

Comments of the Center for Economic Justice

**Proposed Addition of Part 227 (Regulation 202) to Title 11 NYCRR,
Force-Placed Insurance**

Docket DFS-39-13-00022-P

November 7, 2013

The Center for Economic Justice (CEJ) appreciates the work of the Department of Financial Services (DFS) to investigate and stop the excessive charges and abusive practices suffered by borrowers and investors because of the kickback culture of the force-placed insurance (FPI) market. We applaud the DFS for the settlements with FPI insurers that seek to stop the kickbacks and cause borrowers to be charged reasonable amounts by servicers for FPI and to stop unnecessary placement of FPI in the first place. We applaud the proposed regulation as codification of the settlement agreements and a template for other states to follow.

We believe the proposed regulation can be strengthened to eliminate a particular form of kickback – the provision of subsidized insurance tracking and other activities whose expenses should not be included in FPI charges to borrowers.

In the investigative hearings, DFS elicited evidence of kickbacks in the form of free or subsidized services. For example, GMAC witnesses testified that they paid nothing for insurance tracking or other services provided by Balboa because the FPI and related services were a “turnkey” operation. Borrowers were charged excessive amounts for FPI so to allow Balboa to provide GMAC with a host of free and valuable services.

DFS has recognized this method of kickback and prohibited the practice with proposed Section 227.6:

(g) (1) No insurer, insurance producer, or affiliate shall provide free or below cost outsourced services to a servicer or a person or entity affiliated with a servicer.

However, DFS has included two exceptions which undercut the general prohibition in 227.6(g)(1). Section 227.6(g)(2) states

(2) Notwithstanding paragraph (1) of this subdivision, the following practices associated with tracking functions that an insurer or its affiliate perform for the insurers' own benefit to identify and protect the insurer from exposure shall not be prohibited:

(i) An insurer or its affiliate monitoring a servicer's mortgage portfolio for lapses of or insufficient homeowners' voluntary insurance policies for a reduced fee, solely to the extent such monitoring is performed for the purpose of managing the insurer's exposure to lost premium and losses on properties on which no other insurance coverage is in effect, or

(ii) An insurer or its affiliate performing administrative services associated with providing and subsequently cancelling force-placed insurance on properties on which force-placed insurance is not required.

CEJ respectfully requests that these exemptions in Section 227.6(g)(2) be removed because insurers will use (g)(2)(i) to claim all or nearly all insurance tracking expenses are made for the purpose of managing exposure to lost premium and losses. We request that 227.6(g)(2)(ii) be removed because the costs of false placement – cancelling FPI coverage that had been placed when voluntary coverage had actually been in place – should be borne by the entity responsible for insurance tracking, which is the mortgage servicer. We also request a definition of permissible loss ratio and more explicit expense caps.

CEJ recommends the following changes:

(g) ~~(1)~~ No insurer, insurance producer, or affiliate shall provide free or below cost outsourced services, including, but not limited to insurance tracking, to a servicer or a person or entity affiliated with a servicer.

~~(2) Notwithstanding paragraph (1) of this subdivision, the following practices associated with tracking functions that an insurer or its affiliate perform for the insurers' own benefit to identify and protect the insurer from exposure shall not be prohibited:~~

~~(i) An insurer or its affiliate monitoring a servicer's mortgage portfolio for lapses of or insufficient homeowners' voluntary insurance policies for a reduced fee, solely to the extent such monitoring is performed for the purpose of managing the insurer's exposure to lost premium and losses on properties on which no other insurance coverage is in effect, or~~

~~(ii) An insurer or its affiliate performing administrative services associated with providing and subsequently cancelling force-placed insurance on properties on which force-placed insurance is not required.~~

CEJ recommends the addition of the following definition to Section 227.1:

(l) Insurance Tracking means all activities related to the servicer's responsibility to determine if the borrower has required insurance in place and includes:

1. Development and maintenance of a database used by the servicer to track required insurance on borrower's loans, including a separate database for insurance evidence maintained by the servicer or its agent and maintaining insurance information in the mortgage servicer's system of record;
2. Boarding insurance information on new loans into insurance tracking databases or the mortgage servicing system of record;
3. All communications by the servicer or its agent with the borrower's voluntary insurance company or voluntary insurance producer;
4. All communications by the servicer or on behalf of the servicer to the borrower regarding required evidence of insurance, including, notification letters to borrowers regarding required insurance, regarding missing evidence of required insurance and regarding placement of force-placed insurance and subsequent charges on the borrower's loan; and
5. All customer service call center operations related to communications in 3 and 4.

Discussion of 227.6(g)(2)(i)

As a preliminary matter, it is clear that insurance tracking, as defined above, is the responsibility of the servicer and not the FPI insurer. Federal law and regulations, including the recent mortgage servicing rule of the Consumer Financial Protection Bureau and provisions in the Flood Disaster Protection Act, place the responsibility on the lender/servicer to monitor the presence of required insurance, to provide notifications to borrowers in the absence of required insurance and to charge borrowers for FPI only if certain notifications have been made. The fact that servicers are responsible for insurance tracking is also evidenced by the March 2012 Fannie Mae Request for Proposal for insurance tracking and FPI services. Fannie identified insurance tracking as a separate activity from the provision of FPI and wrote:

The fact that insurance tracking is not an expense properly included in LPI rates is further demonstrated by the Fannie Mae Request for Proposal for Insurance Tracking and LPI servicers. Fannie not only identified insurance tracking as a separate activity from provision of LPI, but specifically identified the issue that including tracking expenses in LPI rates caused mortgage owners to pay servicers twice for insurance tracking – once in the service fee mortgage owners pay to servicers and second in inflated LPI rates when mortgage owners are forced to pay for LPI when a borrower defaults. The Fannie RFP from March 2013 states:

After extensive internal review, Fannie Mae believes that current Lender Placed Insurance costs are not market competitive and can be improved through unit price reductions and fee transparency to the benefit of both the taxpayers and homeowners.

Current Situation

Fannie Mae's current Lender Placed Insurance situation is as follows:

1. Homeowners are required to maintain voluntary hazard insurance on Fannie Mae insured properties.
2. Lender Placed Insurance must be acquired by mortgage Servicers when a property is no longer eligible for Voluntary Insurance, or when the Servicer cannot obtain proof of adequate Voluntary Insurance from the homeowner, irrespective of whether or not that homeowner is current or delinquent on the loan.
3. The cost of Lender Placed Insurance is higher than the cost of voluntary hazard insurance. Homeowners are billed for the Lender Placed Insurance premiums. However, if the homeowner does not pay the premium (for example, if the property has already been vacated), then Servicers pass on the premium costs to Fannie Mae.
4. Servicers are responsible for providing tracking services, per Fannie Mae Guidelines. Many large Servicers have chosen to outsource the Insurance Tracking and associated administrative process to third parties, the largest of which are affiliated with Lender Placed Insurers.
5. Lender Placed Insurers often pay commissions/fees to Servicers for placing business with them. The cost of such commissions/fees is recovered in part or in whole by the Lender Placed Insurer from the premiums, which the Servicers pass on to Fannie Mae.
6. The existing system may encourage Servicers to purchase Lender Placed Insurance from Providers that pay high commissions/fees to the Servicers and provide tracking, rather than those that offer the best pricing and terms to Fannie Mae. Thus, the Lender Placed Insurers and Servicers have little incentive to hold premium costs down. In addition, Fannie Mae is often paying twice for Insurance Tracking services; once via the servicing fee that Fannie Mae pays to Servicers, and again via the Lender Placed Insurance premiums, since those premiums may include or subsidize the costs of tracking services (to the extent that insurers are providing such services).

In appropriate Circumstances, Lender Placed Insurance is necessary and important to the preservation of Fannie Mae assets. However, much of the current Lender Placed Insurance cost borne by Fannie Mae results from an incentive arrangement between Lender Placed Insurers and Servicers that disadvantages Fannie Mae and the homeowner.

CEJ believes the DFS agrees with this basic proposition and that the small percentage of the borrowers in a loan portfolio charged for FPI should be shouldering the costs of the portfolio-wide expense of insurance tracking. If no single borrower failed to maintain required insurance and no FPI coverage was ever issued under the master policy and no FPI premium was ever charged by the FPI insurer to the servicer, the servicer would still incur the costs of tracking insurance on every loan in the covered portfolio.

CEJ's concern with 227.6(g)(1) is that FPI insurers will claim all or nearly all insurance costs as insurance costs through this exemption. CEJ has seen the likely claims already. In 2013, American Security Insurance Company (ASIC) made a rate filing for FPI. The Florida Office of Insurance Regulation (OIR) attempted to obtain expense information from ASIC regarding details of insurance tracking expenses and which expenses were included in proposed rates and which were excluded. The OIR requested the following in reference to a chart showing the various activities along the "waterfall" of insurance tracking:

Provide for each box relative to American Security and its servicers total time and dollars spent on each activity split between bank mortgage and insurance function and separately document how much is included in rate filing indications for any expense category Commissions, Other Acquisition or General Expense.

In response, ASIC refused to provide the requested expense break-out and claimed any such break-out was impossible because insurance tracking was one continuous process:

The Sample Monthly Insurance Tracking Waterfall illustrates the process by which an insurer issuing lender placed insurance ascertains and manages its exposure and also minimizes the unnecessary placement of policies for periods during which standard homeowners coverage is in place. Because the lender-placed insurer issues a master policy under which all properties not otherwise insured by an acceptable homeowners policy are automatically and continuously insured, the onus falls on the insurer to identify those properties with respect to which it is on risk. As the determination of adequate capital, purchase of reinsurance, and completion of other important insurance functions are predicated on the ability to accurately identify and monitor exposures, the entire process is clearly part of the insurance function, supporting risk and exposure management aims.

While a number of levels of achievement of a reduction in the number of potential lender placed policies is shown in the Tracking Waterfall, these represent artificial markers or signposts describing conditions alongside a continuous process, not separate functions or processes in themselves. To give an example: much of the activity along the waterfall chart is accomplished via mail or phone calls. The mail processing and phone calls are not performed by discrete units portioned in the manner of the chart. They are instead performed by comprehensive mail units, or phone call units, consistent with the continuous process described above. Costs for phone calls and mail are recorded in the aggregate. However a finer distinction does not exist, as all the costs relate to a single continuous process. The measurement of expense is only available to us at the process

level, and not at a sub-process level of distinction. Thus, while the chart is useful to illustrate the effectiveness of this process, we cannot provide expense information specifically attributable to each step in the process.

We attach ASIC's correspondence with OIR and our detailed response to ASIC's claims, including a refutation of the argument that an insurer must perform insurance tracking for "risk and exposure management" at pages 5-7. Among several reasons why insurance tracking is not necessary for the insurer to perform risk and exposure management is the fact that insurers underwrite a servicer at the loan portfolio level without any reference to individual properties. As shown in scheduled rating templates in filings made across the states, the factors used by ASIC and other LPI insurer to underwrite a loan portfolio are all characteristics of the loan portfolio and do not reference individual filings.

The take-away from the ASIC response to the OIR request for expense information – as well as similar responses by QBE companies in Florida in response to similar requests for expense information – is that insurers will use the 227.6(g)(2)(i) exception to improperly include insurance tracking expenses in rate filings.

Additional evidence of insurer intent to evade the prohibition against offering free or below-cost services is found in court pleadings in which representatives of the servicer and FPI insurers argue that the DFS settlement provision identical to 227.6(g) with FPI insurers allows insurance tracking expenses to be included in FPI rates. For example, in a pleading in a lawsuit over excessive FPI charges, Wells Fargo argues:¹

Further, whether or not the filed-rate doctrine is an absolute *bar* to any cause of action, it would be difficult to assert that an 11% commission is "unreasonable" or "inappropriate" in Florida, where the insurance commissioner expressly approved this commission rate. The same goes for including the cost of tracking expenses in LPI premiums in New York, which has ruled that tracking expenses may appropriately be included.

Discussion of 227.6(g)(2)(ii)

As discussed above, insurance tracking is the responsibility of the servicer. If false placement of FPI occurs, it is a result of a failure of the servicer or the servicer's insurance tracking agent to obtain required evidence of insurance. Allowing the costs of issuing and canceling falsely-placed FPI to be included in FPI rates is inappropriate and unfair for several reasons.

