Overview of Lender-Placed Home Insurance

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NAIC Public Hearing on Lender-Placed Insurance

August 9, 2012

The Center for Economic Justice

CEJ is a non-profit organization advocating on behalf of consumers on insurance, credit and utility issues.

Birny Birnbaum has been active on credit-related insurance issues, including LPI, for over 20 years.

Topics Covered

1. Mortgage Servicers and Requirements for Continuous Insurance Coverage
2. Responsibilities of Mortgage Servicers vs. LPI Insurers
3. Overview of LPI Product and Markets
4. NAIC Activities on LPI
5. Recent Actions by Other Regulators and Organizations on LPI
6. Issues of Concern for Consumers

Role of Mortgage Services

Mortgage Owners: Fannie Mae, Freddie Mac, Private Investors. Fannie and Freddie own – directly or indirectly – half of over 50 total million mortgages

Mortgage Servicers: Manage mortgages on behalf of owners. Largest services are Wells Fargo ($1.84 trillion), Bank of America ($1.69 trillion), Chase ($1.11 Trillion) and Citi ($515 Million) out a countrywide total of $10.2 trillion.

Role of Mortgage Services

Servicing mortgages includes many activities, including, for example, collecting and disbursing mortgage payments, establishing escrow and paying insurance and taxes from escrow, processing defaults and foreclosures.

One requirement of mortgage servicers by mortgage owners is to maintain continuous insurance coverage on the property serving as collateral for the loan.

Ensuring Continuous Insurance Coverage

Lender-Placed Insurance (LPI) is an important tool for mortgage servicers to meet this requirement and for mortgage markets to operate smoothly.

Maintaining continuous insurance coverage involves tracking loans for evidence of required insurance and placing insurance on properties for which the borrower has not maintained the required insurance.

Continuous Insurance Coverage: Responsibilities

Activity	Servicer vs. Insurer
Tracking Insurance	
Loading Insurance Information into Database	Servicer
Maintaining/Monitoring Insurance Tracking DB	Servicer
Contacting Borrowers, Problems with Insurance	Servicer
Customer Service Borrowers Insurance Evidence	Servicer
Contacting Insurers/Agents Insurance Evidence	Servicer

Continuous Insurance Coverage: Responsibilities

Activity	Servicer vs. Insurer
Placing Insurance	
Notifying Insurer to Issue Binder or Policy	Servicer
Issuing Temporary Binder	**Insurer**
Determining Coverage Amount	Servicer
Servicer Payment to Insurer	Servicer/**Insurer**
Billing Borrower for LPI Premium	Servicer
Setting up Escrow when necessary for LPI	Servicer
Refunds to Servicer	**Insurer**
Refunds to Borrower	Servicer
Issuing Permanent Policy	**Insurer**
Customer Service about Insurance Placement	Servicer
Customer Service about Borrower Refunds	Servicer
Customer Service about LPI Claims	**Insurer**

Operation of Insurance Tracking and LPI

Servicer is Responsible for Insurance Tracking – Included in Mortgage Servicing Fee Paid by Mortgage Owners

Based on Insurance Tracking Results, Servicer Directs LPI Insurer to Issue Coverage Under Group LPI Policy

Insurance Tracking Typically Outsourced to Insurer Providing LPI

False Placements: 10% to 20%

Full Refund for False Placement: "Flat Cancellation"

LPI Product

- Group Policy Covering All Properties in Loan Portfolio
- Automatic Coverage from Date of Lapse of Borrower's Coverage
- Limited Coverage Compared to HO Policy– No Personal Property, No Additional Living Expense, No Liability.
- No Underwriting of Individual Properties
- Hazard, Flood, Excess Flood, Wind, Excess Wind Perils

LPI Pricing

- Historically Simple Rating: Rate per $100 of coverage; a few states with territorial rating.

- Schedule Rating

- New Filings with New Rating Factors
    - Amount of Coverage Curve
    - Territorial Rating
    - By Peril Rating
    - Age of Home Rating
    - Loan Status – Current, Delinquent

Flow of Funds for LPI

Servicer pays LPI Insurer for LPI Issued over specified period (weekly, monthly).

