NEW YORKERS FOR RESPONSIBLE LENDING

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Brian Montgomery
Associate Counsel
Financial Frauds and Consumer Protection Division
NYS Department of Financial Services
One State Street
New York, New York 10004

RE: Regulation of force-placed insurance, proposed 11 NYCRR 227 (Insurance Regulation 202)

Dear Mr. Montgomery:

The undersigned members of the New Yorkers for Responsible Lending coalition (NYRL) are pleased to submit comments to the Department of Financial Services regarding its request for comment on proposed force-placed insurance regulations. The proposed regulations will provide critically needed protections for homeowners in New York State, and would help reduce the kickbacks force-placed insurers pay to mortgage servicers that inflate the cost of force-placed insurance and push New York homeowners into foreclosure. Our groups strongly support the proposed regulations, and believe that they should be strengthened to further reduce the pervasive abuses in the force-placed insurance market.

NYRL is a 161-member state-wide coalition that promotes access to fair and affordable financial services and the preservation of assets for all New Yorkers and their communities. NYRL members represent community development financial institutions, community-based organizations, affordable housing groups, advocates for seniors, legal services organizations, housing counselors, and community reinvestment, fair lending, labor and consumer advocacy groups. Coalition members have detailed knowledge of the abusive force-placed insurance practices that have drained more than $970 million from struggling homeowners across New York State over the last nine years. Many New York homeowners have gone into foreclosure or have been put at risk of foreclosure because of the substantially higher monthly mortgage payments that result from abusive force placed insurance practices.

As DFS documented in its May 2012 hearing on force-placed insurance, mortgage servicers' market power enables them to demand illegal kickbacks from force-placed insurers. Force-placed insurance policies are chosen by mortgage servicers but paid for by homeowners, many of whom are low- or moderate-income or live in communities of color. As a result, mortgage servicers choose force-placed insurance policies based on the kickbacks and incentives they receive rather than on price or value for homeowners. This practice creates a perverse incentive

for mortgage servicers to aggressively place homeowners, many of whom are in foreclosure or struggling to keep up with their mortgage payments, into force-placed insurance policies, often without providing adequate notice.

Compensation for mortgage servicers also unnecessarily inflates the cost of the insurance, which can cost substantially—from 2 to 10 times—more than a homeowner's insurance policy in the voluntary market. From 2004 through 2012, force-placed insurance policies written in New York State had an average loss ratio of just 34.5%, compared to typical homeowner's insurance loss ratios of about 60% nationally, clearly indicating that the price for force-placed insurance is excessive. There is absolutely no legitimate explanation for this enormous gap in loss ratios other than extreme price gouging.

Our groups make the following recommendations to the Department of Financial Services to improve the already strong proposed rules:

1. Ban on kickbacks and non-monetary compensation for force-placed insurance should be expanded

We strongly support the proposed regulations' ban on insurers doing business with affiliated mortgage servicers, entering into reinsurance deals or paying any sort of commissions to servicers or their affiliates. These practices have substantially inflated the cost of force-placed insurance and create a strong incentive for servicers to impose force-placed insurance on homeowners, at the expense of renewing voluntary policies.

Before DFS entered into the recent settlement agreements with force-placed insurers prohibiting the practice, affiliates of mortgage servicers often unnecessarily reinsured force-placed insurance policies to share in potential underwriting profits. Since the loss ratios for force-placed insurance are extremely low, using affiliates to reinsure force-placed insurance policies is a low-risk way for the banks that own mortgage servicing companies to further gouge homeowners by claiming a portion of the exorbitant premiums charged for force placed insurance. JPMorgan Chase, for example, reinsured 75% of the force-placed insurance premiums it collected from homeowners through its subsidiary Banc One.[1]

The Department of Financial Services' proposed ban on almost all forms of kickbacks will effectively address mortgage servicers' incentives to push homeowners into extremely expensive force-placed insurance policies. The proposed rules, however, will still allow mortgage servicers to enjoy free- or reduced-cost insurance tracking and other administrative services provided by force-placed insurers or their affiliates. The cost of insurance tracking and administrative services, which covers all homeowners whose loans a servicer administers, is borne exclusively by the homeowners with force-placed insurance in the form of larger premiums. This tracking is a routine servicing expense that should be paid for by servicers or investors, not struggling homeowners. This arrangement unfairly burdens these homeowners, who are often already in default or foreclosure. Therefore, DFS should also prohibit force-placed insurers from providing free or below cost outsourced services, including monitoring servicers' portfolios or performing

[1] See testimony of Banc One and Select Portfolio Servicing at 5/17/12 NYS Department of Financial Services hearing on force-placed insurance. Available: http://www.dfs.ny.gov/insurance/hearing/fp_052012_trans_err.htm

administrative services associated with providing and subsequently cancelling force-placed insurance when it is not required.

