MORTGAGE BANKERS ASSOCIATION

April 24, 2019

Commissioner David Altmaier, Chair
Lender-Placed Insurance Model Act (C) Working Group
National Association of Insurance Commissioners
1100 Walnut Street, Suite 1500
Kansas City, MO 64106-2197

Re: Proposed Real Property Lender-Placed Insurance Model Act

Dear Commissioner Altmaier:

The Mortgage Bankers Association (MBA)[1] has been following the National Association of Insurance Commissioners' work on revisions to a Real Property Lender-Placed Insurance Model Act (the "Model Act") in the course of working with our member companies as well as other financial services trade organizations. We understand that the issue of "insurance tracking" has been a topic of considerable discussion among members of the working group and are concerned about certain incorrect assertions that may have been made regarding a mortgage servicer's responsibility for "insurance tracking" functions.

To clarify, mortgage servicers do not have responsibility for insurance tracking and, consequently, they are not compensated for performing this function. Mortgage servicers are required to ensure continuous insurance coverage on the loans they service. They fulfill this requirement by purchasing a lender placed insurance (LPI) policy that provides automatic and continuous insurance coverage for all properties within the servicer's portfolio. Accordingly, the LPI insurer must monitor coverage at all times to be able to provide automatic coverage upon any lapse. "Insurance tracking", therefore, is performed by LPI carriers as part of their basic insurance underwriting and exposure management processes.

[1] The Mortgage Bankers Association (MBA) is the national association representing the real estate finance industry, an industry that employs more than 280,000 people in virtually every community in the country. Headquartered in Washington, D.C., the association works to ensure the continued strength of the nation's residential and commercial real estate markets, to expand homeownership, and to extend access to affordable housing to all Americans. MBA promotes fair and ethical lending practices and fosters professional excellence among real estate finance employees through a wide range of educational programs and a variety of publications. Its membership of over 2,300 companies includes all elements of real estate finance: mortgage companies, mortgage brokers, commercial banks, thrifts, REITs, Wall Street conduits, life insurance companies, and others in the mortgage lending field. For additional information, visit MBA's Web site: www.mba.org.

MORTGAGE BANKERS ASSOCIATION

In its recent letter to you dated April 4, 2019, the American Bankers Association (ABA) also raised these issues. We support ABA's letter and share its concerns. The ultimate goal of any LPI Model Act is to ensure fair and consistent treatment of consumers. We support this goal and are concerned, that it may be undermined if the Model Act fails to accurately reflect the roles and responsibilities of mortgage servicers versus insurance carriers.

We appreciate your consideration of these important issues. Please feel free to reach out to me at ssinghas@mba.org or 202-557-2826 if you have any questions or if you need additional information.

Sincerely,

Sara Singhas
Director, Loan Administration
Residential Policy & Member Engagement
Mortgage Bankers Association

Sarah Ferman
Senior Government Relations Representative
P: 202-663-5510
sferman@aba.com

April 4, 2019

Commissioner David Altmaier, Chair
Lender-Placed Insurance Model Act (C) Working Group
c/o Aaron Brandenburg
National Association of Insurance Commissioners
1100 Walnut Street, Suite 1500
Kansas City, MO 64106-2197

Re: Proposed Real Property Lender-Placed Insurance Model Act

Dear Commissioner Altmaier:

The *American Bankers Association* ("ABA") appreciates the opportunity to provide subject matter expertise and input on certain aspects of the Real Property Lender-Placed Insurance Model Act (the "Model Act"), as set forth by the Lender-Placed Insurance Model Act Working Group (the "LPI Working Group"), as they relate to mortgage servicing.

The American Bankers Association is the voice of the nation's $18 trillion banking industry, which is composed of small, regional, and large banks that together employ more than 2 million people, safeguard nearly $14 trillion in deposits, and extend more than $10 trillion in loans.

Given the importance of lender-placed insurance ("LPI") in the mortgage lending servicing industry, the ABA has reviewed the draft Model Act that was exposed August 28, 2018 and the comments and documentation provided by the District of Columbia, State of California, the joint industry trade organizations[1] and the Center for Economic Justice. ABA has significant expertise on mortgage lending and servicing and a full understanding of lenders' and servicers' duties. The ABA believes it is important to clarify certain aspects of a lender/servicer's obligations and explain the Model Act's effect, whether intentional or not, on mortgage loan servicers and the mortgage loan market.

The ABA understands that certain interested parties have represented that mortgage servicers are paid by mortgage loan owners/investors for "insurance tracking" and that "insurance tracking" is the sole duty of mortgage servicers. This is simply not the case. Fannie Mae and Freddie Mac, the two largest investors in mortgage loans, have published Servicing Guidelines which address insurance coverage on property securing mortgage loans owned by such investors. While both Servicing Guidelines *require* that mortgage servicers ensure ***continuous insurance coverage*** is in place at all times to protect the investors' interest, the Servicing Guidelines ***do not*** specify how this is to be done and do not require tracking of insurance within a mortgage pool. Private secondary mortgage market investors' requirements generally follow the Guidelines.[2]

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[1] More specifically, the American Bankers Association, American Insurance Association, Consumer Credit Insurance Association, The Council of Insurance Agents & Brokers, and the Property Casualty Insurers Association of America (the "Joint Industry Trades").

[2] Fannie Mae 2006 Servicing Guide II, Chapter 6.; Fannie May Single Family 2011 Servicing Guide, Chapter 6, page 206-1 (same); *see also* Freddie Mac Single Family Seller/Servicer Guide § 58.2(a), requiring the seller/servicer to ensure adequate coverage is in force at all times; and § 58.9: "The Servicer

As a result, lender-placed insurance coverage acquired by mortgage servicers is structured to meet this continuous coverage requirement, which is often met through a variety of contractual arrangements between the mortgage servicer and LPI carriers and providers. Under these arrangements, in the event of a lapse in coverage of the existing property insurance, the LPI insurer immediately assumes all risk of loss to the secured property whether or not the lapse is known to the servicer or the LPI insurer. This ensures that continuous coverage is maintained for the servicer's entire loan portfolio as required by the Servicing Guidelines and facilitates the securitization of mortgages in the secondary market. As a result, in the event any secured property in the portfolio suffers a covered loss at any time during the contract term, property insurance is in place, even if the borrower has failed to provide required coverage for the secured property.

A historical perspective may be useful in eliminating the notion that an LPI carrier has the sole responsibility for "insurance tracking." In decades past, the servicing industry endeavored to meet the continuous coverage requirement by leveraging transactional history at the loan level with poor results. The most common method was for servicers to leverage escrow payment and RESPA-derived records and then report to an LPI carrier any specified exposures in hopes of securing coverage. However, the LPI carriers quickly came to the realization that servicers' methods were underrepresenting exposures.