¹ Opposition to Plaintiff's Motion for Class Certification McKenzie, et al v. Wells Fargo Bank, N.A., et al, Case 3:11-cv-04965-JCS in the US District Court, Northern District of California – San Francisco Division, July 9, 2013 at page 23.

First, the borrowers who are falsely-placed are not charged for FPI, so the costs associated with false placement are borne by those borrowers who are charged for FPI if such expenses are included in the charges to borrowers. Consequently, borrowers charged for FPI are charged for activities which they did not cause or could have stopped. A borrower charged for FPI is not able to prevent false placement of another borrower.

Second, by allowing expenses for false placement to be included in FPI rates, instead of being borne by the servicer whose failure led to the false placement, the service not only has less incentive for avoiding false placement, but the possibility increases dramatically for a borrower who, in fact, does have required insurance, to pay for both voluntary insurance and FPI. Hopefully, many or most borrowers who are false-placed will contact the servicer and get the FPI charges reversed. But, there will surely be some number of borrowers who have required insurance, who are false-placed and, for whatever reason, do not notify the servicer to get the FPI charges reversed. Including expenses associated with false-placement in FPI rates creates incentives for placement or at least reduces incentives to avoid false placement.

Third, the servicer is responsible for insurance tracking, so the cost of errors associated with insurance tracking should be borne by the servicer.

Minimum Loss Ratio Standard

Section 227.7 states that FPI insurers must submit rates with a permissible loss ratio of at least 62%. However, no explanation or support is provided for this permissible loss ratio standard and the term permissible loss ratio is not defined. CEJ suggests and requests that permissible loss ratio be defined in terms of specific loss, loss adjustment expense and other expense categories. We recommend that the loss numerator in the permissible loss ratio include only expected loss and loss adjustment expenses and exclude net reinsurance costs.

We also recommend that expenses other than loss, loss adjustment and net reinsurance costs be capped at 15% because expenses associated with selling and administering a master FPI policy should be significantly less than those associated with, for example, homeowners insurance. An FPI insurer will have dozens or hundreds of policyholders and not the hundreds of thousands of policyholders a homeowners insurance company will have. Consequently, any marketing expense is limited to a small number of potential insureds. In addition, FPI insurers underwrite at the portfolio level and do not incur costs of underwriting an individual property, including obtaining credit scores, CLUE reports, detailed information about the consumer or property. The issuance of coverage under an FPI master policy is less expensive than issuance of a homeowners policy because the issuance of coverage under the FPI master policy is fully automated. When the insurance tracking database or mortgage servicing system of record indicates a lack of required coverage and that required notices have been sent, the cover letter and coverage under the FPI policy are issued automatically. Such differences in sales, underwriting and administrative activities must be reflected in lower expense loads for FPI than homeowners insurance.

From: Lee, Robert
Sent: Tuesday, July 02, 2013 3:48 PM
To: PCFREDMS
Subject: 13-04125
Attachments: Wells Fargo.pdf

From: Lee, Robert
Sent: Tuesday, July 02, 2013 3:47 PM
To: Miriam.McReynolds@assurant.com; 'Ron.Brusky@assurant.com'
Subject: American Security 13-04125 question

Please see the attached from the recent Washington LPI meeting.

Note the first box which is light says Monthly Expirations.

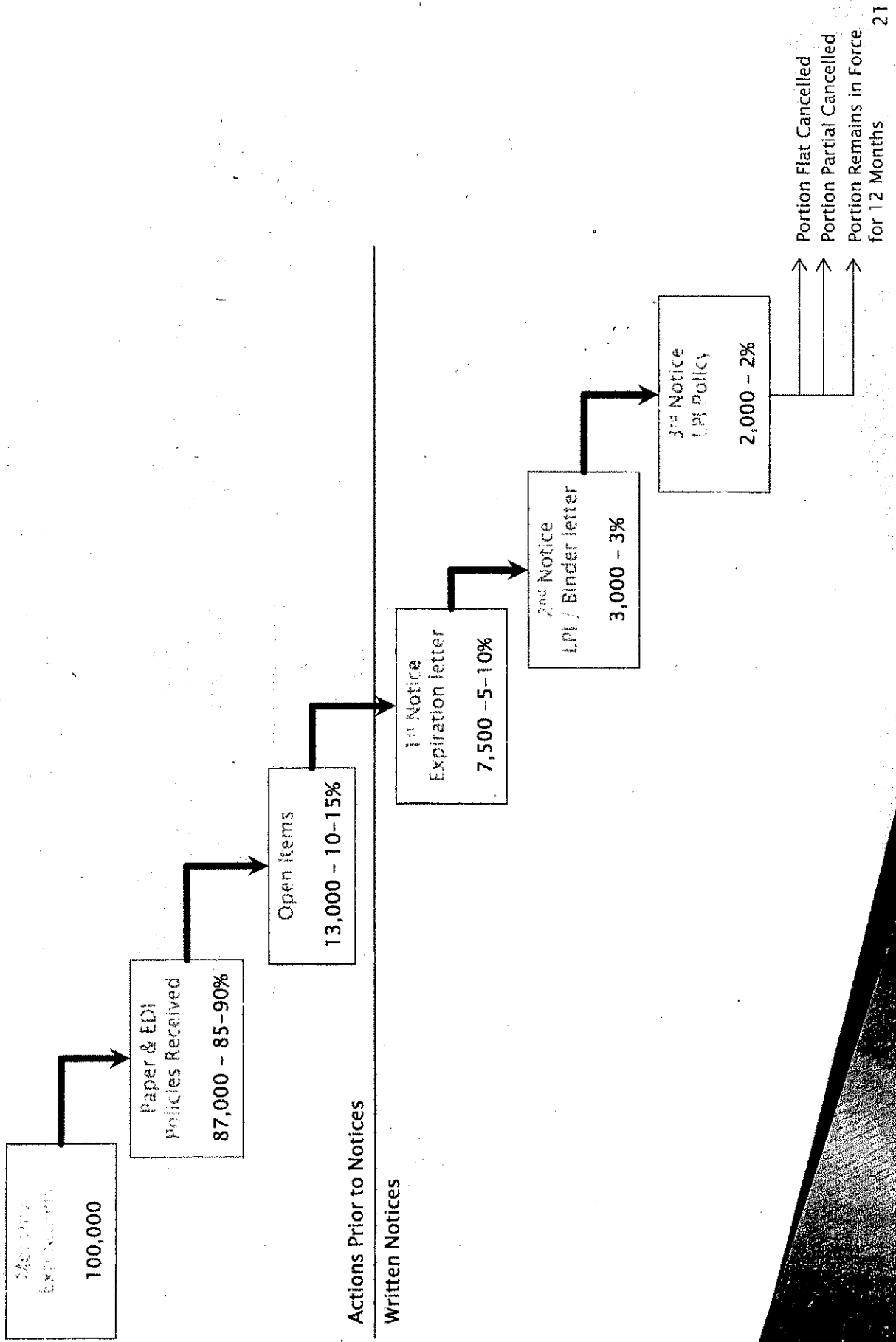
Provide for each box relative to American Security and its servicers total time and dollars spent on each activity split between bank mortgage and insurance function and separately document how much is included in rate filing indications for any expense category Commissions, Other Acquisition or General Expense.

Provide this by 7/16/2013.

Any questions, contact me.

Robert Lee
Actuary
Florida Office of Insurance Regulation
850-413-5360

Sample Monthly Insurance Tracking Waterfall





ASSURANT

**American Security
Insurance Company**
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Atlanta, GA 30339-2210
T 770.763.1000 F 770.859.4403

www.assurant.com

July 12, 2013

Mr. Robert Lee, Actuary
Florida Office of Insurance Regulation
Bureau of Property & Casualty Forms and Rates
P. O. Box 7700
Tallahassee, FL 32314-7700

Re: OIR File Number: FCC 13-04125
Company Filing Number: MONR FL05638AS00156
American Security Insurance Company
Property (Fire)/Commercial – Collateral Protection – Dual Interest
Mortgagee's Interest Protection Program (MIP)
Rate/Rule (File and Use)

Dear Mr. Lee:

Please see the attached document in response to your request for additional information.

Thank you kindly for allowing us to respond.

Feel free to contact me if you need additional information or have any questions.

Sincerely,

Miriam L. McReynolds
Senior Contract Compliance Analyst
Phone No.: 1-800-852-2244, Extension 12514
Fax No.: (770) 859-4366
Email Address: miriam.mcreeynolds@assurant.com

cc: MONR_FL_AS_R6

American Security Insurance Company Mortgagee's Interest Protection Program

Florida

Response to Additional Information Request Sent on July 2nd, 2013

American Security Insurance Company is providing additional information to facilitate the review of this filing.

The Sample Monthly Insurance Tracking Waterfall illustrates the process by which an insurer issuing lender placed insurance ascertains and manages its exposure and also minimizes the unnecessary placement of policies for periods during which standard homeowners coverage is in place. Because the lender-placed insurer issues a master policy under which all properties not otherwise insured by an acceptable homeowners policy are automatically and continuously insured, the onus falls on the insurer to identify those properties with respect to which it is on risk. As the determination of adequate capital, purchase of reinsurance, and completion of other important insurance functions are predicated on the ability to accurately identify and monitor exposures, the entire process is clearly part of the insurance function, supporting risk and exposure management aims.

This process also minimizes the unnecessary placement of policies, where a lender-placed policy is issued for a period during which standard homeowners coverage is in place. The process shown is rigorous, involving a number of steps and tasks to ascertain whether acceptable standard homeowners coverage is in effect on a continuous basis or whether there is in fact a lapse in such coverage necessitating lender-placement of a policy. During this process the borrower is provided multiple opportunities to demonstrate that an acceptable homeowners policy is in fact in place. This process also benefits borrowers in various ways, including the minimization of unnecessary placements, which reduces the insurer's exposure management expenses, as issuance and cancellation of policies represents a frictional cost that adds to the overall cost of the lender placed product and is ultimately reflected in the rate. This process also serves to alert borrowers who may not have realized that their standard homeowners coverage had lapsed, thus enabling them to move more quickly to renew or purchase such coverage from the carriers of their choice.

While a number of levels of achievement of a reduction in the number of potential lender placed policies is shown in the Tracking Waterfall, these represent artificial markers or signposts describing conditions alongside a continuous process, not separate functions or processes in themselves. To give an example: much of the activity along the waterfall chart is accomplished via mail or phone calls. The mail processing and phone calls are not performed by discrete units portioned in the manner of the chart. They are instead performed by comprehensive mail units, or phone call units, consistent with the continuous process described above. Costs for phone calls and mail are recorded in the aggregate. However a finer distinction does not exist, as all the costs relate to a single continuous process. The measurement of expense is only available to us at the process level, and not at a sub-process level of distinction. Thus, while the chart is

useful to illustrate the effectiveness of this process, we cannot provide expense information specifically attributable to each step in the process.

There are other standard insurance processes which occur over periods of time for which the breakdown of expense corresponding to any specific time interval is not generally known. The question asked is not dissimilar from allocating general expense across the life of a policy, or ULAE expense across the life of the claim for the purposes of computing ULAE reserves. Although the total cost is known, apportioning it accurately over the life of claims would require lengthy time and motion studies to accomplish, and general rules of thumb are normally employed for this type of exercise. Such rules of thumb do not exist for the specific query at hand as it relates to lender placed insurance exposure management expenses, however.

It can be noted that even if this type of expense allocation existed, it would be subject to considerable variance. Placement activity and placement rates are strongly influenced by a number of factors - economic conditions, loan quality, foreclosure activity, ability of borrowers to make payments, and availability of insurance in the voluntary market, among others.

Other expense studies showing a different level of granularity and allocation than the Insurance Expense Exhibit have been performed, and service expenses not related to exposure management or direct product expenses have been identified and separated from the remainder of the expenses. These non-insurance expenses have already been removed from the filing, as discussed with the OIR. The remainder of our expenses, including the exposure and risk management expenses identified above, is fully included in our filing to the OIR, as per actuarial standards of practice and OIR regulations.

