October 9, 2012

Monica Jackson
Office of the Executive Secretary
Consumer Financial Protection Bureau
1700 G Street, N.W.
Washington, DC 20552

Re: Docket No. CFPB-2012-0034
Proposed 12 CFR Part 1024, Mortgage Servicing Standards, **Force-Placed Insurance**

Dear Ms. Jackson;

The Center for Economic Justice[1] (CEJ) and the Consumer Federation of America[2] (CFA) offer the following comments on the force-placed insurance provisions of the proposed 12 CFR Part 1024. CEJ and CFA have extensive experience with credit-related insurance, generally, and with force-placed insurance, specifically. Additionally, we endorse the comments in this docket by the National Consumer Law Center.

Background: The Mechanics of Force-Placed Insurance (FPI)

Servicers purchase a group master insurance policy or policies providing hazard coverage for all properties serving as collateral for all loans in the servicing portfolio. The master policy provides coverage as needed if and when the borrower fails to maintain required insurance on the property serving as collateral. The mortgage servicer pays a periodic premium to the FPI insurer based on the amount of coverage provided during that period. The FPI insurance rates used to determine the premium charge to the mortgage servicer are subject to state insurance regulation, but these rates determine the premium charge to the mortgage servicer from the insurer and the premium payment due from the mortgage servicer to the insurer. The FPI insurer does not charge individual borrowers with the FPI premium. Rather, the mortgage servicer may, but is not required to, recoup the premium payments made by the servicer to the insurer for the FPI placed on a borrower's property. Consequently, the charge by the mortgage servicer to the borrower for FPI is not a premium charge subject to state insurance regulatory oversight.

Reasonable Basis to Force-Place Insurance

The proposed regulation requires the servicer to have a reasonable basis to place FPI before it charges a borrower for the FPI, but provides no definition of reasonable basis. The proposed staff commentary provides the following:

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[1] The **Center for Economic Justice** (CEJ) is a non-profit organization that advocates on behalf of low-income and minority consumers on insurance, credit and utility issues before administrative agencies to promote greater availability and affordability of the basic services necessary for individual and community economic development.

[2] The **Consumer Federation of America** is an association of nearly 300 pro-consumer groups that was established in 1968 to advance consumers' interests through research, advocacy and education.

> 1. *Borrowers with escrow.* A servicer has a reasonable basis to believe that a borrower with an escrow account established for hazard insurance has failed to maintain hazard insurance if, for example, by a reasonable time prior to the expiration date of the borrower's hazard insurance (*e.g.,* 30 days before the expiration date), the servicer has not received a renewal bill. The receipt by a servicer of a notice of cancellation or non-renewal from the borrower's insurance company before payment is due on the borrower's hazard insurance premium also provides a servicer with a reasonable basis to believe that the borrower has failed to maintain hazard insurance.
> 2. *Borrowers without escrow.* A servicer has a reasonable basis to believe the borrower without an escrow account established for hazard insurance has failed to maintain hazard insurance if, for example, a servicer receives a notice of cancellation or nonrenewal from the borrower's insurance company.

The proposed staff commentary provides inaccurate and insufficient guidance. In both instances (with and without escrow), the commentary states that receipt by the servicer of a notice of cancellation or non-renewal from the borrower's insurance company is a reasonable basis to force-place insurance. This is incorrect because such a notice indicates only that the borrower no longer has coverage from that insurance company. Such a notice does not indicate the failure of the borrower to obtain replacement coverage.

The proposed commentary also states that, for borrowers with escrow, a reasonable basis to force-place is the failure to receive a renewal notice. Again this is inaccurate and insufficient guidance. There are many reasons why a servicer (or, more accurately, the FPI vendor providing insurance tracking for the servicer), might not receive the insurance company's renewal notice. The failure to receive a notice is the basis for a follow-up action by the servicer – to verify the non-renewal of coverage, to discover simply a failure to copy the servicer on correspondence or to learn if new coverage has been obtained by the borrower.

The staff commentary provides an unreasonable basis to force-place insurance and fails to recognize that servicers' insurance-tracking vendors routinely do far more to verify the absence of coverage than the two examples cited in the commentary.

In addition, the reasonableness of efforts to determine if a borrower has required coverage should be objectively measured by the ratio of false placements to total FPI placements. A false placement is the placement of FPI incorrectly because the borrower did, in fact, have required insurance coverage in place. In the event of a false placement, the borrower receives a full refund, known as a flat cancellation.

False placements harm borrowers, even though there is a full refund at some point, because there is some lag between the charging of the borrower for FPI and the refund reversing the charge. During the period between charge and refund, the amount owed by the borrower increases along with the monthly payment requirement. With large increases in monthly payment requirements due to false FPI placement, a borrower can easily become delinquent with potential harm to her credit record on file with consumer reporting agencies.