The solution to the aforementioned was for LPI carriers to work with lenders and their data to fully identify all exposures themselves more accurately and efficiently, thereby making them more willing to provide the LPI coverage and at rates that reflected their ability to collect premium on all exposures, rather than just a disproportionate number of losses. In all scenarios tracking of the insurance is only a mechanism. The servicer's obligation is *solely* to ensure there is coverage and has the right to decide how to effectuate such.[3] In effect, Servicers hold and have no risk of property loss on those loans eligible and required for coverage.

A servicer is not compensated by investors for "insurance tracking." A servicer is solely tasked with ensuring that any collateralized property maintains adequate property insurance to cover damage from unforeseen casualty losses.[4] As stated, servicers contract with LPI carriers to transfer all risk of loss. Any associated "insurance tracking" under these types of arrangements is the responsibility of the LPI carrier to

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must follow up to verify that adequate coverage has been obtained ***and remains in force***. If the Borrower does not or cannot obtain such coverage, the Servicer must do so." (emphasis added).

[3] Fannie Mae Servicing Guide A2-1-01: General Servicer Duties and Responsibilities (07/12/2017) states: "Most of the policies and standards described in the Servicing Guide are intended to set forth the broad parameters under which the servicer must exercise sound and professional judgment as a mortgage loan servicer in the performance of its duties. As a result, *in most instances Fannie Mae has not set forth absolute requirements* because it believes that the servicer needs to maintain the discretion to apply appropriate judgment in dealing with borrowers and mortgage loans on a case by case basis, consistent with Fannie Mae's servicing policies. Further, even where Fannie Mae has set forth a "requirement," it has not enumerated *specifically how the servicer should implement it*…."

[4] Fannie Mae Servicing Guide A2-1-01: The Servicing Guide goes further in detailing: "In performing the services and duties incident to the servicing of mortgage loans, the servicer must take whatever action necessary to protect the beneficial interest of Fannie Mae and an MBS trust in the security property as long as it is authorized to do so by the terms of the mortgage loan. Among other things, this generally includes, but is not limited to: … maintaining adequate property insurance to cover damage from unforeseen casualty losses."

undertake for the managing of its own risk and reporting obligations. Once Servicers have complied with the Fannie Mae and Freddie Mac continuous coverage requirements through contracting with an LPI carrier, Servicers are not required to do tracking, nor is tracking something they are compensated for. Any position to the contrary is unsupported by the realities of the marketplace and current requirements.

Again, the ABA is appreciative of the opportunity to respond to provide input regarding the impact of the LPI Model Act on servicers. We hope that this letter provides clarity, and we stand ready to discuss further if requested.

Sincerely,

Sarah Ferman

Sarah Ferman
Senior Government Relations Representative
American Bankers Association

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April 30, 2018

Commissioner David Altmaier, Chair
Lender-Placed Insurance Model Act (C) Working Group
c/o Aaron Brandenburg
National Association of Insurance Commissioners
1100 Walnut Street, Suite 1500
Kansas City, MO 64106-2197

Re: Real Property Lender-Placed Insurance Model Act (January 29, 2018 Draft) – *Comments* of the *Industry Trade Associations*

Dear Commissioner Altmaier:

The *American Bankers Association*, the *American Insurance Association*, the *Consumer Credit Insurance Association*, *The Council of Insurance Agents & Brokers*, and the *Property Casualty Insurers Association of America* (collectively "Industry") write to support the January 29, 2018 draft of the Real Property Lender-Placed Insurance Model Act (the "Model Act"), as set forth by the Lender-Placed Insurance Model Act Working Group (the "LPI Working Group").

The Model Act reflects several years of regulatory diligence by the NAIC on behalf of state insurance regulators, primarily demonstrated via the recently concluded multistate market conduct examinations and associated Regulatory Settlement Agreements (the "Multistate") of certain real property lender-placed insurers ("LPI Insurers"). The Multistate included 50 subscribing jurisdictions and was the culmination of more than two years of regulatory examination, substantial inquiry, thoughtful consideration, and lengthy communication between regulators and LPI Insurers. At the same time, there are other writers of lender-placed insurance ("LPI"), with smaller market shares, that did not participate in the negotiation of the Multistate terms, upon which the Model Act is largely based, and who find some of the terms unduly

burdensome. The Industry supports the direction of the Model Act, as it codifies and clarifies existing regulatory parameters that state regulators believe are necessary mainly to protect consumers, but also to protect the viability of the real property LPI market. But the Industry equally urges the Working Group to consider the concerns of smaller writers and the opportunity for new market entrants so that the Model Act does not lead to further contraction of the LPI market.

The Center for Economic Justice ("CEJ") provided comments on the Model Act dated March 9, 2018 (the "CEJ Model Additions"), which as proposed would reverse the already established industry practices set forth in the Multistate. While the CEJ purports to represent the interest of consumers, we believe the CEJ's Additions would serve only as a detriment to consumers. The CEJ Additions also incorrectly attempt to regulate mortgage servicers. Mortgage servicers are subject to the jurisdiction of state and federal banking laws, associated regulators and the Consumer Financial Protection Bureau ("CFPB"), as detailed below. It should not be the intent of the Model Act to supplant that framework and regulate mortgage servicers.

The Industry has been actively involved in the discussions conducted with both the LPI Working Group (since its inception) and the former Creditor-Placed Insurance Model Act Working Group ("CPI Working Group"). The Industry supports the LPI Working Group's decision to create the Model Act instead of modifying the Creditor-Placed Insurance Model Act to include real property. The Industry notes that the CEJ Additions run contrary to that decision and incorrectly modify the Model Act to include personal property and other concepts that are inapplicable to a model act intended solely to apply to real property.

The Industry incorporates by reference its June 2, 2017 letter submitted to the CPI Working Group, attached hereto as an exhibit, which addressed many of the same points discussed throughout this letter. In addition to the comments previously provided, we offer the following for the LPI Working Group's consideration:

I. <u>The Model Act Should Apply Strictly to Real Property and Related Mortgages.</u>

The Model Act correctly reflects its applicability to real property and related mortgages only, which the Industry strongly supports. The CEJ Additions attempt to circumvent the LPI Working Group's decision to bifurcate the CPI Model Act and the Model Act by seeking to: (i) add vehicles and personal property to the Model Act by including them in the definition of "Individual Lender-Placed Insurance," (ii) include manufactured and mobile homes in the Scope, and (iii) refer to credit transactions instead of mortgage transactions. The Industry reasserts its support for the bifurcation of personal and real property and stands behind the LPI Working Group's determination to create a new model act solely concerning real property, to avoid the potential problems described in detail in Industry's June 2, 2017 letter.