Servicer bills Borrower for LPI Premium

"Retroactive" Billing

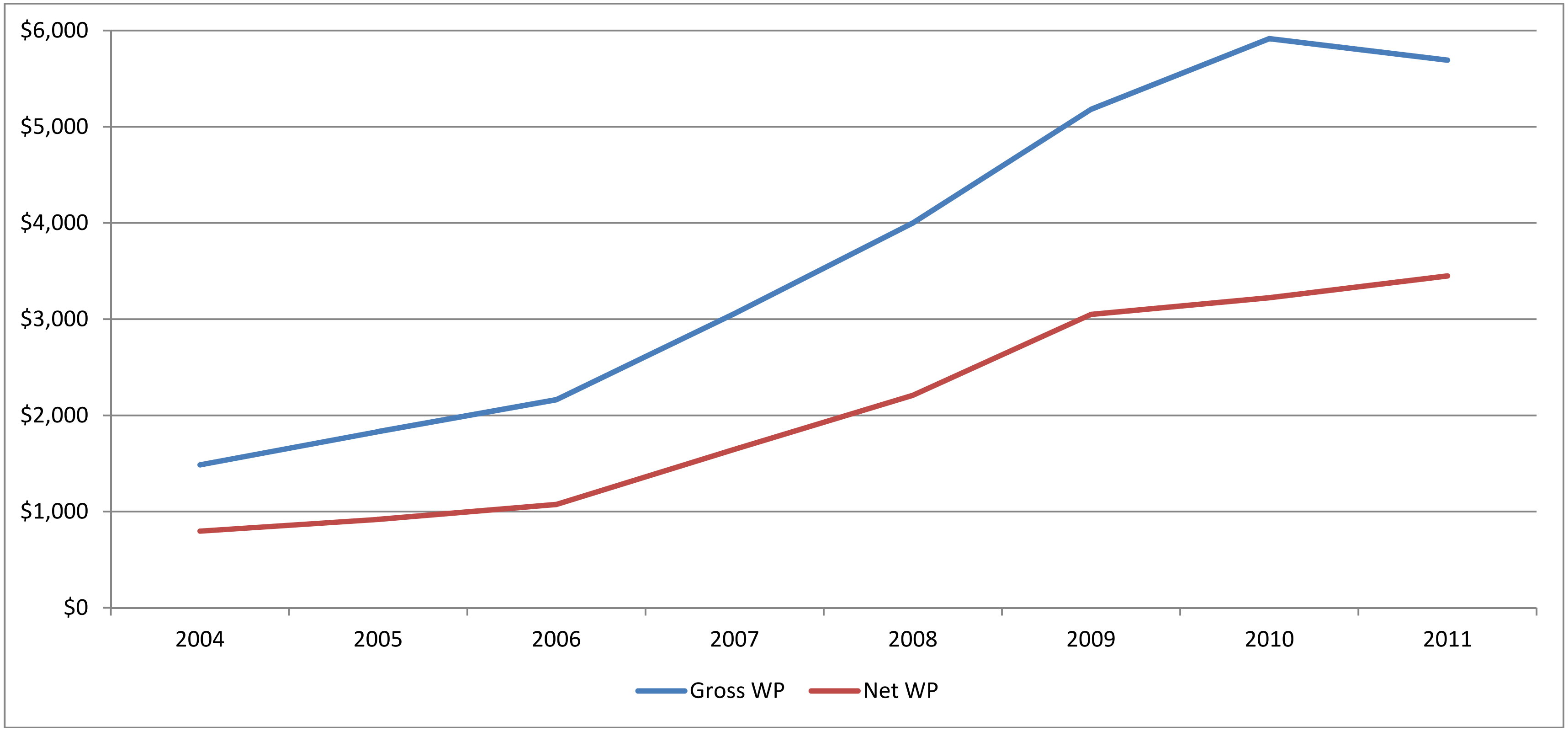
In the event of Borrower Default / Foreclosure, Mortgage Owner Pays LPI Premiums

LPI Premiums Have Quadrupled Since 2004

Year	*Gross Written Premium ($ Millions)*	*Net Written Premium ($ Millions)*
2004	$1,485	$796
2005	$1,832	$919
2006	$2,163	$1,074
2007	$3,058	$1,647
2008	$4,000	$2,209
2009	$5,181	$3,049
2010	$5,915	$3,223
2011	$5,692	$3,450
2004-2011	$29,326	$16,368

