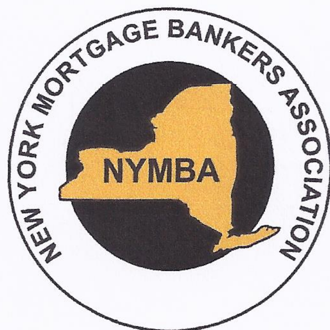

November 14, 2014

Brian Montgomery
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RE: Proposed Rule Making on Lender Placed Insurance, I.D. No. DFS-39-13-00022-RP

Dear Mr. Montgomery:

The New York Mortgage Bankers Association (NYMBA)[1] and the Mortgage Bankers Association (MBA)[2] appreciate the opportunity to comment on the New York Department of Financial Services' (NYDFS) proposed rule 11 NYCRR 227 (Insurance Regulation 202) relating to Lender Placed Insurance (LPI) (the Proposed Rules). The Proposed Rules incorporate previously submitted public comments to the NYDFS' prior proposed rules relating to LPI and changes the industry's understanding of monitoring for the existence of appropriate insurance coverage on the collateral (Insurance Tracking).[3] Specifically, the Proposed Rules:

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[1] The New York Mortgage Bankers Association, Inc. (NYMBA), founded in 2014, is a statewide organization devoted exclusively to the field of real estate finance. NYMBA's rapidly growing membership comprises of both bank and non-bank mortgage lenders and servicers, as well as a wide variety of mortgage industry-related firms. The NYMBA was formed to encourage its members to engage only in sound and ethical business practices, and to inform its members of changes in the laws and regulations affecting the mortgage business. The association helps those engaged in or affected by the mortgage business to be better informed and more knowledgeable. It is dedicated to the maintenance of a strong real estate finance system. This involves support for a strong economy, a public-private partnership for the production and maintenance of single and multi-family homeownership opportunities, and a strong secondary mortgage market.

[2] The Mortgage Bankers Association (MBA) is the national association representing the real estate finance industry, an industry that employs more than 280,000 people in virtually every community in the country. Headquartered in Washington, D.C., the association works to ensure the continued strength of the nation's residential and commercial real estate markets; to expand homeownership and extend access to affordable housing to all Americans. MBA promotes fair and ethical lending practices and fosters professional excellence among real estate finance employees through a wide range of educational programs and a variety of publications. Its membership of over 2,200 companies includes all elements of real estate finance: mortgage companies, mortgage brokers, commercial banks, thrifts, Wall Street conduits, life insurance companies and others in the mortgage lending field.

[3] The NYMBA and MBA believe that their members have different operating methods that may result in different servicers performing varying parts of the proposed definition of "insurance tracking" services for themselves with other parts being performed by their LPI carrier or another provider. The MBA is not addressing these variations in its Comment Letter.

- create a new definition of "Insurance Tracking" by delineating various functions in the context of when those functions are performed (Proposed 227.1(f) (1) and (2));
- mandate that expenses relating to Insurance Tracking must be excluded from the rate (Proposed 227.7 (c)(3); and
- add a requirement that Insurance Tracking may not be provided to a servicer at a reduced fee or no separately identifiable charge (Proposed 227.6 (g)).

The stated intent of the Proposed Rules is to protect homeowners and investors, however, the effect will actually increase costs for all borrowers.

The Proposed Rules' treatment of some Insurance Tracking expenses as a servicer responsibility, rather than an insurer underwriting or exposure management expense, based on when the Insurance Tracking is done in relation to borrower-obtained voluntary insurance, does not take into consideration the rationale behind the insurance tracking process. Simply put, insurance tracking is a process to protect the LPI carrier from uninsured losses and, therefore, the costs are appropriately borne by the LPI carrier. The Proposed Rules effectively transfer to servicers some of the LPI carrier's expenses related to protecting itself against these insurance risks.

It is critical that LPI insurers be able to monitor coverage at all times since the insurer agrees to provide automatic coverage upon lapse to all loans in a servicer's portfolio. Insurance Tracking expenses should not be treated distinctly and cannot easily be separated when incurred by the LPI carrier, whether "pre" or "post" lapse of the voluntary policy. Given the LPI carrier's exposure resulting from their automatic coverage program, we see no reason why part of their expenses should be arbitrarily transferred to mortgage servicers.

The Proposed Rules will not reduce costs for borrowers and will likely result in greater pass through costs to borrowers. Requiring servicers to pay for part of an LPI insurer function will impose on all borrowers the cost of Insurance Tracking, including the majority of borrowers who honor their contractual promises to maintain continuous insurance coverage on their properties. Currently the costs appropriately fall on the small percentage of borrowers who breach those promises and are the reason that tracking is necessary in the first place.

We also note that the consent orders that the NYDFS entered into with various LPI insurers excluded expenses for tracking functions from "free or below-cost outsourced services" without the proposed time distinction between a pre- and post-lapse of the voluntary policy.

For these reasons, we would encourage the NYDFS to revise the relevant sections of the Proposed Rules (Sections 227.1(f), 227.6(g), 227.7(c)(3), and 227.7(f)) to make them consistent with the consent orders. In support of this, we would note the following:

The LPI Insurer Assumes the Risk, so it is Best Suited to Manage the Exposure (*i.e.* Perform the Tracking)

The ability of lenders to sell mortgages in the secondary market increases capital available to borrowers and lowers interest rates. As part of the securitization process, investors require lenders and their servicers to ensure that the collateral securing the purchased loans is

adequately insured against the risk of loss "at all times."[4] In the absence of such risk mitigation, secondary market mortgage purchasers either will not purchase these loans at all or will insist on a higher return to account for the greater risk, which would increase mortgage interest rates.