II. <u>Regulation of Servicers and Disclosures to Mortgagors Should Not Be Included.</u>

The Model Act correctly reflects its applicability only to LPI Insurers and does not include mortgage servicers as a regulated party. Mortgage servicers fall within a robust and complex regulatory structure, under the purview of both federal and state law and banking and mortgage

regulations. The 2010 Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank"), under Section 1463(a), established a number of requirements for servicers regarding LPI.

Since 2013, the CFPB has issued six major rulemakings to implement Dodd-Frank that govern servicing practices. The rules are comprehensive and apply to payment crediting, periodic statement requirements, error resolution, information requests, LPI, communications with delinquent borrowers (including successors in interest), loss mitigation, and other items. These rules are still being developed today. The new CFPB regulations are detailed and meticulously engineered, and any layering of additional requirements could complicate the provisions or spoil balances built into current federal provisions.

As part of this significant regulatory development, Dodd-Frank amended Section 6 of the Real Estate Settlement Procedures Act of 1974 ("RESPA") to establish new servicer duties with respect to servicers' purchase of LPI on a property secured by a mortgage loan. Additionally, Dodd-Frank created the CFPB to implement and enforce compliance with consumer financial laws. In February 2013, the CFPB issued its final rule implementing Mortgage Servicing Rules under RESPA, adopting a new regulation, 12 C.F.R. § 1024.37. The regulation focuses on the relationship between the servicer and the borrower with respect to specific requirements the servicer must follow to ensure there is a reasonable basis to place LPI, including multiple notices to consumers subject to standards set forth by the CFPB. The content of such notices would be inappropriate to modify in a model act and would create uncertainty and confusion.

III. The Model Act Correctly Excludes "Insurance Tracking."

The Model Act correctly excludes "insurance tracking" (exposure management) from its scope, as insurance tracking was omitted from the Multistate. The industry firmly believes that exposure management – accomplished through insurance tracking, *i.e.*, determining which properties within a servicer's portfolio lack borrower obtained insurance coverage and are, therefore, insured by the LPI Insurer – should be performed by LPI Insurers on their own behalf to diligently manage their own exposure. As the LPI Working Group is aware, LPI has no underwriting – accepting all appropriate risk within a servicer's portfolio – and, therefore, must manage its exposure to ensure it maintains proper capital reserves, surplus, and reinsurance, as well as to meet other statutory filing requirements via insurance tracking. The omission of "insurance tracking" is a key element that the Industry believes is necessary to the adoption of the Model Act.

IV. The Model Act Should Not Address Loss Ratios.

The Model Act includes a mandatory rate refiling provision for an annual loss ratio of less than 35 percent in any line of real property LPI experienced by an LPI Insurer for two consecutive years. Although larger participants agreed to this after lengthy consideration in the Multistate and believe it is a representation of a fair annual loss ratio for a catastrophe-

exposed insurance line, the threshold may be too high for a small writer of LPI, which would barely be able to make up for its years with poorer loss experience.

As a result, a loss ratio threshold should not be included in the Model Act. Each state has its own methodology for evaluating rates and should evaluate rates on a case-by-case basis, as they do for all other lines of business. Any loss ratio threshold chosen would be artificial. As far as we know, no other line of property insurance is subject to a loss ratio threshold. LPI should not be treated differently than other property lines.

If a threshold is included, the loss ratio threshold should be reduced to 20 percent to accommodate smaller carriers (or be applicable only at a premium threshold), and the term loss ratio should be defined. For example, the Model Act should define what is included in a loss ratio such as ALAE, reinsurance costs, actuarially based uncertainties, or catastrophe loads.

The LPI Working Group's proposal for a four year period in which a LPI Insurer must re-file real property LPI insurance rates is also consistent with the terms of the Multistate. The Model Act also includes language mandating that LPI programs and rates be filed (not necessarily approved) with State Commissioners, which affords the states the right to manage such filings in accordance with their rating laws, *i.e.*, file and use, file and approve, etc.

V. Single Interest Insurance Is Preserved; The Model Act Should Distinguish Single Interest and Dual Interest Insurance Policies.

The CEJ suggests that single interest insurance should be prohibited. The Industry cannot disagree more. LPI is not a homeowner's insurance product and is not intended to be. LPI is purchased by lenders to protect their property interest in response to a borrower's breach of contract and in lieu of lenders' other available remedy: foreclosure and eviction of the homeowner.

The impact of the Model Act should not be to reduce the availability of LPI sought by lenders to protect their interests. If single-interest insurance is prohibited, lenders will no longer have the ability to purchase a viable single-interest insurance product in the admitted market that meets their insurance needs, in order to protect their interests. Without single-interest insurance, in the event of contractual non-compliance with the loan conditions by the borrower, the lending institution may seek to remove its risk of uninsured collateral via foreclosure.

VI. The Model Act Should Consider the Burden of Reporting in Addition to MCAS Reporting.

The new MCAS reporting, coupled with new reporting in each state on an individual state and countrywide basis as contemplated in Section 9.E., makes being in this market segment increasingly burdensome and may discourage new entrants. The Industry suggests the Working Group consider whether the reporting required under the Model Act is duplicative

of information that will be gleaned through MCAS and, to the extent this may be, that those requirements be removed from the Model Act. Further, the reporting threshold in Section 9.E. should apply only when an insurer has premiums in excess of $500,000 in a state in the prior calendar year.

VII. Implementation Expenses are Necessary to Ensure a Competitive LPI Market

The Model Act appropriately includes the reimbursement of certain implementation expenses, which is aligned with regulators' goals. The reimbursement of implementation expenses increases competition by removing barriers to entry for smaller LPI Insurers and allows servicers to switch to other LPI participants by removing a primary obstacle: the cost of changing LPI Insurers. This alleviates the possibility of a servicer being "locked in" to a certain LPI Insurer because of the burdensome costs of changing LPI Insurers and their programs. Along similar lines, the LPI Working Group should be careful not to inadvertently restrict other consumer-beneficial components provided by LPI market participants, such as brokers, in the Model Act. These components, such as compliance advice, catastrophe updates, claims advocacy, and premium benchmarking, are generally provided at a *de minimis* cost or as a value add, similar to all other insurance markets, and all benefit the consumer.

VIII. Private Causes of Action and Increased Penalties are Unnecessary

The Model Act appropriately excludes any rights of private causes of action and includes the standard penalties from other NAIC Model Acts. The right to a private cause of action is not included in existing NAIC Model Acts, and there is no indication that this has discouraged litigation regarding real property LPI in the past. The Model Act aptly includes penalties that are consistent with those in other NAIC Model Acts.

IX. Term of Insurance Coverage

The Model Act addresses how the effective dates for LPI coverage should be set. Other comments received on this issue appear to be a solution in search of an issue that does not appear to exist.

