic policy with four sections:

- a. Declarations. Describes property, insured amount, name of insured, effective date, and expiration date.
- b. Insuring Agreement. Lists premiums, the obligations and actions required of insured in the case of a loss or claim and states what the insurer agrees to do and the conditions under which it will do them.
- c. Conditions. Explains those conditions or actions which suspend or restrict coverage.
- d. Exclusions. Lists perils not covered under the policy.

The policy insures only against fire and lightning; therefore, an extended coverage endorsement must be purchased to cover additional perils such as windstorm, hail, riot, smoke damage, etc.

Flood Insurance - Coverage made available to residents of a community on a subsidized or unsubsidized premium rate basis. Available only after the governing body of a community qualifies the community for coverage under the National Flood Insurance Act. Available from licensed agents under a program administered by the Federal Insurance Administration (FIA). FIA has a "Write Your Own (WYO)" program in which private insurance companies can participate; such companies must be licensed and regulated by states to engage in the business of property insurance in those states in which they wish to sell flood insurance.

Form - An attachment to an insurance policy that completes the policy's coverage.

Friendly Fire - A fire that occurs in the place designed for it, such as a fireplace or furnace. A hostile fire is one that occurs where it is not supposed to occur. Fire insurance covers only losses from hostile fires. A friendly fire can become a hostile fire if it spreads out of the place designed for it.

Hazard - Circumstances that increase the likelihood or probable severity of a loss (e.g., storage of flammable liquids in a basement).

Indemnity - Compensation for a loss.

Insurable Interest - Any lawful and substantial economic interest in the safety or preservation of property from loss, destruction, or pecuniary damage. No property may be insured unless the party named in the policy has an insurable interest in that property.

Insurable Value (Risk) - Condition in which an applicant for an insurance policy has met the standards of the insurance company. NOTE: Certain HUD documents use the term "insurable value" to mean the value of an insured property. This is not the standard insurance industry usage of this term. The insurance industry generally defines the value of an insured property as "replacement cost."

Insured - Party covered by an insurance policy.

Insurer - Company offering protection for individuals or property through the sale of insurance policies.

Interior Robbery Policy - Covers the inside of an insured's business premises if it experiences a loss of money, securities, personal property and damage or destruction of real or personal property due to robbery or attempted robbery.

Joint Loss Apportionment - Division of a loss among insurance policies in proportion to the share that each policy bears to the total coverage applicable to the loss.

Joint Loss Payee - Beneficiary that receives payments for a loss or benefit from several insurers that have divided the risk on a joint loss apportionment basis or an insurance company that receives a portion of a payment from a payer.

Liability Insurance - Coverage for all sums for which an insured becomes legally obligated to pay for bodily injury or property damage (and sometimes other wrongs) to which the policy applies.



Loss - Damage through an insured's negligent acts and/or omissions that results in bodily injury and/or property damage to a third party, damage to an insured's property, or an amount an insurance company has a legal obligation to pay.

Loss Draft - Documentary instrument used to transfer money from an insurance company to an insured party in payment of a claim.

Mortgagee Clause - An endorsement to the standard fire policy to protect the interest of the mortgage lender up to the policy's limits.

Non-Owned Vehicle - A vehicle leased or owned by an employee but driven for business purposes.

Payee or Recipient - An insured or beneficiary who receives a loss or benefit payment from an insurer or an insurance company that receives a payment from another insurance company.

Performance Bond - Guarantees a contractor will perform under a contract in accordance with all specifications of the bid submitted.

Peril - A risk to a property (e.g., fire, wind, explosion).

Replacement Cost - Amount of money necessary to replace the damage or destroyed property of the insured with property of like kind and quality and without deduction for depreciation of the property.

Subrogation - Surrender of rights against a third party by an insured to an insurance company that has paid a claim. For example, a neighbor causes a fire that damages your property. Your insurance company pays your claim for loss from the fire. Under subrogation, you give up to the insurer your right to sue the neighbor. The insurance company then has the right to initiate legal action against the neighbor to recover the amount of the claim.

Surety Bond. A contract by which one party agrees to make good the default, debt, or performance failure of another. Uses the following terms:

- a. Principal. Party that has primary responsibility to perform the obligation.
- b. Surety. Party that has secondary responsibility to perform the obligation if the principal fails to perform,
- c. Obliges. Party to whom the right of performance is owed.

Umbrella Insurance - Excess liability coverage over and above the limits of a basic business liability insurance policy.

Use and Occupancy Insurance - Business interruption insurance that provides indirect loss coverage by endorsement to other standard policies. Covers an insured for loss of the use of equipment due to damage from a named peril. Provides protection against loss of income because of the interruption of business by a covered peril.