Servicers are able to meet the insurance requirement without lapses in coverage by contracting with LPI carriers who are willing and have the existing capability to provide automatic, sight-unseen, and continuous insurance coverage for all properties within the servicer's portfolio. This coverage comes into existence automatically upon the lapse of the voluntary policy, whether the LPI insurer is aware of the lapse or not. This automatic and continuous issuance enables lenders and servicers to meet the secondary market's requirement of continuous, acceptable insurance coverage. The automatic coverage provided by LPI carriers helps lower the interest rates charged to all borrowers by lowering the risks associated with uninsured losses.

The LPI insurers are best-suited to undertake the tracking process for their own benefit. The exposure management nature of Insurance Tracking is not dependent on the expiration of the voluntary policy. Instead, it is the process by which LPI insurers understand their exposure as to the entire servicer portfolio at any given time. Understanding of this total exposure is critical to the LPI insurer's management of its risk.

The functions performed prior to the lapse of voluntary insurance would be the same as the functions performed after the lapse, but under the Proposed Rules they would have to be segmented in order to appropriately allocate costs. This would result in increased costs and inefficiencies through redundant systems and processes since many of the same systems, personnel and other resources are involved both pre- and post-lapse. It would also create administrative burdens for the LPI carriers and servicers in trying to allocate the costs of performing a single function based on an arbitrary timing distinction.

Making Tracking a Servicer Function Could Actually Lead to Higher LPI Rates & Borrowing Costs

Insurance Tracking is not required of, or a core competency for servicers, and they therefore have limited capability to assume Insurance Tracking responsibility. Requiring servicers to incur the cost of Insurance Tracking in order to avoid the inclusion of those costs in the LPI rates would only increase servicing costs, which would ultimately result in higher costs to all borrowers, including the majority of borrowers that comply with their contractual promises to maintain adequate coverage on their properties.

The Proposed Rules Conflict with Other Authorities

As noted above, the consent orders entered into by the NYDFS and certain LPI carriers recognize the reality that Insurance Tracking for purposes of exposure management, at all times, is an insurer cost properly included in the insurance rate. The orders do so by carving out all tracking costs incurred for exposure management from the prohibition on LPI carriers providing servicers with free or below-cost services. Based on the consent orders, LPI carriers filed and received approval for new rates with the NYDFS.

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[4] See, Fannie Mae Single Family Servicing Guide Part II, Chapter 6, stating: "Part of a servicer's responsibility for protecting Fannie Mae's interest in the security property is to ensure that hazard insurance (including flood insurance), under the terms specified in Fannie Mae's Guides, is in place at all times."

The NYDFS consent orders are not the only authority recognizing an insurer's exposure management expenses. A virtually identical carve-out appears in the recent Florida consent order regarding LPI, and the California Department of Insurance expressly held that Insurance Tracking expenses are properly included in LPI rates.[5] Similarly, the National Association of Insurance Commissioners (NAIC) Creditor Placed Insurance Model Act includes Insurance Tracking as an appropriate "other acquisition" cost to be considered in determining whether rates are appropriate.[6] The Proposed Rules are inconsistent with those consent orders and model regulation and the analyses underlying them.

LPI Exposure Management (*i.e.* Tracking Insurance) is a Necessary Substitute for Standard Market Underwriting

Insurers must understand their exposure and price appropriately for the risks they take to remain solvent and able to pay claims over time. In the LPI context, this involves continuously tracking from the inception of the loan the status of the borrower obtained coverage on the properties the LPI insurer has already agreed to cover if the BOI lapses. The LPI insurer must understand which properties it is covering, and may be required to cover, at any given point in time, where those properties are and the amount of coverage afforded among other factors.

In the non-LPI context there is no dispute that the property-specific underwriting expenses an insurer incurs to understand its risk are exposure management costs which are properly reflected in the rate charged for the coverage as acquisition expense. For LPI insurers, who must cover all properties in a portfolio sight unseen, tracking is necessary to affect the inability to conduct such property-specific underwriting. Monitoring coverage on all properties in the potential risk pool enables LPI carriers to better understand the risk they are taking. Continuous Insurance Tracking is therefore an LPI carrier exposure management function just as traditional underwriting is for non-LPI carriers and the cost of that Insurance Tracking is just as proper to include in the LPI rate as an acquisition expense as underwriting functions which are part of the acquisition expense built into non-LPI rates.

LPI Carriers do not have the Unilateral Discretion to Implement Market Changes

As a practical matter, it should also be noted that LPI carriers do not have the ability to unilaterally revise their contracts with servicers to charge for the costs of Insurance Tracking prior to lapse of the BOI. As such, LPI carriers simply would not be able to meet the requirements absent consent from servicers, and even if consent is provided, it is unlikely that such consent could be secured prior to the effective date of the Proposed Rulemaking.

The NYMBA and the MBA appreciate the opportunity to comment on this proposed rulemaking. For the reasons stated above we would encourage the NYDFS to exclude Sections 227.1(f), 227.6(g), 227.7(c)(3), and 227.7(f) from the final Insurance Regulation 202 (11 NYCRR 227).

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[5] See, In the Matter of the Rates, Rating Plans, or Rating Systems of American Security Insurance Company, Case No. OV-01-01-8309 (April 18, 2002).

[6] See, NAIC 375-1, Section 8.E.

We look forward to discussing our letter and our recommendation further. If you have any questions, please feel free to contact Marianne Collins at (518) 963-0593 (mcollins@nymba.org) or Pete Mills at (202) 557-2878 (pmills@mba.org).

Respectfully,

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