**Supplemental Comments of the Center for Economic Justice
Objecting to Approval of American Security Insurance Company
Florida Lender-Placed Insurance Rate Filing, OIR # 13-04125**

July 15, 2013

On July 12, 2013, ASIC sent a response to the following question from OIR regarding ASIC's "sample monthly insurance tracking waterfall" presented at the FHFA LPI meeting in June 2013:

Provide for each box relative to American Security and its servicers total time and dollars spent on each activity split between bank mortgage and insurance function and separately document how much is included in rate filing indications for any expense category Commissions, Other Acquisition or General Expense."

ASIC's response fails to answer OIR's question. Instead, ASIC argues that all expenses associated with insurance tracking activities should be included in LPI rates. This argument is incorrect and, if accepted, would allow LPI insurers to include kickbacks to mortgage servicers in LPI rates with the result that mortgage servicers will charge unreasonable and excessive amounts to borrowers for LPI and then claim, falsely, that the charges to borrowers were approved by state insurance regulators.

ASIC's July 12, 2013 non-substantive response underscores the requirement for OIR to disapprove the proposed filing and to take action to disapprove the current rates of ASIC.

ASIC's argument that insurance tracking is part of the insurance function – "supporting risk and exposure management" – is illogical and demonstrably incorrect.

Insurance tracking is a function of and the responsibility of the mortgage servicer. This fact is admitted by ASIC in its March 1, 2013 cover letter to the filing:

Any type of real estate loan involving a commercial or residential structure requires the borrower to keep sufficient insurance coverage in force to satisfy the lender's interest should the structure (collateral) be destroyed or damaged. In order to make sure this requirement is met, **most lenders have a department which keeps track of all the insurance policies covering properties for outstanding loans.** If borrower provided coverage is cancelled or expired, **the lender begins sending a series of follow-up letters** to the borrower reminding the borrower of his obligation to keep insurance in force. **If the borrower fails to comply, the lender will request issuance of the policy.**

This description, unlike that of the July 12, 2013 ASIC response, is consistent with regulatory requirements of servicers as well as contractual requirements of servicers by mortgage owners. The mortgage servicing rule promulgated by the Consumer Financial Protection Bureau in January 2013 sets out specific requirements of **servicers** regarding notification to borrowers prior to the servicer charging for LPI, among other requirements of the servicer. The CFPB's rule clearly contemplates that insurance tracking is the responsibility of the servicer. Consequently, expenses associated with insurance tracking are the responsibility of the servicer.

The fact that insurance tracking is not an expense properly included in LPI rates is further demonstrated by the Fannie Mae Request for Proposal for Insurance Tracking and LPI servicers. Fannie not only identified insurance tracking as a separate activity from provision of LPI, but specifically identified the issue that including tracking expenses in LPI rates caused mortgage owners to pay servicers twice for insurance tracking – once in the service fee mortgage owners pay to servicers and second in inflated LPI rates when mortgage owners are forced to pay for LPI when a borrower defaults. The Fannie RFP from March 2013 states:

After extensive internal review, Fannie Mae believes that current Lender Placed Insurance costs are not market competitive and can be improved through unit price reductions and fee transparency to the benefit of both the taxpayers and homeowners.

Current Situation

Fannie Mae's current Lender Placed Insurance situation is as follows:

1. Homeowners are required to maintain voluntary hazard insurance on Fannie Mae insured properties.
2. Lender Placed Insurance must be acquired by mortgage Servicers when a property is no longer eligible for Voluntary Insurance, or when the Servicer cannot obtain proof of adequate Voluntary Insurance from the homeowner, irrespective of whether or not that homeowner is current or delinquent on the loan.
3. The cost of Lender Placed Insurance is higher than the cost of voluntary hazard insurance. Homeowners are billed for the Lender Placed Insurance premiums. However, if the homeowner does not pay the premium (for example, if the property has already been vacated), then Servicers pass on the premium costs to Fannie Mae.
4. Servicers are responsible for providing tracking services, per Fannie Mae Guidelines. Many large Servicers have chosen to outsource the Insurance Tracking and associated administrative process to third parties, the largest of which are affiliated with Lender Placed Insurers.
5. Lender Placed Insurers often pay commissions/fees to Servicers for placing business with them. The cost of such commissions/fees is recovered in part or in whole by the Lender Placed Insurer from the premiums, which the Servicers pass on to Fannie Mae.

6. The existing system may encourage Servicers to purchase Lender Placed Insurance from Providers that pay high commissions/fees to the Servicers and provide tracking, rather than those that offer the best pricing and terms to Fannie Mae. Thus, the Lender Placed Insurers and Servicers have little incentive to hold premium costs down. In addition, Fannie Mae is often paying twice for Insurance Tracking services; once via the servicing fee that Fannie Mae pays to Servicers, and again via the Lender Placed Insurance premiums, since those premiums may include or subsidize the costs of tracking services (to the extent that insurers are providing such services).

In appropriate Circumstances, Lender Placed Insurance is necessary and important to the preservation of Fannie Mae assets. However, much of the current Lender Placed Insurance cost borne by Fannie Mae results from an incentive arrangement between Lender Placed Insurers and Servicers that disadvantages Fannie Mae and the homeowner.

“Supporting Risk and Exposure Management”

ASIC’s argument that insurance tracking – “the entire process is part of the insurance function” – is necessary to support “risk and exposure management aims” is incorrect and contradicts both the statement by ASIC in its March 1, 2013 cover letter, cited above, and statements in response to OIR questions that “non-insurance expenses have already been removed from the filing”¹ by ASIC.

It is clear that insurance tracking is not equivalent to the “determination of adequate capital, purchase of reinsurance . . . are predicated on the ability to accurately identify and monitor exposures” as claimed by ASIC. While a sound insurance tracking practice by the servicer is important for the LPI insurer, that fact does not equate to insurance tracking being an expense properly included in LPI rates. Insurance tracking is not necessary for the determination of adequate capital and the purchase of reinsurance. This fact is borne out by the following:

LPI is underwritten and priced, through schedule rating, at the servicer portfolio level. An LPI insurer like Assurant is able to underwrite and price at the portfolio level because characteristics of the loan portfolio reveal to Assurant the likelihood and location of LPI placements. If Assurant or other LPI insurers were not able to underwrite based on portfolio characteristics – as opposed to actual numbers of LPI policies in place – the LPI insurers would never be able to write a new master policy.

¹ Page 2 of ASIC July 12, 2013 response to OIR

Current LPI coverages in force are not necessarily a guide to future LPI placements. LPI placements – LPI coverages in-force – can vary dramatically over a 12-month period. If ASIC or other LPI insurers relied upon LPI coverages in force for capital and reinsurance determinations, the LPI insurers would have had to stop writing LPI insurance in 2007 when LPI exposures increased by 50% from 2006 or would have had to stop writing LPI again in 2008 when LPI exposures increased by 33% from 2007. The changes in LPI exposures are even more dramatic when looking at Florida alone. Needless to say, ASIC and other LPI insurers wrote the additional business.

In addition, LPI placements are affected by broader economic conditions and Assurant is aware of this, as noted below. Changing economic conditions in the country or in particular regions, including the unemployment rate, and changing procedures for foreclosure significantly impact the LPI placement rates. These factors are clearly more important for projecting capital and reinsurance needs than current coverages in-force.

ASIC's LPI exposures have grown significantly when existing servicer clients acquired additional servicing portfolios or Assurant acquired new clients. The ability to accommodate this change in LPI exposures is clearly not dependent on insurance tracking activity. In a conference call with investment analysts discussing results for first quarter 2013, Assurant CEO Robert Pollack stated,

“We now provide insurance and related services for nearly 33 million loans. This represents a 16% increase from first quarter of last year, even though we believe the nationwide inventory of mortgage loans declined over that period. Our strategy of aligning with market leaders continues to pay off. In the next 2 quarters, we will add another 900,000 loans from portfolio acquisitions of 2 of our clients.”²

In that conference call, Assurant CFP Michael John Peninger stated,

“We onboarded 1.7 million loans in the first quarter. And, as Rob mentioned, we expect to add another 900,000 loans over the next two quarters. These 2.6 million new loans will produce premiums starting later this year. The changing composition of our loan portfolio, combined with macro trends will lead to lower placement rates in the future; however the new loans will help sustain our revenues over the course of 2013.”³

² Assurant Earnings Call Transcript 2013 First Quarter, attached, at pages 2 - 3

³ Assurant Earnings Call Transcript 2013 First Quarter, attached, at page 4.

Later in the call, Peninger and Pollock stated the following:⁴

Michael John Peninger

“Well, there's a lot of expenses associated with onboarding the loan, Sean, and we've got a couple of things going on, just adding the loans, getting them onto the system, and then you've got - going forward, you've got the service requirement for those. And we're certainly committed to maintaining the highest levels of service that we've had in the past, so that requires a certain amount of staff to do that. We have a very sophisticated system that helps us in this. So there's - they're not all purely variable cost, but there are certainly some of those, and we want to be sure that we're maintaining our customer service levels.”

Robert B. Pollock

“And some of those expenses come before the premium shows up. And that's always been how this business has worked and I think will continue to. So these portfolio additions are not coming from existing clients, which is a little bit different than if they come from someone we have already. There's expenses if we lose from one of our clients but it goes to another. We know all the processes, procedures. We know something about the loans. When they come from a portfolio we don't have, there's more work involved.”

Assurant's Reinsurance Program Clearly Does Not Depend on Insurance Tracking

The attached article, reflecting an Assurant press release, describes Assurant's 2013 property casualty reinsurance program. The release states that the 2013 catastrophe reinsurance program includes newly issued three-year catastrophe bonds. A reliance on three-year catastrophe bonds cannot be based on current in-force exposures, but must be based on projections of in-force exposures over a three-year period in which the actual in-force LPI exposures will vary dramatically as borrowers either obtain voluntary insurance or have their homes foreclosed.

In summary, while it is important for an LPI insurer to insist that a mortgage servicer have an effective insurance tracking program in place to ensure the LPI insurer is receiving premium for coverages provided, insurance tracking expenses are not necessary for “risk and exposure management” and must be excluded from LPI rates. The quotes from Peninger and Pollock indicate that Assurant, in fact, evaluates risk and exposure at the portfolio level and that “macro” factors play a critical role in evaluating risk and exposure on a going-forward basis.

The earnings call transcript quotes also show that, even though Assurant incurs significant expenses for various hazard outsourcing services provided to servicers like boarding new loans and insurance tracking, Assurant considers these expenses associated with LPI premium revenues. It is essential for insurance regulators to break that linkage in terms of LPI rates. While it is reasonable for Assurant to provide hazard outsourcing services and may even be reasonable for Assurant to require the servicer utilize Assurant for insurance tracking if the

⁴ Assurant Earnings Call Transcript 2013 First Quarter, attached, at page 10

servicer wants to use Assurant for LPI, it is profoundly unreasonable for these non-insurance expenses – which are associated with portfolio wide activities of the servicer – to be included in rates which are ultimately charged by the servicer to only 2% to 3% of the borrowers in the loan portfolio.

ASIC has completely failed to justify the expense provisions in the proposed rates.

ASIC's response to OIR regarding the tracking of expenses by insurance tracking is simply not credible. Moreover, ASIC's only public explanation of expenses in its proposed rates is the unsubstantiated declaration that "these non-insurance expenses have already been removed from the filing, as discussed with OIR."

Regarding expenses associated with the waterfall diagram of insurance tracking activities, the only documents that go out with ASIC's letterhead are the certificates of insurance and LPI policies attached to the 3rd notice letter. All three written notices are sent on the servicer's letterhead. Clearly, the expenses associated with these notices as well as the expense associated with sending the borrower the certificate of insurance and LPI policy are servicer expenses and not reasonably included in LPI rates. While the cost of printing the certificate and LPI policy sent to borrowers is a reasonable LPI expense, the requirement to send notices as well as the LPI certificate and policy is a requirement of the servicer.

In terms of call center expenses, any calls out, as well as processing of paper and EDI documents from insurers, from Assurant to ascertain the existence of required insurance is a responsibility of the servicer outsourced to Assurant and not properly included in LPI rates. The only call center activity reasonably included in LPI rates are borrower calls related to insurance coverage and claims. Clearly, such calls are a tiny percentage of overall call center activity.