Vacancy (Unoccupancy) - Covers vacancy of a building or portions of a building, usually for no more than 60 days.

Vehicle Insurance (Business Automobile Policy) - Coverage for autos used by a business when a liability judgment could possibly arise out of the use of the auto or when the vehicle is subject to damage or destruction. The policy is comprised of four sections:

- a. Terms. Defines the terms used in the policy such as auto, accident injury, etc.
- b. Liability Insurance. Sets forth the limits, inclusions and exclusions of coverage under the policy.
- c. Physical Damage Insurance. Establishes what claims for physical damage will be paid and on what basis (comprehensive - damage to covered vehicles from vandalism, theft, fire, explosion, etc., or collision - damage to covered vehicles resulting from colliding with another vehicle or from overturning the insured auto).
- d. Conditions. Stipulates the actions to be taken in the event of a loss.

Water Damage Insurance - Coverage for damage due to water from accidental discharge; leakage or overflow from plumbing, heating, air conditioning or refrigeration systems; and entrance of rain or snow into a building through open or broken windows, doors and skylights. May also be an endorsement to a standard property insurance policy.

Windstorm (Storm) Insurance - Coverage for damage from windstorms (hurricanes, cyclones, high winds) as part of an extended coverage endorsement. Unless specified in the endorsement, damage to metal smoke stacks, awnings or canopies, signs, antennas, or shrubbery is not covered.

Workers Compensation Insurance - Provides four types of benefits (medical care, death, disability, rehabilitation) for employee, job-related injuries or diseases as a matter of right to the employee, without regard to fault. Purchased from a private company or a state-owned fund.

Wrongful Death - Death caused by a person without legal justification (negligence, willful act).

SECTION 2. REQUIRED INSURANCE FOR ALL HUD-INSURED AND HUD-HELD MULTIFAMILY PROJECTS.

21-4. HUD Insured and HUD-Held Projects. Throughout the life of the mortgage insurance contract, the mortgagee of a HUD-insured project (or the Field Office Loan Management Branch Chief for a HUD-held project) must assure that the mortgagor maintains fire and other hazard (as determined by HUD) insurance on the property pledged as security for the loan. The required types of insurance and amounts of coverage by type generally include:

- A. Fire and Extended Coverage with an Agreed Amount clause (co-insurance) in amounts not less than 80% of the project's current insurable value. The insurance must be provided on a blanket basis and cover the project's buildings, all mortgagor-owned contents and any other buildings and revenues pledged to secure the loan.
- B. Flood Insurance with coverage limits equal to the lesser of the outstanding principal balance of the loan or the maximum amount of insurance available

Act. Flood insurance is required if a project is located in an area of special flood hazard in which insurance coverage is available under the Act.

- C. Boiler Explosion Insurance is required if steam boilers are operated in conjunction with the project. a minimum coverage limit of \$100,000 per accident, per location must be maintained. The insurance must take the form of a Boiler and Machinery Policy Broad Form, including repair and replacement but excluding bodily injury coverage.
1. Inspection Requirements. All directly fired steam, hot water heating, domestic water heaters, and hot water supply tanks indirectly fired with steam must be inspected annually by either a state or local inspection facility or other authorized inspection service created by state or local law to inspect boilers; or an insurance company that has been licensed or registered by a state or locality and whose inspection services are acceptable under state or local ordinances.
  2. Inspection requirements do not apply to hot water boilers and hot water supply tanks that are equipped with ASME labeled pressure relief valves and do not exceed any of the following limitations:
    - a. Heat output of 200,000 BTU/hour;
    - b. Water temperature of 210 degrees Fahrenheit (99 degrees Celsius); and
    - c. Water capacity of 120 gallons.
- D. Fidelity Bonds for Management Agents. Management agents are required to certify that they have obtained fidelity bond or employee dishonesty coverage for all principals of the management entity and all persons who participate directly or indirectly in the management or maintenance of the project or its assets, accounts and records. (See HUD Handbook 4381.5.) Monitoring compliance with this requirement is the responsibility of the Field Office Loan Management Branch Chief and not the mortgagee of a HUD-insured project.

insurance described in Paragraph 21-1 above and also must carry the following types and amounts of insurance for Fire and Extended Coverage (F & EC); the Section 202 program requires the F & EC policy be written on a blanket basis or with an agreed amount clause in amounts not less than 80% of the project's current insurable value. Section 202 projects' policies must name the Borrower as insured and carry a standard mortgagee Clause showing loss of damage payable to the Borrower and "the U.S. of America acting by and through the Secretary, Department of HUD, his/her successor or assign, ATIMA)."