Testimony at public hearings on force-placed insurance earlier this year before the New York State Department of Financial Services and before the National Association of Insurance Commissioners indicate that false placements are 10% to 20% of total FPI placements. Such a high percentage is unreasonable.

We suggest that the staff commentary be revised with the proposed language deleted and replaced with:

> The aggregate standard for evaluating whether a servicer is utilizing necessary procedures to determine if the servicer had a reasonable basis for obtaining force-placed insurance is a ratio of FPI placements with flat cancellation to total FPI placements in a calendar year of 5% or less.

Disclosures

We applaud the proposed disclosure requirements and offer an additional recommendation. One of the requirements for the FPI disclosures to borrowers is a statement that the FPI "May not provide as much coverage as an insurance policy you buy yourself." In fact, FPI almost always provides significantly less coverage than a standard homeowners policy. FPI typically does not provide coverage for contents (personal property) of the home, additional living expense when an event renders the home unlivable or liability coverage in the event, say, a neighbor is injured on the borrower's property.

The intent of the notice and the specific notice requirements, such as the policy may not provide as much coverage, is to alert the consumer to a problem and prompt the consumer to action. However, a statement that the FPI "may not provide as much coverage" is too generic to provide meaningful information to the borrower.

The coverage provided under an FPI policy is set out in the group master policy issued to the mortgage servicer. Consequently, the mortgage servicer knows exactly what coverage is and is not provided by the FPI policy. If the FPI policy does not provide, as is normally the case, coverage for personal property, additional living expense or liability, there is no reason why the servicer's FPI disclosures cannot provide this information to the borrower. We suggest a disclosure requirement including emphasized text:

> The insurance we [bought] [buy]:

- Probably does not provide the same protections as an insurance policy you buy yourself. For example, the insurance we buy does <u>not cover the contents of your home</u>, so in the event of fire or hurricane, this insurance <u>would not replace your personal property</u>. The insurance we buy does not include other protections, like additional living expense in the event of a catastrophe or liability coverage if someone is injured on your property.

Exemption of Flood Insurance

The proposed regulation excludes from the definition of force-placed insurance "hazard insurance to protect against flood loss obtained a servicer as required by the Flood Disaster Protection Act of 1973." The Bureau's rationale for this exclusion is that force-placed flood insurance consumer protections are contained in the Flood Disaster Protection Act and failing to exempt flood insurance would create duplicative regulations.

The FDPA requirements for the purchase and maintenance of flood insurance on properties serving as collateral for mortgage loans include the availability of flood insurance through the National Flood Insurance Program (NFIP). For example:

> REQUIREMENT TO PURCHASE FLOOD INSURANCE
> SEC. 102. (a) After the expiration of sixty days following the date of enactment of this Act, no Federal officer or agency shall approve any financial assistance for acquisition or construction purposes for use in any area that has been identified by the Director as an area having special flood hazards **and in which the sale of flood insurance has been made available under the National Flood Insurance Act of 1968**, unless the building or mobile home and any personal property to which such financial assistance relates is covered by flood insurance in an amount at least equal to its development or project cost (less estimated land cost) **or to the maximum limit of coverage made available with respect to the particular type of property under the National Flood Insurance Act of 1968, whichever is less. . . .**
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> (b) REQUIREMENT FOR MORTGAGE LOANS.--
> (1) REGULATED LENDING INSTITUTIONS.--Each Federal entity for lending regulation (after consultation and coordination with the Financial Institutions Examination Council established under the Federal Financial Institutions Examination Council Act of 1974) shall by regulation direct regulated lending institutions not to make, increase, extend, or renew any loan secured by improved real estate or a mobile home located or to be located in an area that has been identified by the Director as an area having special flood hazards **and in which flood insurance has been made available under the National Flood Insurance Act of 1968**, unless the building or mobile home and any personal property securing such loan is covered for the term of the loan by flood insurance in an amount at least equal to the outstanding principal balance of the loan or the maximum limit of coverage made available under the Act with respect to the particular type of property, whichever is less.
> (2) FEDERAL AGENCY LENDERS.--A Federal agency lender may not make, increase, extend, or renew any loan secured by improved real estate or a mobile home located or to be located in an area that has been identified by the Director as an area having special flood hazards **and in which flood insurance has been made available under the National Flood Insurance Act of 1968**, unless the building or mobile home and any personal property securing such loan is covered for the term of the loan by flood insurance in the amount provided in paragraph (1). Each Federal agency lender shall

issue any regulations necessary to carry out this paragraph. Such regulations shall be consistent with and substantially identical to the regulations issued under paragraph (1).
(3) GOVERNMENT-SPONSORED ENTERPRISES FOR HOUSING.--The Federal National Mortgage Association and the Federal Home Loan Mortgage Corporation shall implement procedures reasonably designed to ensure that, for any loan that is--
(A) secured by improved real estate or a mobile home located in an area that has been identified, at the time of the origination of the loan or at any time during the term of the loan, by the Director as an area having special flood hazards **and in which flood insurance is available under the National Flood Insurance Act of 1968,** and