ASIC's claim that it is unable to break down insurance tracking expenses by activity is not credible. ASIC states, "However, a finer distinction does not exist, as all the costs relate to a single continuous process. The measurement of expense is only available to us at the process level, and not at a sub-process level of distinction." As the attached article from the MIT Sloan Management Review from 2011 attests, Assurant collects very detailed data on its call center operations in order to perform predictive modeling on customer calls. Given this level of data collection and analysis, it is difficult to believe that ASIC does not track customer calls by type of calls and cannot identify which calls are associated with responses to first or second notices and which calls are associated with LPI claims, for example.

ASIC's claim that certain expenses cannot be assigned to a specific time frame is not credible. The issue is not allocating general expenses over the life of a policy or ULAE over the life of a claim. Rather, the issue is what expenses were actually incurred for specific activities during the calendar year for purposes of reporting in the statutory annual statement. While there can be variance in expenses by category across different time periods, this is addressed by utilizing a multi-period time frame for analysis of the expenses. The issue of expense variation is not addressed by failing to categorize the expenses.

In conclusion, ASIC has failed to respond to OIR's request for expense provision support and has failed to justify the expense provisions in the proposed filing. Since the current ASIC rates clearly contain expenses not properly associated with the provision of LPI, ASIC's current rates are excessive and must be disapproved.

MITSloan Management Review

Interview by Michael S. Hopkins and Leslie Brokaw

Matchmaking With Math: How Analytics Beats Intuition to Win Customers

lytics?” And the answer is sort of subjectively, yes, we want those benefits, but next year.

There are early adopters and there are adopters. I wouldn't call what we do an early adoption of a technology; it's using very state-of-the-art tools just in a little bit of a different way. I think our creativity is in how we deployed it.

The program you developed at Assurant — called “RAMP,” for “Real-time Analytics Matching Platform” — is now available to other organizations that have to manage inbound calls. What do you see in organizations that makes it hard to apply analytics in this kind of an effective way?

The first one is, “I don't have the IT resource to go do this right now.” You have to go compile the evidence, and that's not a trivial task for most IT departments. It's all data that they have, but in these days everyone's stressed and pushed for projects and IT time.

Another objection is the perception that this is just a skills-based routing solution and that we already *have* skills-based routing. That's an inter-

esting one to overcome because, first off, this use of analytics is not skills-based routing. It's evidence-based or success-based routing. We don't really care about a CSR's skills as defined by a skills-based routing system, and in fact we tell you that the skills that you assign a CSR are practically *irrelevant*.

Those are legitimate objections. What do you say to get someone started down the path that could enable them to get results like yours?

Well, we have proof that it works. But hearing about 187% improvement over baseline at Assurant is hard to believe at times. So we say, let us prove it to you by giving us some teaser data.

We can show you, based on your data, that you are not fully optimized and that you are relatively randomized in your routing — because effectively that's the premise statement here. We are taking randomness and chaos and making order out of it.

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Matchmaking With Math: How Analytics Beats Intuition to Win Customers

In sales, the rapport between a prospective buyer and seller can be the deciding factor. Using analytics, Assurant Solutions has tripled its success. (A case-study interview.)

INTERVIEW BY MICHAEL S. HOPKINS AND LESLIE BROKAW

ASSURANT SOLUTIONS SELLS credit insurance and debt protection products. Maybe you've bought a product like theirs. If you lose your job or have medical problems and are unable to make a credit card payment, Assurant Solutions will help you cover it.

Like a lot of insurance products, payment protection is a discretionary add-on often made at the point of purchase. But when customers get the bill and see the additional fee of, say, \$10.95 per month for payment protection, maybe they think, "Well, I'll take my chances" and decide to cancel.

When those customers call, they reach Assurant Solutions customer service representatives, because the company manages insurance activation, claims, underwriting and customer retention (for many industry-leading banks and lending institutions).

It's in that last piece — that attempt to retain customers, beat the churn and stem a high exit rate — that Assurant Solutions faced a now-universal management challenge. As a call center positioned as the pivot point of all customer inter-

By implementing analytics-driven matching of customers and service reps, Assurant Solutions improved call center performance three fold.

THE LEADING QUESTION
 If analytics are brought to bear on a call center, how are operations and results affected?

FINDINGS

- ▶ Many conventional beliefs about call centers prove to be wrong. For instance, customers will wait longer than expected.
- ▶ Evidence trumps intuition when predicting outcomes.
- ▶ Conflicting goals can be reconciled in real time by analytically driven models.



action for its clients, Assurant had access to hoards of data as well as the ability to create the kinds of rules and systems that any operationally optimized call center would deploy. With skills-based routing, customized desks with screen pops, and high-end voice recording and quality assurance tools, its efforts were state-of-the-art.

But it wanted to do better. Its 16% retention rate was consistent with the best industry standards, but that still meant that 5 out of 6 customers weren't convinced to keep their coverage, let alone consider other products. That's a lot of room for opportunity.

So Assurant Solutions tried something new: deep analytics. And it invented an operations system that capitalized on what the analytics prescribed.

The result? The success rate of its call center nearly *tripled*.

What Assurant Solutions found was that all the conventional tenets about contact centers "are not necessarily wrong, but they're obsolete," says Cameron Hurst, vice president of Targeted Solutions at Assurant. Hurst previously headed up development for HSBC's Indian offshore Global Technology group and served as HSBC's group head of contact center technology after HSBC acquired the call center software company he founded in 1992, so he was already expert in getting the most out of data to run call centers. Or so he thought.

But, he says, "we operated under the fallacy — and I believe it's fallacious reasoning — that if we improve the operational experience to the nth degree, squeeze every operational improvement we can out of the business, our customers will reflect these improvements by their satisfaction, and that satisfaction will be reflected in retention. And that was fundamentally wrong. We learned that operational efficiency and those traditional metrics of customer experience like abandon rate, service levels and average speed to answer are *not* the things that keep a customer on the books." Assurant Solutions was looking for the key to customer retention — but was looking in the wrong place.

So management attacked the challenge from a different angle. They brought in people like mathematicians and actuaries — people who didn't know anything about running call centers — and they asked different kinds of questions, using analytics to answer them. "We're an insurance company," Hurst says, "so it's in our DNA to be very data-driven. We are able to look at large volumes of historical data and find ways to mine for gold nuggets or needles in haystacks. But this use of analytics was fresh for us."

What they found surprised them. In a sense, it was simple: They found that technology could assist the company in retaining customers by leveraging the fact that some customer service reps are extremely successful at dealing with certain types of customers. Matching each *specific* in-calling customer to a *specific* CSR made a difference. Not just an incremental difference. A huge difference. Science and analytics couldn't quite establish *why* a particular rapport would be likely to happen, but they could look at past experience and predict with a lot of accuracy *that* a rapport would be likely to happen.

In the interview that follows, Hurst explains how Assurant Solutions figured out the right questions to ask, used analytics to focus on new ways to match customers with reps and figured out the best ways to solve the problem of conflicting goals. He spoke to *MIT Sloan Management Review* editor-in-chief Michael S. Hopkins.

Different Questions, Different Results

Most organizations already mine their data for insights. How can they apply analytics in new ways that will discover untapped opportunities for value creation?

One of the first questions anyone would have, reading about your experience, is how did you get answers to questions you didn't even know you should be asking? What triggered the epiphany that caused you to start looking at things differently?

The epiphany occurred because we knew we wanted more. We wanted to retain more customers, and we

wanted to get more wallet share by up-selling them.

And so we put the problem to a different group. We went to the decision sciences group, to the actuaries and the mathematicians, and we asked them, "Is there anything you can see that we can do better or that we can optimize more?" They weren't looking at it from the perspective of "How do I run a contact center?" In fact, these people don't know anything about contact



It's the old adage in business: People do business with people they want to do business with. If you're successful at establishing rapport with your customer, you have a higher probability of selling them. We drive rapport by finding attributes that enable us to create likeness across that CSR-and-customer synapse.

— CAMERON HURST

centers. So I think the first important step was to have a different set of eyes looking at the problem, and looking at it from a completely different discipline.

If they didn't know how a contact center runs, or what things have been effective, where did they start?

The first thing that was interesting about their approach was that rather than thinking about the average speed of answering phone calls, or the average "handle time," or service level metrics, or individual customer experiences or using QA tools to find out what we did right and what we did wrong — all the things we usually consider when looking at customer and representative interaction — they started thinking of it purely from the perspective of, "We've got success and we've got failure."

Success and failure are very easy things to establish in our business. You either retained a customer calling in to cancel or you didn't. If you retained them, you did it by either a cross-sell, up-sell or down-sell.

So this is what they started asking: What was true when we retained a customer? What was true when we lost a customer? What was false when we retained a customer? And what was false when we lost a customer? For example, we learned that certain CSRs generally performed better with customers in higher premium categories while others did not. These are a few of the discoveries we made, but there were more. Putting these many independent variables together into scoring models gave us the basis for our affinity-based routing.

That broadens the information they were looking for, right?

Definitely. These are data-oriented people, so they just simply said, "Give us everything — all the data you've got." And we had a lot, because we've been running this business for years. We had information

about our customers that seemed, from the perspective of call center routing, totally irrelevant. We had a lot of data in the contact center about agents' performance, the time they spend on calls and the like. They took the whole data set and started crunching it through our statistical modeling tools.

The approach they took was to break down our customers into very discrete groups. To see what's true about our customers. Any bank or insurance company or financial services company that sells products to customers is tempted to cluster their customers into discrete groups. Almost everyone does.

The thing is, it's not 10 clusters that define your unique customer groups, it's usually hundreds of clusters. That was the first process, to find out all the different kinds of customers that we have: customers with high balances who tend to pay off early, customers who have high credit-to-balance ratios, customers who have low credit scores. The more variables that go into the creation of a cluster, obviously the more clusters you can have; so, not just customers with high balances who tend to pay off early, but customers with those characteristics who *also* have low credit scores.

When you've got it down to that granular level, you can then look at all the different customer interactions that we had with people in that cluster and say, "How did we do in this particular case? How did we do in that one?"

Wait — are you looking at every single interaction?

Yes. It wasn't on an aggregate macro but on an individual basis, every single interaction that we recorded over the last four or five years. Looking at all of these interactions let the team see patterns that establish that *this* CSR tends to do well, historically and evidentially, with customers in *these* specific sets of clusters.

What they also discovered was that the results were completely different from the existing paradigms in the contact center.

Sales as Matchmaking (Because “Variability” Means There’s Someone for Everyone)

What it means to understand — and act on — the critical difference between theoretically inferring why something might be likely to happen and evidentially knowing that it is likely to happen.

Let me stop you. As you’ve said, call centers tend to be pretty statistically driven places from the start. You named a bunch of the metrics that you would be looking at from the customer service side, and I’m sure you would have known when a customer called in what his products were and what his history was, and potentially matched him up with CSRs who had expertise in those particular product lines, yes?

That’s what everyone does in the call center world. When they sit down to write and build their routing strategies for how they’re going to move their macro clusters of customers around to CSR groups, they do it almost 100% on *anecdote*. We say that CSRs have expertise in an area. The problem is that expertise is a subjective term. When you deal with what we’ll call carbon-based intelligence — that is, inferential judgments made by us humans — versus silicon-based intelligence, or computerized judgments based on analytics, the carbon-based intelligence will say that this rep goes into this segment because they have expertise. They took a test. Or they grade out well in the QA tools.

What the evidence showed us is that the carbon-based intelligence tends to judge incorrectly. The silicon never does. If the model is set up properly and it has the ability to detect performance through whatever way you tell it to detect performance — by noting cross-sell, down-sell, up-sell, whatever — it will always measure a CSR’s performance correctly and in an unbiased way.

So for the first time you’re looking at both ends of the equation in some different ways. You’ve just described the CSR end, where you have this incredible database that reveals patterns about performance with different groups of customers, in spite of what you may or may not have inferred. What happens on the customer side? Are you looking at them in a different way?