- A. Public Liability Insurance on a Comprehensive General Liability Form with limits of not less than \$500,000 per occurrence. This insurance protects the mortgagor from claims for bodily injury and/or death and for property damage sustained by a third party as a result of the mortgagor's operations including any use or occupancy of its facilities, grounds and structures. Where applicable, similar coverage may be required to be provided by independent contractors working for the mortgagor.
- B. Motor Vehicle Liability Insurance for mortgagor owned or operated vehicles, including non-owned and/or hired vehicles operated for the benefit of the mortgagor. Coverage limits must not be less than \$300,000 for one person and \$500,000 for more than one person to protect the mortgagor from claims for bodily injury and death and not less than \$50,000 against claims for damage to property.
- C. Workers Compensation and Employers Liability Insurance for all employees of the mortgagor and other facilities from which revenues are pledged to project operations.
- D. Blanket Fidelity Bond in an amount equal to two months gross revenues or \$50,000, whichever is greater. The bond must cover all officials and employees of the mortgagor, including non compensated officials.
- E. Use and Occupancy Insurance (Rental Value). Such coverage must be maintained for each building from which revenues are pledged to payment of debt service requirements. The amount of coverage must be sufficient (in the event of loss) to enable the mortgagor to deposit the proceeds of a claim in an

escrow account from which required debt service payments may be made. The amount must equal the sum that would normally have been available for such purposes from the revenues of the damaged building during the time the building cannot produce revenue due to a loss caused by perils covered by the project's Fire and Extended Coverage insurance.

- 21-6. Recommended Insurance for HUD-Insured, Coinsured, and HUD-held Projects. The insurance types and amounts of coverage described in Paragraph 21-5 for Section 202 projects are recommended for all HUD-insured, coinsured, and HUD-held projects as a further protection for the property secured by the mortgage loan.
- 21-7. Mortgagee or HUD Requirements to Assure Adequate Insurance is In Place
- A. Requirements for HUD-Insured Projects. For all HUD-insured projects, the terms of the mortgage insurance require the mortgagee to assure that required insurance is in place. Form HUD-92329, "Property Insurance Schedule," provides the mortgagee the insurable values and a description of the property which must be insured by the mortgagor and Form FHA-2447, "Property Insurance Requirements," describes the required insurance. Form HUD-2434 (formerly FHA-2434), "Mortgagee's Certificate," executed by the mortgagee, includes a reference to the required insurance and assures that the insurance will have a standard Mortgagee Clause attached making all losses payable to the mortgagee and the Secretary as their interests may appear (ATIMA). The mortgagee is responsible for establishing procedures to ensure that the mortgagor's insurance meets HEM requirements throughout the life of the mortgage insurance.
- B. Requirements for HUD-Held Projects. For all HUD-held projects, excluding Section 202 projects, the Loan Management Branch Chief must assure that required insurance is in place during the life of the mortgage note. (For Section 202 projects, Headquarters staff are responsible for ensuring compliance with insurance requirements contained in Handbook 4571.1 Rev 2. Appendices 28 and 29

of that Handbook provide the insurable values and a description of the property which must be insured by the mortgagor as well as the Property Insurance Requirements. Field Offices are to forward all insurance policies on Section 202 projects to Headquarters.) For other HUD-held projects, Form HUD-92329, "Property Insurance Schedule," and the attached Form FHA-2447, "Property Insurance Requirements," provide this information. Except for Workers Compensation insurance, all insurance policies must make all losses payable to the Secretary an additional insured. The Mortgagor must provide certified duplicate copies of all required insurance policies to the Field Office Loan Management Branch Chief. Loan Management staff must maintain an expiration date file for all policies and fidelity bonds and assure that all required insurance policies are provided to the Field Office Loan Management Branch Chief. Loan Management staff must assure that required insurance is maintained. (See Section 4, Assuring Continuing and Adequate Coverage, below.)

SECTION 3. OPTIONAL INSURANCE OR ADDITIONAL LEVELS OF COVERAGE WHICH MAY BE CONSIDERED FOR ALL HUD-INSURED, COINSURED, AND HUD-HELD PROJECTS.

21-8. Individual circumstances of a project may warrant consideration of additional forms of insurance or amounts of coverage for the property in addition to those discussed in Section 2 above. Loan Management staff may assist the mortgagor to evaluate the need for optional insurance on a case-by-case basis using the general guidelines of this chapter. Examples of the kinds of circumstances which may require additional insurance or amounts of coverage are:

- A. A high risk location for the project (e.g., an area with a high crime rate).
- B. Project exposure to unique perils (e.g., hurricane, earthquake).
- C. Unique project features or inclusions (e.g., swimming pool).