DFS should expand its proposed regulations to make clear that no mortgage servicers or affiliated entities are permitted to receive any fee, commission, kickback, reinsurance contract, service such as insurance tracking or administration, or other thing of value in exchange for purchasing force-placed insurance.

DFS should also develop a protocol for supervision that includes regular data collection and reporting to ensure that force-placed insurers are complying with these standards.

2. Strengthen Minimum Loss Ratio and Rate Filing Requirements

The proposed regulations' requirements that force-placed insurers file rates with an expected 62% minimum loss ratio, re-file rates immediately if insurers report loss ratios less than 40%, and re-file rates supported by data and actuarial analysis every three years are critical to address force-placed insurers' long-standing practice of price-gouging. During the past nine years, force-placed insurers in New York State have enjoyed a loss ratio of only 34.5% despite two recent catastrophic storms. Requiring a minimum loss ratio of 62% will bring force-placed insurance loss ratios in line with voluntary homeowner's insurance loss ratios and should, in conjunction with the proposed regulations' anti-kickback provisions, substantially decrease the price of force-placed insurance in New York.

DFS should further improve this protection by increasing the minimum loss ratio required to 80%. Force-placed insurers face substantially lower administrative and underwriting expenses than insurers that sell voluntary homeowner's insurance policies and can reasonably be expected to file rates with an 80% minimum loss ratio.[2] The resulting lower force-placed insurance prices would substantially increase the chances that New Yorkers in foreclosure who have force-placed insurance imposed will be able to secure affordable loan modifications or reinstate their mortgages.

3. Coverage Limits, Sufficiency of Demonstration and Timely Premium Refunds

The proposed regulations on coverage limits, sufficiency of demonstration and refunds of unearned premiums are all important protections that address common force-placed insurance abuses. Mortgage servicers and force-placed insurers often make it difficult for homeowners to provide proof of insurance, and delay refunds of unearned force-placed insurance premiums when homeowners are able to provide this proof.

The proposed coverage limits strike the right balance between protecting homeowners from overcharges and from being exposed to unexpected risk as a result of inadequate insurance coverage. Homeowners whose mortgages are underwater are sometimes charged for coverage to insure the outstanding principal balance of their mortgages, which can unfairly inflate force-placed insurance costs when the principal balance exceeds the replacement value of improvements on the property. Conversely, homeowners with small mortgage balances can be

[2] See testimony of Center for Economic Justice at 5/17/12 NYS Department of Financial Services hearing on force-placed insurance. Available:
http://www.dfs.ny.gov/insurance/hearing/fp_052012/Birny_Birnbaum_Center_for_Economic_Justice_testimony.pdf

exposed to unexpected risk when single-interest force-placed insurance policies cover only the unpaid balance of loans that are significantly smaller than the replacement value of the improvements on mortgaged properties. Requiring force-placed insurers to provide coverage at the last known voluntary coverage amount that was compliant with mortgage loan requirements will ensure that people receive the amount of coverage they expect and prevent force-placed insurers and servicers from gouging underwater homeowners. In cases in which the last known coverage amount was not compliant with mortgage loan requirements, the default coverage amount of the replacement cost of the improvements on the mortgaged property is appropriate to ensure homeowners receive adequate coverage but are not charged for unnecessary coverage.

4. Expand the proposed regulations to cover mortgage servicers as well as force-placed insurers

The proposed regulations effectively address force-placed insurers' role in gouging homeowners who require force-placed insurance coverage, but fail to address the abusive tactics mortgage servicers employ when homeowners fall behind on their insurance or escrow payments. Although many insurance-related servicing tasks are in fact carried out by force-placed insurers or their affiliates that will be covered by the proposed regulations, the rules governing notice to homeowners and bans on kickbacks should be expanded to include servicers. In addition, DFS should use its authority to regulate mortgage servicers to protect homeowners from mortgage-servicer specific force-placed insurance abuses including servicers' unnecessary cancelation of homeowners' voluntary policies, and retroactive billing.

Require servicers to advance payment for property insurance for all homeowners whose insurance policies are canceled for non-payment

DFS should expand the proposed regulations to require mortgage servicers to continue payments of homeowners' existing insurance policies or reestablish the policies if homeowners miss payments of hazard, homeowner's, wind, excess wind, flood or excess flood insurance premiums. DFS should require that, if homeowners fall behind on their insurance payments, servicers must advance their own funds to pay past due premiums and reinstate the homeowners' insurance coverage. If homeowners do not have existing escrow accounts, servicers must establish escrow accounts to pay future premiums. DFS should make clear that servicers must exhaust all options to keep homeowners' existing insurance policies in place before resorting to force-placed insurance.