Yes. There are obvious characteristics that we can study in our core systems. Think about what a bank or an insurance company would collect about its customers. Credit score, demographics, maybe some psychographics. We might know how many children they have.

You can predict what you think they’re going to do in the future, as long as you have a large enough customer base with enough interactions and enough variability to look at. Because what this whole thing is based on is variability. There’s a high degree of variability in your customer base, and there’s a high degree of variability in your CSR base. We learned to exploit that variability.

It’s the old adage in business: People do business with people they want to do business with. If you are successful at first establishing rapport with your customer, you have a higher probability of selling them, because there’s a trust relationship versus just taking orders.

We drive rapport and affinity in conversations by finding attributes that we can exploit to match, that create likeness across the CSR-and-customer synapse. It scales to potentially dozens of variables that operate dependently and independently of each other to drive this affinity/rapport relationship.

Having said all this, probably the most significant aspect of our use of analytics to drive conversational affinity was the persistency factor. That is, the length of time that customers remain on the books. We established almost right away that we could save a larger number of customers, as well as more profitable ones, through our new routing engine. But what we wouldn’t learn until later was the fact that we were keeping these customers longer than ever before. This was really exciting to us! As the months went by and we watched the new system operate, we observed an overall higher persistency rate for our saved customers compared to the old system. And since we’re talking about subscription-style products in our business, the longer the customers keep the product, the more revenue we generate. This turned out to be a much more important factor than a pure save or saved fee rate.

Some of this affinity matching is like a version of online dating.

That’s a beautiful metaphor, although there’s one breakdown in it. I would suppose that online dating sites work in a somewhat anecdotal way. It’s driven some-

what based in fact, but it's also very psychographic.

We also go down to a deep level of granularity. Not body type and hair color like online sites might ask, but we do know that, for instance, certain CSRs perform well with customers that have \$80 premium fees, but they don't do so well with customers that have \$10 premium fees. We don't necessarily know the reason why. Nor do we need to.

And therein lies the difference. In our system there isn't a lot of science behind why these differences exist, why a rep might be good with \$80 versus \$10. It's just evident that that person is good with a certain customer type. So we operate off the fact that it's true, based on the body of data that we have about the customer base and our past CSRs' interactions with those

customers. On the other hand, matchmaking sites wouldn't have a lot of historical data about a *particular* individual's interactions with their service (unless, of course, they use it frequently), so they operate off a body of data about people's general characteristics and what makes them interesting to each other.

So do you see the difference? We've become purely evidence-driven: "This CSR always does well with this particular customer type because we've seen it happen."

I would describe it like this: The science does not explain why an affinity will be likely to exist, but it does show that an affinity will be likely to exist.

Exactly.

How Analytics Solves the Problem of Conflicting Goals

What do you do when models predicting things such as best CSR match, willingness of a customer to wait and value of a customer to the company all recommend actions that are in conflict?

It sounds like the kind of information you have about customers is not that different from the kind of information you might have had before this whole process began, and that it's really on the CSR side that you have all this new data, plus the data about what happens in each specific interaction between a customer and a CSR. Is that what drives your models?

That's right. There's one other element that goes into the solution that drives revenue: the predicted economic value of a particular customer. Now, there's not a lot of new science in that, and we have models that tell us how to calculate that. But it's important to the solution, because in a call center we sometimes have to decide which customer to focus on. We like the idea that there's a CSR for everyone, but that's not always true because of call volumes and agent availability. So if your goal is long-term revenue, you can use these economic predictors to determine *which* customers we should be focusing on.

There was a problem we didn't quite know how to solve right out of the gate, and that was the fact that the best matches are almost always not available. In other words, if we have 50 callers in queue and 1,000 CSRs on the floor, we can create 50,000 different solutions, and we make those calculations 10, 15 times a second. One of the 1,000 CSRs is the

best match, so that's the score to beat — the number that shows how often we make that perfect match.

The vast majority of the time, though, those matches weren't immediately possible because that CSR was on the phone, so we had to factor in another predictive model, and that was "time to available." That's not a massively complex model, because the industry has been solving that kind of problem for a long time.

But when you layer "time to available" into the actual scoring engine, you get some interesting results. If an agent's average handle time is three minutes, 30 seconds, and he or she has been on the phone three minutes, 15 seconds, then we can predict they're about 15 seconds away to available. Then we can weigh in our prediction of customer tolerance or customer survivability — how long they're willing to wait in the queue before just hanging up.

We know how long we keep customers in queue. We know what the outcomes are when they've been in queue, and we can find out where the curve starts to steepen in terms of abandon rates or bad outcome rates. We connect that information with our CSR's predictive availability curve. If the optimal match is too far away, maybe 45 seconds or three minutes away, then the score for that optimal match becomes dampened and someone else might look more attractive to

us. Because while they may not have perfect affinity, the fact that they're going to become available sooner certainly makes them look more attractive to us.

When you became more rigorously evidence-based, what did you discover about what might have been wrong in your old assumptions?

The conventional wisdom in the contact center is 80/20 — 80% of calls answered in 20 seconds or less. That's a promise that most businesses make, because they believe that drives satisfaction.

What we learned is that satisfaction has almost nothing to do with that. Obviously the faster you answer, the better, over a larger body of interactions. But we found most customers are willing to wait much, much longer, on the order of 39 to 49 seconds, before annoyance affects outcome.

So our observation was, if customers are willing to wait, why are we trying so hard to force them into that 80/20 or 80/25 window? The longer we're willing to wait, the better the match is, the better the outcomes, the more revenue generated.

We've done tests that push all the way out to 60/60 — 60% of calls answered in 60 seconds or less. At some point there is a negative effect on abandon rates. But what we were surprised to learn is that there is no negative effect on abandon rates until you start approaching 60 seconds. Which obviously means we've got that time to work with in order to find the most ideal customer/CSR match. It leads to a very, very direct impact on revenue. A direct correlation between time and revenue.

To see this work so obviously is amazing, because to go from 80/20 and then jump it to 80/40, and then within a few days to see immediate results in terms of save rates and saved fee rates, it's stunning. It makes you wonder why the rest of the world doesn't get this.

Summarize the results you've seen. The problem was that you were at a 15% to 16% retention rate despite operating in a fairly optimized state-of-the-art way. What's happened since?

We've seen our retention rates, our actual save rates, go as high as 30% to 33%. But that's not the end of the story. For us, we're more focused on *saved fee rate*. Save rate is if two people call in, save one, lose one, that's 50%. But if two people call in and one is worth \$80 to you and the other is worth \$20, you save the \$80 one, you've got an 80% saved fee rate, because you saved \$80 out of a total \$100 eligible.

This relates back to what you said earlier about having to make choices about which customer to serve during busy periods?

Yeah. We use those predicted economic availability models to help us focus on the more valuable customers. That's not to say we discard the less valuable ones, because diversity in our customer base matches the diversity in our CSR force, so if a \$20 customer calls in, we've got a \$20 CSR to match him to. But our focus is on revenue, so saved fee rate is more important to us.

So while our save rates went into the 33-ish range, even as high as 35%, our saved fee rates went into the 47% to 49% ranges. We've seen days where we've been in the 58% range. Effectively that means that 58 cents of every dollar that was at risk has been saved. Those are very substantial numbers for us in our business.

Just so we can do the apples-to-apples comparison, what was the saved fee rate before?

The same as the overall save rate, 15% to 16%. And that's actually a very exciting point to us, that our saved fee rates went up so much more than save rates, because we were focusing on saved fee as opposed to just saved customers alone.

If It Makes So Much Money, Why Doesn't Everyone Do It?

What are the impediments to adopting evidence-based analytics? What can organizations do to overcome them?

Why don't more people see the bottom-line impact of this sort of analytics?

In my own space, in the contact center world, I still am amazed when I come across very, very large Fortune 50 organizations that are still running very,

very old technology. They don't have the appetite to adopt it yet. Their current system is basically working, it's been doing fine.

You scratch your head, saying, "Yeah, but don't you want all the benefits that you can get from ana-

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News Releases

Assurant Finalizes Comprehensive 2013 Property Catastrophe Reinsurance Program Purchases \$185 Million in New Catastrophe Bond Coverage

NEW YORK, July 1, 2013 -- Assurant, Inc. (NYSE: AIZ), a premier provider of specialized insurance and insurance-related products and services, today announces it finalized the structure of the Company's 2013 Property Catastrophe Reinsurance Program, including \$185 million of newly issued three-year, fully collateralized catastrophe bonds.

"Assurant's reinsurance program supports the protection we provide for more than 2.2 million policyholders," said Gene Mergelmeyer, president and CEO of Assurant Specialty Property. "Assurant diversified and expanded our reinsurance coverage by nearly 20 percent this year, leveraging traditional catastrophe reinsurance and catastrophe bonds at lower rates."

Comprehensive Risk Management

Multiple factors are considered in evaluating the size and components of our reinsurance program including the estimated claims loss potential from various perils, the cost efficiency of the reinsurance coverage available and the credit quality, financial strength and claims paying ability of the reinsurers in the program.

Assurant placed its traditional catastrophe program in two phases, in January and June 2013, with more than 50 reinsurers rated A- or better by A.M. Best. The company supplements the traditional 2013 per-occurrence program through reinsurers, with multi-year fully collateralized coverage, financed with catastrophe bonds to further diversify sources of reinsurance capacity. The program provides protection against earnings volatility and helps safeguard Assurant's balance sheet.

Overall, the 2013 Property Catastrophe Reinsurance Program includes:

- **Per-occurrence catastrophe coverage**, providing protection of up to \$1.82 billion in excess of a \$240 million retention or risk retained by the Company. This year's coverage is structured in seven layers, placed 100 percent through traditional reinsurance and catastrophe bonds.
- **Catastrophe bonds**, providing \$315 million of multi-year, fully collateralized hurricane coverage: \$130 million issued in January 2012 by Ibis Re II Ltd. and \$185 million issued in June 2013 by Ibis Re II Ltd. The reinsurance purchased in 2013 from Ibis Re II Ltd. consists of three separate layers of coverage for protection against losses from individual hurricane events, including catastrophe prone areas along the Gulf and East Coasts of the United States, Hawaii and Puerto Rico.
- **Multiple storm protection coverage**, lowering the program retention to \$140 million subsequent to the first event and providing for a maximum recovery of \$100 million for the second and subsequent events.
- **Florida Hurricane Catastrophe Fund (FHCF)¹ coverage**, providing Florida-specific coverage for 90 percent of losses up to \$503 million in excess of a \$192 million retention level.
- **Multi-year traditional and collateralized capacity**, providing \$140 million of limit for coverage in addition to the IBIS Re II, Ltd. on a multi-year basis (\$70 million multi-year traditional, and \$70 million multi-year collateralized, respectively). This additional limit was placed to further enhance Assurant's long-

term protection from catastrophic perils.

An illustration of the 2013 Assurant catastrophe program's layered structure is available in the Newsroom section of www.assurant.com.

In the event of Florida hurricanes, Assurant's catastrophe program for per-occurrence coverage is net of any reimbursements from the FHCF. Traditional reinsurance is the only portion of the program that provides for an automatic reinstatement of coverage for a second occurrence under terms similar to the first occurrence. There is additional per-occurrence coverage of \$102 million in excess of a \$10 million retention for the Caribbean and \$250 million in excess of a \$9 million retention with an \$8 million co-participation for Latin America.

Base pre-tax reinsurance premiums for the entire catastrophe program, which reduce net earned premiums in Assurant's financial statements, are estimated to be \$245 million in 2013, compared with \$233 million in 2012. The increase reflects additional coverage primarily resulting from growth in our exposure in catastrophe prone areas, which now accounts for more than 60 percent of the business. Actual reinsurance premiums will vary if exposure growth changes significantly from estimates or if reinstatement premiums are required due to reportable catastrophe events.

A comparison of the reinsurance retentions, limits and premiums for the prior and current programs is shown below².