X. The CEJ Additions

The CEJ Additions include inflammatory rhetoric that has no place in a model act under consideration by the NAIC and is counterproductive to a reasoned discussion of the issues. For example, pejorative terms like "kickbacks" and "reverse competition," for which there is no evidence in the LPI industry, are used in place of meaningful language a state legislature can duly consider. The Multistate addressed all perceived abuses, which the CEJ Additions refuse to acknowledge.

Again, the Industry appreciates the working group's diligent efforts to craft the Model Act and urges the LPI Working Group to move forward with the Model Act, as amended to consider Industry's feedback, as it includes the prescriptive measures that are appropriate for the

protection of consumers and the viability of the LPI market, and it addresses concerns of smaller participants not included in the Multistate. The Model Act is the culmination of laborious efforts by much of the industry and regulators and a reflection of existing best practices, which benefit consumers and help promote a healthy real property LPI market.

[Signatures on next page.]

Attachment

Sincerely,

Lisa Brown
Assistant General Counsel &
Director, Compliance Resources
American Insurance Association

Tom Keepers
Executive Director & EVP
Consumer Credit Industry Association

Sarah Ferman
Sr. Gov't Relations Representative
Bank Insurance Council
American Bankers Association

John P. Fielding
General Counsel
The Council of Insurance Agents & Brokers

Robert W. Woody
Vice President, Policy
Property Casualty Insurers Association of America

June 2, 2017

Commissioner David Altmaier, Chair
Creditor-Placed Insurance Model Act Review Working Group
c/o Aaron Brandenburg
National Association of Insurance Commissioners
1100 Walnut Street, Suite 1500
Kansas City, MO 64106-2197

Re: Creditor-Placed Insurance Model Act (April 17, 2017 Draft) Comments of the *Property Casualty Insurers Association of America, American Insurance Association, Consumer Credit Industry Association, and The Council of Insurance Agents & Brokers*

Dear Commissioner Altmaier:

The Property Casualty Insurers Association of American, the American Insurance Association, the Consumer Credit Industry Association, and The Council of Insurance Agents & Brokers (collectively "Industry") write to oppose the April 17, 2017 draft of the Creditor-Placed Insurance ("CPI") Model Act (the "Model Act") to incorporate real property lender placed insurance ("LPI") into the Model Act.

The significantly revised draft of the Model Act would harm many mortgage borrowers by increasing mortgage costs. While the Model Act focuses on insurance companies and producers involved in providing CPI and does not apply to lenders, to the extent it applies to residential mortgage loans and LPI coverage, it could adversely affect the *credit* relationship between mortgage servicers and borrowers by, among other things, altering the process CPI and LPI insurers have used to manage risk on an insurance product that is not underwritten. Affected mortgage originators and servicers would have to take on insurance tracking, a task that is more appropriate for LPI insurers, and which would be to the detriment of consumers as detailed below.

Industry has been actively involved in the numerous discussions conducted by the Creditor-Placed Insurance Model Act Review Working Group over the last several years in support of efforts to revise the Model Act, and good progress was being made; so we were very surprised to see that the new draft represents such a

significant departure in several ways from earlier drafts. Based on those discussions, we had believed it was possible to broaden the scope of the existing Model Act, which applies only to CPI placed on personal property loans, to include LPI placed on residential mortgage loans. But after reviewing the new draft of the Model Act, we do not believe that is possible. The new draft reveals that the issues involving LPI placed on residential mortgage loans differ significantly from those involving CPI placed on personal property loans as we demonstrate through the Industry comments to the April 17, 2017 draft in this letter, as well as the attached Industry redline version of the draft with its accompanying memorandum. Therefore, we recommend that the Working Group leave the scope of the CPI Model Act to auto and personal property loans, and begin anew with a separate draft of the Model Act that would govern LPI on residential mortgage loans.

We are specifically concerned with how the new draft of the Model Act addresses insurance tracking costs and the limitations on the coverage amount for LPI. We also are concerned about how the new draft addresses contingent commissions on LPI and the Model Act's applicability to blanket insurance, as well as several other issues.

I. Background

A. The Need for LPI Connected to Residential Mortgage Loans and How LPI Works

The nature of the mortgage market is such that mortgage lenders and the companies they, or investors, retain to service the loans – servicers – are obligated to ensure that the collateral securing a mortgage loan is *at all times*[1] adequately insured against the risk of loss. (The term "mortgage lender" refers to the loan originator, or to the holder of the loan if it is sold, and the term "servicer" refers to the entity responsible for servicing the loan.[2] Sometimes the mortgage lender and the servicer are one in the same. For purposes of this comment letter, we refer to both merely as "servicers.") A mortgage loan agreement[3] requires a borrower to continuously maintain hazard insurance on a residence (referred to as borrower-obtained insurance, or "BOI"). If the borrower fails to do so, the mortgage loan agreement permits the servicer to buy substitute insurance so the servicer can maintain required insurance, which the servicer does by arranging for LPI coverage

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[1] *Fannie Mae Single Family Servicing Guide*, Part II, Chapter 6, states: "Part of a servicer's responsibility for protecting Fannie Mae's interest in the security property is to ensure that hazard insurance (including flood insurance), under the terms specified in Fannie Mae's Guides, is in place at all times."

[2] The Real Estate Settlement Procedures Act, RESPA, defines the term "servicing" to mean "receiving any scheduled periodic payments from a borrower pursuant to the terms of any loan, including amounts for escrow accounts described in section 10 [12 U.S.C. § 2609], and making the payments of principal and interest and such other payments with respect to the amounts received from the borrower as may be required pursuant to the terms of the loan." 12 U.S.C. § 2605(i)(3).

[3] More specifically, the security instrument that spells out the duty to maintain coverage.

– thus satisfying the servicer's obligation to have insurance in place on the property at all times.

To effect substitute coverage where needed,[4] in most states the servicer obtains LPI in the form of a master policy in the name of the servicer (that is, the servicer is the named insured), with individual certificates being issued to the borrowers to cover each insured property. The borrower is contractually bound by the mortgage agreement to reimburse the mortgage lender for premiums the lender pays for LPI coverage. And the mortgage lender's interest in the property is co-extensive with that of the borrower; the mortgage lender and investor and the borrower have an interest in having a damaged structure rebuilt to pre-loss status, and all of the parties have the right to file a claim under the LPI policy up to the coverage limits as provided under the policy. This is an obvious benefit to the consumer and the general public; if not for the LPI policy, a loss would be uninsured, which would lead to unrepaired properties (which often become a public nuisance and a safety concern).

B. How LPI is Regulated

The requirement that a servicer maintain hazard insurance on loan collateral, in combination with the related contractual obligation for a borrower to maintain hazard insurance, implicates both mortgage servicing laws and state insurance laws in a unique way. So we now examine the two regulatory regimes involved.

Generally speaking, two groups of regulators are involved in the regulation of LPI on residential mortgages. First, because LPI is an insurance product, each individual state insurance department regulates the terms of the LPI product as well as the insurers and producers involved in placing the product. The Model Act recognizes this state involvement.