Requiring servicers to maintain homeowners' voluntary insurance policies would substantially reduce the need for force-placed insurance and would help prevent foreclosures. Voluntary premiums are far less expensive than force-placed insurance, and requiring servicers to advance these premiums rather than impose force-placed insurance would help many New York families reduce both defaults that occur as a direct result of excessive force-placed insurance charges, and foreclosures that occur when force-placed premiums block homeowners from affordable loan modifications.

Limit retroactive charges

Mortgage servicers are responsible for tracking insurance coverage on the loans they service. When there is a lapse in a homeowner's insurance coverage, the servicer, typically through an insurance tracking vendor, notifies the force-placed insurer. It is the servicer's responsibility to identify lapses in insurance and notify homeowners of these lapses in a timely fashion.

Servicers often delay notifying homeowners about force placed insurance for months, unfairly piling thousands of dollars of debt onto homeowners who are unaware that their homeowner's insurance policies have been canceled. For example, Mr. W, a Bronx homeowner, was forced into foreclosure because he did not receive timely notice of force-placed insurance:

Mr. W, who lives in the Bronx with his wife and two children, fell behind on his mortgage after his monthly payments suddenly increased by more than $1,400 because his servicer failed to notify him that it had placed force-placed insurance until the policy had been in effect for a full year. Although Mr. W paid his annual homeowner's insurance premium at closing and made timely mortgage and escrow payments, his insurance was canceled for non-payment because his servicer never made insurance payments from his escrow account. Mr. W was not notified of the cancellation and continued paying his loan and escrow payments, but the servicer imposed a force-placed insurance policy anyway without notice, and failed to bill Mr. W for the cost of the policy. About a year later, the force-placed policy was renewed and he was suddenly billed for the past year's and the upcoming year's worth of force-placed insurance premiums, costing more than $13,000. Once his servicer increased his payments by $1,400 per month to cover the alleged shortfall, Mr. W was no longer able to pay his mortgage. To make matters worse, Mr. W. was not immediately informed that he had the option to purchase his own insurance at a lower cost even after numerous phone calls to his servicer to inquire about the increase in his mortgage payments. When he realized that he could do so, he searched and found a far less expensive policy. Mr. W is now in foreclosure as a direct result of the force-placed insurance.

Mr. W's experience with force-placed insurance illustrates the pressing need for timely notice by servicers and insurance tracking vendors and for strict limits on retroactive billing. The proposed regulation's clarification that insurance tracking companies affiliated with force-placed insurers should follow the force-placed insurance notice provisions in the Real Estate Settlement Procedures Act (RESPA) will help ensure that homeowners receive informative notices about force-placed insurance, but RESPA fails to address abusive retroactive billing practices.

DFS should improve on RESPA's notice requirement by requiring servicers or force-placed insurers and their affiliates to provide the first required notice within 15 days of a force-placed insurance policy coming into effect, and should not allow retroactive charges for more than 60 days' worth of force-placed insurance coverage. It is reasonable to expect that servicers (or their vendors) may fail to identify a lapse in insurance at the instant the lapse occurs or even for a short period of time following the lapse. It is unreasonable, however, to allow a servicer to delay sending notices in order to retroactively charge a borrower for a lengthy period of force placed insurance coverage.

The Department of Financial Services has demonstrated its commitment to cracking down on abusive force-placed insurance practices over the past two years, and the proposed regulations will go a long way to addressing the rampant corruption and widespread abuses that characterize the force-placed insurance industry. We urge DFS to strengthen the proposed regulations further

by expanding them to cover servicers, and by closing the last loopholes that could still allow force-placed insurers and servicers to gouge homeowners in New York State.

Thank you for the opportunity to comment.

Sincerely,

Albany County Rural Housing Alliance, Inc.
Bedford-Stuyvesant Community Legal Services
Chhaya Community Development Corporation
Cypress Hills Local Development Corporation
District Council 37 Municipal Employees Legal Services
Empire Justice Center
JASA/Legal Services for the Elderly in Queens
The Legal Aid Society
Legal Services NYC
Legal Services NYC – Bronx
Long Island Housing Services, Inc.
Margert Community Corporation
MFY Legal Services, Inc.
Nassau/Suffolk Law Services
Neighborhood Preservation Coalition of NYS, Inc.
New Economy Project
New York Public Interest Research Group
Pratt Area Community Council
Queens Legal Services
South Brooklyn Legal Services
Staten Island Legal Services
SUNY Buffalo Law School Consumer Financial Advocacy Clinic
Westchester Residential Opportunities, Inc.
Western New York Law Center