BILLING CODE: 8070-01P

FEDERAL HOUSING FINANCE AGENCY

No. 2013-N-05

Lender Placed Insurance, Terms and Conditions

AGENCY: Federal Housing Finance Agency.

ACTION: Notice; input accepted.

This Notice sets forth an approach to address certain practices relating to lender placed insurance that the Federal Housing Finance Agency (FHFA) considers contrary to prudent business practice, to appropriate administration of Fannie Mae and Freddie Mac (the Enterprises) guaranteed loans, and which expose the Enterprises to potential losses as well as litigation and reputation risks. While FHFA plans a broader review of issues relating to the market for lender placed insurance, that includes receiving input from government and private sector parties, the practices that are addressed here are considered sufficiently distinct as to merit early action by the Agency acting as Conservator for the Enterprises.

Background

The FHFA oversees the operations of Fannie Mae and Freddie Mac. The Enterprises are in conservatorships, and, as Conservator, FHFA has statutory obligations in its conduct of the conservatorships, including preserving and conserving assets.[1] The Enterprises have diverse relationships with seller-servicers, ranging from loan originations to the administration of properties in default. These relationships are

---

[1] The duties and authorities of the Conservator are set forth primarily at 12 U.S.C. 4617.

governed by their seller-servicer guides and, in certain cases, by individual contracts. Part of the administration by servicers of the interests of the Enterprises relate to the maintenance of properties.

Lender placed (or forced place) insurance involves the imposition of property and casualty insurance on a property that does not have the coverage required by their mortgage instruments. This commonly occurs due to lapse of voluntary insurance coverage for non-payment of premium. The absence of coverage triggers notifications to borrowers advising them of the need to provide proof of adequate coverage and warning that, in the absence of this proof, insurance will be forced placed, possibly at higher rates and with diminished coverage.

Protection of property values is important to homeowners, communities, and to the Enterprises. At the same time, provision of such insurance products at an appropriate cost is of concern as well. Reportedly, premiums for lender placed insurance are generally double those for voluntary insurance and, in certain instances, significantly higher. FHFA recognizes that some greater risks are involved with lender placed insurance and that lender placed insurance carriers do not have the opportunity to underwrite the properties they insure, however, the multiples involved may not reflect claims experience and other measures. Loss ratios for lender placed insurance are significantly below those for voluntary hazard insurance and some states already have required or have considered rate reductions of 30 percent or more.

The Enterprises, operating in conservatorship and supported by taxpayers, may be affected by such costs where a servicer pays the higher premiums and is unable to recoup the cost from the homeowner or at a foreclosure sale, and the expense is passed along to the Enterprise for reimbursement.

In the wake of the financial crisis, demands for lender placed insurance have risen and, as a result, so have Enterprise expenses related to such coverage. Concerns about lender placed insurance costs, compensation, and practices have been raised by the National Association of Insurance Commissioners, state regulators, the Consumer Financial Protection Bureau, state attorneys general, and consumer organizations. Generally, the focus has centered on excessive rates and costs passed onto borrowers, as well as commissions and other compensation paid to servicers by carriers.

In order to keep lender placed insurance costs to the Enterprises as low as possible, practices that provide incentives for or do not deter higher costs should be avoided.

Approach to Certain Lender Placed Insurance Practices

For mortgages that the Enterprises purchase or guarantee, FHFA anticipates that the Enterprises will put in place restriction on lender placed insurance practices enumerated below. Before any such restrictions take effect, FHFA seeks input from the public and interested parties for 60 days from the publication of this Notice. After considering input received, FHFA will determine what elements of the restrictions may or may not be maintained, amended or revised in its direction to the Enterprises. Four months subsequent to the receipt of such input, and in consultation with the Conservator, Fannie Mae and Freddie Mac will provide aligned guidance to sellers and servicers, including implementation schedules related to these particular lender placed insurance practices.[2]

[2] Actions by the Enterprises only affect loans that they purchase or guarantee; their seller-servicer guides have no effect on practices of insurers except for dealings with the Enterprises.

The specific practices related to lender placed insurance that FHFA has determined pose risks to the Enterprises or run contrary to the duties of the Conservator and for which actions are specified are practices where there are concerns regarding conflicts between parties to the insurance agreement, including:

1. Certain Sales Commissions. The Enterprises shall prohibit sellers and servicers from receiving, directly or indirectly, remuneration associated with placing coverage with or maintaining placement with particular insurance providers.

2. Certain Reinsurance Activities. The Enterprises shall prohibit sellers and servicers from receiving, directly or indirectly, remuneration associated with an insurance provider ceding premiums to a reinsurer that is owned by, affiliated with or controlled by the sellers or servicer.

Input

FHFA invites input from any person with views on the planned practice limitations set forth above. FHFA also invites input on enhancing the transparency and consumer and investor protections related to lender placed insurance as well as regarding other practices that may operate to the detriment of the Enterprises operating in conservatorships. Further, FHFA is interested in whether there is data or information that would run contrary to the intended results sought by FHFA. Finally, FHFA is interested in the amount of time and difficulties associated with altering contracts between contractors and Enterprise servicers as would result from the planned approach.

FHFA will accept public input through its Office of Housing and Regulatory Policy (OHRP), no later than [INSERT DATE 60 DAYS AFTER PUBLICATION IN THE FEDERAL REGISTER], as the agency moves forward with its deliberations on appropriate action. Communications may be addressed to Federal Housing Finance Agency, OHRP, Constitution Center, 400 Seventh Street SW., Ninth Floor, Washington, DC 20024, or emailed to LPIinput@fhfa.gov. Communications to FHFA may be made public and posted without change on the FHFA Web site at http://www.fhfa.gov, and would include any personal information provided, such as name, address (mailing and email), and telephone numbers.

Edward J. DeMarco

Edward J. DeMarco,
Acting Director, Federal Housing Finance Agency.

3-25-2013
Date