2009-2011 GWP Understated, Reporting Errors by QBE

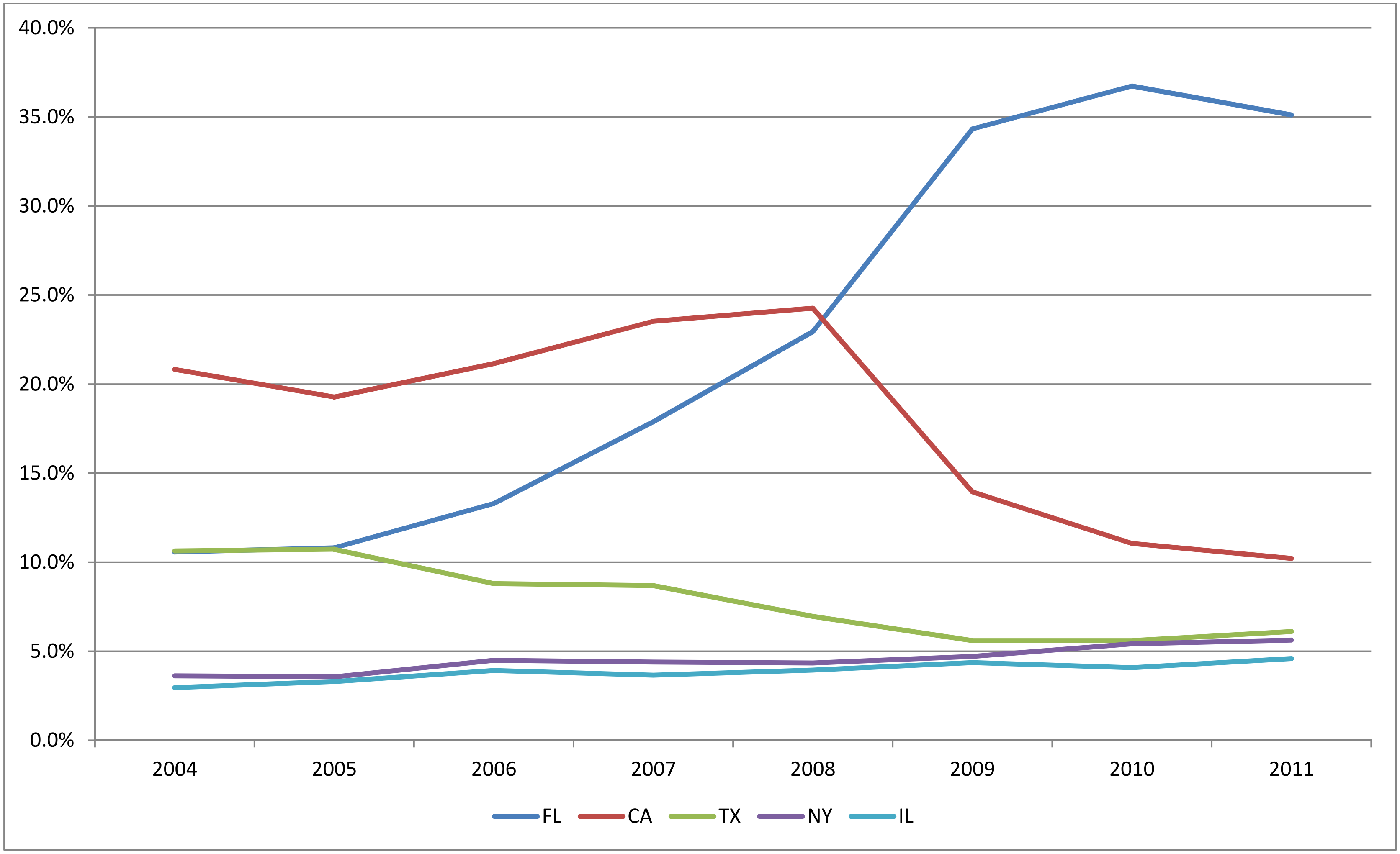
LPI Premiums Have Quadrupled Since 2004



LPI Premium by State: Florida Has Become Ground Zero

	2004	2005	2006	2007	2008	2009	2010	2011
FL	10.6%	10.8%	13.3%	17.9%	22.9%	34.3%	36.7%	35.1%
CA	20.8%	19.3%	21.2%	23.5%	24.3%	14.0%	11.1%	10.2%
TX	10.6%	10.7%	8.8%	8.7%	7.0%	5.6%	5.6%	6.1%
NY	3.6%	3.6%	4.5%	4.4%	4.3%	4.7%	5.4%	5.6%
IL	3.0%	3.3%	3.9%	3.7%	3.9%	4.4%	4.1%	4.6%
NJ	2.9%	2.7%	2.9%	2.7%	2.7%	2.9%	3.4%	4.0%
MI	4.2%	4.4%	4.4%	5.8%	3.6%	2.7%	2.2%	2.0%
OH	3.6%	3.8%	3.5%	2.7%	2.4%	2.2%	2.3%	2.9%
GA	3.4%	3.2%	3.2%	2.4%	2.3%	2.3%	2.3%	2.3%
PA	2.6%	2.6%	2.7%	1.8%	1.8%	1.8%	1.7%	1.8%