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21-9. Examples of additional types of insurance which may be considered include:

- A. Windstorm (with a hurricane endorsement, if appropriate).
- B. Burglary Insurance.
- C. Contractor Performance Bonds for major contract work such as capital improvements, maintenance, or food-service.
- D. Liability insurance if security services are provided at the project.
- E. Directors and Officers Liability Insurance for nonprofit mortgagors. Such policies, when approved by HUD as a project expense, must have an exclusion stating that directors and officers are not protected from sanctions imposed by the Federal Government.
- F. Construction endorsements for property damage and personal injury when construction (such as roof replacement) is underway.
- G. Liability insurance if resident programs are conducted at the project.
- H. Earthquake Insurance in areas prone to earthquakes.

21-10. Other Insurance Issues

- A. Insurance for Providers of Contract Services
  - 1. Any insurance requirements for parties that provide contract services to the project should be clearly defined in the contract document.

The Mortgagor must use its own judgement in determining which contractor activities are sufficiently hazardous to warrant an insurance requirement. Affected providers of contract services should provide insurance certificates to the mortgagor that name the mortgagee (in HUD-insured projects), the Secretary, and mortgagor, as their interests may appear, as additionally insured.

- 2. Care must be taken to assure that contractors carry insurance appropriate to the work or service agreed to in the contract. Unusual perils



inherent in the nature of the work must be covered and contractor insurance should include generally accepted coverage such as Public Liability, Performance Bond, Workers Compensation, Vehicle Liability, Blanket Fidelity Bond, and Builders Risk Insurance.

SECTION 4. ASSURING CONTINUING AND ADEQUATE COVERAGE

21-11. Insurable Value.

- A. Definition. The term "insurable value" referenced in various HUD documents means the replacement cost of the building(s) insured, i.e., the cost to rebuild the building(s) should it suffer a complete and total loss due to fire or other perils.
- B. Updating Insurable Value. over time, insurable value must be adjusted due to changes in construction costs, building codes or other statutory requirements, or other related issues. Mortgagees (for HUD-insured projects) and Loan Management staff (for HUD-held projects) must assure that the insurable value of the property is reviewed and updated, if necessary, as insurance policies renew. This requires maintaining familiarity with changes in costs and other issues in the jurisdiction in which the project is located.

21-12. Monitoring Receipt of Policies and Certificates of Insurance

- A. For illustration, mortgagees for HUD-insured projects usually maintain an expiration date file to assure that mortgagors renew required insurance policies on a timely basis. For HUD-held projects only, the Loan Management Branch Chief should maintain such a "tickler" file to assure that mortgagors renew required insurance policies on time. Field Offices may use their own systems, either computerized or manual, to achieve this objective. Whatever control system is used, no less than the following information should be recorded for each project: Project Name; Project Number; Insurance Company Name(s); Last Date Renewed; Date of the 90-day Letter; Date of Receipt of

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proof of insurance; Date of any Noncompliance Letter; Date of Review of Insurance Coverage; Date(s) of Follow-up Actions and type(s) of actions.

B. For HUD-hold projects only, the Loan Management Branch Chief should use the following procedures:

1. Notify the mortgagor 90 days prior to policy expiration of the requirement for continuing coverage and that HUD must be provided certified duplicate copies of policies or certificates of insurance as evidence that insurance of the type and coverage required will be maintained.
2. Include in the notification a requirement that the mortgagor begin renewal activities at least 60 days in advance of policy expiration.
3. Require that copies of the renewal policies or certificates of insurance be provided to HUD no later than 30 days prior to the expiration date.
4. If the renewal policies or certificates of insurance are not provided by the mortgagor within the 30 day time frame, follow-up action must be taken:
  - a. Notify the mortgagor of the noncompliance. Request copies of the policies or certificates of insurance or a Notice of Unavailability of Insurance within 10 business days.
  - b. Initiate appropriate sanctions if the copies are not received within the established time frame.

C. Reference is made to HUD Handbook 4350.4, Insured Multifamily Mortgagee Servicing and Field Office Remote Monitoring Handbook, for additional information about mortgagees' responsibilities regarding insurance requirements.

21-13. Notice of Unavailability of Insurance. When a mortgagor is unable to obtain insurance, the mortgagee (or mortgagor of a HUD-held project) must notify HUD within 30 days of the cancellation of the insurance and of the refusal of the insurance company to renew the insurance. For projects with insured mortgages, a Notice of Unavailability of Insurance is prepared by the mortgagee

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and sent to the Field Office Loan Management Branch Chief. When a Notice of Unavailability of Insurance is received,

the Loan Management Branch Chief should take the following steps:

- A. Review with the mortgagee the steps outlined in Paragraph 21-15 below to assure that the unavailability is not related to cost; and
- B. Help determine if the mortgagee or mortgagor may be eligible for insurance under any FAIR (Fair Access to Insurance Requirements) Plan available in the locality. For information, contact the Insurance Commission for the state in which the project is located. (See Appendix 5). Refer the mortgagee or mortgagor to the FAIR plan, if appropriate.