Second, because LPI is written in connection with the extension of credit for personal, family or household purposes, the Consumer Financial Protection Bureau, via Regulation X,[5] regulates servicers' activity in placing LPI. Regulation X implements much of the Real Estate Settlement Procedures Act,[6] as do the federal financial services regulators (Federal Reserve Board, the Federal Deposit Insurance Corporation, the Office of the Comptroller of the Currency, National Credit Union Administration and the Farm Credit Administration) to some extent. In other words, the focus of the consumer credit regulator is on the mortgage loan

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[4] For clarity, servicers are required to ensure coverage is in place on all properties at all times. To accomplish that, servicers contract with insurance companies to provide coverage on their entire portfolio via automatic issuance. Since the insurance company assumes the risk on the servicer's entire portfolio upon contract execution, the insurance company needs to manage that risk via the exposure management process.

[5] 12 C.F.R. § 1024.37.

[6] 12 U.S.C. Ch. 26.

agreement between the mortgage lender and the borrower, which includes the borrower's obligation to maintain required insurance and the servicer's obligation to place LPI only when all borrower protections have been satisfied.

There should be very little overlap between the two regulatory regimes.

1. State Regulation of LPI Insurers and Producers

The existing CPI Model Act states that it applies to "an insurer or producer transacting creditor-placed insurance as defined in this Act" (Sec. 2(A) of the Model Act); *generally, it does not apply to lenders*. Thus, the Model Act focuses on the terms of the CPI product, how it is offered, and how it is paid for. Specifically:

- Section 4 of the Model Act establishes the term of a CPI policy – when CPI coverage can first become effective, and the date by which coverage must terminate.
- Section 5 restricts the amount of coverage on which CPI premium calculations can be based.
- Section 6 prohibits CPI from covering certain types of risks.
- Section 8 lists the parameters to be used in approving CPI rates.
- Section 9 requires a CPI insurer to refund unearned premiums.
- Section 10 sets forth the parameters for claims payments.
- Section 11 lists the requirements for the servicer (the master policyholder) to be able to seek reimbursement from the borrower for CPI premiums.
- Section 12 discusses remittance of premiums and commissions.
- Section 13 requires the mortgage lender to provide the borrower with certain disclosures.

2. CFPB Regulation of Servicers

The 2010 Dodd-Frank Act established certain requirements on servicers regarding CPI. It focuses on the relationship between the servicer and the borrower. The newly formed Consumer Financial Protection Bureau ("CFPB") was granted the authority to regulate mortgage lenders and servicers with respect to CPI.[7] CFPB regulations provide that a "servicer may not assess on a borrower a premium charge *or fee related to [CPI]* unless the servicer has a reasonable basis to believe that the borrower has failed to comply with the mortgage loan contract's requirement to maintain hazard [homeowner's] insurance."[8] Additionally, "all charges related to [CPI] assessed to a borrower by or through the servicer must be bona fide and reasonable." "A bona fide and reasonable charge is a charge for a service actually performed that bears a reasonable relationship to the servicer's cost of providing the service, and is not otherwise prohibited by applicable law."[9]

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[7] See 12 U.S.C. § 2605.
[8] 12 C.F.R. § 1024.37(b).
[9] 12 C.F.R. § 1024.37(h).

The distinction between the two regulatory approaches – a state insurance department for the LPI product and insurance producers, and the CFPB for the placement of LPI with respect to a specific property – is important when considering how the Model Act should address insurance tracking costs, limitations on the coverage amount for LPI, contingent commissions on LPI, and the Model Act's applicability to blanket insurance.

II. Analysis and Recommendations

A. Insurance Tracking Costs Should Continue to be Included in the Calculation of LPI Premium Rather than Being Passed on to the Servicer.

Insurance tracking costs should continue to be used to calculate LPI premiums for two reasons: First, because of a critical distinction between the servicer's role and that of the LPI insurer with respect to LPI coverage, *the servicer has no need to actually track insurance coverage, while the LPI insurer must do so to manage its own outstanding risk*. Second, if tracking costs are not permitted to be included in the calculation of LPI premium, the LPI insurer will pass the cost onto the servicer[10] and potentially on to consumers in connection with future originations via various fees and points. Even though servicers cannot require borrowers to pay for LPI premiums and related costs, including tracking costs, servicers will need to increase their pricing structure for borrowers to account for the added costs of either performing tracking or outsourcing it to a third party other than the LPI insurer.

1. *A LPI Insurer Needs Tracking Information to Manage its own LPI Risk, as Exposure Management (i.e., Insurance Tracking) is a Direct Substitute for Standard Market Underwriting.*

The actors in the secondary mortgage market – private mortgage investors, Fannie Mae, and Freddie Mac – require the servicer to ensure hazard insurance is in place at all times, and the servicer obtains LPI coverage to satisfy that requirement.

The master LPI policy provides that insurance coverage begins immediately upon the lapse of borrower-obtained insurance ("BOI"), called "automatic issuance"; consequently, the servicer can be confident it has satisfied its insurance obligation to the mortgage investor once it buys the LPI policy. The servicer need do nothing else, because whether or not it chooses to track BOI, every property in the portfolio will be covered – either by BOI, or by LPI insurance automatically upon the lapse of BOI. *There will be no lapse in coverage, which, as laid out above, is to the benefit of the consumer and the general public*.

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[10] Which will undoubtedly harm servicers, especially small servicers, because it will increase their costs.

On the other hand, the LPI insurer must track insurance coverage to prudently manage its own risk (especially considering the broad and unknown risk that exists with automatic issuance), and it has the systems in place to do so. To ensure hazard insurance is in place at all times, LPI insurers commit to a servicer to provide *automatic, sight-unseen, continuous* insurance coverage for all uninsured properties – those where BOI coverage has lapsed – within the servicer's portfolio. These are properties whose borrowers have breached their contractual obligation to at all times maintain adequate BOI coverage. LPI coverage for a particular property comes into existence automatically upon the lapse of a BOI policy for tracked loans – but independent of whether anyone is aware of the lapse in coverage. This automatic and continuous issuance of coverage for a particular property enables servicers to meet the secondary market's requirement to continuously maintain acceptable hazard insurance coverage at all times. (Some smaller community banks track insurance, but the LPI coverage involved likely is not automatic coverage.)

The following activities relate directly to insurance tracking, and all are required for the LPI insurer to comply with its obligation to the servicer and for the servicer, through the LPI insurer, to comply with the consumer protection requirements set forth in the CFPB's Regulation X:

- Processing all correspondence related to an existing homeowner's policy.
- Populating insurance data into the tracking system.
- Mailing three CFPB-required letters to borrowers to determine whether required homeowner's coverage is in place. (Note that LPI insurers were sending these letters to borrowers well before the regulatory requirement was put in place, as a means to avoid false placements of LPI.) These letters are on the servicer's letterhead only because it helps borrowers recognize that the letters relate to their mortgage loan, but the letters enhance the *LPI insurer's* ability to determine whether LPI needs to be placed, so the expenses associated with the "letter cycle" are appropriate for inclusion in insurance tracking costs.
- Maintaining call centers to service customers who have questions in response to the notice letters.