LPI Premium by State: Florida Has Become Ground Zero



Assurant and QBE Write Almost All LPI ($ Millions NWP)

Year	Assurant	QBE/Balboa	Countrywide
2004	$543	$237	$796
2005	$641	$242	$919
2006	$851	$210	$1,074
2007	$1,219	$418	$1,647
2008	$1,640	$563	$2,209
2009	$1,745	$1,294	$3,049
2010	$1,810	$1,402	$3,223
2011	$2,022	$1,419	$3,450
2004-11	$10,471	$5,785	$16,368

Assurant and QBE Are the Market for LPI:

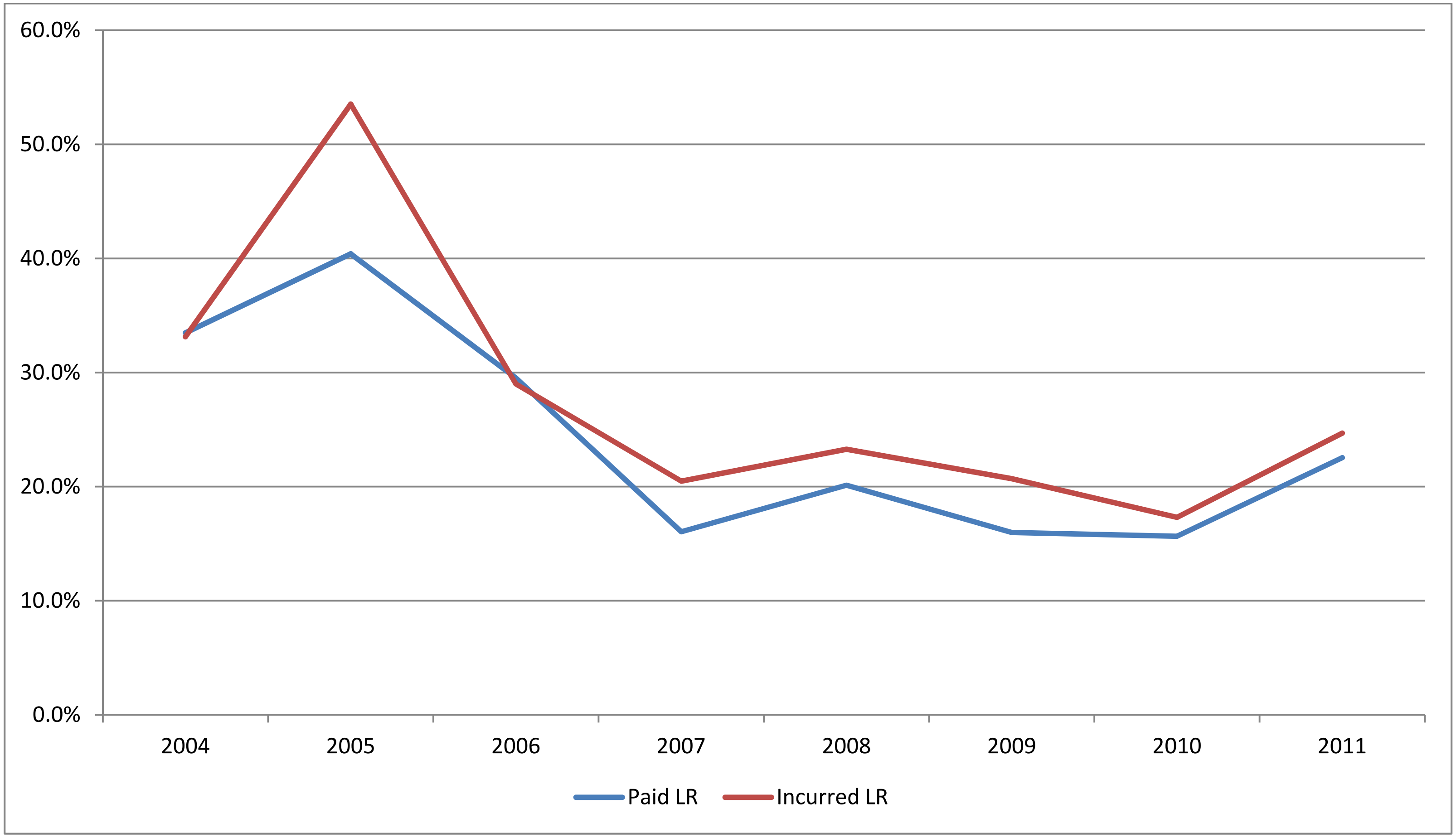
Countrywide Market Share

Year	Assurant	QBE/Balboa	Assurant + QBE/Balboa
2004	68.2%	29.8%	98.0%
2005	69.7%	26.4%	96.1%
2006	79.2%	19.5%	98.7%
2007	74.0%	25.4%	99.4%
2008	74.2%	25.5%	99.7%
2009	57.2%	42.4%	99.7%
2010	56.2%	43.5%	99.7%
2011	58.6%	41.1%	99.7%