	<u>2013</u> (\$ in millions)	<u>2012</u> (\$ in millions)
Florida Hurricane Catastrophe Fund (FHCF)¹		
Gross limit	503	465
Less: co-participation	(50)	(47)
Net limit	453	418
Retention	192	181
Per-Occurrence Catastrophe Reinsurance Program		
Annual Traditional Reinsurance Limit	1,365	1,261
Multi-Year Traditional Reinsurance Limit	70	0
Multi-Year Collateralized Reinsurance Limit	70	0
Catastrophe Bond Limit	315	280
Less: co-participation	0	(20)
Net limit ³	1,820	1,521
Retention	240	240
Multiple Storm Protection Cover		
Retention	140	120
Limit	100	100
Otherwise Recoverable Limit	100	100
Premium Expense	(estimated)	(actual)
Catastrophe Reinsurance Program	245	233

About Assurant

Assurant is a premier provider of specialized insurance products and related services in North America and select

worldwide markets. Its four key businesses-Assurant Employee Benefits, Assurant Health, Assurant Solutions and Assurant Specialty Property- partner with clients who are leaders in their industries and build leadership positions in a number of specialty insurance market segments worldwide.

Assurant, a Fortune 500 company and a member of the S&P 500, is traded on the New York Stock Exchange under the symbol AIZ. Assurant has approximately \$29 billion in assets and \$8 billion in annual revenue.

For more information on Assurant, please visit <http://www.assurant.com> and follow us on Twitter ([@AssurantNews](https://twitter.com/AssurantNews)).

Safe Harbor Statement: Some of the statements included in this press release, particularly those regarding reinsurance coverage or anticipating future financial performance, may constitute forward-looking statements that involve a number of risks and uncertainties. Our actual results may differ materially from those projected in any forward-looking statements. For a discussion of the factors that could affect our actual results please refer to the risk factors identified from time to time in our SEC reports, including but not limited to our 2012 Annual Report on Form 10-K and our first quarter 2013 Quarterly Report on Form 10-Q, each as filed with the SEC.

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¹ 2013 Florida Hurricane Catastrophe Fund limits and retention are estimated based on Florida exposure projected as of June 30, 2013.

² 2013 retention, limits and reinsurance premiums are estimated and can change with growth of the business. Certain 2012 estimates have been updated to reflect actual amounts.

³ 2012 Net Limit includes \$12 million from the 2012 catastrophe bond and \$13 million of the 2010 catastrophe bond above our traditional program. For 2013, there is no additional catastrophe bond coverage above the traditional program limit.

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Assurant Management Discusses Q1 2013 Results - Earnings Call Transcript

Executives

Francesca Luthi - Senior Vice President of Investor Relations

Robert B. Pollock - Chief Executive Officer, President and Executive Director

Michael John Peninger - Chief Financial Officer and Executive Vice President

Christopher J. Pagano - Chief Investment Officer, Executive Vice President, Treasurer and President of Assurant Asset Management

Analysts

Christopher Giovanni - Goldman Sachs Group Inc., Research Division

Seth Weiss - BofA Merrill Lynch, Research Division

A. Mark Finkelstein - Evercore Partners Inc., Research Division

John M. Nadel - Sterne Agee & Leach Inc., Research Division

Sean Dargan - Macquarie Research

Mark D. Hughes - SunTrust Robinson Humphrey, Inc., Research Division

Steven D. Schwartz - Raymond James & Associates, Inc., Research Division

John A. Hall - Wells Fargo Securities, LLC, Research Division

Assurant ([AIZ](#)) Q1 2013 Earnings Call April 25, 2013 8:00 AM ET

Operator

Welcome to Assurant's First Quarter 2013 Earnings Conference Call and Webcast. [Operator Instructions] It is now my pleasure to turn the floor over to Francesca Luthi, Senior Vice President, Investor Relations.

Francesca Luthi

Thank you, Zach, and good morning, everyone. We look forward to discussing our first quarter 2013 results with you today. Joining me for Assurant's conference call are Rob Pollock, our President and Chief Executive Officer; Mike Peninger, our Chief Financial Officer; and Chris Pagano, our Chief Investment Officer and Treasurer.

Yesterday afternoon, we issued a news release announcing our first quarter 2013 results. Both the release and corresponding financial supplement are available at [assurant.com](#). We'll start today's call with brief remarks from Rob and Mike, with Chris participating in the Q&A session.

Some of the statements we make on today's call may be forward-looking, and actual results may differ materially from those projected in these statements. Additional information on factors that could cause actual results to differ

materially from those projected are provided in yesterday's news release, as well as in our SEC reports including our 2012 Form 10-K and upcoming first quarter 2013 10-Q.

Today's call also will contain non-GAAP financial measures, which we believe are meaningful in evaluating the company's performance. For more details on these measures, the most comparable GAAP measures and a reconciliation of the 2, please refer to the news release and financial supplement posted at assurant.com.

Now I will turn the call over to Rob.

Robert B. Pollock

Thanks, Francesca, and good morning, everyone. In the first quarter, we continued to build our foundation for profitable growth. While earnings were down, we expanded and further adapted our business in several areas to address market needs.

For example, at Assurant Solutions, we're growing premiums and taking expense actions in underperforming areas to further improve efficiency. At Specialty Property, we're growing our track loan portfolio, moving ahead with the implementation of our new product and resolving lender-placed matters.

At Health, we're executing on our strategy centered on affordable and accessible products as details of health care reform are finalized. And at Employee Benefits, we're gaining momentum in our voluntary products through targeted distribution. These represent several of the actions we're taking to advance long-term growth, enhance profitability and help consumers protect what matters most for them.

Let me now update you on our key performance metrics for the quarter. Annualized operating return on equity, excluding accumulated other comprehensive income, or AOCI, was 10%. Book value per diluted share excluding AOCI increased by 2%, and net earned premiums and fees increased by 4%, driven by growth at Solutions and Specialty Property.

Our capital position provides us great flexibility, which was further enhanced by our recent debt offering. We continue to regard our stock as attractively priced and believe repurchases are a prudent use of capital. Through April 19, share buybacks for 2013 totaled \$96 million.

Share repurchase activity in the first quarter was affected by settlement discussions with the New York Department of Financial Services. We resumed buybacks following the agreement. Returning cash to investors is an integral part of our disciplined approach to capital management. Our segments generate free cash flow that will allow us to both return capital to shareholders and make ongoing investments to build our business.

Now I'll offer some updates on each of our businesses. Assurant Solutions remains focused on achieving a 14% ROE in 2014. Returns in domestic service contracts continue to exceed our target. On the new business front, our vehicle service contract business benefited from a rebounding U.S. auto market.

Looking ahead, we expect mobile to become an increasingly important contributor to our results. We are making steady progress in growing our mobile franchise by developing innovative offerings and expanding relationships with existing clients.

During the quarter, we launched a small but important program with TIM, the largest mobile carrier in Italy, allowing us to broaden our mobile footprint in Europe. In Latin America, the rollout of our Telefónica partnership continues and is going well.

Achieving our 14% ROE goal will require continued expense management. While the U.K. narrowed its operating loss in the first quarter, macroeconomic conditions remain challenging. We are committed to meeting our goal of U.K. profitability in the third quarter, but it will require further expense reductions.

At Assurant Specialty Property, we are pleased by the continued progress in our multifamily housing business. We now provide our renters and resident bond products through many of the nation's largest property managers. We believe we can expand this business even further in the future.

Revenues also increased in our lender-placed business. We now provide insurance and related services for nearly 33 million loans. This represents a 16% increase from the first quarter of last year, even though we believe the

nationwide inventory of mortgage loans declined over that period.

Our strategy of aligning with market leaders continues to pay off. In the next 2 quarters, we will add another 900,000 loans from portfolio acquisitions by 2 of our clients. Our growth is a testament to our robust capabilities, rigorous processes and high-quality service.

The rollout of our new lender-placed product is on track and will be implemented in 28 states by the end of the second quarter. Our new product forms and rates submitted to New York in March are pending review. In Florida, we will participate in a rate review next month to discuss our previously submitted filing.

During the quarter, the FHFA issued a notice of several potential changes to lender-placed insurance on GSE loans, such as the elimination of commissions and client reinsurance. We anticipate FHFA will publish final regulations later this year. We believe our new product offers solutions to the issues that emerged in the wake of the housing crisis and provides additional flexibility for mortgage servicers. As a leader, we have the capacity, expertise and capabilities to support both our clients and the GSEs as the housing market evolves.

At Assurant Health, we posted a net operating loss for the quarter that was driven by an increased tax liability related to the health care reform. At the same time, Health total sales grew for the fourth consecutive quarter, affirming that choice and affordability are important to consumers.

Major medical product sales increased as we benefited from our network partnership with Aetna. Sales of health access and supplemental products now comprise an increasing portion of total sales. We're encouraged by our sales momentum. We're moving ahead with a new suite of products to cover the essential health benefits required in 2014. We continue to believe our broad product portfolio allows us to meet a variety of consumer preferences.

At Assurant Employee Benefits, our easy-to-use administrative and enrollment systems give us a competitive advantage in the small employer market. We were encouraged that new business sales increased 19% over the first quarter of 2012. Key drivers of this growth were our enhanced demo network and expanding relationships with key brokers, including those focused on voluntary offerings.

Looking ahead, we remain committed to achieving steady improvements across each of our businesses by meeting the needs of consumers and clients, and, in turn, delivering long-term value to our shareholders. And with that, I'll turn to Mike for more detailed comments on our results.

Michael John Peninger

Thanks, Rob. I'll start with Assurant Solutions, where net operating income declined by \$6 million year-over-year, excluding a \$2.4 million disclosed item in the first quarter of 2012. Higher mortality in our preneed business and the previously disclosed loss of a mobile client contributed to the decline. Mortality experience can vary by quarter, and we expect preneed's results to improve during the rest of the year.

Domestic net earned premiums and fees increased significantly, primarily due to accelerated growth at a large service contract client. Our vehicle service contract business also grew as auto sales continued to rebound. This premium growth offset declines in other accounts, including the lost mobile account. We continue to expect modest growth in domestic premiums and fees over the rest of the year.

Continued expansion in Latin America across all products and the previous expense management efforts in Europe drove a 90 basis point improvement in the international combined ratio, excluding the first quarter 2012 disclosed item. Our international operations remain on track to deliver a 100 to 200 basis point improvement in the combined ratio for the full year, excluding disclosed items.

In the U.S., our combined ratio was 96.9% for the quarter, a slight increase from the prior year but well below our long-term target of 98%, as expense actions taken last year are improving results.

At Specialty Property, net operating income declined year-over-year. The decrease was driven by the \$14 million settlement agreement in New York, \$5.6 million of losses from hailstorms in the southeast and \$4.4 million of unfavorable loss development from Superstorm Sandy.

Significant loan volume growth during the past year contributed to higher expenses in the quarter as we expanded capacity to service new loans. Excluding these factors, Specialty Property's underlying results were solid,

demonstrating our leading market position.

Net earned premiums and fees increased by 9% due to premium production from lender-placed loan portfolios added in 2012 and contributions from multifamily housing products.

Our placement rate in the first quarter remained elevated at 2.89%, largely driven by loan portfolios acquired in the fourth quarter of 2012. Absent these loans, placement rates would have declined slightly.

We onboarded 1.7 million loans in the first quarter. And as Rob mentioned, we expect to add another 900,000 loans over the next 2 quarters. These 2.6 million new loans will produce premiums starting later this year. The changing composition of our loan portfolio, combined with macro trends, will lead to lower placement rates in the future; however, the new loans will help sustain our revenues over the course of 2013.

Given the increase in loan volume, we now expect our expense ratio, excluding disclosed items, to increase versus 2012 as we further expand capacity to support this growth and continue to enhance our customer service capabilities. We will update you later on our further progress at Specialty Property once we roll out our new lender-placed insurance product in other states and see the FHFA's final regulations.

Assurant Health reported a net operating loss for the quarter, reflecting the continued impact of health care reform. We increased our estimate of compensation expenses that are nondeductible under the Affordable Care Act. This change in estimate resulted in a \$10 million addition to our income tax expense in the first quarter.

Pretax earnings were in line with our expectations. In the first quarter, Health earned \$14.5 million compared to \$19.5 million in the first quarter of 2012. The decrease was driven by the continuing decline in individual major medical premiums and fewer small group lives. We are pleased with recent sales momentum, which has moderated the rate of revenue decline compared to past quarters. Also total insured lives continues to grow.