Because LPI is placed automatically – with little or no underwriting – LPI insurers must be able to manage their risk contemporaneously with the change in their LPI risk profile associated with the placement of LPI. LPI insurers engage in insurance tracking to manage this risk. This includes an assessment of risk to determine aggregation risk; the amount of premium associated with the risk assumed; probable maximum losses; the amount of capital needed to pay claims, including, but not limited to, occurrence of a catastrophe and regulatory required capital; and reinsurance. If the LPI insurer fails to obtain this information accurately and on a timely basis – which it does via *insurance tracking* – the insurer could see increases in direct and contributive losses; higher reinsurance costs, or a need to obtain additional reinsurance; an inability to timely pay claims after a catastrophe

due to a lack of knowledge of property addresses; uncertainty as to how much capital needs to be held to protect policyholders; and a high rate of false LPI coverage placement (where BOI coverage has not lapsed). Further, much of the foregoing would ultimately affect the cost of LPI coverage, which would affect borrowers whose BOI coverage has lapsed. Consequently, exposure management is critical. Indeed, as John Rollins, FCAS, MAAA, of Rollins Analytics, has testified before the NAIC, "underwriting expenses are different for [LPI] due to [the nature of] the product itself – a bulk master policy – as well as the unique activities associated with administering the book of risk." And because the inclusion of prospective expense levels is one of the basic tenets of actuarial ratemaking, "[r]atemaking actuaries should incorporate the results and properly measure the insurance-related expenses in the development of rates."[11] In sum, it is difficult and risky for an insurer to provide LPI if it is not also engaged in tracking.

Tracking asks whether coverage is needed, and if so, how much and what type (*i.e.*, flood, wind, hazard). It is a risk management tool used by insurers. Who should bear that cost? If the servicer pays for hazard insurance tracking, the cost will be passed on to all of the borrowers in a loan portfolio (to their detriment)– with the large majority of borrowers who continue to maintain required insurance subsidizing the cost of insurance for the very few[12] who fail to live up to their contractual obligation. Conversely, because tracking costs are included in the calculation of LPI premium – as the existing Model Act provides – only those borrowers who have breached their loan agreement (and who receive the *benefit* of having their home remain insured) pay for insurance tracking.

In the non-LPI context, there is no dispute that the property-specific underwriting expenses an insurer incurs to understand its risk are exposure management costs, which are properly reflected in the rate charged for the coverage as an acquisition expense. For LPI insurers who must cover all properties in a portfolio sight unseen, insurance tracking serves as the effective substitute for such property-specific underwriting. Monitoring coverage on all properties in the potential risk pool enables LPI carriers to better understand the risk they are taking. Continuous insurance tracking is therefore an exposure management function for LPI insurers, just as traditional underwriting is for non-LPI carriers. Consequently, the cost of insurance tracking in the LPI context is just as proper to include in the LPI rate (as an acquisition expense) as the cost of traditional underwriting in the non-LPI context is proper to include in a non-LPI rate (as an acquisition expense).

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[11] Testimony of John W. Rollins, FCAS, MAAA, before the NAIC on August 9, 2012, available at: http://www.naic.org/documents/committees_c_120809_public_hearing_lender_placed_insurance_testimony_rollins.pdf

[12] CPI insurers send notice letters to between 5 and 10 percent of their portfolio, with CPI ultimately being placed on between 1.5 and 2 percent of the portfolio.

By way of summary, the Working Group should keep several important points in mind regarding insurance tracking costs as it proceeds with its deliberations:

- Some have claimed that holders of mortgage loans pay insurance tracking costs to servicers and, consequently, that the inclusion of tracking costs in the calculation of LPI premium would have the borrower being charged twice for insurance tracking. This claim is false. A LPI insurer's tracking of whether required insurance is in place on all properties in a loan portfolio has nothing to do with a mortgage servicer's tracking a mortgage loan portfolio for loan management purposes. *The two tracking regimes serve very different purposes*: A mortgage servicer tracks a mortgage loan portfolio on behalf of loan owners/holders/investors to ensure borrowers meet their payment obligations and to remedy a borrower's failure to do so. Insurance tracking is different; a LPI insurer manages its claims exposure by tracking which properties are insured by LPI.

- There is a difference between the tracking aspects of a loan, such as payment history and escrow management, and the tracking aspects of insurance. Insurance tracking relates directly to the establishment and maintenance of required insurance; it has nothing to do with tracking loans.

- Some have attempted to argue on a theoretical basis that if only one property in a loan portfolio requires the placement of LPI coverage, then the inclusion of tracking costs in the LPI premium necessarily results in a single borrower paying for insurance tracking for the entire portfolio. This claim is senseless and does not remotely approximate reality. If there were only one borrower who failed to abide by the loan's contractual requirements, the servicer would simply commence a default action, eliminating the need for any LPI and the concurrent need for the LPI insurer to track. Rather, reality reflects that while few in number (historically, 2 percent or so), there is a group of borrowers who do not maintain adequate hazard insurance, and for that group, LPI is a preferential alternative to the servicer's pursuing an action of default against a borrower.

- Loan servicing is an "end-to-end" function and only efficient if performed that way, absent any artificial separation of duties between the servicer and the LPI provider.

Some have also argued that LPI insurers do not need to track hazard insurance coverage to manage exposure; instead, the argument goes, they rely on a historical average risk distribution model that is applied to the particular portfolio covered by a LPI policy. This claim is also false. The implication from this assertion is that LPI insurers are indifferent to the actual exposure they have with respect to a particular portfolio at any time, which is incorrect and makes no business sense. LPI

insurers track insurance on individual properties to manage their risk. While initially a LPI insurer will set rates based on experience, risk constantly changes and requires assessment through insurance tracking of required hazard insurance. It is not fiscally responsible to do otherwise – nor is it responsible to outsource insurance tracking to a servicer or other third party.

2. Some Servicers Would be Harmed if They Have to Conduct Insurance Tracking, Which Would be to the Detriment of the Consumer.

Prohibiting the inclusion of tracking costs in the calculation of LPI Premium will hurt those servicers who rely on the LPI insurer to track insurance coverage. If LPI insurers are not able to recover their tracking costs, they will pass those costs onto the servicer. The servicer would not be able to pass those costs onto borrowers directly because Regulation X prohibits a servicer from "assess[ing] on a borrower a premium charge *or fee related to [LPI]* unless the servicer has a reasonable basis to believe that the borrower has failed to comply with the mortgage loan contract's requirement to maintain hazard insurance."[13] Instead, affected servicers would likely pass on the increased cost to loan originators by reducing the purchase price of the loan, and loan originators would make up for that price differential by increasing the lending rate on residential mortgages.