21-14. Reviewing Coverage to Compare with HUD Requirements for HUD-Held Projects

- A. The Housing Management Division Director should request a current replacement cost estimate from the Housing Development Division Director using the procedures described in Chapter 5 of HUD Handbook 4355.1, Flexible Subsidy Handbook.
- B. Loan Management staff must review insurance policies for HUD-held projects to assure that:
  - 1. The insurable value indicated on Form HUD-92329 is up-to-date and reflects current replacement costs for the property insured; and
  - 2. The amount of coverage included in the policies meets HUD requirements as described in Section 2.
- C. A checklist/worksheet is provided as Appendix 1 to assist Loan management staff to conduct this analysis.
- D. Notify the mortgagor immediately in writing if coverage is not adequate and require that the insurance be upgraded within 10 days or that HUD be notified within that same time frame if an upgrade is not possible. Follow the guidelines established in Paragraph 21-15 below if cost is the reason for inadequate coverage.

- 21-15. Cost of Insurance Generally, costs which are competitive (consistent with insurance costs for noninsured projects of the same type in the same location) and which the project's budget can

afford may be allowable by HUD. If the project's current budget cannot sustain the cost of required premiums (evidenced by quotes from three different insurance carriers), the following steps should be taken to ensure that required insurance coverage is maintained.

- A. The mortgagor should request a rent increase to cover the increased cost of insurance premiums.
- B. If it is necessary to increase deductibles to reduce premium costs, the Reserve Fund for Replacements should be adequate or should be increased to include the amount of deductibles anticipated per claim with the number of anticipated claims factored in.

SECTION 5. LOSS SETTLEMENT DRAFTS

21-16. When a claim is submitted to an insurance company because of damage or other occurrences, the insurer issues loss settlement drafts as payment of benefits due the insured. Loss settlement drafts are instruments which authorize the transfer of funds from the insurer to the insured. Loss settlement drafts may take a variety of forms including a check, a letter of credit, a letter authorizing a transfer of funds from one bank account to another, or a notice authorizing a wire transfer of funds.

- A. All loss settlement drafts issued by an insurer must name the mortgagor, the mortgagee (if HUD-insured), and the Secretary as joint payees.
- B. Loss settlement drafts ordinarily are issued to the mortgagor. The mortgagor must review the draft to assure that the required joint payees are referenced. If not, the loss settlement draft must be returned to the insurer with instructions that it be revised and reissued.
- C. Following review of the draft, the mortgagor must endorse the draft, forward it to the mortgagee (if HUD-insured) for endorsement, and then to the Loan Management Branch Chief for endorsement on behalf

of HUD. (Note: Endorsement by HUD may make the loss settlement draft a negotiable instrument. Care must be taken to safeguard the draft properly and to mail it promptly.)

- 21-17. The mortgagee and mortgagor are responsible for assuring that restoration of property damage covered by the loss settlement draft is completed.
- A. In the case of HUD-insured projects, the mortgagee's endorsement of the loss settlement draft is confirmation to HUD that the restoration has taken place satisfactorily. The Loan Management Branch Chief normally will endorse such loss settlement drafts and return them to the mortgagor.
  - B. In the case of HUD-held projects, the Loan Management Branch Chief must ensure that the restoration has occurred satisfactorily. If the loss is more than \$15,000 a physical inspection of the repairs, documented in writing, must take place before the Loan Management Branch Chief will endorse the loss settlement draft and return it to the mortgagor.
    - 1. If the amount of the loss is large (generally between \$5,000 and \$15,000), in the judgment of the Loan Management Branch Chief, inspections may be scheduled before, during, and/or after restoration work, or during the next scheduled management review or physical inspection of the project.
    - 2. If the amount of the loss is under \$5,000, the repairs usually may be inspected during the next scheduled management review or physical inspection.
    - 3. Generally, the greater the extent of the damage the greater the involvement of the Loan Management Branch Chief in the oversight of restoration work. Factors such as the financial and physical condition of the project should be considered. For example, will the financial condition of the project lead to a lower quality restoration in the interests of saving money? Does the age and condition of the building require that current building codes be met during the restoration?

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- 4. Some restoration requiring plans and specifications or a lengthy period for completion may require multiple inspections. For example, if restoration requires new plumbing or wiring, inspections should take place before the work is

enclosed by new walls and before final acceptance of the contractor's work.

