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Lender-Placed Insurance Model Act (C) Working Group

Virtual Meeting

October 19, 2020

The Lender-Placed Insurance Model Act (C) Working Group of the Property and Casualty Insurance (C) Committee met
Oct. 19, 2020. The following Working Group members participated: David Altmaier, Chair (FL); Elizabeth Kelleher Dwyer, Vice Chair (RI); Erica DeMesa and Tina Zhao (CA); Angela King (DC); Warren Byrd (LA); Mike Chaney (MS); Mark Worman (TX); Rebecca Nichols (VA).

1. Discussed Comments on the Draft Model

Commissioner Altmaier noted that the Working Group has not met in quite some time but said he would like to review comments received on the draft model related to lender-placed homeowners insurance and possibly consider the model for adoption to present to the Property and Casualty Insurance (C) Committee at the Fall National Meeting.

Birny Birnbaum (Center for Economic Justice—CEJ) said there are two main issues he would like to discuss. He said there is a need for a prohibition on the lender-servicer having a financial interest in the placement of lender-placed insurance (LPI) other than the protection of the property serving as collateral for the mortgage. He said reverse competition exists in this market, and insurers compete for business by providing considerations to the lender-servicer, unrelated to insurance. He said this drives up the cost of insurance. He said there were kickbacks following the 2008 financial crisis when borrowers were overcharged, and money went to lender-servicers instead of protecting property serving as collateral. Mr. Birnbaum said LPI insurers continue to seek kickbacks.

Mr. Birnbaum said insurance tracking is a responsibility of the lender-servicer and not an appropriate expense to include in LPI rates. He said tracking involves setting up a database on the required insurance, gathering information from insurers and borrowers of required insurance, using the database to update the system, and sending notices to borrowers. He said these lender-servicer responsibilities apply to every loan in the portfolio. The lender-servicer is compensated through loan interest fees or servicer fees. He said federal regulations have been issued by the Consumer Financial Protection Bureau (CFPB), and Fannie Mae and Freddie Mac have servicer guidelines having to do with tracking activities. Mr. Birnbaum said a portfolio-wide expense is the responsibility of the lender-servicer. He said it is unfair to charge the small percentage of borrowers for tracking costs related to all borrowers  If every borrower maintained the required insurance and there were no claims, the servicer would still be required to perform the tracking function. He said insurers do not need individual tracking data to manage their exposure. He said the cancellation rate is high with LPI, and insurers underwrite by evaluating characteristics of the loan portfolio and then estimate a placement rate for LPI. He said Fannie guidelines specify what servicers must do in verifying that the insurer coverage meets Fannie requirements. He said individual tracking information is not required to underwrite or price LPI. New York has prohibited the inclusion of tracking expenses in LPI rates. However, LPI insurers continue to operate in New York but charge servicers amounts for tracking that better reflect the cost of tracking and exclude those expenses from LPI rates. Mr. Birnbaum stated the prohibition of tracking expenses from LPI rates does not limit the ability of state insurance regulators to evaluate LPI rates. He also noted a second issue of the model requiring dual interest coverage. He said consumers should have rights in an insurance claim, and single interest coverage excludes such rights for consumers.

Commissioner Chaney asked for additional information about dual interest coverage. Mr. Birnbaum said single interest coverage is typically found in auto insurance or collateral protection products. He said it is typically blanket coverage for which there is no separate charge to borrowers, so the lender has the only interest. He said there are no rights regarding a claim for the borrower, but in LPI, it is the borrower’s home, so an individual having single interest coverage with damage to the property has no rights to challenge the lender if the borrower wants to make a claim. He said with dual interest coverage, the borrower has some rights under the policy. Commissioner Chaney said in the 2012 hearings, some people abandoned their homes, and the homes were foreclosed. Mr. Birnbaum said the majority of policies are dual coverage in homeowners. He said the bank already owns foreclosed homes, and it is a real-estate owned (REO) property with REO insurance at that point. He said making a requirement for dual interest does not reduce the lender’s rights, but it does give borrowers rights in the event the borrower wants to make a claim on the insurance they have been charged for.

Superintendent Dwyer asked if the industry believes the Fannie Mae and Freddie Mac guidelines and CFPB Regulation X do not apply. Chrys Lemon (McIntyre & Lemon) said Regulation X and Fannie Mae and Freddie Mac guidelines focus on lenders and servicers, while the model focuses on insurance aspects. Superintendent Dwyer said both require the lender to track and have evidence of insurance before placing or charging insurance. She said the proposal is that the insurer would do that work and share it with the lender. Mr. Lemon said the lender has outsourced the tracking to the insurer because insurers’ risk management is important as part of the acquisition. Superintendent Dwyer asked why a lender can put the charge on the consumer by saying it is insurer tracking instead of having the lender pay for it. Mr. Lemon said it is not the lender’s risk but the insurer’s risk. Superintendent Dwyer said there cannot be a charge placed unless there is evidence. Superintendent Dwyer said Regulation X, 12 CFR § 1024.37, states the servicer cannot accept premium unless it has reasonable basis to believe the borrower has failed to comply. She said she wants to know why that is not the responsibility of the lender. Mr. Lemon said he would follow up with additional information on this matter.

Mr. Lemon said multistate agreements were entered into five years ago, and most states have entered into those agreements that reflect the current regulatory setting. He said the draft model reflects the settlements. He said what the CEJ said about insurance tracking is not accurate, and it is important for states to control rate-making authority and process. Hs said he is in favor of the Working Group voting on the draft.

Commissioner Chaney asked what it costs to track coverage. Mr. Birnbaum said there is a range of cost for insurance tracking between 40 cents and 50 cents to 80 cents and 90 cents per loan per month. He said this is around $10 per loan per year, so a portfolio with 100,000 loans would have $1 million in tracking expenses. He said these expenses are not charged to the entire portfolio but to only 1,000 or 2,000 borrowers out of 100,000 borrowers. Commissioner Chaney asked if the expense is so low per loan, how do individuals have trouble paying it. Mr. Birnbaum said it is a lot, and that is why lenders are fighting to maintain kickbacks. He said if tracking costs are allowed to be in the LPI premium and then the servicer passes the charge to the borrower, then it is a kickback because the servicer is getting free or low-cost tracking services and is being paid again by the LPI insurer, and this is being paid for by the low percentage of borrowers being charged for the LPI insurance. Mr. Lemon said the servicer is not compensated. Mr. Birnbaum said there is not evidence of that assertion.

Ms. DeMesa said California has an issue with tracking expenses and has submitted a redline version of a modified model.

Commissioner Chaney said he is going to move to adopt the model but will wait so the industry can respond to Superintendent Dwyer’s inquiry. Superintendent Dwyer said she will likely vote against the model. Commissioner Altmaier said he believes all policies are dual interest in Florida. He said he has talked to his actuarial staff about tracking expenses, and he does not believe it would be appropriate to prohibit tracking expenses in Florida as the state wishes to retain the ability to review expenses in rate filings and judge whether expenses are appropriate to pass to consumers. He noted that the absence of a prohibition is not permission as the state insurance regulator might find the expense inappropriate and reject it.

Commissioner Altmaier said the draft model would be exposed for a 15-day public comment period ending Nov. 3. He said the Working Group will meet in November to consider adoption of the model.

Having no further business, the Lender-Placed Insurance (C) Working Group adjourned.

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