Countrywide LPI Loss Ratios: Paid and Incurred

Year	*Paid/Written Loss Ratio*	*Incurred/Earned Loss Ratio*
2004	33.5%	33.1%
2005	40.4%	53.5%
2006	29.5%	29.0%
2007	16.0%	20.5%
2008	20.1%	23.3%
2009	16.0%	20.7%
2010	15.7%	17.3%
2011	22.5%	24.7%
2004-2011	21.0%	24.2%

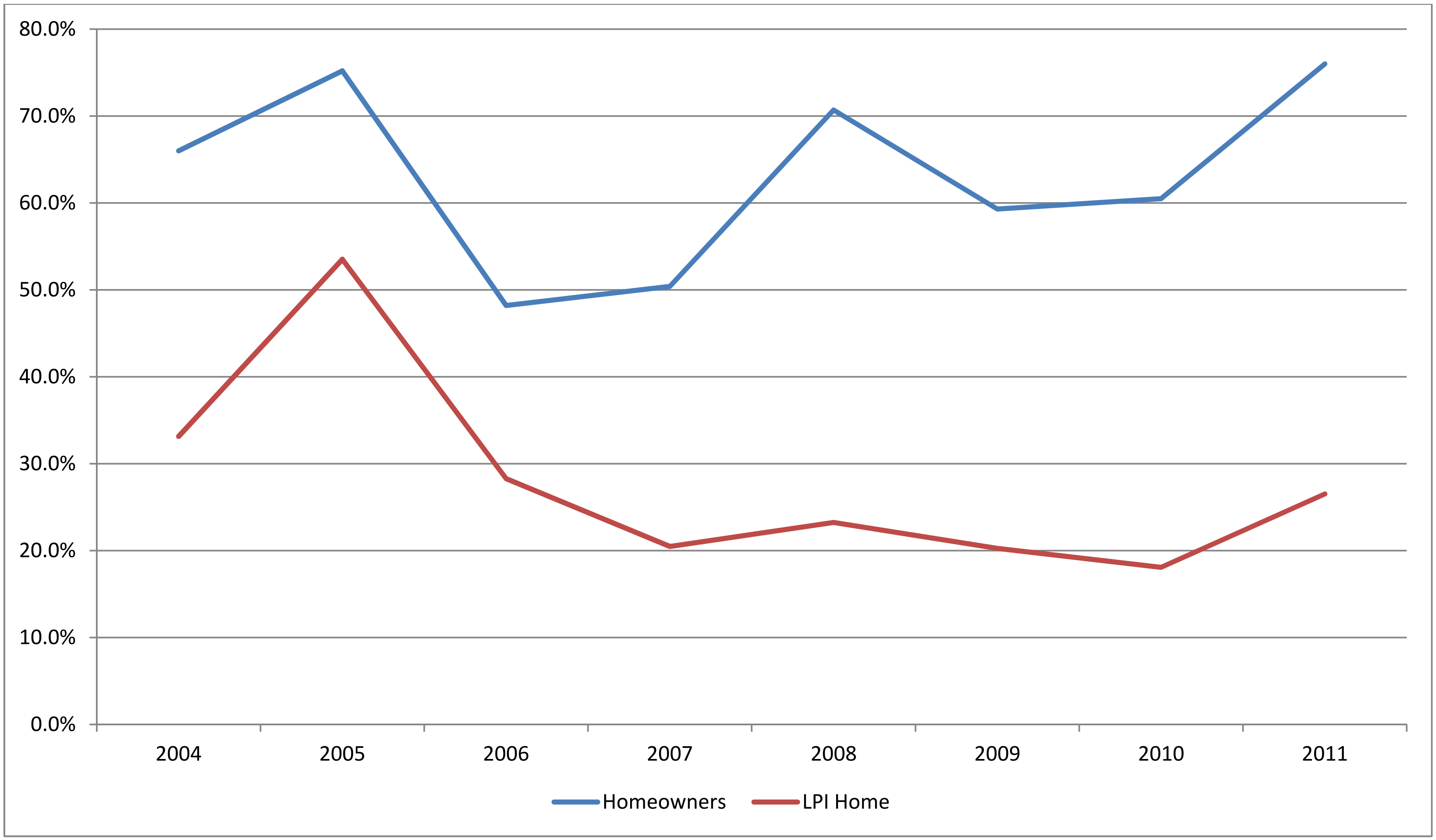
Countrywide LPI Loss Ratios: Paid and Incurred