C. The Loan Management Branch Chief may require that loss settlement draft progress payments be placed in escrow until all Loan Management inspections are completed and the work is determined to be satisfactory.

21-18. For HUD-held projects, the Loan Management Branch Chief must determine that, in addition to satisfactory restoration, the terms of any Work Out Agreement in effect are being met.

A. If the terms are being met, the Loan Management Branch Chief will normally endorse the loss settlement draft and return it to the mortgagor following completion of procedures described in Paragraph 5-2.

B. If the terms are not being met, the Loan Management Branch Chief should attempt to get the mortgagor's endorsement on the draft and forward it to the Office of Mortgage Insurance Accounting and Servicing, Headquarters, for application to the mortgage delinquency. If the mortgagor's endorsement cannot be obtained, the loss settlement draft should be returned to the mortgagor without the Secretary's endorsement.

21-19. Endorsement. Drafts or checks that require the endorsement of HUD as one of the payees shall be endorsed as follows:

Pay to the Order of the Named Mortgagor Without Recourse  
Secretary  
Department of Housing and Urban Development

By:  
Chief, Loan Management Branch of the  
Field Office

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Sample  
Insurance Review Checklist

Type	Does Mortgagor Coverage Meet Requirements? Requirement	Yes	No
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Fire and Extended	80% Coinsurance on buildings and contents.	___	___
Flood Insurance	Outstanding principal of the loan or maximum available under National Flood Insurance Act, whichever is lesser. (Must meet requirements of the Act to qualify.)	___	___
Public Liability on a Comprehensive General Liability Form	Limits not less than \$500,000 per occurrence.	___	___
Major Vehicle Liability (for owned, nonowned and/or hired vehicle)	Bodily Injury and Death: Not less than \$300,000 for 1 person; \$500,000 for more than one person. Property Damage not less than \$50,000 per occurrence.	___	___
Workers' Compensation and Employer Liability	Statutory requirements	___	___
Blanket Liability Bond (for mortgagor entity)	Two months gross revenues or \$50,000, whichever is greater.	___	___
Boiler and Machinery Insurance (generally for steam fired boilers only)	\$100,000 per accident/per location. Specific inspection requirements apply.	___	___

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Type	Requirement	Yes	No
Use and Occupancy	Amount required to enable payment of mortgage payment for duration of loss of income due to covered peril.	___	___
Management Agent Fidelity Bond (Must name mortgagor)	Not less than project's gross potential income for 2 months	___	___

and HUD as loss payees)

Do property circumstances  
subject it to perils requiring  
insurance in addition to that  
listed above? \_\_\_\_\_

Describe the conditions.  
\_\_\_\_\_

Does the property carry insurance adequate to indemnify it for  
losses from such perils? (e.g. Windstorm, Hurricane, Burglary,  
Contractor Performance, Liability Coverage for Resident Programs,  
etc.) \_\_\_\_\_ Yes \_\_\_\_\_ No

What types of additional insurance should the mortgagor carry that  
it does not carry now?  
\_\_\_\_\_

Has the insurable value of the property been adjusted to assure  
that Coinsurance requirements of the Fire and Extended Coverage  
policy are being met? \_\_\_\_\_ Yes \_\_\_\_\_ No

Present Replacement Value \_\_\_\_\_  
(from HD Division) \$ \_\_\_\_\_

Coinsurance Requirement \_\_\_\_\_ % \_\_\_\_\_

Required Insurable Value \_\_\_\_\_ \$ \_\_\_\_\_  
Current Insurable Value \_\_\_\_\_ \$ \_\_\_\_\_

Reviewer: \_\_\_\_\_

Date of Review: \_\_\_\_\_

Next Recommended Review Date: \_\_\_\_\_

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Appendix 2

SAMPLE LETTER TO MORTGAGORS  
GUIDANCE ON COSTS OF INSURANCE

Addressee:

Dear:

The cost of insurance premiums has been rising at an  
alarming rate. The result is that many project owners are  
having difficulty maintaining HUD-required insurance for their  
multifamily projects.



This letter is to remind owners that their HUD mortgage insurance, HUD regulations, and HUD administrative procedures require owners to maintain stipulated insurance coverage. Therefore, options which must be considered in the event insurance becomes prohibitively expensive or unavailable are:

1. Request from HUD a rent increase to cover the cost of increasing insurance premiums.
2. Consider increasing deductibles to reduce cost. Arrange to increase deposits to the Reserve Fund for Replacements to cover anticipated deductibles factoring in the number of claims anticipated. Assure that the mortgagee maintains this deductible "reserve" in cash or in a form which is easily converted to cash.

