6. (2.5 points)

   a. (1 point)

      Identify and briefly describe two ways in which National Flood Insurance Program (NFIP) policies are sold by private companies.

   b. (1.5 points)

      Describe three types of premium subsidies built into the NFIP rating structure.

CONTINUED ON NEXT PAGE

Common errors include:

- The FIO monitors SIFIs, insurance companies with banks, or insurance companies. The FIO does not monitor individual companies.
- The FIO regulates insurance companies. The FIO is not a regulator.
- The FIO preempts state regulation. This is true but is very specific and the answer needed to include if the state regulation interferes with foreign covered agreements.
- The FIO creates model laws. The FIO does not create model laws.
- The FIO designates SIFIs. The Financial Stability Oversight Council designates insures as subject to regulation as a nonbank company supervised the Board of Governors.
- Not unique – Day-to-day oversight of the insurance industry and help identify practices that could lead to systemic crisis.

**Part b**

Candidates were expected to describe the impact of Dodd Frank on three aspects of the insurance industry.

Common errors for include:

- Compliance costs will be passed onto the policyholder. This answer does not make it clear that the compliance costs are due to the dual or increased regulation.
- Discussing the impact of other acts (not Dodd-Frank) on banking and insurance.

| **FALL 2018 EXAM 6US, QUESTION 6** | |
|---|---|
| **TOTAL POINT VALUE: 2.5** | **LEARNING OBJECTIVE: B2** |
| **SAMPLE ANSWERS** | |
| **Part a:** 1 point | |

*Sample Responses for Write-Your-Own Policy (WYO)*

- WYO program: Private companies sell policy through "WYO" program and are reimbursed for administrative expenses by NFIP.
- Through write-your-own program where private insurers write and service policy but risk is reinsured completely by federal government.
- "Write your own" program, where insurers market and issue the policies and are 100% reinsured by NFIP
- Through the write-your-own program private carriers may write and market NFIP policies to consumers

*Sample Responses for Direct Servicing Agent (DSA)*

- Direct Servicing Agent: private service agents/companies contracted with NFIP (contractor company) and sell policies.
- Through direct specialized agents who are in charge of selling the insurance on behalf of the federal government.
- Servicing agents who assign customers to the NFIP
- Direct through a contractor of NFIP/FEMA which serves as intermediary

# SAMPLE ANSWERS AND EXAMINER'S REPORT

**Part b:** 1.5 points

*Sample Responses for Pre-Firm Subsidy*

- If house built/substantially improved before the later of 12/31/74 or 1st FIRM published for community, the owner is charged less than actuarially indicated rate
- Pre-Firm Subsidy – policies w/ homes built before a certain date or before a risk map was made in the area
- Subsidies for properties built before development of FIRM

*Sample Responses for Newly Mapped Subsidy*

- New Mapped Subsidy – for communities mapped after 4/1/2015
- Subsidize premiums for policies that were originally PRPs then mapped to a special hazard flood zone
- First Mapping subsidy – in the first 12 months the community has a change to the FIRM, the community can use the PRP rate

*Sample Responses for Grandfathering Cross-Subsidy*

- Grandfathering Cross Subsidy – buildings whose flood hazard area was reclassified can choose to be assigned a pay rates as per the former classification
- Grandfather subsidy allows policies to be grandfathered into their original rates if their rates would increase due to being mapped to a new FIRM
- Grandfathering subsidy, applies to those previously under a lower rate and just got remapped into a higher rate zone. They can continue to be charged at original rate.

*Sample Answers for Community Rating System (CRS)*

- Community Rating – communities can take steps to reduce their risks beyond the basic NFIP requirements in return for lower premiums
- Cross subsidy where communities that make improvements to receive premium reductions are subsidized by communities that don't receive any rate reduction
- If the community participates in NFIP and educates residents they may be placed in tier and members charged lower rate

Other sample answers:

- Grandfathering Elevation – a property may retain rate if base flood elevation changes on them
- Premium is subject to a maximum increase, even if the increased premium is lower than the indicated rate

**EXAMINER'S REPORT**

Candidate was expected to demonstrate knowledge of the way NFIP policies are sold through private insurance companies or specialized agents for Part A as well as the subsidies that NFIP builds into its rating structure for Part B.

**Part a**

Candidate were expected to identify and describe how insurance companies would use a Write-Your-Own (WYO) arrangement and Direct Servicing Agent (DSA) to distribute NFIP policies.

Common errors include:

- Identifying the arrangement with no description
- Describing a pooling arrangement among companies
- Describing an assigned risk program where insurers must involuntarily write or service NFIP policies
- Describing how companies wrote a unique flood policy rather than an NFIP policy
- Stating that companies would write policies using NFIP rules/rates but assume all risk of loss with no NFIP backing or reinsurance

**Part b**

Candidates were expected to describe three types of premium subsidies built into the NFIP rating structure.

Common errors include:

- Describing subsidies that fall outside of the NFIP rating structure – such as post flood costs covered by FEMA, assistance from the Treasury, or the burden on taxpayers
- Describing issues with the actuarial soundness of the overall program or classes within the program as opposed to the premium subsidies
- Describing situations that would lead to lower than expected premiums – such as repeated losses, limited criteria for risk segmentation, buildings not reconstructed up to current code
- Describing penalties (such as penalties for not complying with standards) or other fees that help fund the program
- Stating the existence of subsidies for communities who participate in NFIP or who comply with minimum risk management standards (as this does not clearly distinguish communities that go above and beyond basic flood management guidelines from those that do)

| **FALL 2018 EXAM 6US, QUESTION 7** | |
|---|---|
| **TOTAL POINT VALUE: 2.75** | **LEARNING OBJECTIVE: B1, B2** |
| **SAMPLE ANSWERS** | |
| **Part a:** 1.50 points | |

- **Assigned Risk Plans** - Voluntary market rejects high-risk drivers. All auto insurers doing business in the state are assigned their proportionate share of high-risk drivers based on the total volume of auto insurance written in the state.
- **JUAs** – Voluntary market rejects high-risk drivers. Agents/brokers forward application to the JUA or to a designated servicing insurer.