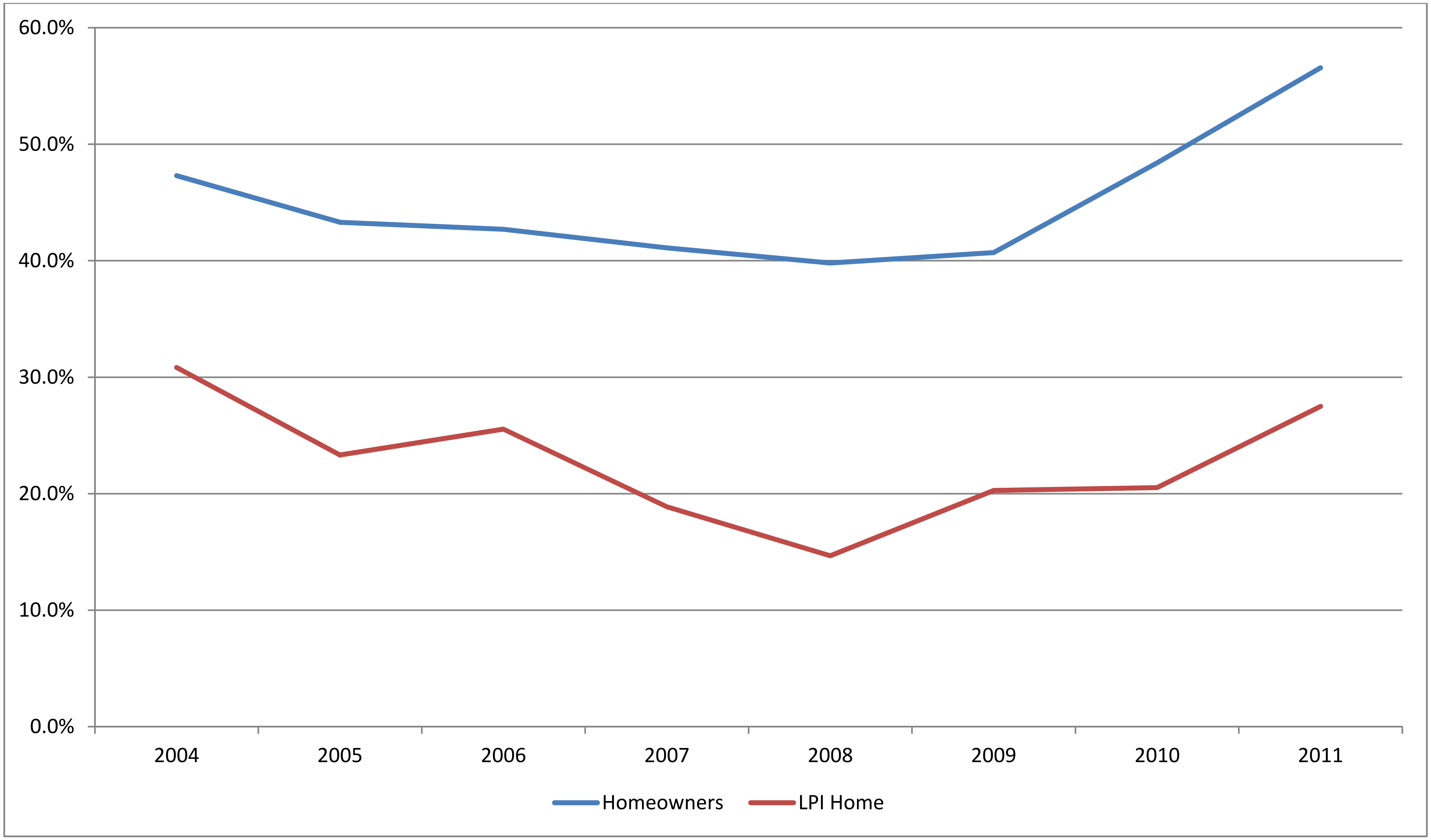
Countrywide Incurred Loss Ratios: HO vs. LPI Home

Year	Homeowners	LPI Home
2004	66.0%	33.1%
2005	75.2%	53.5%
2006	48.2%	28.3%
2007	50.4%	20.5%
2008	70.7%	23.2%
2009	59.3%	20.3%
2010	60.5%	18.1%
2011	76.0%	26.5%