Failure to meet HUD insurance requirements may result in action being taken against mortgagors up to and including assignment of the mortgage to HUD or foreclosure. These potential actions, and the risk of uncovered perils to the project, require that you take all steps necessary to maintain required insurance for your property.

If you have any questions or are having trouble securing affordable insurance, contact us immediately.

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Appendix 3

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SAMPLE LETTER TO MORTGAGORS  
RE: CHANGES IN INSURANCE REQUIREMENTS

Addressee: \_\_\_\_\_

Dear \_\_\_\_\_

HUD has revised its requirements for the type and amount of insurance coverage which must be maintained for every HUD-insured (or HUD-held) project during the life of the mortgage note. The mortgagor must maintain the following insurance:

1. Fire and Extended Coverage
2. Boiler Explosion Insurance (if applicable to the project)
3. Flood Insurance (if applicable to the project's location)

4. Fidelity Bond for the mortgagor's or mortgagor's management agent's employees
5. Workers Compensation and Employer Liability for the mortgagor's or mortgagor's management agent's employees
6. Public Liability Insurance
7. Vehicle Liability Insurance
8. Use and Occupancy (Rental Value) Insurance

Our records do not contain evidence that you carry the following types of insurance as required:

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Please provide copies of the policies to us within 10 business days if you are currently carrying these types of insurance. If you are not, arrange to obtain the required insurance and provide copies of the policies to us within 60 days of receipt of this letter.

Contact your HUD Field Office for a copy of Chapter 21 of HUD Handbook 4350.1 for further guidance on HUD insurance requirements or call us if you have questions.

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INSURANCE COMMISSIONS

STATE/TERRITORY TELEPHONE	TITLE	ADDRESS
AK 907/465-2515	Director	Department of Commerce and Economic Development, Division of Insurance 333 Willoughby Ave., 9th fl P.O. Box D Juneau, AK 99811-0800
AL 205/269-3550	Commissioner	Insurance Department 135 South Union St. Montgomery, AL 36104
AR 501/686-2900	Commissioner	Arkansas Insurance Department 400 University Tower Bldg. 12th & University Streets Little Rock, AR 72204

AS 684/633-4116	Commissioner	Insurance Division Governor's Office American Samoa Government Pago Pago, AS 96799
AZ 602/255-5400	Director	Arizona State Department of Insurance 3030 North 3rd Street Suite 1100 Phoenix, AZ 85012
CA 916/445-5544	Commissioner	Department of Insurance  One City Centre Building Suite 1120, 770 L Street Sacramento, CA 95814

\*Effective as of 3/92; it is the responsibility of HUD Field Offices to keep current information regarding their states.

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CO 303/866-6274	Commissioner	Department of Regulatory Agencies Division of Insurance West Colfax Ave. 5th Floor Denver, CO 80204
CT 203/297-3802	Commissioner	State of Connecticut Insurance Department P.O. Box 816 Hartford, CT 06142-0816
DC 202/727-7424	Superintendent	Washington D.C. Department of Consumer & Regulatory Affairs Insurance Administration 613 G Street, NW, 6th Floor Washington, DC 20001
DE 302/739-4251	Commissioner	State of Delaware Insurance Department Rodney Building 841 Silver Lake Boulevard Dover, DE 19901
FL 904/922-3100	Commissioner	Department of Insurance, Treasurer and Fire Marshall State Capitol Plaza Level Eleven Tallahassee, FL 32399-0300

GA 404/656-2056	Commissioner	Georgia State Insurance Department 2 Martin Luther King Jr. Dr. Floyd Memorial Building 704 West Tower Atlanta, GA 30334
GU 671/477-5117	Commissioner	Department of Revenue & Taxation, Government of Guam Insurance Commissioner 855 West Marine Dr. Agana, GU 96910
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HI 808/586-2790	Commissioner	State of Hawaii, Insurance Division, Department of Commerce & Consumer Affairs P.O. Box 3614 Honolulu, HI 96811
IA 515/281-5705	Commissioner	Iowa Division of Insurance Lucas State Office Building 6th Floor Des Moines, IA 50319
ID 208/334-2250	Director	Department of Insurance 500 South 10th Street Boise, ID 83720
IL 217/782-4515	Director	Department of Insurance 320 West Washington St. 4th Floor Springfield, IL 62767
IN 317/232-2385	Commissioner	Indiana Department of Insurance 311 West Washington St. Suite 300 Indianapolis, IN 46204-2787
KS 913/296-7801	Commissioner	State of Kansas Insurance Department 420 S.W. 9th Street Topeka, KS 66612
KY 502/564-3630	Commissioner	Department of Insurance 229 West Main Street

