



FEMA

W-14058

November 20, 2014

MEMORANDUM FOR: Write Your Own (WYO) Company Principal Coordinators and the National Flood Insurance Program (NFIP) Servicing Agent

A handwritten signature in cursive script, appearing to read "James A. Sadler".

FROM: James A. Sadler, CPCU, AIC  
Director of Claims  
Federal Insurance and Mitigation Administration

SUBJECT: Clarification on: 1) Application of the Dwelling Form Loss Settlement Clause; 2) Use of Flood Insurance Claims Proceeds; and 3) FEMA's Underwriting and Claims Operation Review Tool (U-CORT)

This Bulletin addresses the application of the Loss Settlement Clause of the Standard Flood Insurance Policy (SFIP) Dwelling Form, 44 C.F.R. Part 61, App. A(1), § VII(V). Specifically, it explains the application of the Loss Settlement Clause to the settlement of claims when there is direct physical loss by or from flood to the policyholder's insured property.

The Loss Settlement Clause sets forth three methods of settling insured losses: Replacement Cost Loss Settlement, Special Loss Settlement, and the Actual Cash Value Loss Settlement. This Bulletin addresses the application of the Replacement Cost Loss Settlement and Actual Cash Value Loss Settlement provisions.

#### Replacement Cost Loss Settlement

For dwellings that qualify for the Replacement Cost Loss Settlement, the NFIP will pay to repair or replace the damaged dwelling, after applying the deductible but without deducting the value of its physical depreciation, in an amount equal to either:

- (1) The limit of liability for building coverage as shown on the policyholder's Declaration Page;
- (2) The replacement cost of that part of the dwelling that was damaged, with materials of like kind and quality, and for like use; or
- (3) The necessary amount actually spent to repair or replace the damaged part of the dwelling for like use.

Applying this provision, the NFIP will pay the least of those three amounts.

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Questions related to the Replacement Cost Loss Settlement provision often relate to eligibility for additional payment after repairs and initial payment has been made based on an estimate of replacement cost, and a policyholder seeks additional payment based on the actual cost of repairs. The policyholder is eligible for payment based on actual costs, and the NFIP insurer will need documentation of the actual costs in order to make the additional payment. FEMA will require actual receipts, paid bills, paid invoices, cancelled checks and the like to support payment. If repairs have been completed, it is the policyholder's responsibility to prove that the claim amounts paid plus the value of the deductible(s) and any applicable physical depreciation were spent to repair or replace covered flood damage.

### Actual Cash Value Loss Settlement

Buildings that are not eligible for the Replacement Cost Loss Settlement provision are treated under the Actual Cash Value Loss Settlement provision, which provides compensation based on "[t]he cost to replace an insured item of property at the time of loss, less the value of its physical depreciation" and less the policy deductible.

Significantly, the Actual Cash Value Loss Settlement provision does not provide for a separate and distinct method to calculate the amount of the loss—it only provides a different approach to compensate for the loss. This principle appears to have caused confusion and requires clarification. **If the damage has not been repaired**, the amount of the loss is determined by the adjustment based on principles set forth in the Standard Flood Insurance Policy, other guidance, and on the supported and verifiable estimate prepared by the adjuster and, when available, receipts, and other data showing the estimated cost of repair to further support the adjuster's estimate. **If repairs have been completed**, it is the policyholder's responsibility to prove that the amounts paid on the claim plus the value of the deductible(s) and any applicable physical depreciation<sup>1</sup> were spent to repair or replace covered flood damage. This only can be done by presenting receipts, paid bills, paid invoices, and canceled checks. The amount of loss cannot be determined on an estimate that is not fully supported by the proof discussed above. Any part of a claim or estimate not fully supported by documented proof cannot be presented for payment—statements without supporting documentation are insufficient to justify payment of NFIP funds. The NFIP insurer may hire CPAs or other financial experts to calculate the amount actually spent plus the value of the deductible(s) and applicable depreciation. Only once the value of the loss has been determined, either with receipts documenting repairs and/or a contractor's estimate of new damage that has not yet been repaired but has been verified, can the NFIP insurer calculate the replacement cost or actual cash value loss additional payment, as appropriate. The starting point for either methodology of calculating the settlement amount is the same—the replacement cost of flood damaged insured property with no deduction for the deductible and applicable depreciation. Under the Replacement Cost Loss Settlement provision, no deduction for the value of physical depreciation<sup>1</sup> is applied to the amount of loss, although the deductible is applied. Under the Actual Cash Value Loss Settlement provision, the amount of loss is reduced by both the value of physical depreciation and the applicable deductible(s). This process is consistent with the SFIP's "Our Options After a Loss" clause, 44 C.F.R. Part 61, App. A(1), § VII(K) and (V).

<sup>1</sup>SFIP Dwelling Form, Section VII, V.4 list the types of property that are always settled at Actual Cash Value regardless of the applicable Loss Settlement provision. Notably, the list includes appliances, carpets, and carpet pads, outdoor awnings, outdoor antennas or aerials, and other outdoor equipment.

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A second issue also needs clarification. Where repairs have been made before a request for additional payment is submitted, the NFIP Insurer must determine that funds previously provided were spent to make repairs and that the supplemental request does not duplicate the prior payment. Once payment is made to the policyholder, the NFIP has no control over the use of the funds. The policyholder may use the funds to repair the covered loss, repair losses that are not covered by the SFIP, or for any other use. Also, the deductible and any applicable depreciation are the responsibility of the policyholder and cannot be reimbursed as a part of any additional payment(s). Accordingly, a policyholder's lack of funds to complete repairs does not *per se* show an underpayment. To be eligible for additional NFIP payment, the policyholder must document that funds previously paid were used to repair or replace covered damage and must show with specificity that additional funds to repair covered damage are required. The NFIP insurer should carefully review the evidence of actual loss, together with paid receipts, paid invoices, canceled checks, and other evidence of payment for repairs, to ensure that the insured is not seeking duplicate payments, payment for uncovered losses, or the values of applicable depreciation and the deductible(s) in a request for additional payment.

A third issue that requires clarification is the appropriate use and representation of FEMA's Underwriting and Claims Operation Review Tool (U-CORT) and the meaning of recent revisions to the U-CORT template. U-CORT is a computer-based program designed to document information for operational reviews that is also used for the granting of a waiver of the SFIP's time requirement for policyholders to send the Proof of Loss to their NFIP insurer. The NFIP Insurer documents the basis for a request for a waiver through the use of U-CORT, thus facilitating the expeditious resolution of claims. The revisions to the FEMA U-CORT template merely asks and reminds NFIP insurers of factors they already evaluate during the claim process and prior to making the waiver request.

Any questions or comments should be directed to Russell M. Tinsley, AIC. Mr. Tinsley's email address is [Russell.Tinsley@fema.dhs.gov](mailto:Russell.Tinsley@fema.dhs.gov).

Once again we ask for your cooperation.

cc: Vendors, Government Technical Representatives, IBHS