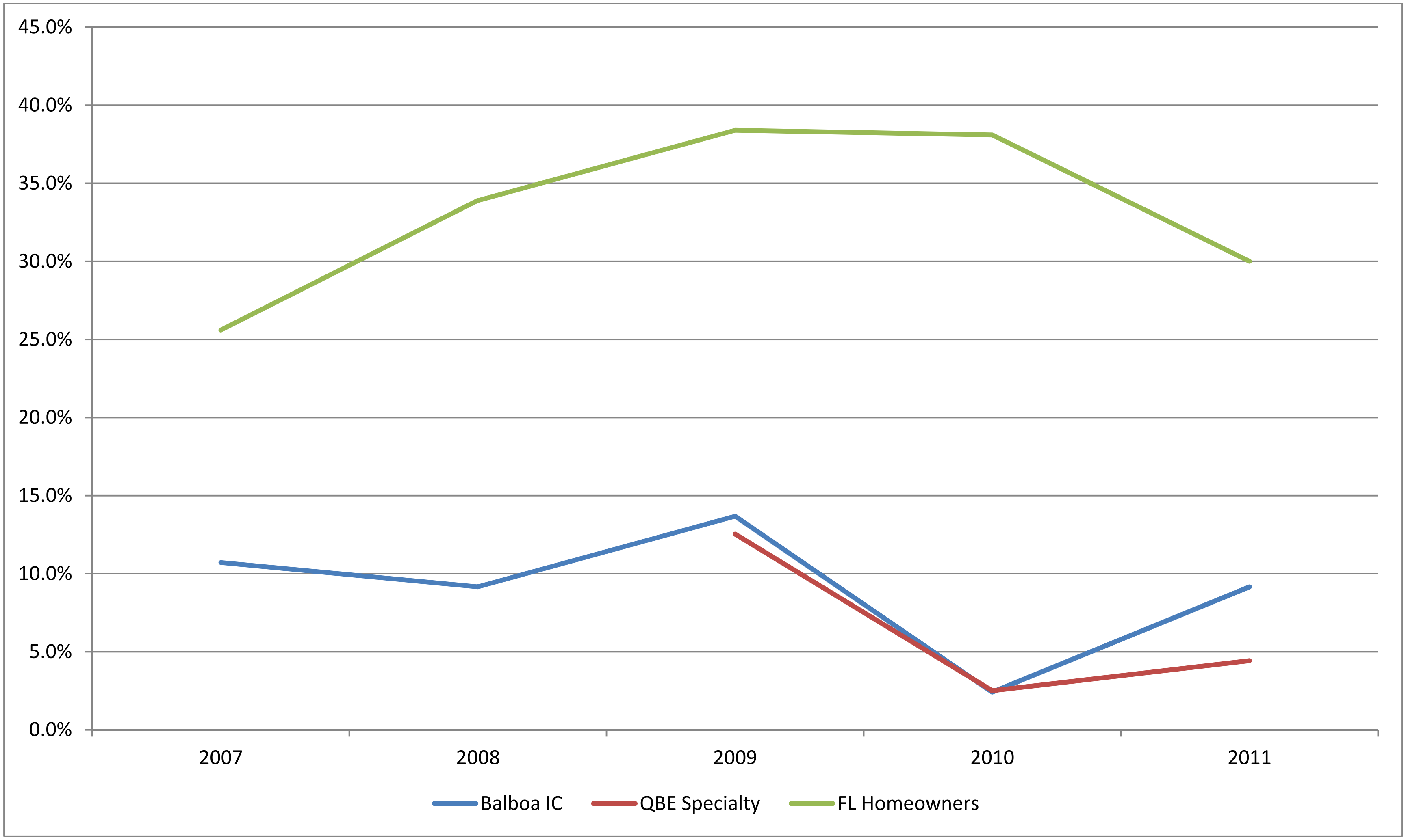
Countrywide Incurred Loss Ratios: HO vs. LPI Home



New York Incurred Loss Ratios: HO vs. LPI Home



Florida HO Loss Ratio and QBE/Balboa LPI Loss Ratio



Balboa/QBE Average LPI Premium in Florida, 2006 - 2011

Year	Exposures	Written Premium	Average Premium
7/06-6/07	15,956	$37,427,737	$2,346
7/07-6/08	25,520	$125,281,407	$4,909
7/08-6/09	45,451	$297,001,037	$6,535
7/09-6/10	97,567	$596,331,000	$6,112
7/10-6/11	119,611	$589,176,927	$4,926

LPI Insurer Profitability: American Security

Net pre-tax income was 33.5%, 42.0% and 31.8% of net written premium in 2009, 2010 and 2011. This compares to profit load in rate filings of 4% to 5%

Net after-tax income was 22.8%, 28.0% and 22.2% of net written premium in 2009, 2010 and 2011.