Affected servicers would have to bring tracking in-house or outsource it to a third party other than the LPI insurer, which would increase their costs. Servicers also would have to change their systems to put in place a system to track insurance coverage. Under this scenario, there would not be the required continuous coverage that is now provided by LPI insurers as automatic issuance. If there were damage to the residence during the gap period, the consumer would bear the loss.

3. Treatment of Tracking Costs in the New Draft of the Model Act

Section 3.J. of the new draft of the Model Act would define insurance tracking to include the following activities:

(i) Developing and maintaining a database to track required insurance on borrowers' loans;

(ii) Maintaining voluntary insurance information on the servicer's loan servicing system or in a system maintained by a third party contractor for the servicer;

(iii) Inputting insurance information on new loans into an insurance tracking database or a servicer's loan servicing system;

(iv) All communications by or on behalf of a servicer with a

[13] 12 C.F.R. § 1024.37(b).

borrower's BOI insurer or BOI insurance producer;

(v) All communications by or on behalf of a servicer with a borrower concerning required insurance, including the CFPB-required written notices concerning charging a borrower's account for insurance;

(vi) All call center and other customer service operations related to CFPB-required written notices and communications with the BOI insurer or BOI insurance producer; and

(vii) A servicer directing an insurer to issue coverage under a LPI policy.

Section 8.E. of the Model Act would prohibit tracking costs from being included in the calculation of CPI premium. Consequently, the servicer would have to absorb the tracking costs, bring all of the tracking functions in-house, or outsource the tracking functions to a different third party and absorb those costs or pass them onto consumers through higher interest rates.

B. Net Debt (Section 5)

Section 5 of the new draft states that the calculation of premiums may be based on CPI/LPI coverage in an amount that does not exceed the net debt. Section 2.O. defines "net debt" as "the amount necessary to liquidate the remaining debt in a single lump-sum payment, excluding all unearned interest and other unearned charges." During previous discussions of the Working Group, there appeared to be no disagreement among stakeholders that the coverage amount for a CPI or LPI policy should be based on *replacement cost* – not on net debt. Section 5.A.(2) could be interpreted to allow for this, but it is not clear. Insuring at replacement cost protects the *borrower's equity* in the collateral, and by doing so, it also protects the servicer's interest in the loan's continuing to be a performing loan in the event of a hazard insurance claim.

If a home is destroyed and the amount of LPI coverage is limited to the net debt, a homeowner could be left without any means to purchase a replacement residence. In sum, permitting LPI coverage to be based to replacement cost could save the mortgage loan from going into default. Instead of net debt, the permitted coverage should be limited to the replacement cost of the property, which is consistent with the coverage amount stated by a standard homeowners insurance policy (HO-4) in the section titled Coverage A (Dwelling Coverage) for "replacement cost."

C. Other Matters

1. Blanket Insurance (Section 2)

Blanket insurance coverages on auto and personal property loans are exempted entirely from the existing Model Act (Section 2(B)(4) and 2(B)(5)). On reading the revised draft, it appears Basic Blanket coverage continues to be exempted, but the exemption for Blanket Vendor Single Interest (VSI) insurance was removed. As nearly identical coverage to Basic Blanket, Blanket VSI should also continue to be excluded from the revised model.

For all blanket coverages, the creditor does not place insurance coverage. Moreover, the creditor is the only insured. The coverage operates to protect only the creditor's loan portfolio and, in all cases, the creditor is responsible for paying the insurance carrier for coverage. For basic blanket insurance, no premium is charged to borrowers, either at loan closing or if BOI coverage lapses. Blanket VSI may have a one-time, nominal fee required of all borrowers in the creditor's loan portfolio at the time of loan closing, regardless of the amount of indebtedness, whether owing $1,000 or $100,000, or the value of the collateral. If a creditor assesses a fee for Blanket VSI, the amount is the same for all borrowers in the loan portfolio and does not relate to an individual certificate issued to the borrower.

In practice, entire sections of the current and revised Model Act proposal are not relevant to the operation of blanket products. For example, with blanket coverages, there are no disclosures to borrowers (Section 13); there is no premium charged to borrowers, so there is no refunding of premium (Section 9); there are no individual certificates issued (Section 7); and an entirely different rating basis is used as compared to that used for CPI (Section 5). CPI uses an individual borrower's outstanding loan balance as a rating basis, whereas blanket coverages use the outstanding loan balance for an entire loan portfolio. Furthermore, blanket coverages do not require primary insurance tracking activities as referenced in Section 3(J)). For these reasons, all Blanket coverages should continue to be exempted from a revised model act.

2. Commissions (Section 12)

Section 12.D.(2) prohibits the payment of commissions to a duly licensed and appointed insurance producer if the producer is a servicer, or a person or entity affiliated with a servicer, on LPI obtained by that servicer. It also prohibits the payment of contingent commissions based on underwriting profitability or loss ratios. We urge the Working Group not to adopt this language, as it fails to recognize the traditional role commissions play in producers' placement of insurance. See, for example, Section 13 of the Producer Licensing Model Act (No. 218-1), which permits commissions to be paid to a person licensed as an insurance producer.

Commission payments to a licensed producer for LPI should be permitted independent of whom a producer works for, even if it is for an insurance agency affiliated with a servicer. To do otherwise would run counter to the framework for "functional regulation" of insurance set forth in the Gramm-Leach-Bliley Act ("GLBA"), enacted in 1999.[14]

The GLBA defines the extent to which a depository institution, such as a bank, or an affiliate, is permitted to engage in insurance activities, including the activities of an insurance producer who works for an insurance agency affiliated with a bank. The GLBA recognizes the primacy of state insurance regulatory authority, but it prohibits a state from discriminating against depository institutions or their affiliates that are engaged in insurance activities authorized by the GLBA or other Federal law. Specifically, Section 301 of the GLBA states that "[t]he insurance activities of any person, [including national banks], shall be functionally regulated by the States, *subject to section 104*.[15] (Emphasis added.) Section 104[16] of the GLBA defines the extent to which a state may regulate the insurance activities of depository institutions.[17] For example, in subsection 104(a), Congress states its intention that the McCarran-Ferguson Act "remains the law of the United States,"[18] but Congress went on to prohibit a state from discriminating against depository institutions or their affiliates involved in insurance activities vis-à-vis persons engaged in the same activities who are not affiliated with a depository institution (or affiliate). Subsection 104(e) states:

> Except as provided in any restrictions described in subsection (d)(2)(B) [the safe harbors for a state to regulate depository institutions, and their affiliates, see *supra* note 13], no State may, by statute, regulation, order, interpretation, or other action, regulate the insurance activities authorized or permitted under this Act or any other provision of Federal law of a depository institution, or affiliate thereof, to the extent that such statute, regulation, order, interpretation, or other action – (1) distinguishes by its terms between depository institutions, or affiliates thereof, and other persons engaged in such activities, in a manner that is in any way adverse to any such depository institution, or affiliate thereof; (2) as interpreted or applied, has or will have an impact on depository institutions, or affiliates thereof, that is substantially more adverse than its impact on other persons providing the same products or

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14 Pub. L. No. 106-102.