Going forward, we expect our effective tax rate to remain very high during the rest of 2013. This is primarily due to higher nondeductible compensation expenses and comparatively lower pretax earnings in 2012. For the full year, we now expect a modest after-tax profit in Health. In the near term, we consider pretax earnings a better gauge of underlying potential of the business than after-tax results.

We continue to believe that the long-term prospects for Health are favorable. We are building a product and distribution platform that will enable us to serve markets that should grow significantly as reform unfolds. At the same time, we will continue to manage our expenses and capital efficiently. As the business grows and pretax earnings increase, effective tax rates will moderate, leading to attractive after-tax returns for shareholders.

At Employee Benefits, investment income declined due to continued low yields and fewer invested assets. This decrease, along with the reduction in the discount rate for new long-term disability claim reserves, reduced segment profitability. As in preneed, we experienced higher mortality in the first quarter, but this was entirely offset by continued strong dental experience. Disability incidents and recovery rates remained stable during the quarter.

Net earned premiums and fees declined modestly due to the residual impact of the previously disclosed loss of 2 disability clients last year. For 2013 overall, we still expect net earned premiums and fees to be in line with 2012 due to continued growth in voluntary products. Expense and capital management will remain a focus throughout the year.

Turning to corporate matters. We recently issued \$700 million of debt at attractive yields. We set aside \$500 million of the proceeds to repay our 2014 notes when they mature next February. The additional debt will increase our after-tax interest expense by \$11 million in 2013. However, after the 2014 notes mature, our after-tax interest expense will decrease by about \$3 million a year, even with the additional \$200 million of debt.

We continue to manage our capital prudently. Consistent with prior years, we took a modest \$21 million of dividends from the operating companies in the first quarter. We still anticipate that dividends for the full year will equal operating earnings. As always, dividends may vary depending on the capital needs of the businesses and rating agency requirements.

For the full year, we continue to expect our Corporate segment operating loss to be in the range of \$65 million to \$70 million, excluding \$50 million of after-tax interest expense and roughly \$11 million of after-tax benefit from amortization of deferred gains.

In summary, while we had some challenges in the quarter, the underlying results in our targeted growth areas are encouraging. Profitable growth, ongoing expense management and prudent capital deployment remain key priorities. We look forward to continued progress over the rest of the year. And with that, I'll ask the operator to open the floor for questions.

Question-and-Answer Session

Operator

[Operator Instructions] Our first question is coming from Chris Giovanni with Goldman Sachs.

Christopher Giovanni - Goldman Sachs Group Inc., Research Division

I guess, first question just on Health. Obviously, there's a lot kind of going on with reform and moving pieces. And just wanted to kind of get your assessment of this business in terms of continuing to be kind of a specialty focus for you guys or what other opportunities you would consider with that segment?

Robert B. Pollock

Sure. So let's go back to when the Affordable Care Act was passed. We evaluated options for the business and concluded our best option was to modify our strategy, focus on affordability and choice, and, quite frankly, I think we've been very pleased with our results today. We said that things were going to be somewhat discontinuous on the results side because the Affordable Care Act provisions would come in over time. But we still feel very positive about where we are in that progression. The sales are up quite a bit, which shows that our product suite is resonating with buyers. And I think the other thing we said is we believe that once all reform is through, and that really won't be done until the end of '14, we're going to have a business that we think we can grow and we think we can earn attractive returns in. And I would say, to date, we are pleased with the results. Remember, in this business, this is not a capital intense business, and so the returns we need to earn on the capital base can produce quite good returns in this segment. And I think we feel quite good about where we are.

Christopher Giovanni - Goldman Sachs Group Inc., Research Division

Okay. And then on the debt offering, I mean, obviously, you have a fair amount of capital already, and you're putting some of that to work here in April. I guess the incremental \$200 million of debt, recognizing sort of opportunistic in terms of the cost of that, but how should we be thinking about the avenues you're exploring to kind of put that debt to work?

Robert B. Pollock

Sure. Let me make a couple of comments. I'll turn it over to Chris. I think we've demonstrated that we are very disciplined in our approach to capital management and take deployment very seriously. We obviously had debt that matures in 2014 and we needed to look at how we deal with that going forward. Chris, maybe you can provide some perspective on that.

Christopher J. Pagano

Yes, Chris. I think I guess the important point to make here is nothing's really changed with respect to our strategy around capital. As we mentioned in the remarks earlier, the incremental \$200 million is not leading to an increase in our after-tax interest expense, so there's no expense-related component of having the extra debt. We have talked about having extra – the opportunity put on incremental leverage. We saw an opportunity in the market. We felt like we got some very long-term attractive yields on the debt. But I don't think – and as Rob mentioned, we're going to continue to be disciplined. We have deployable capital in the form of cash on the balance sheet. We've got operating earnings that we believe we can get at over the course of the year. So tremendous amount of financial flexibility. In terms of deployment, again, the priorities haven't changed, capitalize the operating companies, look for profitable growth opportunities either organically or through M&A and return capital to shareholders, which we've demonstrated that we're willing to do over the last several years. And given where the stock is trading right now, we believe it's very attractive and that it continues to be a prudent use of our deployable capital. So again, those are messages that we have reiterated over the last dozen or so quarters, and it continues to be our strategy going forward.

Christopher Giovanni - Goldman Sachs Group Inc., Research Division

Okay. So it'd be sort of opportunistic around kind of the price versus sort of an imminent need to kind of do a transaction or anything like that at this point?

Christopher J. Pagano

Again, I think again, we looked at the market at the time we felt like there was an opportunity to put some modest leverage at no incremental cost in terms of interest expense and view that capital as another – just additional amount of capital on the balance sheet for deployment.

Operator

We will take our next question from Seth Weiss with Bank of America.

Seth Weiss - BofA Merrill Lynch, Research Division

I want to ask a few questions on Specialty Property and what guidance contemplates in terms of rate action, just to get clarity on that. So if you have 28 states with new product filed and you have rate reviews coming up in New York and Florida, if we look at the guidance that you have in place right now for modestly rising premium increases, where does that contemplate in terms of all those moving parts?

Robert B. Pollock

Well, we've certainly factored the change that went into effect in California. We have rate discussions as a normal course in many states. Those are sort of state-specific. I think the important thing is we try to balance all that we know about volume growth from new loans, rates, various other factors. All those things go into our overall outlook that revenue is going to be up a bit this year.

Christopher J. Pagano

And I'd just add to all of that, what Mike said, we filed in each of the states. We certainly have tried to reflect the experience of the states, which in some cases means there were probably modest declines that were filed through in some of those states. But a key component, Seth, is who actually ends up with our product, and that's something that changes over time. We've seen that over the last few years.

Seth Weiss - BofA Merrill Lynch, Research Division

Okay. And just in terms of Florida, I think this is the one that a lot of us are specifically watching out for. I believe you filed for a flat rate in your March filing. That's obviously different than what QBE was eventually able to push through on their side. I know it's a little bit of a different situation, but curious if you could just sort of comment on QBE's eventual 19% rate decline there versus what you filed with.

Robert B. Pollock

Yes, yes. Sorry, we really can't comment on QBE's filings. What we do, as we do in every state, is go through a lot of actuarial analysis around the specifics of our exposure and the various components of our rate filings until we feel good about the rates we filed for. We've seen over time when we've acquired new loans that our rates in Florida have been quite competitive in the marketplace. So overall, we certainly will be going through the review process with Florida, but we feel like we've given a very – we have a very solid analysis behind our filing.

Seth Weiss - BofA Merrill Lynch, Research Division

Okay. And then just one more, if I could, and this is just a sort of a numbers question. If we think about how much has been filed and approved for versus what's still in the pipeline with – I believe about 14 states still in the pipeline and, of course, New York and California. In terms of the total premium base, how much of that rate is now sort of more in a final state versus how much more will be pushed through the next couple of quarters if we think about in terms of the premium base?

Christopher J. Pagano

Yes, I guess a couple of points here I think that we've said. We're not done in Florida; Florida is our biggest state.

New York is a sizable piece of our volume, as well. But I think the other key thing is – implementation is the key here versus approval because there's a lot of work required to be able to administer these new rates across a servicer's portfolio and provide them with the flexibility our new product provides. So again, we have to do that in stages, and we're going to introduce those additional states in the second quarter. We plan to have them all done by the end of the year, and as we pointed out previously, we think our revenues will be up during 2013.

Operator

And we'll take our next question from Mark Finkelstein with Evercore Partners.

A. Mark Finkelstein - Evercore Partners Inc., Research Division

Just going back to Health. I guess the question is you alluded to focusing on pretax as a gauge for the earnings. I'm trying to understand that comment in the context of, does something structurally happen beyond '13 that maybe mitigates the longer-term impact of this tax impact – tax implication?

Michael John Peninger

Yes, I think what I was trying to get at, Mark, is when you think about the effective rate for the tax rate for the business, you really sort of think about a couple of things. One is the pretax earnings and then, what are the non – the expenses that are nondeductible under the Affordable Care Act. And while pretax earnings are lower than ultimately they will be once the business is through the reform transition, the effective tax rate will be lower at that point. So that's why we really think pretax is a good – a better gauge in the near term, as opposed to saying after-tax with these very high effective tax rates that we're reporting.

Robert B. Pollock

So – and just to add to what Mike said. If we think about this a little bit, our sales are up, but we're still seeing a decline in year-over-year premiums. We think that – we're optimistic we can get that to shift. We think when all the provisions are implemented, the market will grow. And therefore, right to what Mike said, we're going to have the opportunity to increase our pretax earnings, which will help alleviate this whole issue.

A. Mark Finkelstein - Evercore Partners Inc., Research Division

Okay – so the takeaway is that there's nothing that structurally or otherwise can be done to moderate this, I don't know, \$4 million, \$5 million impact a quarter other than growing into this bigger knot.

Robert B. Pollock

We've chosen to illustrate it in the Health segment. If we were an all health company, it would be spread over the whole thing. We could've spread it over all our segments. We just happen to put it in Health.

Michael John Peninger

But that is -- we are applying the provisions of the Affordable Care Act, Mark. So there will be this element of nondeductible expenses. And as Rob said, I do want to emphasize that if we were entirely a health company of our same overall size, the effect of this would be much less noticeable because it adds – I think if you think about our corporate effective tax rate overall, this adds somewhere in the vicinity of 50 basis points or 50 to 100 basis points or something like that. But we choose for, just to give you a better insight, to sort of apply the whole cost of that in the Health segment.

A. Mark Finkelstein - Evercore Partners Inc., Research Division

Okay. So this doesn't in any way change your view of the business model going forward in terms of participation in exchanges, continuing to offer major medical versus the affordable product, et cetera?

Michael John Peninger

That's correct. We think it's an attractive market. We think it will grow and, again, we'll point out again the capital requirements in this business are not that much.

A. Mark Finkelstein - Evercore Partners Inc., Research Division

Okay. Just my final question is can you just talk a little bit about the Employee Benefits segment? Earnings were a little bit soft, expenses high. What's the outlook on this? Is there anything in the quarter that we should be paying attention to outside of the discount rate adjustment?

Robert B. Pollock

Well, as we commented, our life mortality was high and we see that periodically. Mortality on a life block of our size can vary so we had a fair amount of life claims in the quarter. I don't infer any kind of a trend for that. Dental, we continue to be very pleased with the earnings and the growth in that product. The other thing I think actually expenses for benefits are – they're pretty carefully managed there. You're seeing a little bit of impact on the expense ratio because of the continued impact of we lost a couple of large disability clients that we've talked about in the past that – so the top line is suffering the impact of that, which affects the expense ratio. But overall, we expect life to normalize. We continue to think dental is going very well. Voluntary sales are growing. So lots of reasons to feel optimistic about Benefits outlook.

Operator

And we'll take our next question from John Nadel from Sterne Agee.

John M. Nadel - Sterne Agee & Leach Inc., Research Division

I have a question. A little bit following up on Seth's question on the premiums that have been – that you expect anyway to be approved or to be rolled out through the 28 states by the end of the second quarter. I'm just wondering if you can give us some help, I mean, without specifically knowing what servicers are going to choose to do with the more flexible product. If we just look at it on your premium base today, about what percentage of your premiums is reflected with these 28 states?