After-tax return on policyholder surplus was 41.7%, 50.5% and 44.8% of net written premium in 2009, 2010 and 2011.

From 2009 to 2011, American Security distributed $1.143 billion in dividends to policyholders – fully 29.5% of net premiums written over the period and $200 million more than net after-tax income for the period.

Reverse Competition in Credit Insurance Markets: NY Reg 27

(b) In the marketing of credit insurance, the inferior bargaining position of the debtor creates a captive market in which, without appropriate regulation of such insurance, the creditor can dictate the choice of coverages, premium rates, insurer, agent and broker, with such undesirable consequences as: excessive coverage (both as to amount and duration); excessive charges (including payment for nonessential items concealed as unidentifiable extra charges under the heading of insurance); failure to inform debtors of the existence and character of their credit insurance and the charges therefore, and consequent avoidance of the protection provided the debtor by such coverage.

Reverse Competition in Credit Insurance Markets: NY Reg 27

(c) In the absence of regulation, premium rates and compensation for credit insurance tend to be set at levels determined by the rate of return desired by the creditor in the form of dividends or retrospective rate refunds, commissions, fees, or other allowances, instead of on the basis of reasonable cost. Such reverse competition, unless properly controlled, results in insurance charges to debtors that are unreasonably high in relation to the benefits provided to them.

Compensation to Mortgage Services from LPI Premium

- Commissions
- Cash Payments for “Marketing”
- Captive Reinsurance
- Free or Subsidized Services for Mortgage Servicers

NAIC Activity on LPI

Creditor-Placed Insurance Model Act 1996

- “Insurance on collateralized real property” not covered by model
- Drafting Note: States have various definitions of "real property." Accordingly, the states may wish to consider their state definition of "real property," especially with the varying nature of manufactured housing used as a residence.

Revisions to Credit Insurance Experience Exhibit

- Breakout of Creditor-Place Home and Auto, Single and Dual Interest
- Reporting Errors Continue

Recent Activity Regarding LPI: AG Settlement

Earlier this year, most state attorneys general and the United States Department of Justice entered into settlement agreements with several mortgage servicers. The settlement agreements included requirements for LPI.

8. Any force-placed insurance policy must be purchased for a commercially reasonable price.

Recent Activity Regarding LPI:

Consumer Financial Protection Bureau

The CFPB has oversight authority over mortgage servicers and recently published a proposed rule regarding mortgage servicing standards which included service standards for LPI.

Recent Activity Regarding LPI: Fannie Mae

Fannie issued new servicing guidelines in March, since delayed implementation date and encouraged servicers to follow the new guidelines:

The lender-placed vendor selected by the servicer must have premium rates that are competitively priced and commercially reasonable. The servicer must have a documented process in place that demonstrates that the vendor meets this requirement. Fannie Mae reserves the right to require that a servicer change its lender-placed insurance provider if the provider has not demonstrated its ability to file rates within a timely manner.

Recent Activity Regarding LPI: Fannie Mae

Acceptable Lender-Placed Insurance Costs and Insurance Tracking Fees

Fannie Mae is clarifying its requirement for reasonable reimbursable expenses for lender-placed insurance. Any servicer request for reimbursement of lender-placed insurance premiums must **exclude**:

- any lender-placed insurance commission earned on that policy by the servicer or any related entity,
- costs associated with insurance tracking or administration, or
- any other costs beyond the actual cost of the lender-placed insurance policy premium.

Recent Activity Regarding LPI: NY DFS Agreement with Ocwen Financial on Mortgage Servicing Practices

The Department entered into an agreement with Ocwen Financial in December 2011 regarding mortgage servicing practices. The agreement contains a number of service standards for LPI, including:

> 61. To the extent Servicer purchases a master hazard insurance policy for force-placed it shall only purchase a policy that is reasonably priced in relation to the claims that may be incurred.

Recent Activity Regarding LPI: Public Hearings and Rate Review

- New York
- Florida
- California
- Texas

Consumer Issues of Concern with LPI

1. Unnecessary Placement
2. Inadequate Disclosure
3. LPI Sales Through Surplus Lines
4. Excessive Rates and Charges to Borrowers
    a. Unreasonable Expenses
    b. Unreasonable Actuarial Analysis and Assumptions
    c. REO vs. non-REO Experience
    d. Captive Reinsurance
    e. Schedule Rating
5. New Rating Factors
6. New Policy Forms
7. Regulatory Gaps / Overlaps
8. Poor Performance of Insurance Regulators Protecting LPI Consumers