15 15 U.S.C. § 6711.

16 15 U.S.C. § 6701.

17 15 U.S.C. § 6701(d)(2)(B) (expressly preserving states' authority to regulate insurance sales, solicitation and cross marketing activities in 13 areas); 15 U.S.C. § 6701(d)(2)(A) (generally preserving states' authority to regulate insurance sales, solicitation and cross marketing activities if the regulation does not "prevent or significantly interfere" with the ability of a depository institution or an affiliate to engage in the activities).

18 15 U.S.C. § 6701(a).

> services or engaged in the same activities that are not depository institutions, or affiliates thereof, or persons or entities affiliated therewith; [or] (3) effectively prevents a depository institution, or affiliate thereof, from engaging in insurance activities authorized or permitted by this Act or any other provision of Federal law . . . .[19]

Therefore, it would be inappropriate for the Model Act to restrict the ability of an insurance producer to receive commissions in connection with the producer's placement of LPI, merely because the producer works for a servicer or an insurance agency affiliated with the servicer.[20]

Contingent commissions are not something that came up during discussions on the Model Act. Its prohibition is surprising in that it is not specifically tied to lenders, but rather to all producers. Contingent commissions are used in other property and casualty markets. An insurer uses this commission structure to help manage its risk, such as with managing general agents for CPI for autos. Its prohibition does not align with other industry practices and does not seem to further any of the stated purposes (Section 1) of the Model Act.

We urge the Working Group not to adopt the prohibition on contingent commissions, because it would have the unintended impact of creating disparate treatment between MGAs and direct writers. MGAs provide valuable services to insurance carriers. Unlike pure producers, MGAs perform services typically undertaken by carriers, such as underwriting, policy issuance, premium accounting, and claim adjudication. MGAs are typically compensated on the profitability of the underwriting results. This concept is akin to how a direct insurance writer would earn its profits – based on how well it underwrites a risk. A prohibition on contingent commissions for MGAs creates an un-level playing field in favor of the direct writer and puts MGAs at a competitive disadvantage. The disadvantage could ultimately drive MGAs out of the creditor-placed insurance business. This unintended consequence will likely lead to less overall competition in the market-place, and history has shown that reduction of competition leads to increased costs for the consumer.

3. "Reverse Competition" (Section 3)

Section 3.Q. defines "reverse competition" to mean:

> competition among insurers that regularly takes the form of insurers vying with each other for the favor of persons who control, or may control, the placement of the insurance with insurers. Reverse competition tends to

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[19] 15 U.S.C. § 6701(e).

[20] Notably, the two largest providers of LPI on residential real property (Assurant and National General) have entered into Regulatory Agreements with the majority of states, which specifically detail prohibited practices as they relate to commissions.

> increase insurance premiums or prevent the lowering of premiums in order that greater compensation may be paid to persons for such business as a means of obtaining the placement of business. In these situations, the competitive pressure to obtain business by paying higher compensation to these persons overwhelms any downward pressures consumers may exert on the price of insurance, thus causing prices to rise or remain higher than they would otherwise.

The definition's inclusion in the Model Act would betray a fundamental misunderstanding of LPI: the product exists because a borrower has failed to protect the lender's interest in the loan collateral, which is a contractual obligation. The product is not designed to replace a BOI policy that has not lapsed. Providing the borrower with the best possible coverage at the lowest possible price has never been the objective of LPI. LPI is designed to ensure the smooth functioning of the residential mortgage market by protecting loan collateral by keeping servicers, and their investors, solvent in the face of individual and catastrophic losses to the collateral securing their loan portfolio. These products benefit borrowers; but they are not the focus of the benefit. Moreover, the borrower has complete control over whether to eliminate LPI on his property. No insurers are "vying with each other for the favor of persons who control, or may control, the placement of LPI with insurers."

4. Loss Ratio (Section 3)

The definition of "loss ratio" in Section 3.N. should be revised to reflect how it has historically been defined: "the ratio derived from a calculation of written premium to reserves, incurred losses, loss claim cost and refund liability."

5. Claims (Section 10)

Subsections 10(B) and 10(E) do not appear to apply to residential real property transactions, as both subsections reference the "salvage" value of the property. Therefore, to the extent that the scope of subsections B and E covers LPI on residential mortgage loans, modifications to the language would be needed.

6. Disclosures to the Debtor (Section 13)

Subsection 13(C) prohibits a lender from imposing LPI charges absent sufficient notice, and it provides a "safe harbor" for the notice requirement if certain requirements are satisfied. We urge the Working Group to add an additional safe harbor for a lender that complies with the notice requirements set forth by the Consumer Financial Protection Bureau in its regulation governing LPI, Regulation X.[21]

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[21] 12 C.F.R. § 1024.37(c).

7. Exclusion of Excess and Surplus Lines Carriers (Sections 7 and 8)

Sections 7 and 8 of the CPI Model Act imply an expectation that creditor-placed insurance will be written on an admitted basis. We strongly discourage this, as it would create less overall competition in the CPI marketplace. Excess and Surplus (E&S) carriers serve an important role in the industry, and excluding them from the market will not benefit borrowers or decrease premiums. In fact, excluding E&S will have the opposite effect, as it will increase premiums due to less competition. E&S carriers are also able to offer coverage enhancements beneficial to the industry that are not otherwise available in the admitted market, such as paying replacement cost irrespective of whether the property is repaired or restored.

III. Conclusion

By including LPI in the current draft, the Model Act contains language that would harm both servicers and consumers by disrupting the systems currently used by those servicers and by increasing mortgage costs to consumers. As the attached redlined draft of the new version of the Model Act reveals, the existing draft of the Model Act would require extensive revisions for the Model Act to properly apply both to CPI on personal property and auto loans and LPI on residential mortgage loans. In doing so, the document would have so many exceptions, carve-outs and provisos, at best it would be difficult for all parties to understand and apply. Therefore, we urge the Working Group to start anew with the Model Act with respect to LPI, and leave the scope of the current version of the Model Act to CPI placed on automobiles and personal property.

[Signatures on next page.]

Sincerely,

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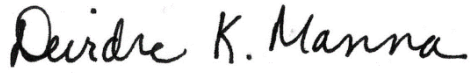

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