Robert B. Pollock

As we mentioned in the fourth quarter, we started with smaller states. I think that continued, and, John, you know that our biggest states are pending, clearly Florida. That all being said, I think that we'll have them all implemented by the end of the year. I think that we'll have resolution on where we are in Florida by the end of the second quarter. And we'll be able to provide more fuller details as the market unfolds. In terms of provisions with servicers, one of the great things about the new product is it affords servicers choices, and we're going to have to see how those unfold. It also provides us with the capability to handle things that are contemplated both in the New York settlement and the FHFA. Last thing I'd just say there is the servicers do a lot of things around the process, including performing important billing and collection features. So we'll work with them as this all works through to provide a smooth transition to everyone involved.

John M. Nadel - Sterne Agee & Leach Inc., Research Division

Okay. And I have a hypothetical for you. The New York settlement is obviously saying no more of these reinsurance or coinsurance arrangements with the lenders or servicers. The FHFA seems to be moving in that direction. And obviously, New York is lobbying hard every other state to incorporate a couple of these items, including that elimination of the sharing of premiums, I guess they call it. To the extent that, that gets passed all the way through, in your entire book you're no longer able to share those premiums or coinsure with your servicers, how much premium comes back from that? Because I know you comingle that amount with the flood program with the government, and it's just we don't know what portion relates to the lender-placed business. Can you give us some help on that?

Robert B. Pollock

Sure. Well, first, we only have, as we've mentioned previously, reinsurance with that small handful of clients, okay? It's full risk transfer that they participated in. So I'll let Mike amplify, but this will have implications on capital requirements in the business. It's a subset of the total you've mentioned, John. And Mike, you just want to talk?

Michael John Peninger

Really, we haven't chosen to break that out, John, and I think once all these regs come clear, it will play out.

John M. Nadel - Sterne Agee & Leach Inc., Research Division

Okay. And is it enough in terms of dollars of premiums that if this did play out that way and you recaptured all those premiums, is it enough that it would perhaps change your reinsurance program significantly? I mean, I assume there's still more than enough capacity from a pure sort of catastrophe reinsurance program perspective that this wouldn't really be a problem.

Robert B. Pollock

Yes. Chris, you want to comment on that?

Christopher J. Pagano

Yes. I think from the perspective of the program, I don't anticipate this leading to any changes in how we structure our program, and we'll comment more on that in the second quarter once we finish the placement. But as Mike mentioned, this would affect our capital holding. We would need to hold incremental capital at the property segment, kind of the rule of thumb is 50% of premium. And again, as this unfolds, we'll adjust accordingly.

John M. Nadel - Sterne Agee & Leach Inc., Research Division

But it's fair to assume that – I mean, if you're -- if this is really true full risk transfer, then, frankly, your margin on those premiums that you recapture shouldn't really change, correct?

Robert B. Pollock

That's correct.

John M. Nadel - Sterne Agee & Leach Inc., Research Division

Okay. Last question for you is this. I mean, you touched on a little bit in terms of pay is to buybacks earlier and, obviously, a ton of capital flexibility. I know we've got a reset over time on the size of the Specialty Property business, but can you help us with some insights maybe into how you and the board have thought about or discussed dividend policy? Because it seems to me that there's a real opportunity at Assurant to create a – well, I guess I'll say it this way more succinctly, to put a significant yield on the stock that can very well be supported by free cash flow, even if or even when Specialty Property earnings reset lower.

Robert B. Pollock

Okay. So the first thing is we've increased our dividend every year since we've been a public company, and I believe when we first went public, that dividend was \$0.07 a quarter. It's now \$0.21 a quarter. I think if you look at all the players in the financial services area, we're one of a small handful who've increased their dividend every year. So we've not been shy about increasing our dividend over time. Chris, you could just elaborate on how you view the use of cash dividend versus other deployment.

Christopher J. Pagano

Yes, sure. And again, John, just another comment on the dividend policy. That is typically, per policy, we have that conversation in the second quarter with the board. We're going to have to do that in the upcoming meeting. Other alternatives, a one-time special dividend is certainly out there, might have some short-term benefit but our capital management policy is focused on the long term. And when we have the opportunity to repurchase stock at a 15% discount to book value, which is roughly where it's trading right now, we think that's the better use of deployable capital and will contribute to long-term – the growth of long-term shareholder value. So we consider all of the things that you're talking about. We feel very comfortable, though, with our policy at this point. And again, we believe the stock's attractive and have been back in the market and continue to believe it's a good use of the capital we have at the holding company.

Operator

And we'll take our next question from Sean Dargan with Macquarie Securities.

Sean Dargan - Macquarie Research

I have a couple of questions about Specialty Property. First, the uptick in the expense ratio, which you attribute to the new loan portfolios, is that kind of a run rate expense ratio we should expect throughout the rest of the year?

Michael John Peninger

Well, there's a lot of expenses associated with onboarding the loan, Sean, and we've got a couple of things going on, just adding the loans, getting them onto the system, and then you've got – going forward, you've got the service requirement for those. And we're certainly committed to maintaining the highest levels of service that we've had in the past, so that requires a certain amount of staff to do that. We have a very sophisticated system that helps us in this. So there's – they're not all purely variable cost, but there are certainly some of those, and we want to be sure that we're maintaining our customer service levels.

Robert B. Pollock

And some of those expenses come before the premium shows up. And that's always been how this business has worked and I think will continue to. So these portfolio additions are not coming from existing clients, which is a little bit different than if they come from someone we have already. There's expenses if we lose from one of our clients but it goes to another. We know all the processes, procedures. We know something about the loans. When they come from a portfolio we don't have, there's more work involved.

Sean Dargan - Macquarie Research

Okay, that's helpful. And then I guess why did net written premiums and gross – or I'm sorry, gross written premiums and net earned premiums decline sequentially? I would have thought, given the onboarding, that, that line would have ticked up?

Christopher J. Pagano

The onboarding, the reason – the premium results can sort of vary as you're adding loan portfolio, Sean, because it depends on whether the loans are flat canceled versus coming on at renewal. And so when – and also since our coverage is effective when the date of prior policy, the voluntary policy lapse. Sometimes you get extra premium when it comes on board, which distorts the quarterly pattern of premiums.

Robert B. Pollock

But we add that over time. And I think one of the things to remember is we've added 1.7 million loans that you see in our totals here that have not yet produced premium but will later in the year.

Operator

And our next question comes from Mark Hughes with SunTrust.

Mark D. Hughes - SunTrust Robinson Humphrey, Inc., Research Division

Along that same line, the 900,000 loans that you're going to be bringing on, are those going to be flat canceled?

Robert B. Pollock

Yes, they are.

Mark D. Hughes - SunTrust Robinson Humphrey, Inc., Research Division

Okay. And then in the voluntary business, you've had a couple of very strong quarters in a row. What is the sustainability of that? Is that because the brokers are charged up to sell those products? Is there underlying demand that is that strong? What's happening there?

Robert B. Pollock

Yes. Well, we think that to those couple of things. One, I would say that our brokers are, in fact, more interested in voluntary because a lot of this is driven by the continued and sort of relentless increase in medical costs, which have small employers and brokers actually more interested in the voluntary benefits or the voluntary platform as a way to provide their employees with a good solid benefit package. And we really think that in addition to having a broad product suite, we have the system's capabilities and the technology to interface with the employer systems to make voluntary a very easy to offer package for small employers because one of the real challenges in the voluntary business is the administrative complexity of it. And we think that's where we have a better mousetrap. And I think that's starting to resonate in the market.

Operator

And we'll take our next question from Steven Schwartz with Raymond James & Associates.

Steven D. Schwartz - Raymond James & Associates, Inc., Research Division

Going back on – actually, the last 2 questions were kind of what I wanted to get to. The growth in the loan's track of Specialty Property in the quarter was substantial, more than I was expecting. That increase came from where?

Michael John Peninger

Well, we added 1.7 million in the quarter. I think we had talked about 1.3 million. We had another 400,000 that came in and then we had the 900,000 portfolio that Rob alluded to in his prepared remarks.

Robert B. Pollock

And just remember that we have not had premium on those loans yet come through.

Steven D. Schwartz - Raymond James & Associates, Inc., Research Division

Okay. And then I'm getting a little bit confused here. Flat cancel, they cancel and give them to you; is that accurate?

Robert B. Pollock

Yes. I mean, look, in essence, the policy and new offering will go out. We'll have to make sure that they don't have coverage elsewhere. And if that's the case, then we will start earning immediately.

Steven D. Schwartz - Raymond James & Associates, Inc., Research Division

So – but you just told me you weren't earning immediately.

Robert B. Pollock

Well, that's right. That's because we have included the things. But we've got to run things through our latter cycle so we know that those loans are there, but they've got to run through our latter cycle. We have to verify that they don't have coverage elsewhere. And when that happens, we'll start earning the premium.

Steven D. Schwartz - Raymond James & Associates, Inc., Research Division

Okay. So the new loans do not affect your – they artificially lower the placement rate; is that an accurate statement?

Robert B. Pollock

No. We've adjusted for that in the rate we've provided, yes.

Steven D. Schwartz - Raymond James & Associates, Inc., Research Division

Okay. And then the placement rate on the new 900,000? Would you say that...

Robert B. Pollock

Yes. Those are coming from clients where we don't really have a line of sight, Steven. So we'll onboard them, and once we've done that, we should have a line of sight on what will happen.

Steven D. Schwartz - Raymond James & Associates, Inc., Research Division

Okay. And then on the discount rate adjustment and Employee Benefits, the drag on earnings from that was how much in the quarter?

Robert B. Pollock

It's about \$1 million.

Steven D. Schwartz - Raymond James & Associates, Inc., Research Division

About \$1 million. Okay.

Operator

We'll take our last question from John Hall with Wells Fargo.

John A. Hall - Wells Fargo Securities, LLC, Research Division

I have a sort of a longer view question and something that I've been wrestling with as I look farther out '13 into '14, is really how to understand the rate at which the placement rate ultimately comes down on the Specialty Property book of business. I guess it was 2.89% this quarter, up by as a result of the new loans brought on. But how should we think about – as the real estate market recovers, is there any sort of period in time historically that you can point us back to, where you've got some data that says as foreclosures improve, and the like, the rate came down from X to Y over some period of time.

Robert B. Pollock

Yes. So if you go back and look at our 2011 Investor Day, we tried to provide some insight into that, John. I would say at that point in time, we thought it would be over a 5-year period, and you'd see placement rates trend back to 2006 levels, okay? Now what's changed since then? Because there's a couple of things here that in my mind are macro factors that are difficult to predict. And one is unemployment in the economy and as that remains elevated, I think placement rates stay up. I think a second is the number of seriously delinquent loans, some of which just relates to government policy and how they want to deal with those things. There have been a lot of policy around preventing foreclosure. I don't think we could've foreseen that. I think that's probably kept our placement rates up a bit too. I think the other one we're seeing that we didn't at the time, however, is also how voluntary carriers are dealing with their business in CAT-prone areas. Because we do have an overrepresentation in the CAT-prone areas because often coverage isn't available. So I think those are 3 factors that are driving things. I'd also point back to the comment Mike made, which is if you took out those loans we didn't have in 2012, our placement rate was down modestly in the quarter. And so we are seeing signs that, that it's happening and we expect it will happen as the economy improves.

John A. Hall - Wells Fargo Securities, LLC, Research Division

I guess as we think about what you provided back at the Analyst Day, that 5-year time frame, is that still the time frame over decline that you'd be thinking about now?

Robert B. Pollock

Well, I haven't been very good at predicting this, John, so let's start with that. To me, it's been up and I think one of the reasons it's up is that last factor I brought up. And so I think it's very difficult for us to be able to assess how it will come down. But the other way I look at that is we've also added quite a few loans to the portfolio since we rolled that information out.

Great. I want to thank everyone for joining us this morning. We look forward to updating you on key milestones in the months ahead. And please feel free to reach out to Francesca and Suzanne with any additional questions you might have.

Operator

Thank you. This does conclude today's teleconference. Please disconnect your lines at this time and have a

wonderful day.

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