LA 504/342-5900	Commissioner	Frankfort, KY 40602 Department of Insurance 950 North 5th Street Baton Rouge, LA 70801-9214
MA 617/727-7189	Commissioner	Commonwealth of Massachusetts Division of Insurance 280 Friend Street Boston, MA 02114
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MD 301/333-2520	Commissioner	Department of Licensing & Regulation Insurance Division 501 St. Paul Place Stanbalt Building, 7th Floor South Baltimore, MD 21202
ME 207/582-8707	Superintendent	Bureau of Insurance State Office Building State House Station 34 Augusta, ME 04333
MI 517/373-9273	Commissioner	State of Michigan, Insurance Bureau 611 West Ottawa Street 2nd Floor North Lansing, MI 48933
MN 612/296-6848	Commissioner	Department of Commerce, Insurance, Real Estate Securities Division 133 East 7th Street St. Paul, MN 55101
MO 314/751-4126	Director	Missouri Department of Insurance 301 West High St. 6 North Jefferson City, MO 65102-0690
MS 601/359-3569	Commissioner	Mississippi Department of Insurance 1804 Walter Sillers Bldg. Jackson, MS 39205
MT 406/444-2040	Commissioner	Montana Department of Insurance

126 North Sanders  
Mitchell Building  
Room 270  
Helena, MT 59601

NC  
919/733-7349

Commissioner

North Carolina Department  
of Insurance  
Dobbs Building  
430 North Salisbury St.  
Raleigh, NC 27611

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ND  
701/224-2440

Commissioner

North Dakota Insurance  
Department  
600 E. Boulevard  
Bismark, ND 58505-0320

NE  
402/471-2201

Director

Department of Insurance  
Terminal Building  
941 'O' Street  
Suite 400  
Lincoln, NE 68508

NH  
603/271-2261

Commissioner

New Hampshire Insurance  
Department  
169 Manchester Street  
Concord, NH 03301

NJ  
609/292-5363

Commissioner

Department of Insurance  
20 West State St., CN325  
Trenton, NJ 08625

NM  
505/827-4500

Superintendent

State Corporation Commission  
P O Drawer 1269  
Santa Fe, NM 87504-1269

NV  
702/687-4270

Commissioner

Department of Insurance  
1665 Hot Springs Rd.  
Carson City, NV 89710

NY  
212/602-0429

Superintendent

New York State Insurance  
Department  
160 west Broadway  
New York, NY 10013

OH  
614/644-2658

Director

Ohio Department of Insurance  
2100 Stella Court  
Columbus, OH 43266-0566

OK 405/521-2828	Commissioner	Department of Insurance 1901 North Walnut Oklahoma City, OK 73105
OR 503/378-4271	Commissioner	Department of Insurance & Finance, Insurance Division 21 Labor and Industries Bldg. Salem, OR 97310

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PA 717/787-5173	Commissioner	State of Pennsylvania Insurance Department Strawberry Square 13th Floor Harrisburg, PA 17120
PR 809/722-8686	Commissioner	Fernandez Juncos Station 1607 Ponce de Leon Ave. Santurce, PR 00910
RI 401/277-2223	Commissioner	Department of Business Regulation, Insurance Division 233 Richmond St., Ste. 237 Providence, RI 02903-4237
SC 803/737-6117	Commissioner	Department of Insurance 1612 Marion St. Columbia, SC 29201
SD 605/773-3563	Director	Department of Commerce & Regulation, Insurance Division Insurance Building 910 E. Sioux Ave. Pierre, SD 57501
TN 615/741-2241	Commissioner	Department of Commerce & Insurance Volunteer Plaza 500 James Robertson Pkwy Nashville, TN 37243-0565
TX 512/463-6468	Commissioner	Texas Department of insurance 333 Guadalupe Street P.O. Box 149104 Austin, TX 78714-9104
UT	Commissioner	Utah Insurance Department

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VA 804/786-7694	Commissioner	Virginia Bureau of Insurance 1200 Jefferson Building 1220 Bank St. Richmond, VA 23219
VI 809/774-2991	Commissioner	Insurance Department Kongens Gade # 18 St. Thomas, VI 00802
VT 802/828-3301	Commissioner	Department of Banking, Insurance & Securities 120 State ST. Montpelier, VT 05602
WA 206/753-7301	Commissioner	State of Washington office of Insurance Commission Insurance Building AQ21 Olympia, WA 98504
WI 608/266-0102	Commissioner	Office of the Commission of Insurance 121 East Wilson Madison, WI 53702
WV 304/348-3394	Commissioner	Insurance Commission 2019 Washington Street East Charleston, WV 25305
WY 307/777-7401	Commissioner	Wyoming Insurance Department Herschler Building 122 West 25th Street Cheyenne, WY 82002