(e) PLACEMENT OF FLOOD INSURANCE BY LENDER.--
(1) NOTIFICATION TO BORROWER OF LACK OF COVERAGE.--If, at the time of origination or at any time during the term of a loan secured by improved real estate or by a mobile home located in an area that has been identified by the Director (at the time of the origination of the loan or at any time during the term of the loan) **as an area having special flood hazards and in which flood insurance is available under the National Flood Insurance Act of 1968,** the lender or servicer for the loan determines that the building or mobile home and any personal property securing the loan is not covered by flood insurance or is covered by such insurance in an amount less than the amount required for the property pursuant to paragraph (1), (2), or (3) of subsection (b), the lender or servicer shall notify the borrower under the loan that the borrower should obtain, at the borrower's expense, an amount of flood insurance for the building or mobile home and such personal property that is not less than the amount under subsection (b)(1), for the term of the loan.
(2) PURCHASE OF COVERAGE ON BEHALF OF BORROWER.--If the borrower fails to purchase such flood insurance within 45 days after notification under paragraph (1), the lender or servicer for the loan shall purchase the insurance on behalf of the borrower and may charge the borrower for the cost of premiums and fees incurred by the lender or servicer for the loan in purchasing the insurance.

[emphasis added]

Consequently, it is reasonable to interpret the force-placed insurance provisions of the FDPA to require a servicer to obtain and place a flood policy from the NFIP if the borrower fails to maintain required flood insurance.

In practice, the master FPI policy or polices obtained by servicers provide coverage for dwelling fire (e.g., "regular" hazards), wind-only (in locations where the standard homeowners policies exclude wind) and flood. The FPI flood is generally not coverage from the NFIP even for amounts up to the maximum amount of coverage offered by the NFIP. Just as FPI hazard coverage is far more expensive than a homeowners policy, FPI flood is far more expensive than NFIP flood coverage.

We suggest a more limited exclusion for flood insurance from the definition of force-placed insurance, as follows:

> 1024.37(a)(2)(i) Hazard insurance to protect against flood loss obtained by a servicer as required by the Flood Disaster Protection Act of 1973 and obtained by the servicer through the National Flood Insurance Program.

The proposed change would ensure that the various FPI consumer protections in the proposed rule, including requirements for reasonable charges to borrowers, would apply when the servicer force-places private flood insurance.

Reasonable Charges

Proposed Section 1024.37 (h) specifies limitations on FPI charges to borrowers. No staff commentary regarding this part is proposed.

As discussed above in the background section, state insurance regulators have jurisdiction over premium charges by an insurer to a policyholder and, consequently, have oversight over the premium charges of a FPI insurer to the mortgage servicer for the group FPI policy issued to the mortgage servicer and naming the mortgage servicer as the insured. State insurance regulators have no authority over the charges, if any, of a mortgage servicer to a borrower for FPI. The mortgage servicer, in its role charging the borrower for force-placed insurance, is not an entity regulated by state insurance regulators – not an insurer and not an agent of the insurer. Consequently, there are no charges from the servicer to the borrower that are subject to State regulation as the business of insurance.

In addition, we recommend that (h)(2) include specific guidance regarding prohibited charges. These additional provisions are consistent with those expressed in a servicing guideline bulletin issued by Fannie Mae earlier this year, though not yet fully implemented.[3]

> *Limitations on force-placed insurance charges.*
> (1) *In general.* Except for charges ~~subject to State regulation as the business of insurance and charges~~ authorized by the Flood Disaster Protection Act of 1973, all charges related to force-placed insurance assessed to a borrower by or through the servicer must be bona fide and reasonable.
> (2) *Bona fide and reasonable charge.*
> A bona fide and reasonable charge is a charge for a service actually performed that bears a reasonable relationship to the servicer's cost of providing the service, and is not otherwise prohibited by applicable law. A bona fide and reasonable charge by the servicer to the borrower, shall, regardless of the amounts paid by the servicer to the insurance company providing force-placed insurance:

[3] Detailed analysis of unreasonable expenses included in FPI charges is provided in CEJ's testimony before the Florida Office of Insurance Regulation regarding FPI rates of Praetorian Insurance Company of July 3, 2012.

(i) not include any commission or other compensation paid by the force-placed insurance company or its agent to the servicer or any affiliate of the servicer;
(ii) not include any costs associated with insurance tracking;
(iii) not include any costs for activities for which the servicer is being reimbursed by the owner of the mortgage;
(iv) not include any costs associated with administration of reinsurance programs with insurance companies affiliated with the servicer;
(v) not include any costs for subsidy of unrelated servicer activities; and
(vi) not include any other costs unless directly related to the provision of force-placed insurance.

Thank you for your consideration,

Sincerely,

Birny Birnbaum
Executive Director
Center for Economic Justice

J. Robert Hunter
Director of Insurance
Consumer Federation of America